

Fund manager

Nikko Asset Management New Zealand Limited (Nikko AM).

Nikko AM is Asia's premier global asset manager. We actively manage NZ\$5.0 billion of investments for a diverse group of clients, including superannuation schemes, charitable trusts, KiwiSaver scheme providers, corporations and local government along with providing services to financial intermediaries through wrap platforms.

We offer investment management services in domestic sectors (equities, fixed interest and cash) through our Auckland-based investment team and employ offshore managers to manage global sectors (global equities, global bonds and alternative investments).

Portfolio managers

Fergus McDonald, Head of Bonds and Currency – Fergus is responsible for the investment strategy and portfolio construction of Bond, Cash and Currency mandates. He has been actively involved in the New Zealand financial markets since 1981 and has considerable experience in developing and managing a diverse range of fixed interest and option portfolios.

Ian Bellew, Fixed Income Manager – Ian joined Nikko AM in 1998 and is responsible for the implementation of investment strategy and day to day management of the fixed income and option portfolios. Ian also contributes to team decision making by analysing economic information and identifying global and domestic investment trends.

Fund launch

January 2011 (a similar portfolio has been operated by Nikko AM since January 1992).

Investment objective

The objective of the Fund is to construct a portfolio of authorised investments that outperform the Fund's benchmark by 1.0% per annum over a rolling three year period before fees, expenses and taxes.

Benchmark

S&P/NZX NZ Government Stock Index

Investment philosophy

The Fund is managed by Nikko AM's fixed interest team and is designed to provide regular quarterly income with the potential for capital gain from NZD fixed interest markets. The Fund currently obtains investment exposures by investing into the Nikko AM Wholesale NZ Bond Fund, a wholesale unit trust managed by Nikko AM.

Structure and taxation

The Fund vehicle is a Unit Trust and Portfolio Investment Entity (PIE) which is priced daily. Unit holders elect their own Portfolio Investment Rate. Information is provided to the IRD and unit holders on an annual basis.

PIE eligibility

Nikko AM may take any action it deems appropriate to ensure the Fund remains eligible to be a PIE. This includes the ability of Nikko AM to compulsorily withdraw a unit holder's units and pay the proceeds to that unit holder's nominated bank account.

Distributions

Quarterly. Last business days of March, June, September and December.

Hedging policy

All assets are NZD denominated.

Investment restrictions

Nikko AM Wholesale NZ Bond Fund – the wholesale unit trust that the Nikko AM NZ Bond Fund invests into.

- Authorised investments are cash, deposits and debt securities issued or guaranteed by any New Zealand registered bank, or equivalent overseas institution, SOE, New Zealand and foreign Government, New Zealand local authority, New Zealand and overseas corporate, trust vehicles and derivative instruments.
- A minimum of 25% of the Fund is to be invested in securities issued or guaranteed by the New Zealand Government or securities accepted by the RBNZ's Overnight Reserve Repo Facility.
- A minimum of 50% of the Fund is restricted to debt securities with a credit rating equal to or higher than New Zealand Government.
- Cash and cash equivalent investments must have a minimum credit rating of Standard & Poor's A1 short-term and A long-term.
- Up to 5% of the Fund may be exposed to assets rated below A-.
- Portfolio modified duration range of +/- 1.5 years around index duration.

Management fees and other charges

A management fee of 0.60% per annum calculated as a percentage of the gross asset value of the Fund will be calculated and deducted from the Fund. This fee is calculated daily and is payable to Nikko AM. The management fee may be reduced or waived at our discretion.

Nikko AM may recover expenses (including the Trustee fee) up to a maximum of 0.25% per annum from the Fund.

Buy/sell spread

Nil

Trustee

Public Trust

Custodian

Public Trust as legal custodian, BNP Paribas Fund Services Australasia Pty Limited delegated as functional custodian.

Minimum investment

Initial investment	\$5,000
Further investments	\$1,000

The Manager may accept applications for investments below the minimum investment amount at its discretion.

