Nikko AM Wholesale Conservative Fund

Fund manager

Nikko Asset Management New Zealand Limited (Nikko AM NZ).

In New Zealand we actively manage around 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

July 2016

Investment objective

To achieve a return which exceeds the weighted composite benchmark return by 1.00% p.a. over a rolling three year period before fees, expenses and taxes (if any).

Benchmark

Benchmark performance is calculated on a weighted composite of the relevant sector indices.

Distributions

Generally does not distribute but may do so at the Manager's discretion.

Currency management

Currency hedging contracts, if any, are held in the sector funds listed in the asset allocation.

Trustee

Public Trust

Custodian

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

Buy/sell spread

0.0473% / 0.0473%

Structure

The Fund vehicle is a Portfolio Investment Entity (PIE) which is priced daily. Investors elect their own Prescribed Investor Rate. The Fund invests directly into PIEs for the New Zealand sectors and either directly or indirectly via an appropriate vehicle(s) for the global sectors. Information is provided to the IR and investors on an annual basis.

Management fees and other charges

Investment management fees will be negotiated separately with each investor and invoiced outside the Fund. Nikko AM NZ, as manager, will directly meet costs required for the operation of the Fund, including, but not limited to, trustee fees, custody and sub-custodial fees, and administration fees (administration fees in respect of the Corporate Bond fund may be charged). There is no investment management fee charged to the Nikko AM Wholesale Conservative Fund by other Nikko AM NZ funds forming the Nikko AM Wholesale Conservative Fund composite. Management fees and administration costs charged by JP Morgan Alternative Asset Management Inc (JPMAAM) are included in the unit price of the Nikko AM Wholesale Multi-Strategy Fund that the Nikko AM Wholesale Conservative Fund invests in. Contact Nikko AM NZ for more details.

Performance fees (if any) are recognised in the unit price of the Conservative Fund for the following sector funds:

- Nikko AM Wholesale Option Fund – 15% of returns in excess return over benchmark, accrued on a daily basis, payable annually, subject to recovery of any previous period negative returns before entitlement.
- Nikko AM Wholesale Multi-Strategy Fund (indirectly via investment in JPM Multi-Strategy Fund II, Ltd). A performance fee of 10% of returns above US 3-month T-Bill after all fees accrued on a monthly basis, payable annually, subject to recovery of any previous period negative returns before entitlement, is charged by JP Morgan Alternative Asset Management Inc in the JPM Multi-Strategy Fund II, Ltd. There are no direct charges or fees in the Nikko AM Wholesale Multi-Strategy Fund.

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Performance (NZD gross returns)

	Fund	Benchmark	Excess
1 month	0.25%	0.04%	0.21%
3 months			
6 months			
1 year			
2 years (pa)			
3 years (pa)			
5 years (pa)			

Fund size

NZ$0.5 million

Compliance

The Fund complied with its investment mandate during the month.

Asset allocation

Sector	Fund	Benchmark
NZ Cash Fund	10.00%	10.00%
NZ Bond Fund	15.04%	15.00%
Corporate Bond Fund	10.00%	10.00%
Option Fund	5.00%	5.00%
Global Bond Fund	30.07%	30.00%
Core Equity Fund	7.52%	7.50%
Property Fund	4.98%	5.00%
Global Equity Funds	12.39%	12.50%
Multi-Strategy Fund	5.00%	5.00%

[1] Global Bond Fund 100% hedged

[2] Global equities 69% hedged on gross basis.

Currency exposure

NZ dollar exposure of the Conservative Fund: 93.0%

Sector performance (NZD gross returns)

	1 month		3 months		1 year		3 years pa		5 years pa	
	Fund	B'mark	Fund	B'mark	Fund	B'mark	Fund	B'mark	Fund	B'mark
NZ Cash Fund	0.26%	0.19%								
NZ Bond Fund	0.21%	-0.14%								
Corporate Bond Fund	0.23%	-0.14%								
Option Fund	1.23%	0.52%								
Global Bond Fund	0.15%	0.12%								
Core Equity Fund	0.24%	-0.02%								
Property Fund	-1.69%	-1.38%								
Global Equity Funds	1.00%	0.37%								
Multi-Strategy Fund	0.15%	0.39%								

Indices used:

NZ Bond Fund – Bloomberg NZ Bond Govt 0+ Yr Index

Option Fund – Bloomberg NZBond Bank Bill Index+ 4.0% p.a.

