nikko am
Nikko Asset Management

NIKKO AM NZ CORPORATE BOND FUND

Monthly Fact Sheet 31 May 2017

Investment objective

The objective of the Fund is to construct a portfolio of permitted investments that outperform the Fund's benchmark return by 1.5% 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
1.11%	2.34%	2.99%	3.61%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
4.92%	5.76%	5.53%	6.70%

* July 2009

Distributions

Cents per unit	Mar	Jun	Sep	Dec
2017	0.80			
2016	1.15	0.85	0.90	1.20
2015	1.25	1.30	1.20	0.75
2014	1.60	0.80	1.50	1.25

Asset allocation (% of fund)

Corporate bonds	44.4%
NZ registered banks	42.4%
Local authority	8.6%
NZ government, govt depts & govt guaranteed	2.5%
Settlements	2.1%

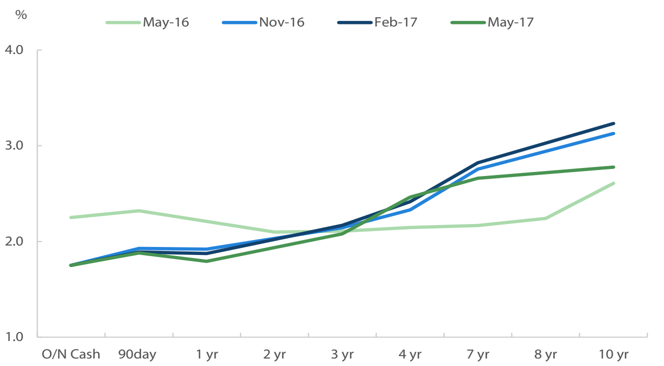
Credit rating profile

S&P rating	% portfolio	Number of holdings
AAA	3.5%	7
AA	42.2%	36
A	24.8%	18
BBB	27.4%	27
Settlements	2.1%	

Duration and yield

Duration	Fund 3.63 years versus benchmark 4.62 years
Yield	Fund (gross) 3.82% versus benchmark 2.31%

New Zealand yield curve



Top 10 issuers (% of fund)

Westpac Bank	6.9%	Auckland Council	5.0%
ANZ Bank	6.6%	Ak Intl Airport	5.0%
BNZ	6.4%	Transpower	4.7%
Fonterra Co-op	6.1%	ASB	4.7%
Rabobank	6.1%	Kiwi Bank	4.6%

Fund commentary

The higher portfolio running yield and a moderate contraction in credit margins was a positive for performance. The moderate underweight duration position was a detractor. The Corporate Bond Fund will typically be positioned around 3.5 years in duration with less interest rate risk than the NZ Government Bond benchmark.

Market commentary

The month of May continued the good performance of NZ bonds as interest rates moved lower in yield. Similar to the previous month there was a reasonably large difference in performance across the different sectors of the NZ bond market. The Bloomberg NZ Government Bond index returned 1.27%, The NZX 1-10 year swaps retuned +0.91% and the Corporate A +0.95 %.

NZ interest rates moved in line with falling global interest rates, in particular longer maturity US interest rates are now back to pre-election lows in yield. Locally, there was strong offshore demand for NZ Government bonds and fixed rate swaps. Governments were the best performers with larger falls in yield than comparative maturities of swaps, with some of the swap receiving demand offset by domestic bank paying in shorter maturities. The move lower in government bonds during May was fairly consistent along the yield curve, whereas in April longer maturity bonds had much larger falls in yield in a 'bull flattening' of the yield curve. For the month the NZ Government 2019 bond moved lower in yield by 15.5 basis points, the NZ Government 2021 bond was 24.5 basis points lower, and the NZ Government 2027 finished 29 basis points lower. Swap margins have widened and the shape of the swap yield curve which corporate bond margins are priced over flattened with the spread between the 2and 10-year swap rate narrowing from +1.07% to +0.98%.

NZ credit margins continued to contract in spread and credit has generally outperformed similar maturities of swap and governments since the start of this year. The portfolio has benefited from having higher weightings to credit with both a higher running yield and margin contraction. We continue to have a positive view on credit and expect having a higher portfolio running yield will be one of the main attributors to outperformance over the course of this year. We prefer to hold more mid curve maturity (4-7 years) credit rather than longer government bonds that have a lower yield and greater interest rate risk. At this stage we expect movements in NZ bond yields to remain relatively muted, but we may adjust the fund duration if we see opportunities.

The NZ economy continues to perform well although forecasters expect some slowing of activity with capacity constraints in sectors such as construction. The Reserve Bank has indicated they see stable cash rates with risks evenly balanced at present, this should help anchor the front end of the yield curve at current levels. Credit/housing related excesses are being more actively curtailed, which lessens the odds of imbalances building. High immigration is growth positive, but momentum is broad based and numerous support factors remain, which should allow annual GDP growth to hover around 2.5-3% over 2017.