

# Nikko AM Wholesale Option Fund

## Fund manager

Nikko Asset Management New Zealand Limited (Nikko AM).

Nikko AM is Asia's premier global asset manager. In New Zealand we actively manage NZ\$5 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).

## Fund launch

April 2007 – a similar portfolio has been operated by Nikko AM since September 2003.

## Investment objective

To invest the portfolio in the authorised investments such that the portfolio earns a gross return of Bloomberg NZBond Bank Bill Index plus 4.0% per annum over a rolling three year period before fees.

## Benchmark

Bloomberg NZBond Bank Bill Index plus 4.0% per annum (from 1 July 2016)

## Investment process

The Fund invests into cash deposits and bank bills with highly rated financial institutions. The assets are then used as collateral security for derivatives, in particular, selling options on long-term NZ, US, UK, Euro bloc or Australian government stock.

Most options are written for one month and provide the institutional purchaser with a payout if interest rates move by more than a prescribed margin in one particular direction. The Fund earns a premium for writing (selling) the options. The Fund will write options on government bonds with maturities between 5 and 15 years.

## 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.

## Distributions

At any date for any period fixed by the Manager

## Currency management

All premium income is converted into NZD upon receipt and any currency margin deposits are hedged to NZD within an operational range of 98.5% to 101.5%.

## Management fees and other charges

Investment management fees and performance 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.

**Performance fee:** Negotiated separately with each investor and invoiced outside the Fund.

## Buy/sell spread

Nil

## Trustee

Public Trust

## Custodian

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

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## Performance (NZD gross returns)

	Fund	Benchmark*	Excess
1 month	-0.74%	0.53%	-1.27%
3 months	1.96%	1.60%	0.35%
6 months	4.35%	3.35%	1.00%
1 year	16.14%	7.07%	9.07%
2 years (pa)	11.43%	7.50%	3.93%
3 years (pa)	13.12%	7.33%	5.78%
5 years (pa)	7.61%	7.16%	0.45%

\* S&P/NZX Bank Bills 90 Day Index plus 4.0% per annum prior to 1 July 2016

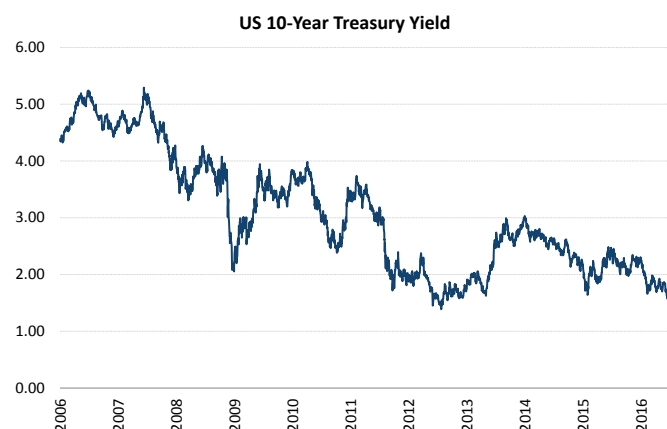
## Fund size

NZ\$180 million

## Compliance

The Fund complied with its investment mandate during the month.

## Commentary



The Nikko AM Wholesale Option Fund fell by 0.74% in June. The month was eventful, delivering surprises that produced widely ranging and volatile markets. The event that was most unexpected by financial markets was the UK public voting to leave the EU in the 23 June referendum. Markets assumed the “remain” vote would carry the day, however as votes were being counted and the reality of a “shock” result began to set in, chaotic trading conditions ensued with wild swings in illiquid asset markets, especially in currency markets.

The GBP/USD traded in a 17 cent range, reaching a 30-year low and having its largest one-day fall under the free-float regime. In this “risk off” environment there was strong buying of US Treasury bonds with the 10-year bond yield falling from 1.74% before the poll closed to an intraday low of 1.4% as the UK result became more certain. The monthly trading range was 1.85% to 1.4%. The sharp fall in yields meant a number of call options were exercised resulting in the negative returns for June.

Earlier in the month, the US May non-farm payrolls report rose by just 38,000 – much weaker than anticipated and confirmed a slowdown in US employment. Soon after, US Federal Chair Yellen seemed to back off her previous guidance that a tightening in monetary policy was likely in coming months. Later the Fed’s Open Market Committee (FOMC) confirmed with the Fed saying there is no urgency to raise rates. The UK vote to exit the EU is also further confirmation that the Fed will be slow and cautious in any policy tightening. The general consensus is that Brexit will lead to marginally slower global growth and more geopolitical tensions as a number of countries ready themselves for general elections over the next year. With heightened investor anxiety surrounding these events little upward movement in interest rates is likely over 2016 and into 2017.

Even though the Option Fund registered a negative return in June, conditions remain favourable for an acceptable level of performance over the months ahead.