Multi-Strategy Fund – Bloomberg NZBond Bank Bill Index + 2.5% p.a.

Global Bond Fund – Barclays Capital Global Aggregate Index (100% hedged into NZD)

Property Fund – S&P/NZX All Real Estate (Industry Group) Gross with Imputation Index

Global Equities – MSCI ACWI, with net dividends reinvested unhedged in NZD and MSCI ACWI, with net dividends reinvested 139% hedged to NZD

Corporate Bond Fund – Bloomberg NZ Bond Govt 0+ Yr Index

Core Equity Fund – S&P/NZX 50 Index Gross with Imputation Index

New Zealand bonds and options

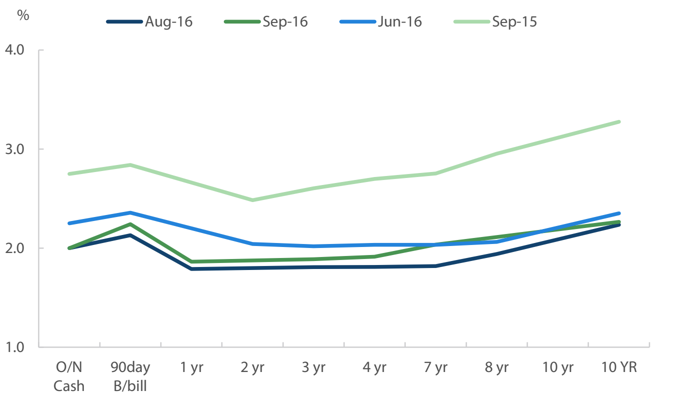
New Zealand bond

Sector allocation	Fund
Government stock	27.1%
SOE and local authority	18.7%
NZ registered banks	39.4%
Corporate debt	14.8%

S&P Rating	Fund
AAA	9.8%
AA	65.9%
A	20.2%
BBB	4.1%

Top 5 corporate issuers	Fund
NZ Local Government Funding Authority	11.3%
Bank of New Zealand	9.3%
Rabobank	7.2%
Fonterra Co-operative Group	6.3%
Westpac Banking Corp	5.7%

New Zealand yield curve



Duration	Fund 4.8 years versus benchmark 4.7 years
Yield	Fund (gross) 3.1% versus benchmark 2.0%

Commentary

The Nikko AM Wholesale NZ Bond Fund returned 0.21% for the month of September. Over the month the Bloomberg NZ Government Bond Index produced a return of -0.14% for the month while the All Swap Index returned 0.06%, and the NZ Bond Corporate A Index returned 0.16%.

In summary for the month, portfolios 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. Government bonds have been the best performing bond sector for most of the year as interest rates fell and credit margins widened, however there was some catch up from other sectors as Governments performed poorly over the month on a relative basis. The Fund outperformed as corporate bonds and swaps delivered a better return, as they didn't move higher in yield to the same extent as similar maturities of government bonds. Corporate bonds also have the advantage of a higher running yield which helps to dampen the volatility of returns.

NZ interest rates were volatile intra-month with the NZ Government 2033 bond moving higher in yield by close to 40 basis points before retracing most of this move and finishing at 2.61%. For the month government bond maturities from 1 to 7 years closed approximately 10 basis points higher in yield with longer bonds less impacted. Swap margins contracted in spread to government bonds as the underlying swap rates didn't move higher in yield to the same extent as government bonds.

Over the quarter interest rates still managed to finish lower in yield despite rising in September. Government bonds were only marginally lower in yield, but swap rates performed better, falling an additional 10-15 basis points compared to similar maturities of government bonds. The shape of the NZ swap yield curve has remained relatively stable over the past three months with the 2-10 year swap spread currently at 47 basis points. Credit markets tentatively settled and (the accrual trade of) having a higher yielding portfolio is showing some benefit as the higher yield isn't eroded by widening credit margins. 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 New Zealand economy is performing well on a relative basis compared to other developed economies; business and consumer confidence, GDP, inflation, and dairy prices have been improving. Interest rates are low and supportive of activity with the possibility of a further rate cut. Challenges are the high level of the NZD that continues to frustrate the Reserve Bank and they would like to see house price appreciation slow. The direction of NZ short-term interest rates will continue to be influenced by local factors with low cash rates anchoring the front end of the yield curve. Bonds 5-years and longer in maturity will likely remain more heavily influenced by global events and movements in US bond rates.

