nikko am
Nikko Asset Management

NIKKO AM NZ BOND FUND

Monthly Fact Sheet 31 January 2017

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
0.30%	-1.86%	-2.70%	1.97%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
3.30%	5.08%	4.63%	5.58%

* January 2011

Distributions

Cents per unit	Mar	Jun	Sep	Dec
2016	1.40	1.25	1.05	1.25
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	28.1%
SOE and local authority	17.6%
NZ registered banks	39.6%
Corporate debt	14.7%

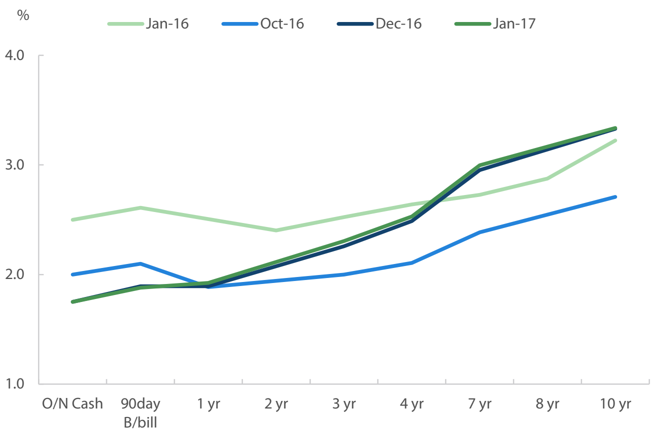
Credit quality (% of fund)

AAA	12.6%
AA	63.1%
A	19.5%
BBB	4.8%

Duration and yield

Duration	Fund 4.16 years versus benchmark 4.45 years
Yield	Fund (gross) 3.8% versus benchmark 2.72%

New Zealand yield curve



Top 5 corporate issuers (% of fund)*

NZ Local Government Funding Agency	10.7%
Bank of New Zealand	8.3%
Westpac Banking Corporation	6.7%
RaboBank	6.6%
Fonterra Co-Operative Group	6.1%

* excludes central government

Commentary

The Nikko AM NZ Bond Fund returned 0.30% for January (net of fees). For the month the Bloomberg NZ Government Bond index produced a return of 0.06% while the All Swap index returned 0.07%, and the NZ Bond Corporate A Index returned 0.35%.

NZ interest rates finished January little changed, however there was a reasonable amount of volatility in interest rates movements during the month. The NZ Government 2019 bond finished higher in yield by 5 basis points (2.32%), and traded in a 20 basis point range, the NZ Government 2027 bond was unchanged (3.36%), and the NZ Government 2033 finished 3 basis points lower in yield (3.69%), after trading in a 35 basis point range over the month. Swap spreads to government bonds were relatively stable over the month with spreads inside 7 years in maturity narrowing marginally, whilst 10 year spreads widened and steepened the upward shape of the yield curve to a spread of +1.14% between the 2 and 10 year swap rates. NZ credit margins were stable to slightly narrower over the month with limited market activity due to the holiday season. A higher running yield from corporate holdings and yield curve positioning was of benefit to the fund over the month. Also of benefit the fund shortening its duration by selling its holding of NZ Government 2033 bonds at the low of the monthly range in yield and reinvested in shorter maturities which were less impacted when interest rates subsequently moved back higher in yield.

The NZ economy remains in expansionary mode, very strong immigration, tourism, and strength in other areas of the economy have picked up the slack from a weak dairy sector. Inflation appears to be recovering across a broad base and it is the first time back in the target band for some time and we expect inflation to remain contained over the near term. Given the relative strength of the NZ economy, higher growth and interest rates it is likely the NZD will continue to remain reasonably well supported, and expect dips to remain relatively shallow. With this background NZ short-term rates out to 3 years in maturity will continue to be primarily influenced by local factors and the actions of the Reserve Bank. The cash rate at 1.75% should help anchor the front end of the yield curve. The market is currently pricing an earlier start to interest rate increases than the Reserve Bank, and we believe the bank may be slower to raise interest rates as this is likely the path of least regret with uncertainties still remaining in the global economy, while inflation remains relatively benign and the NZ dollar high on a TWI basis. Longer term interest rates in NZ will likely be more heavily influenced by offshore events with the NZ 10-year interest rate following the direction of the US. There is already a reasonable amount of good news factored in with interest rates moving markedly higher over the last quarter of 2016, markets may have got ahead of actual policy in the US, and Trump will most likely continue to be a source of “surprises”. The medium term directional bias is most likely upward, but we don’t expect large movements higher in yield from here and expect a reasonable amount of volatility along the way.