Factsheet 31 July 2022

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

- Bond markets had large swings in rates through July with rates finishing lower by month end.
- The swap yield curve is slightly inverted with 2-year rates lower than 10-year rates.
- New issuance has been modest supporting credit sector performance.

Fund Highlights

- NZ bond fund returns were strong as rates fell especially in the last week of July.
- The fund duration is longer than benchmark, this positioning added to the month's returns.
- The holding of inflation linked bonds performed well as inflation remains stubbornly high.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale[1]	2.10%	2.14%	-4.07%	0.55%	3.08%	4.68%
Benchmark[2]	1.76%	1.99%	-3.96%	0.05%	2.30%	3.04%
Retail[3]	2.04%	1.97%	-4.73%	-0.20%	2.30%	3.84%
KiwiSaver[3]	1.97%	1.92%	-4.82%	-0.21%	-	-

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).

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.

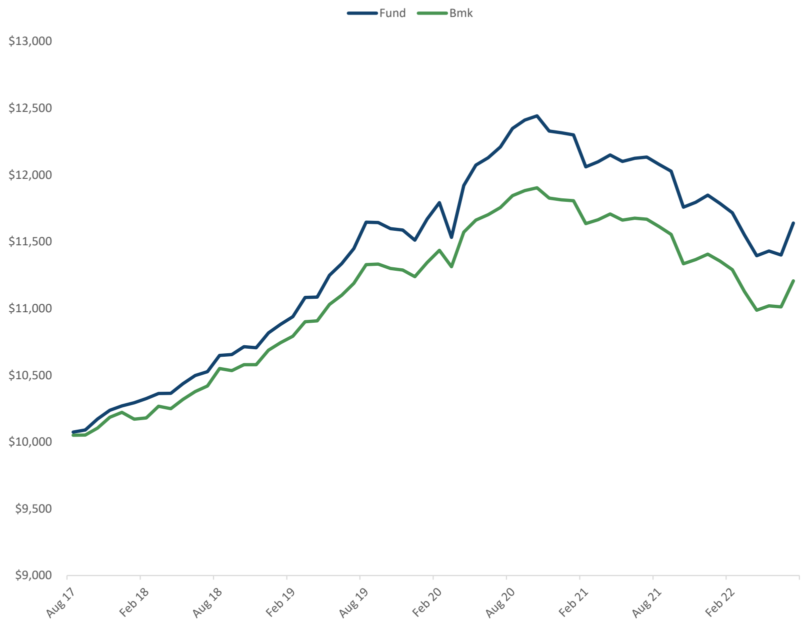
Overview

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.

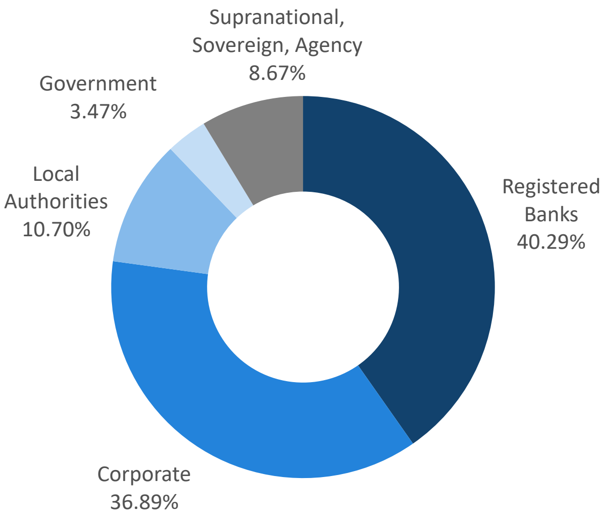
Objective

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

Five Year Cumulative Performance, $10,000 invested[1,2]



Asset Allocation



Top 5 Corporate Issuers	%
Westpac New Zealand Ltd	9.8
ASB Bank Ltd	9.1
Kiwibank Ltd	7.7
Housing New Zealand Ltd	6.9
Bank of New Zealand	5.3

Credit Quality (% of fund)	%
AAA	19.0
AA	39.8
A	15.6
BBB	25.0
BB	0.7

Duration
Fund 3.57 years vs Benchmark 3.07 years
Yield to Maturity
Fund (gross) 4.26% vs Benchmark 4.11%
Green, sustainability and social bonds
20.34% of the fund

Market Commentary

NZ bond returns were strong as interest rates fell as investor attention swung from being concerned about soaring inflation to being concerned about the negative growth impact tightening monetary conditions may bring. The Reserve Bank hiked the Official Cash Rate by another 0.5%, despite this being the third consecutive 0.5% lift the increase was well signalled and expected by the market. The Bank indicated they remain comfortable with their forecasts as set out in the May Monetary Policy Statement which sees reducing inflation as the number one task even if this is at the cost of economic growth. One year government bond yields finished 5 bps (basis points) lower, the 2-year 20 bps lower, the 5-year finished 39 bps lower, and the 10-year bond and 2051 government bond were 44 bps lower, and 39 bps lower in yield respectively. After adding ASB and BNZ 5-year bonds and some longer maturity bonds in June, July was a relatively quiet month benefiting from the previous month's duration extension. The swap curve and credit issues tended to outperform similar maturities of government bonds. To put this in context the 2-year swap was down 32 bp to 3.74%, 5-years fell 49 bp to 3.55% and 10-years down 53bp to 3.58%. This market action helped the fund's return as it holds less low yielding government bonds and more high grade credit that is priced as a margin relative to swap rates. Credit performed well as credit margins contracted with strong demand continuing to be seen. We believe that some lower rated bonds look expensive on a relative basis and continue to sell those that look expensive in terms of credit margin. We remain cautious on fund positioning in terms of interest rate risk while a large degree of uncertainty remains, however there have been opportunities to add value with interest rates moving in both directions, rather than just higher. We are happy to add quality mid-curve bonds at yields around the mid 4% levels believing they will perform well over the medium term. Although the cash rate will go higher in the near-term, growth concerns are increasing as higher rates increase the probability of an economic slowdown which in turn will limit how high bond yields go and how long they will remain elevated.

Fund Commentary

The fund generated a strong return over July as yields fell across the yield curve. Gross returns comfortably exceeded the performance of the Bloomberg NZ Bond Credit benchmark. Credit holdings continued to perform well with a higher yield accruing to the portfolio and a mild contraction in margins contributing to returns. Inflation linked bonds performed well, bouncing back from June's under performance. Swap margins contracted relative to similar maturities of governments and this was helpful as the fund generally holds few government bonds due to their lower yield and more investment grade credit which is priced as a margin above swap. Portfolio duration was extended over June and July was a quieter month for activity however the previous month's work helped deliver July's out performance as yields declined. The fund achieves a higher yield relative to benchmark selected from holding credit issues and a small weighting to inflation linked government bonds, we continue to believe this should benefit returns over the medium term. A gradual recycle into new deals at higher levels is our plan. We continue to sell bonds that look expensive and switching into bonds that in our view have a good chance of delivering acceptable future returns.

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: 0.70%, refer PDS for more details
KiwiSaver fund: 0.80%, refer PDS for more details

Hedging

Any foreign currency exposure to be hedged to NZD within operational range of 97.5%-102.5%

Buy / Sell spread:	Strategy size	Strategy Launch
Click to view	$592.2m	July 2009

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.

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