New Zealand corporate bond

Sector allocation	Fund
Corporate bonds	39.3%
NZ registered banks	49.2%
Local authority	6.4%
NZ government and government equivalent	5.1%

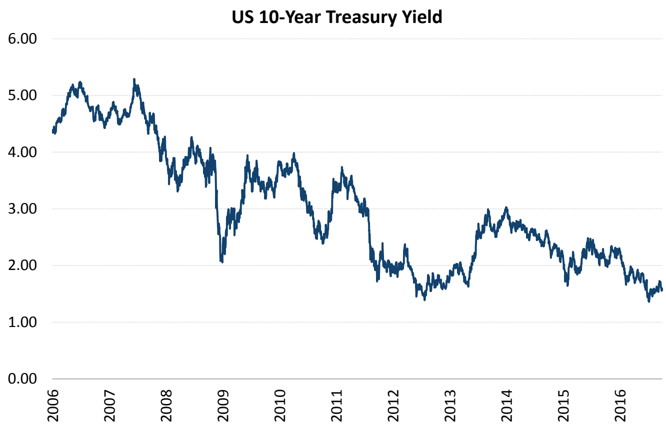
Credit rating profile S&P rating	% portfolio	Number of holdings
AAA	3.4%	9
AA	47.7%	55
A	21.5%	23
BBB	27.4%	30

Top 10 issuers			
Westpac Banking	9%	Rabo Bank	6%
Bank of New Zealand	9%	NZ Government	5%
ANZ Bank	9%	Transpower	5%
ASB Bank	7%	Kiwi Bank	4%
Fonterra	6%	Auckland City Council	3%

Duration and yield

Duration	Fund 3.9 years versus benchmark 4.7 years
Yield	Fund (gross) 3.5% versus benchmark 2.0%

Options



The Nikko AM Wholesale Option Fund continued to perform well over September, gaining 1.23%. This return compares favourably to the return generated from cash and bond markets as the low nominal yields on fixed income assets begin to constrict returns from these sectors.

Income generated by the Option Fund by writing options on 10-year US Treasury bonds is not significantly impacted by low bond yields and we anticipate Fund returns will continue to outperform more traditional fixed income investment strategies over the year ahead.

US 10-year bonds traded in a 23 basis point range over the month - this range is modest, but larger than the 18 bp range seen in August. Bond yields started the month at 1.58% and closed at similar levels. The intra month low was 1.52% and the high point was 1.75%. Due to the narrow trading range, bond yields stayed within the option bands established so no options were exercised. A low level of volatility in markets at present has led to option premium income being lower than average, but still high enough to generate an attractive level of return.

The Federal Reserve seem to be inching closer to their second rate rise, the first was December 2015. The US economy is steadily improving and we believe the Fed needs to protect their credibility by raising rates soon. While a move in rates in 2016 is probable, the Fed will be careful not to unsettle markets and therefore forward guidance on future moves is likely to indicate only a modest and slow increase. The US Presidential election is occurring on 8 November and financial markets will undoubtedly undergo mood and sentiment swings around this event. While a change in President is an important event in the political life of America we believe any economic impact will be much more subdued. It is unhelpful that the roll of the Federal Reserve is becoming more politicised and is perhaps another reason why the Fed seems sensitive to limit the impact of policy changes on financial markets.

We believe the yield movement on longer dated Treasury bonds is likely to be muted even if short-term rates rise as investors' global search for yield will ensure the demand for relatively high yielding US bonds remains strong.

We continue to believe this environment remains favourable for the Option Fund, especially when viewed in the context of a modest return outlook from other sectors of financial markets.

Global bond

Credit quality rating	
AAA	28.66%
AA+, AA. AA-	12.04%
A+, A, A-	39.26%
BBB	19.87%
BB	0.17%

Sector allocation	Fund	Index
Governments	43.40%	52.20%
Agency	5.90%	9.20%
Credit	21.30%	20.80%
Collateralised & MBS	30.10%	11.70%
Emerging market debt	4.80%	6.10%
Cash, derivatives, other	-5.50%	0.00%

Duration and yield

Duration	Fund 6.60 years versus benchmark 6.79 years
Yield to Maturity	Fund 3.35% versus benchmark 3.02%

Commentary

During September the **Bank of Japan (BoJ)** unveiled a new policy framework which involves 'Quantitative and Qualitative Monetary Easing (QQE) with Yield Curve Control' and an 'inflation-overshooting commitment'. The measures are designed to address the impact of low yields on financial institutions.

