

Nikko AM Wholesale Global Bond Fund

Fund manager

Goldman Sachs Asset Management Australia Pty Ltd – via Nikko Asset Management New Zealand Limited.

Nikko AM is Asia's premier global asset manager. In New Zealand we actively manage NZ\$4.8 billion of investments for a diverse group of clients, including superannuation schemes, charitable trusts, KiwiSaver scheme providers, corporations and local government along with providing services to financial intermediaries through wrap platforms.

We offer investment management services in domestic sectors (equities, fixed interest and cash) through our Auckland-based investment team and employ offshore managers to manage global sectors (global equities, global bonds and alternative investments).

Nikko AM utilise Goldman Sachs Asset Management Australia Pty Ltd (GSAM) for the management of global fixed interest assets.

Established in 1988, GSAM is one of the world's leading asset managers with US\$702 billion in assets under management. GSAM's Global Fixed Income Team manages US\$306 billion of global fixed income assets and has a breadth of investment management expertise with over 200 investment professionals. The globally integrated team has independent strategy teams capturing value across top down (duration, cross sector and country) and bottom up (investment grade credit, high yield, MBS/ABS, government/agency and emerging market debt) strategies.

GSAM was appointed to manage Nikko AM's global fixed interest assets in June 2012.

Fund launch

December 2007 – a similar portfolio has been operated by Nikko AM since March 2002.

Investment objective

Over a rolling three year period, to target a return which exceeds the benchmark by 1% per annum, before fees.

Benchmark

Barclays Capital Global Aggregate Index hedged into NZD

Structure and taxation

The Fund vehicle is a Unit Trust and Portfolio Investment Entity (PIE) which is priced daily. Unit holders elect their own Portfolio Investor Rate. Information is provided to the IRD and unit holders on an annual basis.

Investment process

GSAM's investment philosophy and style is such that they aim to generate outperformance over time without being unduly exposed to one particular investment strategy or market circumstance. GSAM's global approach enables them to capture diverse sources of excess returns and their risk management process ensures the portfolio is not dependent on any particular market inefficiency that may dissipate. The GSAM global fixed interest portfolio is constructed in such a way that aims, over time, to react well to different economic conditions.

The management of GSAM's global fixed interest portfolios is team-based with investment decisions taken collectively, following thorough discussion and debate. The investment process encompasses three key steps:

Step 1: Build a risk budget that takes account of the investment objectives, guidelines and benchmark of the mandate.

Step 2: Identify attractive investment opportunities and implement the best ideas from the specialist top down and bottom up investment strategy teams.

Step 3: Monitor risk and attribution to ensure risks are consistent with investment guidelines.

Distributions

At any date for any period fixed by the Manager

Hedging policy

Assets are 100% hedged into NZD

Management fees and other charges

Investment management fees will be negotiated separately with each investor and invoiced outside the Fund.

All Fund statutory and operating costs will be met directly by the Manager.

Buy/sell spread

Nil

Trustee

Public Trust

Custodian

Public Trust as legal custodian, BNP Paribas Fund Services Australasia Pty Limited delegated as functional custodian.

Selected investors only

Participation in the Fund is limited to persons or entities who are New Zealand resident, and:

(a) whose principal business is the investment of money; or

(b) who, in the ordinary course of and for the purposes of their business, habitually invest money;

and, consequently (or for other reasons) do not constitute "the public" for the purposes of the Securities Act 1978 (**Exempt Person**). Nikko AM will not therefore be required to produce a registered prospectus or an investment statement in relation to the proposed investment (such documents otherwise being required were this offer to be made to persons or entities that are not Exempt Persons), and such documents will not be produced accordingly. Investors in the Fund will be required to acknowledge their status as an Exempt Person as part of their subscription in the Fund. Investors in the Fund will also be required to undertake to Nikko AM that any transfers of interests in the Fund will only be to Exempt Persons.

