nikko am
Nikko Asset Management

NIKKO AM NZ BOND FUND

Monthly Fact Sheet 30 November 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

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

Fund description

The Fund aims to provide investors with regular income by constructing an actively managed investment portfolio of New Zealand bonds, deposits and cash with the potential for capital gain from New Zealand dollar fixed interest markets.

The Fund gains its investment exposure by investing into the Nikko AM Wholesale NZ Bond 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 0.60% 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 0.125% per annum.

Buy/sell spread

Nil

Investment restrictions

Nikko AM Wholesale NZ Bond Fund

- A minimum of 25% of the wholesale 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 wholesale fund is restricted to debt securities with a credit rating equal to or higher than New Zealand Government.
- Minimum of 95% of the wholesale fund to be invested in assets rated A- or better.
- Portfolio modified duration range of +/- 1.5 years around index duration.
- Cash and cash equivalent investments must have a minimum credit rating of Standard & Poor's A1 short-term and A long-term.

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
-1.48%	-2.76%	-0.55%	3.48%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
4.90%	5.50%	4.96%	5.81%

* January 2011

Distributions

Cents per unit	Mar	Jun	Sep	Dec
2016	1.40	1.25	1.05	
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 (% of fund)

Government stock	27.7%
SOE and local authority	17.8%
NZ registered banks	39.7%
Corporate debt	14.8%

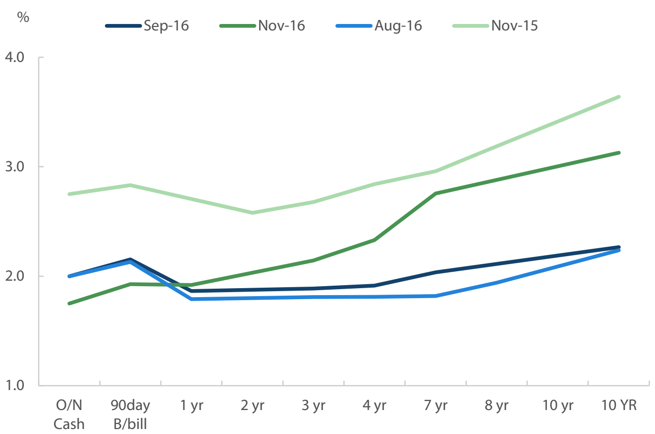
Credit rating profile

S&P rating	% portfolio
AAA	13%
AA	63%
A	19%
BBB	5%

Duration and yield

Duration	Fund 4.57 years versus benchmark 4.48 years
Yield	Fund (gross) 3.62% versus benchmark 2.52%

New Zealand yield curve



Top 5 corporate issuers (% of fund)*

NZ Local Government Funding Agency	10.8%
Bank of New Zealand	8.5%
Westpac Banking Corporation	6.6%
RaboBank	6.5%
Fonterra Co-Operative Group	6.1%

* excludes central government

Commentary

Returns from the NZ bond indices were negative in November as interest rates moved higher in yield. For the month the Bloomberg NZ Government bond index produced a return of -1.37% while the All Swap index returned -1.18%, and the NZ Bond Corporate A Index returned -0.66%.

It was a difficult month for bonds with yields moving higher through the month after the result of the US elections. Market sentiment turned negative for bonds on the perception that President Elect Trump's expansionary policies of tax cuts and a higher fiscal spend will promote growth, higher inflation and larger borrowings for the US. With more protectionist trade policies there will also likely be "winners and losers" which could impact our major trading partners. NZ longer-term interest rates are typically highly correlated with movements in US interest rates, whereas shorter maturities are more influenced by local factors with low cash rates anchoring the front end of the yield curve. NZ interest rates followed similar moves to the US and the shape of the NZ yield curve steepened considerably (widening from a spread of 70 basis points between the 2 and 10-year swap rates to 100 basis points). Longer maturity bonds were the worst performing bond assets, and there was little difference between the performances of government bonds versus similar maturities of swap. The NZ Government 2019 bond moved higher in yield by 15 basis points, the NZ Government 2021 bond was 30 basis points higher, and the NZ Government 2027 finished 42 basis points higher in yield. Funds that were positioned with shorter durations (less exposure to changes in interest rates) performed better as their prices declined less when interest rates moved higher in yield. Corporate bonds also moved higher in yield although credit margins were relatively stable, and the higher running yield of corporate holdings will help benefit the Fund over the medium term.

Longer term interest rates in NZ have been under some pressure over the past 3 months as economic news has generally been on an improving trend; business and consumer confidence, GDP, inflation outcomes, and dairy prices have been improving. Interest rates are low and supportive of activity, and there will be additional spends following the recent Kaikoura earth quake. At this stage it appears we may have seen the low in yields in NZ and the sentiment bias is for higher interest rates, however with the latest move higher in yields there is now a lot of "positive economic sentiment" factored in with a higher and steeper yield curve and the market may want to see some more solid proof of improvement before taking yields higher. 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. The accrual trade of having a higher yielding portfolio is helping to offset some of the move higher in interest rates. At the same time we don't want to have an undue amount of risk to rising interest rates and the Fund will likely be positioned shorter in duration than its index.