Sterling credit markets received technical support from accommodative monetary policy, with the Bank of England (BoE) commencing its Corporate Bond Purchase Scheme (CBPS).

Government bonds displayed mixed performance over the quarter. In the US, 10-year yields closed 12 bps higher at 1.59%, UK down 12 bps to 0.75%, German 1bp up to -0.12% and Japanese up 13bps to -0.09%.

The **Fund** outperformed over the month and quarter ended September. Over the quarter, country allocation added the most value (+0.38%), followed by the allocation to government/ swaps and securitized securities (0.16% and 0.10% respectively). Emerging market debt detracted value (-0.07%).

Agency MBS outperformed duration-neutral US Treasuries by 64bps over the quarter. The sector benefitted from low volatility and demand from foreign investors and domestic and commercial banks looking for yield. GSAM believes collateralized loan obligations and asset backed securities offer attractive spreads with strong credit protection and remain among the most compelling sectors in securitized products.

.**Investment grade corporate** spreads finished the quarter 134bps over sovereigns. The Fund's modest overweight reflects GSAM view that spreads could potentially drift wider in this late stage of the credit cycle. GSAM's are mindful of weakness arising from slowly deteriorating fundamentals as economic and political ramifications of Brexit begin to emerge. However, any widening of spreads is expected to be moderate given accommodative central banks programs in Europe and the UK.

Core Equity

Sector allocation	Fund	Index
Healthcare	19.5%	16.9%
Utilities	16.0%	15.8%
Industrials	13.1%	14.6%
Consumer discretionary	12.3%	10.1%
Telecommunications	9.3%	10.1%
Materials	9.1%	9.1%
Consumer staples	6.7%	3.8%
Energy	5.8%	4.4%
Real Estate	3.5%	9.6%
Cash	3.1%	0.0%
Information technology	1.6%	2.5%
Financials	0.0%	3.1%

Attribution

What helped		What hurt	
Summerset Group	OW	Japara Healthcare	OW
Chorus Ltd	UW	Contact Energy	OW
Metlife Care	OW	Fisher & Paykel	OW

OW: overweight; UW: underweight; NP: neutral position; NH: no holding

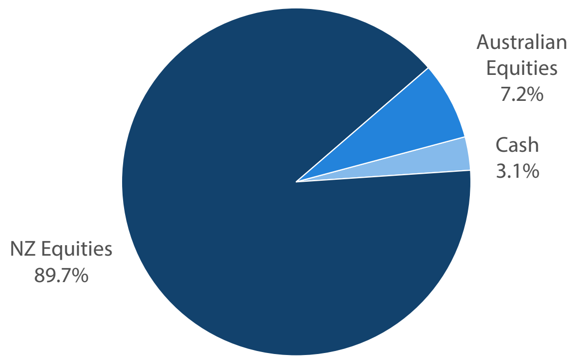
Largest deviations from index

Overweight	Underweight
Contact Energy	Ryman Healthcare
Infratil Limited	Mercury NZ Limited
Summerset Group Holdings	Kiwi Property Group

Top 10 holdings

Fletcher Building	Infratil Limited
Contact Energy	Sky City Entertainment
Auckland International Airport	Summerset Group Holdings
Spark New Zealand	MetlifeCare
Fisher & Paykel Healthcare	Restaurant Brands
Number of holdings in fund	**34**

Asset allocation



Hedging

Australian listed stocks are unhedged

Commentary

The S&P/NZX 50 Index Gross (with imps) rose 7.26% for the quarter bringing the YTD return to 17.6%. Although the quarterly return is impressive it hides a fall from lifetime highs and a modest recovery during the month of September. The S&P/ASX200 Accumulation Index, S&P500 and FTSE100 returned +5.1%, +3.3% and +6.1% respectively in local currencies.

The Fund performed in-line with the benchmark during the quarter returning 7.32% versus the benchmark of 7.26%.

