

Factsheet 31 January 2022

NIKKO AM NZ CASH STRATEGY

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

Market Overview

- Fourth quarter inflation printed a robust 5.9% y/y slightly higher than market expectations (5.7%) and the Reserve Bank's November forecast (5.7%).
- Inflation was broad based, tradable prices up 6.9% y/y and non-tradable prices up 5.3% y/y.
- The acceleration in non-tradable inflation should be concerning to the Reserve Bank as it tends to be more persistent/less transitory than tradable inflation and has higher risk of creating a price feedback loop in a tight labour market.

Fund Highlights

- The fund holds a longer than benchmark duration position to benefit from slope in the credit and bank bill curves.
- Duration is actively managed with fund positions reflecting the likely path of the OCR over the coming months along with what is priced into security yields.
- The fund holds a range of securities including floating rate notes which provide some protection against a rising cash rate.

Performance

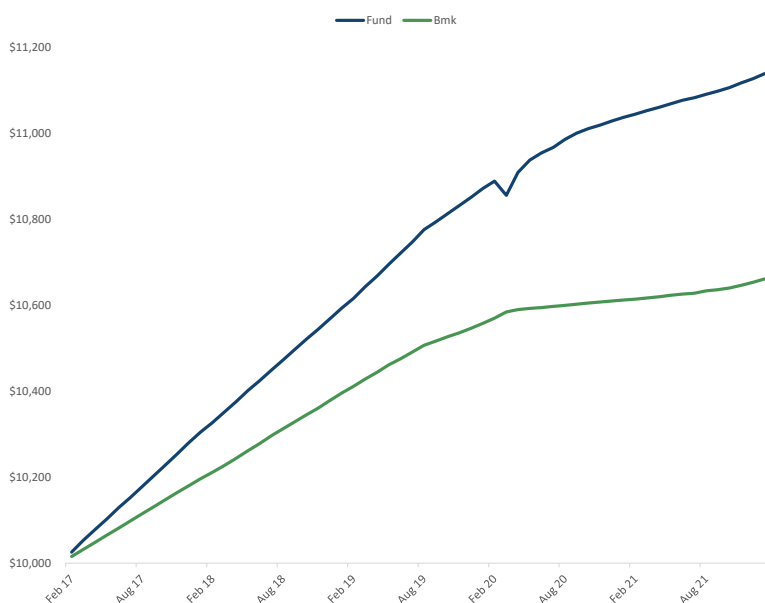
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale ¹	0.11%	0.30%	0.92%	1.69%	2.18%	3.05%
Benchmark ²	0.07%	0.20%	0.46%	0.84%	1.29%	2.10%
Retail ³	0.08%	0.23%	0.64%	1.36%	1.84%	
KiwiSaver ³	0.07%	0.20%	0.50%	1.34%		

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

2. Benchmark: Bloomberg NZBond Bank Bill 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^{1, 2}



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.

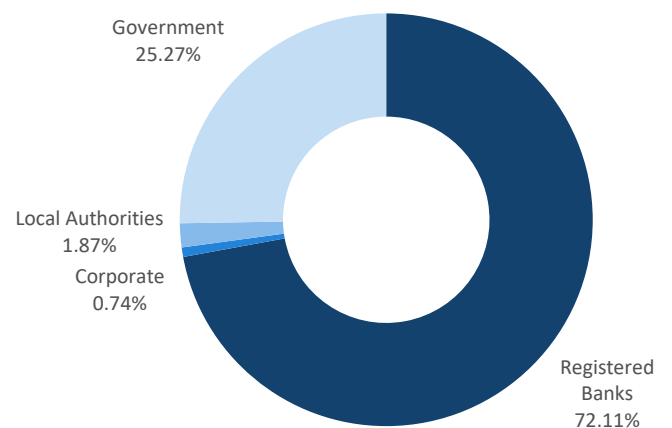
Overview

The strategy aims to generate income by constructing an actively managed investment portfolio of short-term deposits and bonds whilst preserving capital value.

Objective

The fund aims to outperform the benchmark return by 0.20% per annum before fees, expenses and taxes over a rolling three year period.

Asset Allocation



Top 5 Issuers	(%)	Credit Quality	(%)	Duration
Westpac New Zealand Ltd	14.65	AAA	25.3	Fund 97 days vs Benchmark 45 days
Tax Management NZ Limited	12.67	AA	43.1	
NZ Tax Trading Co	12.02	A	31.6	
ANZ Bank New Zealand	9.24			Yield to Maturity
ASB Bank Ltd	8.48			Fund (gross) 1.5% vs Benchmark 0.93%

Market Commentary

2022 started off thematically in much the same way as 2021 played out –the inevitable arrival of Omicron occurred resulting in the entire country moving to the “red” management setting, meanwhile inflation has continued to accelerate driven by the cocktail of loose monetary policy, strong government stimulus and Covid derived restrictions. The eventual arrival of Omicron and more restrictive economic settings was widely expected being a key factor for both the rates market and the Reserve Bank. Likewise, the continuation of strong inflation is unsurprising given the tightness of the labour market, supply chain constraints and accommodative monetary and fiscal policy settings.