Nikko AM NZ Unit Trusts (Retail)

Fund Summary

Nikko AM NZ Bond Fund

31 May 2016

Performance

(NZD returns; before tax, after fees and expenses)

1 month	3 months	6 months	1 year
0.70%	1.81%	4.05%	6.71%
2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
6.94%	5.20%	6.20%	6.51%

* January 2011

Distributions

cents per unit	Mar	Jun	Sep	Dec
2016	1.40			
2015	0.90	1.25	1.15	1.30
2014	0.90	0.50	0.80	0.80
2013	1.10	1.25	1.30	1.25

Asset allocation

Government Stock	28.3%
SOE and Local Authority	16.9%
NZ Registered Banks	39.7%
Corporate Debt	15.1%

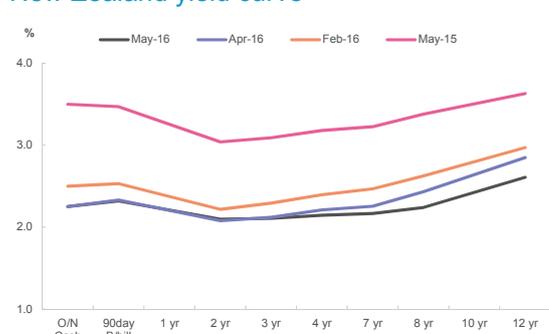
Credit rating profile

S&P Rating	% of portfolio
AAA	0.8%
AA	73.7%
A	20.7%
BBB	4.8%

Duration and yield

Duration	Fund 4.5 years	vs benchmark 4.44 years
Yield	Fund (gross) 3.4%	vs benchmark 2.23%

New Zealand yield curve



Top five corporate issuer exposures (% of fund)

NZ Local Government Funding Authority	11%
Bank of New Zealand	8%
Rabobank	8%
ANZ Banking Group	6%
Fonterra Co-operative Group	6%

Commentary

Over the month there was a relatively large difference in performance across the various New Zealand bond indices with New Zealand Governments the better performing sector.

The New Zealand Government Bond Index produced a return of 0.84% for the month while the All Swap Index returned 0.25%, and the New Zealand Corporate A Index returned 0.39%. New Zealand government bonds were supported by strong demand during the month, with longer bonds the best performers. The New Zealand yield curve continues to flatten as offshore concerns (continued uncertainty around the US and its possible interest rate rises) impact longer maturity bonds locally. The New Zealand government maturities inside three years were slightly higher in yield, whereas the 2021 maturity finished 7 basis points lower in yield and the 2023 maturity rallied strongly finishing 26 basis points lower in yield. Locally the New Zealand budget gave further support to government bonds, forecasting a much reduced bond issuance programme which saw bonds rally strongly. New Zealand interest rates are now near historic lows, but it is important to note that they are still high relative to interest rates available in other developed countries. We continue to expect a reasonable amount of interest in New Zealand assets with attractive yields and the currency showing some stability.

Swap rates underperformed government bonds. Swap maturities five years and shorter widened in spread by approximately 8 basis points relative to similar maturities of government bonds. The move wider in the 10 year swap was more pronounced with a 20 basis point expansion in spread. Widening swap margins impact corporate bonds in that swap rates form a component of the yield on corporate bond issues.

A positive feature of the month was credit margins stabilising and narrowing slightly. Credit margins have absorbed some of the negative impact of widening swap spreads, particularly for bond issues popular with retail investors who are more focussed on the absolute nominal yield level. We have continued to extend the duration of the Fund's credit holdings to take advantage of higher credit margins. New Zealand government bonds have been the best performers recently; however over our three year investment horizon we expect credit to add value over lower yielding government and swap bond investments. The accrual trade of having a higher yielding portfolio should ultimately be of benefit, with a positive shaped yield curve as bonds roll down the yield curve and move lower in yield as they become closer to maturity.

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