The retirement stocks had a strong period with the largest positive contributors to relative return coming from the overweight positions in **Summerset Group** (SUM) and **Metlifecare** (MET). Both companies reported strong operating results with additional support coming from valuation uplifts.

The nil position in Chorus added relative value as the stock fell sharply on concerns for lost copper lines and accelerating fibre uptake which leads to higher capex. This dynamic was the core reason for a nil holding recently.

Kiwi Property Group added relative value (nil holding) as the stock fell while the market considered challenging valuation metrics for the company and an extensive development pipeline.

Performance was hurt by **Japara Healthcare** (JHC) which fell 17.2% after continuing concerns for Government funding, a below expectations outlook in its result and big misses from other sector companies results. We continue to see value in Japara in the medium term.

Contact Energy (CEN) had a poor quarter with the stock lower against a positive market notwithstanding compelling valuation support. The result announcement during the quarter was average and outlook comments concerned the market.

Fisher & Paykel Healthcare (FPH) pulled back following a very strong, multi-year rally. The stock was hurt by a modestly negative tone to their AGM update and pending legal action between FPH and their Australian competitor, Resmed.

A number of changes were made over the quarter. Companies sold included NEXTDC (NXT) Orion Healthcare (OHE), NZ Oil and Gas (NZO), Xero (XRO) and Westpac Bank (WBC). Additionally **Fisher and Paykel Healthcare** (FPH) was reduced from a substantial overweight position. New companies introduced over the period included **Aconex** (ACX), **Investore Property** (IPL), **Comvita** (CVT) and **Chorus** (CNU).

(**Bold** denotes stock held in portfolio)

Property

Attribution

What helped		What hurt	
Summerset Group	OW	Property Link Group	OW
Metlifecare	OW	Argosy property	OW
Investore Property	OW	Precinct Properties	UW

OW: overweight; UW: underweight; NP: neutral position; NH: no holding

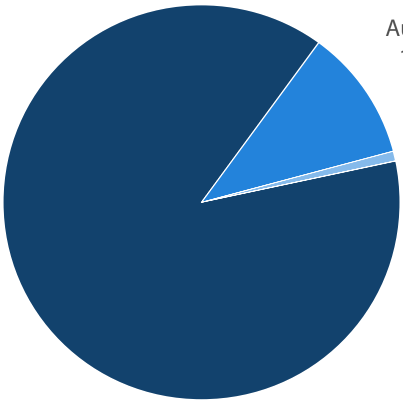
Top 5 holdings

Argosy Property	Goodman Property Trust
Kiwi Property Group	Precinct Properties
Stride Stapled	
Number of holdings in fund	**22**

Hedging

Australian listed stocks are 94% hedged to NZD

Asset allocation



Commentary

Global markets were volatile towards the end of the quarter with the US Federal Reserve getting closer to raising interest rates, the US election approaching and geo-political events such as North Korea conducting another nuclear test and the cease fire in Syria failing. Despite the volatility, all major markets produced good returns for the quarter with the MSCI World index up 5%. The NZ Property sector was well behind the broader market with the S&P/NZX 50 index up 7.3% for the quarter. The Australian property sector also underperformed, down 1.1% as measured by the S&P/ASX 300 Real Estate index which compares to a 5.1% return for the S&P/ASX 200 index.

The Fund ended the quarter down 1.69%, 0.31% behind the benchmark. The retirement stocks had a strong quarter with the largest positive contributors to relative return coming from out of benchmark positions in **Summerset Group** (SUM) and **Metlifecare** (MET) while an overweight position in new listing **Investore Property** (IPL) also helped. SUM and MET both announced strong results with the stocks up 21.6% and 13.7% respectively. IPL ended the period up 6.0% following its listing in July. The largest detractors from relative performance was a position in new Australian listing **Propertylink Group** (PLG), overweight **Argosy Property** (ARG) and underweight **Precinct Properties** (PCT). Despite no new information, PLG fell 18.5% (in AUD) from its listing price while ARG lost 0.5% and PCT rose 5.9%.

Key portfolio changes over the quarter included adding **Arvida Group** (ARV), IPL and PLG while divesting of **Growthpoint Properties** (GOZ). Other changes included reducing the overweight in **Stride Property** (SPG) and adding to **Vital Healthcare** (VHP).

