nikko am
Nikko Asset Management

NIKKO AM NZ CORPORATE BOND 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 1.5% per annum over a rolling three year period before fees, expenses and taxes.

Benchmark

Bloomberg NZBond Govt 0+ Yr Index (from 1 July 2016)

Fund description

The Fund is designed to provide regular income by constructing an actively managed investment portfolio of New Zealand bonds, deposits and cash, while protecting the capital value of investors' funds.

The Fund gains its exposure by investing directly into market securities and is managed by the Nikko AM NZ Fixed Income team.

Distributions

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

Currency management

Foreign currency exposures created as a consequence of capital markets investments are hedged to NZD within an operational range of 97.5% to 102.5%.

Management fees and other charges

A management fee of 0.70% 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 0.25% 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

Below are the investment ranges for the credit rating exposures and the sector limits in which the Fund will primarily invest.

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

Credit Rating	Fund Exposures	Maximum exposure per issuer
AAA	0% ⇔ 100%	15.0%
AA- to AA+	0% ⇔ 100%	10.0%
A- to A+	0% ⇔ 80%	7.5%
BBB- to BBB+	0% ⇔ 30%	5.0%

Sector Limits	Maximum
NZ Government, Government Department or Government Guaranteed	100%
NZ Corporate and Bank Debt	100%
NZD Kauri Bonds	40%
Offshore issued NZ Corporate Debt Hedged to NZD	20%
NZ Mortgage Backed and Asset Backed Securities	20%

Performance

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

1 month	3 months	6 months	1 year
0.16%	1.76%	3.30%	5.85%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
7.14%	6.74%	6.31%	7.17%

* July 2009

Distributions

Cents per unit	Mar	Jun	Sep	Dec
2016	1.15	0.85	0.90	
2015	1.25	1.30	1.20	0.75
2014	1.60	0.80	1.50	1.25
2013	1.30	1.30	0.80	1.10

Asset allocation (% of fund)

Corporate bonds	39.3%
NZ registered banks	49.2%
Local authority	6.4%
NZ government and government equivalent	5.1%

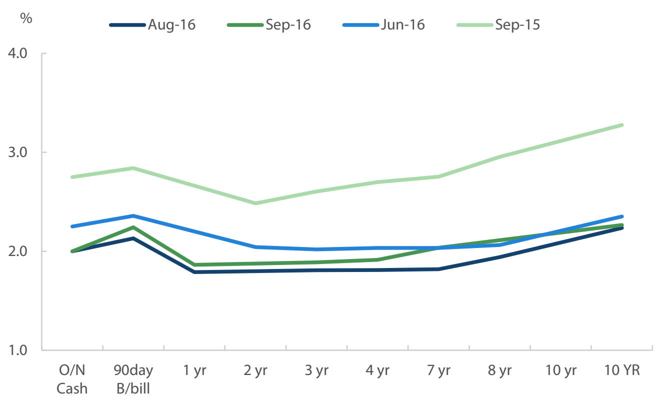
Credit rating profile

S&P rating	% portfolio	Number of holdings
AAA	3.4%	9
AA	47.7%	55
A	21.5%	23
BBB	27.4%	30

Duration and yield

Duration	Fund 3.9 years versus benchmark 4.7 years
Yield	Fund (gross) 3.5% versus benchmark 2.0%

New Zealand yield curve



Top 10 issuers (% of fund)

Westpac Banking	9%	Rabo Bank	6%
Bank of New Zealand	9%	NZ Government	5%
ANZ Bank	9%	Transpower	5%
ASB Bank	7%	Kiwi Bank	4%
Fonterra	6%	Auckland City Council	3%

Commentary

Government bonds have been the best performing bond sector for most of the year as interest rates fell and credit margins widened, however there was some catch up from other sectors as Governments performed poorly over the month on a relative basis. Over the month corporate bonds and swaps delivered a better return as they didn't move higher in yield to the same extent as similar maturities of government bonds. Corporate bonds also have the advantage of a higher running yield which helps to dampen the volatility of returns. NZ interest rates were volatile intra-month with the NZ Government 2033 bond moving higher in yield by close to 40 basis points before retracing most of this move and finishing at 2.61%. For the month government bond maturities from 1 to 7 years closed approximately 10 basis points higher in yield with longer bonds less impacted. Swap margins contracted in spread to government bonds as the underlying swap rates didn't move higher in yield to the same extent as government bonds.

Over the quarter interest rates still managed to finish lower in yield despite rising in September. Government bonds were only marginally lower in yield, but swap rates performed better, falling an additional 10-15 basis points compared to similar maturities of government bonds. The shape of the NZ swap yield curve has remained relatively stable over the past three months with the 2-10 year swap spread currently at 47 basis points. Credit markets tentatively settled and (the accrual trade of) having a higher yielding portfolio is showing some benefit as the higher yield isn't eroded by widening credit margins. With a positive shaped yield curve bonds roll down the yield curve and move lower in yield as they become closer to maturity. We expect credit to outperform lower yielding government and swap bond investments over our three year investment horizon.

NZ is performing well on a relative basis compared to other developed economies; business and consumer confidence, GDP, inflation and dairy prices have been improving. Interest rates are low and supportive of activity with the possibility of a further rate cut. Challenges are the high level of the NZD continues to frustrate the Reserve Bank and they would like to see house price appreciation slow. The direction of NZ short-term interest rates will continue to be influenced by local factors with low cash rates anchoring the front end of the yield curve. Bonds 5-years and longer in maturity will likely remain more heavily influenced by global events and movements in US bond rates.