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General Enquiries: NZenquiries@nikkoam.com | +64 9 307 6363

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Performance (NZD gross returns)

| | Fund % | Benchmark % | Excess % |
|----------------------|-------------|-------------|--------------|
| 1 month | 1.44 | 0.99 | 0.45 |
| 3 months | 3.56 | 3.91 | -0.35 |
| 6 months | 4.69 | 4.73 | -0.04 |
| 1 year | 5.88 | 5.41 | 0.48 |
| 2 years (pa) | 7.65 | 8.38 | -0.73 |
| 3 years (pa) | 6.79 | 6.80 | -0.01 |
| 5 years (pa) | 7.38 | 7.53 | -0.15 |
| 10 years (pa) | 7.74 | 7.92 | -0.18 |

Fund size \$272 million

Asset allocation

| Credit quality rating | |
|-----------------------|-------|
| AAA | 41.2% |
| AA+, AA, AA- | 10.9% |
| A+, A, A- | 29.4% |
| BBB | 20.3% |
| BB | 0.3% |
| Unrated | 0.3% |

| Sector allocation | Fund | Index |
|--------------------------|-------|--------|
| Governments | 42.0% | 51.9% |
| Agency | 3.9% | 9.4% |
| Credit | 27.0% | 20.4% |
| Collateralised & MBS | 24.9% | 12.1% |
| Emerging market debt | 4.6% | 6.2% |
| Cash, derivatives, other | -2.4% | 0.0% |
| Number of holdings | 459 | 17,127 |

Duration and yield

| | | |
|-------------------|-----------------|-------------------------|
| Duration | Fund 5.83 years | vs benchmark 6.55 years |
| Yield to Maturity | Fund 3.73% | vs benchmark 3.33% |

Commentary

Government bond yields fell across developed markets over March quarter. In the US, the 10-year yield closed the month 50 basis points lower at 1.77%. Rates on UK government bonds followed this trend, ending the month down 55 bps at 1.42%. In Japan, the 10-year yield fell 30 bps to close at -0.04%. In Europe, German 10-year yields edged down 48 basis points to end the quarter at 0.15%.

The **fund underperformed** over the quarter by 0.35%. Country allocation and sector allocation were the main detractors at 0.15% each. Stock selection within governments and swaps sector and emerging market debt were small detractors.

GSAM maintained their short in US rates though the Fed surprised the markets with a dovish stance in the March policy meeting. GSAM believes firming core inflation and improving wage growth data, along with some stabilising in commodities, support a short position in US rates. In Europe, the ECB announced an increase in monthly asset purchases by €20bn, to €80bn a month, and the buying of euro-denominated bonds of investment grade, non-financial Eurozone companies as part of its most recent QE expansion. This was in addition to a further cut to the deposit rate by 10 basis points, to -40 basis points, and a 5 basis points cut to benchmark refinancing and lending rates, to 0% and 0.25%, respectively. We maintained our neutral position in European rates in March.

Within the G10, GSAM remains long European rates, and short in the US and UK. GSAM added to their short position in Japan as rates at the long end have rallied since the Bank of Japan introduced negative rates. Base case expectation is for the Bank of Japan to remain on hold at its April 28 policy meeting, as inflation has not markedly deteriorated since January and policymakers will likely want to wait a bit longer to see the impact of the first cut before moving further negative. In the periphery, GSAM remains marginally long Italy and Spain and believe low Eurozone inflation will likely keep the pressure on the ECB to maintain its accommodative stance with a bias to ease further. In Australia, low inflation and deteriorating terms of trade are likely to see the Reserve Bank of Australia maintain an easing bias, even in the face of potentially tighter Fed policy. In Canada, domestic demand is softening and lower oil prices will likely remain a drag on the economy. GSAM are long Australian and Canadian rates.

Agency mortgage-backed securities (MBS) outperformed duration-neutral US Treasuries by 15 basis points in March and underperformed by 38 basis points over the quarter. In March MBS benefitted from dovish commentary from the Federal Reserve (Fed) and support from overall risk asset spread tightening. Net supply over the first quarter was muted at \$35bn owing partially to negative housing seasonals. US commercial banks, which surpassed expectations in 2015 by purchasing \$150bn in agency MBS, only purchased \$10bn of MBS in the first quarter. GSAM ended the quarter covering some of their underweight to agency MBS as valuations on spread products rallied and MBS were positioned to benefit from expected seasonal demand from Japanese buyers following their fiscal year-end. However, as we move away from quarter-end, GSAM are positioned with a small underweight to agency MBS and expect the supply-demand picture for MBS to turn negative.

Investment grade corporate credit spreads finished the quarter 158 basis points over sovereigns. GSAM currently holds a modest long position in corporate credit. Markets remain challenged in the near term by factors such as weak global growth, commodity market volatility and late-cycle credit activity both representing risks and creating opportunities. GSAM now holds a marginally more constructive outlook on oil prices and expect monetary policy could continue to be supportive in both Europe and the US. Supportive actions from the European Central Bank (ECB) and a potentially more dovish Fed would positively impact risk assets, however GSAM also believed present conditions merit a cautious approach with particular focus on tactical positioning and security selection.