

Factsheet 31 July 2023

NIKKO AM NZ BOND STRATEGY

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

Market Overview

- NZ interest rates finished slightly higher in yield after a volatile month.
- The Reserve Bank (RB) have likely finished hiking rates but there is still uncertainty around inflation and the economy.
- NZ credit has performed well - tightening in margin as supply reduced.

Fund Highlights

- The fund's return was modestly positive as a higher income accrual outweighed the impact of the move higher in rates.
- The fund's duration was moved modestly longer when rates were higher during the month.
- Moving toward barbell yield curve positioning - to construct a higher fund yield and participate in capital gains if rates move lower.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale ¹	0.06%	-1.00%	-0.72%	-2.95%	1.35%	3.51%
Benchmark ²	0.01%	-1.51%	-1.85%	-3.99%	0.11%	2.38%
Retail ³	0.00%	-1.14%	-1.33%	-3.57%	0.66%	2.74%

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

2. Current benchmark: Bloomberg NZBond Composite 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^{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.

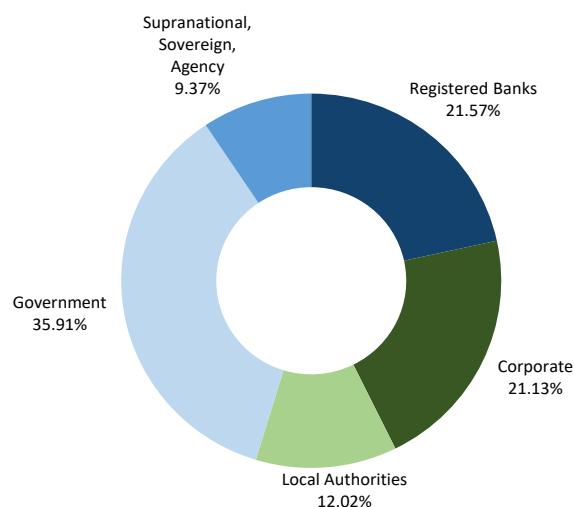
Overview

The fund aims to provide investors with regular 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 0.60% per annum before fees, expenses and taxes over a rolling three-year period.

Asset Allocation



Top 5 Corporate Issuers*	(%)	Credit Quality	(%)	Green, sustainable and social bonds
Housing New Zealand	7.66	AAA	62.36	23.67% of the fund
New Zealand Local Govt Funding Agency	6.39	AA	18.34	Duration
Westpac New Zealand	5.26	A	16.37	Fund 5.3 years vs Benchmark 4.55 years
Kiwibank	5.03	BBB	2.93	Yield to Maturity*
ASB Bank	4.20			Fund (gross) 5.28% vs Benchmark 5.16%

*excludes NZ central government

* Excluding the inflation component of government inflation linked bonds

Market Commentary

NZ bonds managed a modest positive return for the month despite interest rates closing higher in yield. July was a volatile month with interest rates making new cyclical highs early on, and fortunately retracing to be only slightly higher by month end. We added longer maturity bonds to the fund when yields spiked higher which was a positive.

In terms of sector performance longer maturity NZ government bonds performed better than swap rates - rising less in yield, conversely shorter maturities governments underperformed swap. Movements in government bond yields were the; 2yr + 11bps, 5 yr + 12bps and 10 yr + 3.5bps. So far, the increased volume of government issuance has been relatively well absorbed with strong demand for July's syndication and weekly tenders of \$500m going ok. NZ credit has continued to perform supported by strong demand versus new issuance and secondary supply. We see margins as on the tight side and have been selling those bonds which are more expensive to fund better opportunities.

The RB have likely tightened enough, although they won't want rates lower until they are confident inflation is under control. If the economic data continues to remain slower to improve or contradictory this will likely result in rates needing to be higher for longer and may exacerbate volatility.

In uncertain times we generally keep positioning modest relative to benchmark however with rates towards recent highs and given the balance of risks we have been moving towards a barbell yield curve positioning. We believe the front of the yield curve will be the highest yielding part of the curve for the longest and having a higher yield is a consistent way to add value. We achieve this through overweighting the front of the curve in high-quality credit. We will likely continue to add some longer bonds on opportunities when yields are higher as risks to the topside seem relatively modest given what is currently priced in and we want to participate in gains if rates do move lower.

Fund Commentary

The fund return was a slight positive for the month and ahead of Bloomberg NZ Composite benchmark. The move higher in interest rates was the main driver of returns, and the relative sector performance between NZ government bonds and swap had a modest influence. Credit has continued to perform well providing additional yield and gradual margin contraction.

The fund started the month with a modest long duration position which was unhelpful as interest rates finished the month slightly higher. On a positive note, intra-month we added some longer maturity bonds at better levels when yields spiked higher in July which proved of benefit as yields retraced some of their move into month end.

The fund has been moving towards a "barbell" yield curve position, holding higher yielding short maturity bonds, less mid curve and adding longer maturity bonds opportunistically on moves higher in yield. Conversely, we would trim some longer positions if we saw a reasonable move lower in yields.

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:	0.65%, refer PDS for more detail
Hedging		Buy / Sell spread	Strategy size
All investments will be in New Zealand dollars		Click to view	\$444.5m
Strategy Launch			
October 2007			
Exclusions: Controversial weapons.			
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 .			

Compliance

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

Contact Us

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