

# Nikko AM Income Strategy

Monthly Update 30 June 2024

Applies to the Nikko AM Income Fund.

## Market Overview

- Over the June quarter the NZX50 (gross with imputation credits) fell 3.2% while the NZ Composite Bond Index advanced 0.8%.
- The NZ economy feels weak and inflation pressures are falling, however perhaps not as fast as the RBNZ would like.
- Cash was the best performing sector of the local market, increasing by 1.4% over the past three months.

## Fund Highlights

- The Income Fund gained 0.89% over the June month, however fell by around 0.5% over the quarter as the equity market struggled to gain forward momentum.
- There continued to be a wide variance in stock returns over the month and quarter with energy companies such as Meridian, Contact and Mercury benefiting from the renegotiation of the Tiwai point smelter contract on favourable terms.

## Distributions

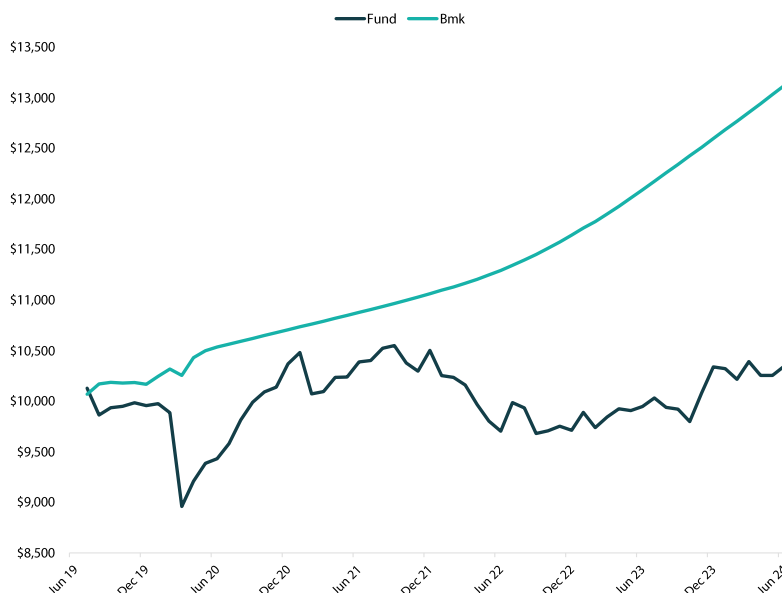
- The defined distribution rate (which is used to calculate the distribution you receive from the fund) is set at the start of each calendar year, based on the price of the fund at that point. The defined distribution rate for 2024 is 6.5%. This income will be distributed in four equal amounts each calendar quarter, based on the price on 1 January 2024.

## Performance

	One month	Three months	One year	Three years (pa)	Five years (pa)	Ten years (pa)
<b>Retail<sup>1</sup></b>	0.89%	-0.43%	4.02%	-0.14%	0.69%	3.04%
<b>Benchmark<sup>2</sup></b>	0.67%	2.05%	8.52%	6.45%	5.58%	6.11%
<b>Market Index<sup>3</sup></b>	0.16%	-0.34%	4.02%	0.21%		

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: 65% Bloomberg NZBond Credit 0+ Yr Index, 35% S&P/NZX 50 Gross Index.

## 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, Senior Fixed Income Manager and Matthew Johnson, Senior 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 Income Issuers*	(%)	Duration	Top 10 Equities	(%)	(%)	
Westpac New Zealand	8.54	Fund 4.23 years	Infratil	4.03	Meridian Energy	2.83
Powerco	5.29	<b>Yield to Maturity</b>	Bank Of New Zealand	3.47	Spark New Zealand	2.72
Kiwi Property	4.40	Fund (gross) 5.98%	Works Finance NZ	3.33	Heartland	2.45
Auckland International Airport	3.78		Chorus	3.25	Scales	2.26
Kiwibank	3.46		Contact Energy	3.09	Kiwibank	2.20

\*Includes cash holdings.

## Fund Commentary

The Income Fund gained 0.89% over June, however fell by around 0.5% over the quarter as the equity market struggled to gain forward momentum. Over the June quarter the NZX50 (gross with imputation credits) fell 3.2% while the NZ Composite Bond Index advanced 0.8%. Cash was the best performing sector of the local market, increasing by 1.4% over the past three months.

Market focus continues to be on the words and actions of the Reserve Bank of NZ and other central banks. The NZ economy feels weak and inflation pressures are falling, however perhaps not as fast as the RBNZ would like. June quarter 2023 and the September quarter CPI prints were 1.1% and 1.8% respectively. These high quarterly numbers are likely to be replaced by much lower ones as 2024 progresses, pushing the annual CPI inflation rate back into the 1% to 3% band with the next stop being close to the RBNZ's desired 2% level by late 2025 or early 2026.

With a softening labour market and weak economic growth, evidenced by GDP per capita falling in the last six quarters, it is only a matter of time before cash rates are cut. The RBNZ is currently sticking to its projections of the first cut occurring in mid-2025 however a strong case is building for rate cuts to start as early as at the 27 November 2024 Monetary Policy Statement. In our view if they wait much longer than this the economy will need more stimulus via deeper rate cuts compared to requiring more modest rate cuts if cuts started earlier. In either case we believe the 2% inflation target will be met but earlier cuts will likely mean less damage to economic output and jobs occurring.

If cash rates move significantly lower over the next year or two, we would expect bond rates to follow and deliver strong returns to the portfolio. In the short term the direction of the NZ bond and equity markets are likely to be influenced by trends and sentiments in the large offshore markets.

The S&P/NZX 50 Gross (with imputation credits) Index fell by 3.2% over the June quarter and down 0.45% over the year-to-date. There continued to be a wide variance in stock returns over the month and quarter with energy companies such as Meridian, Contact and Mercury benefiting from the renegotiation of the Tiwai point smelter contract on favorable terms. Over the month Infratil, Skellerup and Scales had strong price performance however Heartland share price has continued to slide post its capital raise.

The bond sector as measured by the Bloomberg NZ Bond Composite Index increased 0.80% and is up a modest 1.06% so far in 2024. Cash and short-term bonds held their value as the Official Cash Rate remained unchanged, however longer-term bonds have performed well recently as signs that inflation globally is falling increase. It is only a matter of when, not if, more central banks start their rate cutting cycle.

We continue to believe investors should seek income from a diverse range of sources. Looking ahead over the medium term a lower rate environment should be supportive of both bond and equity returns. The Income Fund remains invested in a range of NZ companies listed on the NZX that pay a consistent level of dividends or who have the likelihood of doing so in the future. In addition to dividend income, we expect 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

<b>Estimated annual fund charges (incl. GST)</b>	0.80%, refer PDS for more details.	<b>Hedging:</b>	All investments will be in New Zealand dollars.	<b>Strategy Launch:</b>	October 2017
<b>Exclusions:</b>	Controversial weapons.	<b>Distributions:</b>	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.	<b>Strategy size:</b>	\$3m
<b>Restrictions:</b>	Adult entertainment, gambling, fossil fuels, alcohol stocks, tobacco stocks. For more information please refer to the Statement of Investment Policy and Objectives (SIPO) on our website <a href="https://www.nikkoam.co.nz/invest/retail">https://www.nikkoam.co.nz/invest/retail</a> .			<b>Buy / Sell spread:</b>	<a href="#">Click to view</a>

## Compliance

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

## Contact Us

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