NIKKO AM NZ CASH FUND

Monthly Fact Sheet 30 September 2016

Investment objective

The objective of the Fund is to construct a portfolio of permitted investments that outperform the Fund's benchmark return by 0.2% per annum over a rolling three year period before fees, expenses and taxes.

Benchmark

Bloomberg NZBond Bank Bill Index (from 1 July 2016)

Fund description

The Fund aims to provide investors with regular income by constructing an actively managed investment portfolio of short term deposits and bonds whilst preserving capital value.

The Fund gains its investment exposures by investing into the Nikko AM Wholesale NZ Cash Fund which is managed by the Nikko AM NZ Fixed Income team.

Distributions

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

Management fees and other charges

A management fee of 0.25% per annum calculated as a percentage of the net asset value of the Fund will be deducted from the Fund.

Nikko AM may also recover expenses (including the Trustee fee) from the Fund up to a maximum of 0.15% per annum of the Fund's net asset value. As at the time of publication these expenses are estimated to be 0.08% per annum.

Buy/sell spread

Nil

Investment restrictions

Nikko AM Wholesale NZ Cash Fund

- Authorised investments are cash, deposits and debt securities with an interest rate exposure of up to 365 days, issued or guaranteed by any NZ registered bank, SOE, NZ Government, NZ local authority and NZ and overseas corporate.
- Securities issued by corporates and registered banks must have minimum credit rating of A1 short-term and A long term (Standard and Poors). Derivative counterparties must have A or better credit rating and all derivative exposure shall be covered by cash or physical holdings.

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
0.23%	0.76%	1.45%	3.01%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
3.49%	na	na	3.53%

* June 2014

Distributions

Cents per unit	Mar	Jun	Sep	Dec
2016	1.00	0.55	0.50	
2015	0.75	0.70	0.90	0.70
2014			0.70	0.50

Asset allocation (% of fund)

NZ Government, Government Department or Government Guaranteed	10.9%
NZ registered banks	79.0%
Local authorities	2.2%
Corporate bonds & SOEs	7.9%

Credit rating profile

S&P rating	% portfolio
AAA	0.7%
AA	74.9%
A	24.4%

Top 5 issuers (% of fund)

Bank of New Zealand	21.7%
KiwiBank	15.0%
Westpac Banking Corp	13.7%
Government	10.9%
ASB Bank Limited	10.7%

Duration and yield

Duration	Fund 95 days versus benchmark 45 days
Yield	Fund (gross) 3.10% versus benchmark 2.25% Fund (net) 2.77%* versus OCR 2.00%

* After management fee and expenses

Commentary

The Fund remains a high credit quality, low interest rate risk portfolio. The average credit rating is targeted around AA- S&P with the duration of the portfolio currently 95 days.

Short term interest rates fell over both the month and the quarter. The short end of the yield curve remains inverted which indicates the market is expecting lower rates in the months ahead. Over September the 90-day rate closed down 3 points to 2.25% and the 1-year swap was down 4 points to 2.05%. Over the quarter the 90-day rate closed down 22 points and the 1-year swap was down 17 points.

The RBNZ left the Official Cash Rate (OCR) unchanged at 2% at the September review. Over the quarter the RBNZ has continued to note that despite unprecedented levels of monetary stimulus, global growth remains weak. Uncertainly around political risk, commodity prices and the prospect for global growth is helping keep interest rates at record lows. This is particularly unhelpful from the RBNZ's point of view as global rates relative to New Zealand are keeping the exchange rate high. The RBNZ maintains its strong easing bias, and continues to downplay recent strong domestic economic indicators and focuses on the downside risks.

Our view for some time has been that the New Zealand economy is doing well and that rate cuts appear to be at odds with domestic economic activity. Strong net migration, construction, tourism, agriculture ex-dairy (dairy appears to be improving), strong labour markets and confidence are all supportive. The recent quarterly survey of business opinion in particular points to how strong confidence is and indicates accelerating GDP growth and capacity constraints pressure, but without the pricing pressures that would normally accompany it. The market is pricing a 70% chance of a 25 basis point cut to the OCR in November. We tend to agree with this assessment given the weak inflation backdrop and the RBNZs prior statements.

We can however see risks that the RBNZ moves from an easing bias to being on hold. A case can be made for a rate hike from the US Fed in December. The ECB appears to be building consensus to taper its QE programme and other central banks appear to have lowered the prospect of further easing. This could indicate a NZD weakening, an increase in tradable inflation and an end to the easing cycle. We will continue to monitor this situation as it evolves.

The Cash Fund has a longer than benchmark duration, which should lead to continued strong performance as the Fund is invested to receive the benefit of higher income than the yield relative to the 90-day Bank Bills Index. We have been buying high credit quality commercial paper as a source of added liquidity and portfolio duration. The margins on 12 month term deposits remain attractive. Highly rated short-term fixed and floating rate securities remain in strong demand, and we have been active here at good margins considering the market supply and demand dynamics. This has all been of benefit to the Fund as rates have continued to go lower.