

Factsheet 31 October 2020

# NIKKO AM NZ CORPORATE BOND STRATEGY

Assets are held in the Nikko AM Wholesale NZ Corporate Bond Fund. The Nikko AM NZ Corporate Bond Fund (retail) and Nikko AM KiwiSaver NZ Corporate Bond Fund invest in units in the wholesale fund, which the commentary refers to.

## Market Overview

- NZ interest rates were stable over the month after steep falls earlier in the year.
- Credit has continued to perform well with the increase in new issuance readily absorbed.
- The actions and language of central banks and governments continues to have a strong influence on bond markets.

## Fund Highlights

- The fund produced modest returns over the month but still outperformed returns from cash, and continues to perform well relative to benchmark.
- NZ bank bonds have narrowed further in margin with supply limited.

## Performance

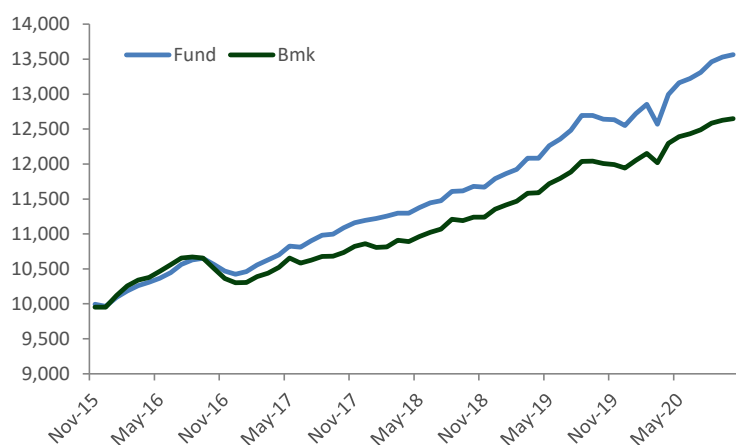
|                        | One month | Three months | One year | Three years (p.a) | Five years (p.a) | Ten years (p.a) |
|------------------------|-----------|--------------|----------|-------------------|------------------|-----------------|
| Wholesale <sup>1</sup> | 0.25%     | 1.90%        | 7.28%    | 6.95%             | 6.29%            | 6.95%           |
| Benchmark <sup>2</sup> | 0.18%     | 1.25%        | 5.35%    | 5.62%             | 4.81%            | 5.25%           |
| Retail <sup>3</sup>    | 0.17%     | 1.69%        | 6.43%    | 6.11%             | 5.44%            | 6.04%           |
| KiwiSaver <sup>3</sup> | 0.18%     | 1.70%        | 6.39%    |                   |                  |                 |

1. Returns are before tax and before the deduction of fees.

2. Current benchmark: Bloomberg NZBond Credit 0+ Yr Index. No tax or fees.

3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

## Five Year Cumulative Performance, \$10,000 invested<sup>1,2</sup>



## Portfolio Manager

**Fergus McDonald,**  
**Head of Bonds and Currency**



Fergus is responsible for the investment of the Bond, Cash and Currency mandates. Fergus has been actively involved in the NZ financial markets since 1981. The portfolio management team for the domestic fixed income funds includes Ian Bellew, Fixed Income Manager and Matthew Johnson, Fixed Income Manager.

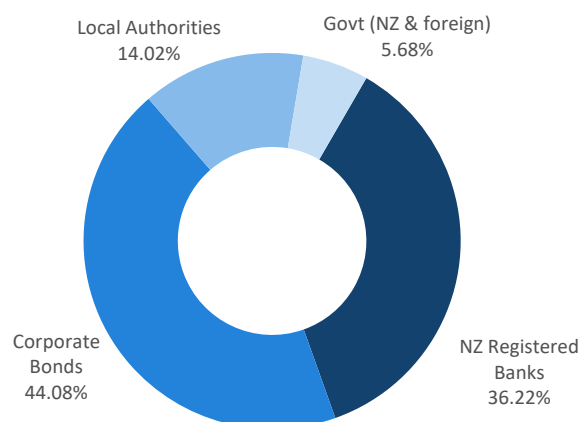
## Overview

The strategy aims to generate income by constructing an actively managed investment portfolio of New Zealand bonds, deposits and cash with the potential for capital gain from New Zealand dollar fixed interest markets.

