

Factsheet 31 December 2022

NIKKO AM INCOME STRATEGY

Applies to: Nikko AM Income Fund (retail).

Market Overview

- Equity markets performed well in general however individual company performance continues to be volatile. The property sector remains under pressure from rising interest rates and downward property revaluations.
- The bond market performed well, even though the Reserve Bank hiked the OCR more aggressively than expected with a 0.75% increase and the likelihood of another 0.75% when the Monetary Policy Committee meet again in February.

Fund Highlights

- The Income Fund declined over December and was modestly higher over the December quarter as bond markets stabilised and equities advanced. A quarterly distribution of 1.03 cents per unit was paid in December.

Distributions

- The defined distribution rate (which is used to calculate the distribution you receive from the fund) is set at the start of each calendar year, based on the price of the fund at that point. The defined distribution rate for 2023 is 5.5%. This income will be distributed in four equal amounts each calendar quarter, based on the price at 1 January 2023.

Performance

	One month	Three months	One year	Three years (pa)	Five years (pa)	Ten years (pa)
Retail ¹	-0.41%	0.33%	-7.52%	-0.82%	0.45%	3.11%
Benchmark ²	0.60%	1.67%	5.23%	4.62%	4.84%	6.36%
Market Index ³	-0.50%	1.51%	-5.99%	-	-	-

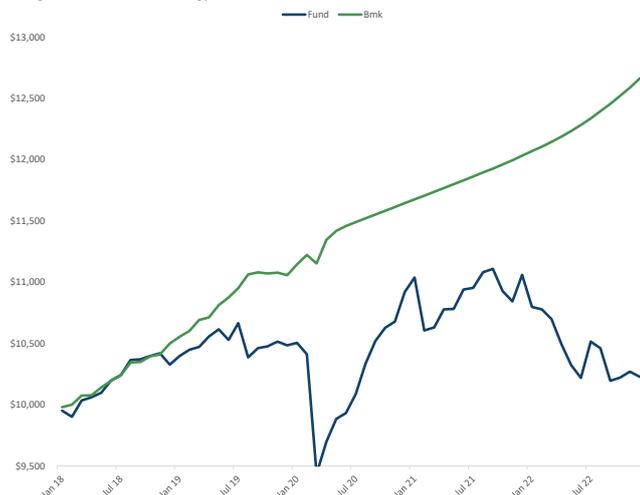
1. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

2. Current benchmark: RBNZ Official Cash Rate +3.00% p.a.

3. Current appropriate market index: 62.5% Bloomberg NZBond Credit 0+ Yr Index, 30% S&P/NZX 50 Gross Index, 7.5% Alternatives exempt.

Five Year Cumulative Performance, \$10,000 invested^{1,2}

Change of investment strategy 01/07/2020



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.

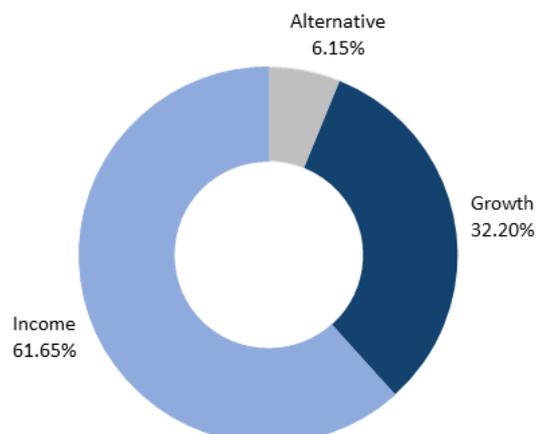
Overview

The strategy aims to provide investors with regular income from an actively managed investment portfolio. The fund invests in NZ fixed interest, Australasian equities and property. Equities with a good dividend stream and a focus on growing value over time are selected as an attractive alternative to fixed income securities. Equity selection is determined by the NZ investment team.

Objective

The objective of this fund is to outperform the RBNZ Official Cash Rate by 3.00% p.a. over a rolling three-year period before fees, expenses and taxes. Prior to June 2020, the objective and strategic asset allocation of fund were materially different. From 1 July 2020 these were amended to include equities.

