

Nikko AM Wholesale Global Bond Fund

Fund manager

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

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).

Nikko AM NZ 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 AUD 1,126 billion in assets under management. GSAM's Global Fixed Income Team manages AUD451 billion of global fixed income assets.

Fund launch

October 2008

Investment objective

To construct a portfolio of authorised investments that outperform the Fund's benchmark return by 1.0% per annum over a rolling three year period before fees.

Benchmark

Bloomberg Barclays Global Aggregate Index (100% hedged into NZD)

Currency management

Foreign currency exposures created as a consequence of capital markets investment remain hedged to NZD within an operational range of 98.5% to 101.5%.

Distributions

Generally on calendar quarters, or at any date for any period determined by the Manager.

Structure and taxation

The Fund vehicle is a Portfolio Investment Entity (PIE) which is priced daily. Investors elect their own Prescribed Investor Rate. Information is provided to the IR and investors 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.

Management fees

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.

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Performance (NZD gross returns)

	Fund	Benchmark	Excess
1 month	-1.39%	-1.55%	0.16%
3 months	-1.93%	-2.28%	0.34%
6 months	1.08%	0.51%	0.58%
1 year	5.71%	5.39%	0.32%
2 years (pa)	5.78%	5.38%	0.39%
3 years (pa)	6.94%	6.85%	0.09%
5 years (pa)	6.87%	6.64%	0.23%
10 years (pa)	7.41%	7.42%	-0.01%

Fund size

NZ\$247million

Asset allocation

Credit quality rating	
AAA	34.1%
AA+, AA, AA-	11.3%
A+, A, A-	37.1%
BBB	17.3%
BB	0.2%

Sector	Fund	Index
Governments	36.1%	51.3%
Agency	4.9%	9.2%
Credit	21.2%	21.1%
Collateralised & MBS	32.1%	12.3%
Emerging market debt	3.7%	6.1%
Cash, derivatives, other	2.0%	0.0%

Duration and yield

Duration	Fund 7.18 years versus benchmark 6.75 years
Yield to Maturity	Fund 3.54% versus benchmark 3.18%

Commentary

Donald J. Trump claimed victory in the US presidential election, and the Republican Party secured both houses of Congress. It is not yet clear how the Trump Administration will prioritize campaign pledges or to what extent they will be implemented. Broadly speaking, policies which may stimulate domestic growth include proposed spending to bolster manufacturing and infrastructure, tax cuts and deregulation. GSAM see potentially negative implications from a strengthening dollar, rising interest rates, more volatility and restrictive trade policies that could dampen global growth. In Europe, Italians voted to reject proposed reforms to the Constitution. The outcome was expected but the margin was much larger than projected by the polls. The populist tide which has claimed victories in the UK and US this year was defied in the Austrian elections, where the Green party backed independent candidate, Alexander Van der Ballen, defeated the far-right Freedom party candidate, Norbert Hofer.

Over the month, anticipation of fiscal expansion in the US and constructive global economic data led to a sell-off in **government bonds**. In the US, the benchmark 10-year yield closed the month 53bps higher at 2.36%. The yield on the UK 10-year government bond reached a pre-Brexit level, ending the month 16 bps higher at 1.41%. In Japan, the 10-year yield

increased by 7bps, ending the month in the positive territory as 0.02%. In Europe, German 10-year yields were up by 11bps, ending the month at 0.27%. In European peripherals, Spanish and Italian 10-year yields rose 35bps and 33bps, respectively. The Fund's duration strategy is neutral US, European and Japanese rates. In response to President-elect Donald Trump's fiscal stimulus plans, inflation expectations have increased, adding to the wage pressures present from a tight labour market. GSAM believe normalization of inflation expectations will encourage normalization of US Federal Reserve (Fed) policy and lead to a steeper yield curve.

Agency mortgage-backed securities (MBS) underperformed duration neutral Treasuries by 47bps in November, owing to an increase in volatility following the US election outcome. The Fund has moved to an underweight position in agency MBS. While GSAM's view was neutral to slightly positive on the sector leading up to the US presidential election, they believe the change in view is prudent given current valuations and current hedge-adjusted carry on these securities. GSAM's view is current market levels—particularly for lower coupons—do not adequately compensate investors for the post-election 50bps selloff in the 10-year US Treasury market and increase in interest rate volatility. Within the sector, and predominantly in Ginnie Mae securities, the Fund is underweight lower coupon securities—where GSAM expect the quality of the outstanding float to continue to deteriorate—and overweight the 4% coupon. GSAM believe senior collateralized loan obligations (CLOs) and Federal Family Education Loan Program (FFELP) asset-backed securities (ABS) offer attractive spread with strong credit protection and remain among the most compelling sectors in securitized products. GSAM are also positive on residential mortgage credit, particularly legacy non-agency MBS, which continue to benefit from negative net supply and show improving collateral performance.

A rise in global sovereign yields put pressure on risk assets, including **investment grade corporates**, over the month of November. The Fund is positioned flat in investment grade credit with a bias to move to a modest overweight. Improved corporate fundamentals and positive seasonals have led GSAM to become modestly positive on the asset class. The corporate bond market may benefit from the potential for stronger growth, tax cuts and looser regulations associated with a Trump presidency. This may offset the negative headwinds of reduced global trade and tighter monetary policy. However, late-stage credit cycle characteristics and remaining uncertainty over the path of near-term US monetary policy leave GSAM cautious on the sector. In terms of the portfolio's positioning; GSAM maintain a down-in-quality bias and a preference for the intermediate part of the corporate term structure. The Fund is overweight European and Sterling corporates, mainly as these regions continue to see support from central banks' corporate buying programmes. GSAM see value in the consumer, electrics and tobacco industries, whilst underweight the media and automotive issuers.

Compliance

The Fund complied with its investment mandate during the month.