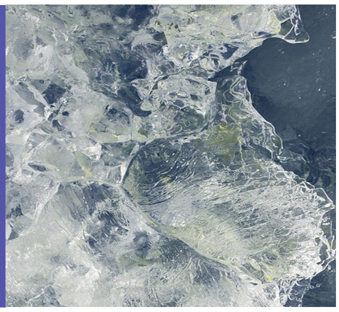
nikko am
Nikko Asset Management

NIKKO AM GLOBAL BOND FUND

Monthly Fact Sheet 30 June 2016



Investment objective

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

Benchmark

Barclays Capital Global Aggregate Index, hedged into NZD

Fund description

The Fund aims to provide investors with regular income by constructing an actively managed investment portfolio of permitted investments, with the potential for capital gains from global fixed interest markets.

The Fund gains its investment exposure by investing into the Nikko AM Wholesale Global Bond Fund. The nominated global manager (Goldman Sachs Asset Management) is responsible for the investment management of the assets of the Nikko AM Wholesale Global Bond Fund.

Currency management

Foreign currency exposures created as a consequence of capital markets investment remain hedged to NZD within an operational range of 98.5% to 101.5%. Currency hedging contracts are held in the Nikko AM Wholesale Global Bond Fund.

Management fees and other charges

A management fee of 0.65% per annum calculated as a percentage of the net asset value of the Fund will be calculated and deducted from the Fund.

Nikko AM may also recover expenses (including the Trustee fee) from the Fund up to a maximum of 0.25% per annum of the Fund's net asset value. Estimate of expenses as at 1 July 2016 are 0.22% per annum.

Buy/sell spread

Nil

Strategic asset allocation

	Target	Range
Nikko AM Wholesale Global Bond Fund	100%	95% ⇔ 100%
Cash on call for investor transactions	0%	0% ⇔ 5%

Refer to the SIPO for full details of permitted investments and restrictions.

Performance

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

1 month	3 months	6 months	1 year
1.47%	2.40%	5.71%	8.51%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
6.50%	na	na	7.27%

* December 2013

Asset allocation

Credit quality rating	Fund
AAA	40.4%
AA+, AA, AA-	13.2%
A+, A, A-	29.1%
BBB	18.2%
BB	0.3%
Unrated	-1.2%

Sector	Fund	Index
Governments	42.3%	52.5%
Agency	8.2%	9.4%
Credit	20.8%	20.3%
Collateralised & MBS	25.5%	11.7%
Emerging market debt	4.4%	6.1%
Cash, derivatives, other	-1.2%	0.0%
Number of holdings	447	17,372

Duration and yield

Duration	Fund 6.38 years versus benchmark 6.76 years
Yield	Fund 3.37% versus benchmark 3.12%

Commentary

Government bonds rallied broadly across developed markets over the month of June. In the US, the benchmark 10-year yield closed the month 38 basis points lower at 1.47%. Rates on UK government bonds rallied over the period, ending the month at 0.86%, down 56 basis points. In Japan, the 10-year yield went further negative to close at -0.22%, down 11 basis points. In Europe, German 10-year yields decreased 27 basis points to end the month at -0.13%. European peripheral bonds rallied over the period, with Spanish and Italian 10-year yields decreasing by 31 basis points and 10 basis points, respectively.

GSAM maintained their short position in US rates over the first half of the month, then covering the short position following the UK vote to leave the European Union, and subsequently re-established a short position at month-end given the recovery in financial conditions and overstretched positioning. In Europe, the portfolio remained neutral in European rates – the UK referendum has increased uncertainty in European growth forecasts and fueled concerns about higher loan losses from Italian banks. Japanese rates rallied on the Brexit result. Prime Minister Shinzo Abe has pledged to use all available policy tools to minimize the uncertainty caused by Brexit in the Japanese market. GSAM maintained their short position in Japan.

Within the G10, GSAM initiated a long UK versus short European front-end rates position in expectation of post-Brexit rate cuts by the Bank of England. GSAM increased the long Canada versus short US position on the belief that the US economy will continue to perform well and that inflation will slowly pick up and maintained the short Japan versus long Europe trade. In the European periphery, GSAM remain long Italy and Spain.

Agency **mortgage-backed securities** (MBS) underperformed duration-neutral US Treasuries by 30 basis points in June, and outperformed by 3 basis points over the second quarter. US Treasuries rallied to a post-financial crisis low after the UK referendum to leave the European Union, contributing to the underperformance of agency MBS. However, agency MBS outperformed most other risk assets following Brexit due to their superior liquidity and a scarcity of positive yielding assets globally.

GSAM are underweight agency MBS, and expect bank demand to weaken due to a decline in agency MBS yields and expectations for increased prepayments and increased supply. GSAM believes senior CLOs and Federal Family Education Loan Program (FFELP) student loan asset-backed securities (ABS) offer attractive spread with strong credit protection and remain among the most compelling sectors in securitised products. GSAM are positive on residential mortgage credit, particularly legacy non-agency MBS, which continue to benefit from negative net supply and show improving collateral performance.

Investment grade corporates weakened in June, largely as a result of uncertainty arising from the UK referendum. Spreads on the Barclays Global Aggregate Corporates Index widened 8 basis points to 154 basis points over sovereigns. US corporates and European corporates both weakened. The UK referendum also had a strong dampening effect on primary markets. Gross new issuance for the month amounted to roughly US$72 billion in the US and US$23 billion in European markets – significantly lower from the previous month.

GSAM shifted to a modest underweight in corporate credit. Uncertainty around the impact of the UK referendum result and nearing US elections are likely to result in some volatility, while the extent of spread tightening from earlier in the year provides an attractive entry point. Additionally, summer seasonals and late cycle trends tend to be negative for credit. However, GSAM think the UK referendum outcome will most directly impact UK and European banking sectors. Within the credit quality spectrum, GSAM maintained a down-in-quality bias to triple-B rated credit as well as a preference for the intermediate part of the corporate term structure. GSAM see value in consumer products, tobacco and pipelines, mainly as a result of single-security, bottom-up views rather than thematic sector-level decisions. GSAM are underweight insurance, media non-cable and energy.