Asset Allocation



Top 5 Fixed Income Issuers*	(%)	Duration*	Top 10 Equities	(%)	(%)	
Westpac New Zealand Ltd	9.79	Fund 3.97 years	Heartland Group	3.27	Stride Stapled	2.21
ASB Bank Ltd	4.22	Yield to Maturity	Spark New Zealand Ltd	3.09	Works Finance NZ Ltd	2.18
Contact Energy Ltd	3.43	Fund (gross) 5.96%	Skellerup Ltd	3.06	Chorus Limited	2.17
Kiwibank Ltd	3.42		Infratil Limited	2.65	EBOS Group Ltd	1.89
Liberty Finance	3.20		Contact Energy Limited	2.46	Meridian Energy Ltd	1.67

*Includes cash holdings.

Fund Commentary

The Income Fund declined over December and was modestly higher over the December quarter as bond markets stabilised and equities advanced. A quarterly distribution of 1.03 cents per unit was paid in December. The S&P/NZX 50 Gross Index fell by almost 0.7% over the month, the bond sector also fell by a little more than 1% as measured by the Bloomberg Corporate Bond Index as longer-term bond rates followed global markets higher. Over the quarter both sectors gained in value, the NZX50 was up a healthy 3.7% and the bond market gained a modest 0.1%

Equities continued to see high levels of volatility in company performances. In general companies and industries that are sensitive to rising interest rates have performed poorly. The property sector falls into this grouping and continues to be under pressure from rising interest rates and downward property revaluations. There may be some respite on this front as the top of the interest rate tightening cycle is in sight, even though the Official Cash Rate will likely plateau at a higher level than previously expected. Looking at the performance of some individual equities, EBOS was a standout over the quarter gaining over 16% as it was confirmed as entering the MSCI Small Cap Index. The fund owns 14 companies in its equities portfolio, over the month nine increased in price and five declined. Scales Corp was the laggard, falling around 6.4%. Ebos and Meridian each gained around 7%.

NZ bond yields moved higher into the December year-end finishing close to year-to-date highs following a lack of buying interest and rising offshore bond yields. This subtracted from the quarters returns after both October and November were positive months. Over the past quarter and year movements in interest rates have been the main driver of returns. The funds duration has varied around benchmark to modestly long, which resulted in good outcomes in October and November when rates were stable to lower but was unhelpful in December when interest rates increased.

Looking forward, there is still considerable uncertainty in terms of how “sticky” inflation will be and what impact tight monetary conditions will have on growth, but with another 3 to 6 months of data we should have a much better idea. NZ bonds can likely generate reasonable returns over the year ahead as there is plenty of yield available through purchasing quality credit rather than going longer on an inverted yield curve.

The Option Fund was down over the month which resulted in the quarterly return being marginally negative. Bond yields increased from 3.8% at the beginning of the quarter to a high of 4.34% in October before closing the year at 3.88%. Bond yields moved through a number of option strike levels over this time resulting in losses for the fund which were not fully compensated by option income.

We continue to believe investors should seek income from a diverse range of sources. Bond rates are looking attractive and even though most equity prices have fallen over the past year we believe the environment remains acceptable for equities, although we concede catalysts for new growth remain elusive and an economic slowdown looks inevitable. The Income Fund remains invested in a range of NZ companies listed on the NZX that pay a consistent level of dividends, or have the likelihood of doing so in future. In addition to receiving a steady stream of dividend income, we expect that over time the industry sectors and business models adopted by these companies should be rewarded by a steady or rising share price.

Key Fund Facts

Distributions Distributions for this fund are defined annually and are effective for the calendar year. The defined rate is gross of tax. Distributions are not a taxable event. Tax will be deducted (refunded) at 31 March and on full or partial withdrawals.	Estimated annual fund charges (incl. GST) 0.80%, refer PDS for more details		
Hedging All investments will be in New Zealand dollars	Buy / Sell spread: Click to view	Strategy size \$4.7m	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. Tobacco manufacturers.			

Compliance

The fund complied with its investment mandate and trust deed during the quarter, except that an error has been identified in the Option Fund where the value of specific options were incorrectly accounted for in the net asset value of the fund on certain days. We are working through the details and will advise the affected clients when the impact analysis is complete later in January.

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 information is for the use of researchers, financial advisers and wholesale clients. 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.