Looking to the coming months, Omicron brings with it uncertainty in its impact on the economy with the experiences of other countries suggesting New Zealand will not be able to stamp out this outbreak as it has with previous variants. Previous outbreaks have seen temporary reductions in economic activity followed by a quick resumption as lockdown restrictions are lifted. One could view Omicron in the same context, however, given the potential scale of an outbreak and the limited capacity of New Zealand’s healthcare system there is a reasonable risk the country moves back to a lockdown framework as a last resort. With government financial support in the form of wage subsidies not part of the red setting and any lockdown derived from a healthcare system overload potentially taking a different format than past lockdowns a period of subdued economic activity could occur.

Whilst Omicron plays out the Reserve Bank will need to grapple with building inflation risks. Fourth quarter inflation printed a robust 5.9% yoy (year on year) - a level not seen since 1990. What’s more, inflation is becoming increasingly broad based in its composition not only elevated across tradeable prices up 6.9% yoy but increasingly seen domestically in non-tradeable prices up 5.3% yoy. This should be of concern to the Reserve Bank as whilst tradeable inflation is arguably more transient and subject to reversals, non-tradeable inflation historically has been much more persistent and brings the risk of a price feedback loop especially in a tight labour market.

Current inflation numbers affirm the Reserve Bank’s recent OCR increases and support a continuation of their measured approach to incrementally increasing the OCR. At our time of writing markets are pricing 0.25% OCR increases at each of the Reserve Bank’s seven meetings in 2022 with some risk of a 0.50% increase front loaded. Elevated inflation notwithstanding, we continue to view a 0.50% increase as unlikely and unnecessary. With market pricing reflecting an OCR move to 2.5% by year-end the inflation slowing impetus from monetary policy is already well and truly in effect only needing time to impact consumption as mortgages are refixed at higher prevailing rates.

Fund Commentary

The fund performed well in January returning 0.11% outperforming the 90-day bank bill index which returned 0.07%. On the back of robust inflation and very low unemployment (3.2%) the market is currently pricing 0.25% OCR increases for each of the seven Reserve Bank meetings in 2022 with some front-loaded risk of a 0.50% increase. The fund continues to implement a barbel strategy to exploit this pricing as an OCR increase of more than 0.25% at the next meeting requires increased economic impetus along with less COVID driven uncertainty to eventuate. In support of this stance, we note the rates market is currently supporting the Reserve Bank’s goals by fully pricing OCR increases at each 2022 meeting date. In doing so the inflation slowing impetus from monetary policy tightening is already well and truly in effect only needing time to impact consumption (typically 9 to 18 months). This intrinsically should give the Reserve Bank headroom to continue its measured approach rather than taking more drastic action.

Key Fund Facts

Distributions		Estimated annual fund charges (incl. GST)	
Wholesale fund:	Calendar quarter	Wholesale:	Negotiated outside of unit price
Retail fund:	Calendar quarter	Retail:	0.30%, refer PDS for more details
KiwiSaver fund:	Does not distribute	KiwiSaver:	0.45%, refer PDS for more details
Hedging		Buy / Sell spread	Strategy size
All investments will be in New Zealand dollars		0.00% / 0.00	\$858.2m
Strategy Launch			
October 2007			
Restrictions			
Adult entertainment, gambling, fossil fuels, alcohol stocks, tobacco stocks. For more information please refer to the Statement of Investment Policy and Objectives (SIPO) which can be found on our website https://www.nikkoam.co.nz/invest/retail .			
Exclusions			
Securities that conduct activities listed on the Schedule to Cluster Munitions Prohibition Act 2009.			

Compliance

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

Contact Us

www.nikkoam.co.nz | nzenquiries@nikkoam.com

This document is issued by Nikko Asset Management New Zealand Limited (Company No. 606057, FSP No. FSP22562), the investment manager of the Nikko AM NZ Investment Scheme, the Nikko AM NZ Wholesale Investment Scheme and the Nikko AM KiwiSaver Scheme. This material has been prepared without taking into account a potential investor’s objectives, financial situation or needs and is not intended to constitute personal financial advice, and must not be relied on as such. Recipients of this document, who are not wholesale investors (in accordance with Schedule 1, Clause 3 Financial Markets Conduct Act 2013), or their duly appointed agent, should consult a Financial Advice Provider and the relevant Product Disclosure Statement. Past performance is not a guarantee of future performance. While we believe the information contained in this presentation is correct at the date of presentation, no warranty of accuracy or reliability is given and no responsibility is accepted for errors or omissions including where provided by a third party. For full details on the retail and KiwiSaver funds, please refer to the relevant Product Disclosure Statement on nikkoam.co.nz.