New Zealand holdings PCT, VHP, MET, PFI and SUM all reported either full year or half year results during the period. Portfolio metrics for the landlords remain strong with low vacancy and gearing along with relatively long weighted average lease terms. The retirement operators continue to benefit from the strong New Zealand housing market which enables them to realise good gains on resales along with growing demand for their units due to the aging population. All of the portfolio's Australian holdings reported results during the period with **Mirvac Group** (MGR) being the pick of the bunch with a result at the top of their guidance and forecast for earnings growth to be 8 – 11% in the coming year, well ahead of what the market had forecast. MGR ended the period up 10.9% (in AUD). Earlier in the quarter IPL, which was demerged from Stride Property (now **Stride Stapled Group** following its capital restructure) along with additional capital raised, started trading. Vital Healthcare also completed its rights issue which raised $160 million which will be used to fund its development pipeline. ARV also announced a $42m capital raising late in the quarter to fund the acquisition of three retirement villages. Most of the property securities continue to recycle capital, selling non-core assets to acquire or develop new properties.

(**Bold** denotes stock held in portfolio.

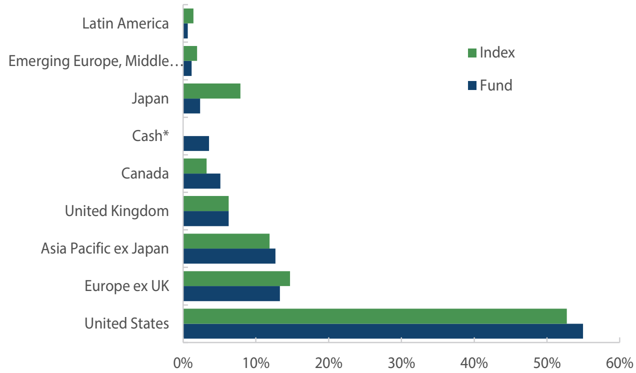
Global Equity

Sector allocation

Sector	Fund	MSCI
Information Technology	17.3%	15.9%
Consumer Discretionary	16.0%	12.3%
Financials	11.0%	16.9%
Health Care	10.5%	11.7%
Consumer Staples	10.3%	10.4%
Industrials	9.5%	10.4%
Energy	7.9%	6.9%
Materials	4.8%	5.0%
Telecommunication Services	3.5%	3.8%
Cash*	3.5%	0.0%
Utilities	3.3%	3.3%
Real Estate	2.4%	3.4%

* includes the sum of the underlying managers' cash allocations

Geographical allocation



Emerging markets **11% of Fund**

Top 10 holdings

Company	Fund	MSCI	Country
Amazon.com	3.23%	0.90%	US
Encana Corp	1.74%	0.03%	Canada
Alphabet, Class A	1.69%	0.64%	US
Taiwan Semiconductor	1.57%	0.39%	Taiwan
Facebook	1.51%	0.80%	US
Berkshire Hathaway	1.45%	0.46%	US
Wells Fargo & Co	1.25%	0.57%	US
Reckitt Benckiser Group	1.22%	0.16%	Britain
Apache Corp	1.17%	0.06%	US
Naspers	1.16%	0.20%	SA

Manager allocations

Manager	Range	Actual
WCM Investment Mgmt	10-30%	26.9%
Principal Global Investors	10-30%	25.8%
Epoch Investments Partners Inc	10-30%	21.2%
Davis Selected Advisors LP	10-30%	22.2%
Nikko AM Limited (Derivatives)	0-10%	2.6%
Nikko AM Limited (Cash)	0-10%	1.3%

Commentary

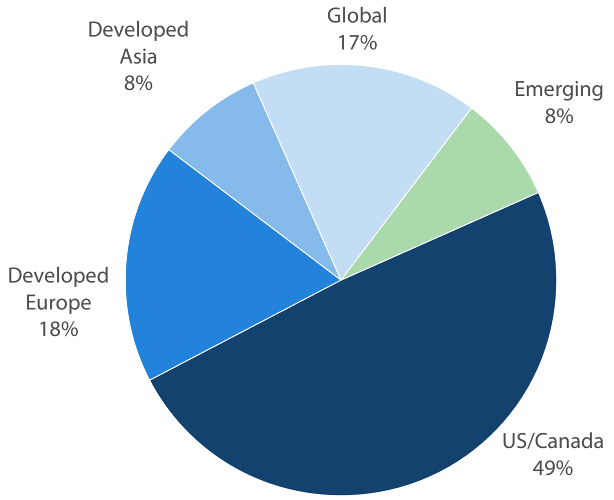
Across equity regions, in local currency, Asia Pacific was the strongest, led by China (up 11%), Taiwan (up 9%) and Japan (up 6%). Performance across Europe was mixed, with Germany and Spain both up more than 7%, while Italy was flat and Denmark fell 7%. The Danish market's sharp decline was largely driven by the diabetes care drug maker Novo Nordisk (down 22%).