## Objective

The fund aims to outperform the benchmark return by 0.70% per annum before fees, expenses and taxes over a rolling three year period.

## Asset Allocation



| Top 5 Corporate Issuers      | %    | Credit Quality (% of fund) | %     | Duration                                |
|------------------------------|------|----------------------------|-------|---|
| NZ Local Govt Funding Agency | 6.73 | AAA                        | 3.67  | Fund 4.25 years vs Benchmark 3.31 years |
| Fonterra Cooperative Group   | 5.23 | AA                         | 40.95 |   |
| Kiwibank                     | 5.06 | A                          | 27.68 | <b>Yield</b>                            |
| Westpac NZ Ltd               | 4.83 | BBB                        | 26.41 | Fund (gross) 1.07% vs Benchmark 0.63%   |
| ASB Bank Ltd                 | 4.74 | BB                         | 1.29  |   |

## Market Commentary

October produced modest returns from the NZ bond market. Short term bonds outperformed longer term bonds as the Reserve Bank continued to talk up the prospect of a negative Official Cash Rate in 2021. The key drivers of returns over the month were an incremental move lower in interest rates out to five years and continuing strong performance from credit holdings, supported by a higher than benchmark portfolio yield.

New Zealand’s inflation rate unexpectedly slowed in the third quarter of 2020 as fuel prices failed to recover previous falls, adding to signs the Reserve Bank may need to deliver more stimulus. The RBNZ Governor signalled he is prepared to use a suite of monetary policy tools to avoid seeing deflation take hold. Governor Orr said “The failure of monetary policy is deflation”, he went on to say “I’d prefer to be battling with the quality problem of re-containing high inflation than the real challenge of battling deflation.”

Further insights from the Reserve Bank reveal all their economic scenarios include very weak inflation pressures. That has been the motivation for their approach of going hard, going early and risking doing too much rather than too little. They concede that some data has surprised on the upside, however the economy is still on life support to some extent that will last for some time ahead. There will be a transition period required before a full economic recovery occurs. This transitional period will require continued policy support especially as the global environment has risk to the downside.

On a sector basis, NZ government bonds and longer duration bonds under performed and corporate and bank bonds were some of the better performers. It is important to note that longer maturity bonds increase more in value than shorter maturities when yields fall due to their longer duration exposure and resultant greater leverage to interest rate movements. For credit, the increase in supply of new issues has not dented demand thus far and sectors where issuance is expected to remain scarce such as banks have continued to tighten in margin. Conversely, some other issuers’ credit margins are reasonably consistent with where they were pre-COVID. We have been investing where we see value with a quality and liquidity bias, as there still remains a reasonable amount of uncertainty around about the economic outlook.

## Fund Commentary

The fund outperformed benchmark over the month. The main positive contributors were strong performances from credit issues supported by a higher than benchmark fund yield. We extended duration by adding some long maturity bonds to enhance the fund’s yield. Credit margins have performed strongly with supply very limited. We will continue to focus on maintaining a higher portfolio yield through buying quality non-government issues.

## Key Fund Facts

### Distributions

Wholesale fund: calendar quarter  
Retail fund: calendar quarter  
KiwiSaver fund: does not distribute

### Estimated annual fund charges (incl. GST)

Wholesale fund: negotiated outside of unit price  
Retail fund: 0.79%, refer PDS for more details  
KiwiSaver fund: 0.80%, refer PDS for more details

### Hedging

All investments will be in New Zealand dollars

### Buy / Sell spread:

[Click to view](#)

### Strategy size

\$344.1m

### Strategy Launch

July 2009

## Compliance

The wholesale fund complied with its investment mandate and trust deed during the month.

## Contact Us

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