Among the major sectors, Information Technology (up 11%) was extremely strong over the quarter, driven by significant gains in heavyweights Apple (up 16%), Microsoft (up 11%), Facebook (up 10%) and Alphabet (up 10%). Materials (up 7.5%) was the next best performing sector, with gains across both the Metals & Mining (up 10%) and Chemicals (up 6%) industries. Defensive sectors lagged the overall market, with Consumer Staples (down 2.5%), Telecoms (down 3.7%) and Utilities (down 5.1%) all in retreat over the quarter.

The Fund outperformed the benchmark over the quarter. Of the four sub-managers, Davis led the charge with a return of 12.41% for the quarter, to outperform by 605 bps. Its strong performance can be attributed to large gains in oil & gas exploration companies, Encana (up 31%) and Apache (up 13%), as well as the world's largest cement producer, LafargeHolcim (up 28%). Another major contributor to Davis' success was Amazon.com (up 14%) which traded up to a new record high of USD 837 per share. While Davis has been reducing their position in Amazon, it is still a significant 5% position in their portfolio. The performance of PGI (6.12%) and WCM (5.99%) were more in line with the benchmark, and performance highlights included large gains in Mercadolibre (up 29%), Taiwan Semiconductor (up 14%) and TD Ameritrade (up 22%). The value manager, Epoch (0.119%), struggled however on account of its overweight to defensive yield plays which underperformed in anticipation of a potential US rate hike in December. Detracting the most from performance, was private prison operator, Corrections Corp of America (down 60%), in response to an announcement by the US Department of Justice in mid-August that it would be gradually moving away from the use of private prisons. Other significant detractors were tobacco companies, Reynolds American (down 14%) and Altria Group (down 9.5%), as well as the utility holding company, PPL Corp (down 10%).

Multi-Strategy

Portfolio composition by geography

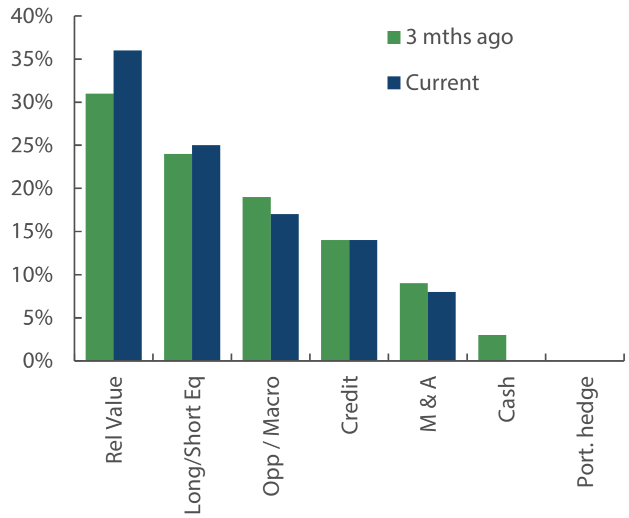


Investment profile

MSF II Ltd currently employs 36 managers

Opportunistic / Macro	7	Merger Arbitrage/Event	2
Long / Short Equities	10	Credit	6
Relative Value	10	Portfolio Hedge	1

Portfolio composition by strategy



Performance of key investments

Name	Strategy	Latest month	Cal YTD
QVT	Relative Value	-0.99%	-4.82%
Deerfield	Long / Short Equities	1.12%	6.76%
Palomino	Opportunistic / Macro	0.59%	0.63
Tyrus Capital Event Fund	Merger Arbitrage / Event Driven	2.32%	7.38%
Pelham	Long / Short Equities	2.04%	1.33%
Key holdings as a percentage of the Fund			**17.3%**