

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	0.69%	0.65%	0.04%
3 months	1.38%	1.47%	-0.08%
6 months	2.71%	2.60%	0.11%
1 year	3.82%	3.12%	0.70%
2 years (pa)	5.46%	4.95%	0.51%
3 years (pa)	6.08%	6.16%	-0.08%
5 years (pa)	6.10%	5.98%	0.12%
10 years (pa)	7.47%	7.53%	-0.06%

Fund size

NZ\$236 million

Asset allocation

Credit quality rating	
AAA	37.7
AA+, AA, AA-	12.4
A+, A, A-	30.3
BBB	19.4
BB	0.2

Sector	Fund	Index
Governments	37.6	51.0
Agency	7.5	9.1
Credit	18.8	21.1
Collateralised & MBS	32.8	12.5
Emerging market debt	2.5	6.3
Cash, derivatives, other	0.8	0.0

Duration and yield

Duration	Fund 6.77 years versus benchmark 6.78 years
Yield to Maturity	Fund 3.13% versus benchmark 2.85%

Fund commentary

The fund slightly outperformed its index over the month. 0.69% vs 0.65%. Country allocation added the most value over the month (0.06%). Duration strategy was a drag on performance (0.04%).

Market commentary (source: GSAM)

Yields in major **government bond** markets declined in May, due to fewer upside economic surprises and political uncertainties, most notably in the US. In Europe, economic activity remains firm but does not appear to be feeding through to higher inflation. In turn, German government bonds remain supported by expectations for a prolonged period of low policy rates. Yields on 10-year government bonds in France, Spain and Italy declined by 12bps, 11bps and 10bps, respectively, to 0.72%, 1.52% and 2.17%, respectively.

The fund is underweight US rates, while neutral European and Japanese rates. GSAM expect the US Federal Reserve (Fed) to raise rates at its June meeting and see increased likelihood of a change in balance sheet policy occurring in the final quarter of this year. Recent US activity and inflation data has moderated, but on the whole, it remains at healthy levels.

Weak inflation data in the first quarter of this year is largely a reflection of idiosyncratic factors that GSAM do not expect to persist. In Europe and Japan, where core inflation remains subdued largely due to low wage growth, GSAM expect policy rates remaining low for the foreseeable future.

GSAM's highest-conviction relative value position in rates is overweight Europe versus other developed markets. GSAM see core inflation remaining below both consensus and European Central Bank (ECB) forecasts, even after the recent relatively substantial downward revision to the ECB's inflation forecast over the medium term. Elsewhere, the fund overweight rates in Sweden versus the UK, and overweight Canadian rates versus the US.

Agency MBS outperformed duration-neutral US Treasuries by 14 bps in May. The sector continues to be supported by low interest rate volatility and firm demand for risk assets. However, the medium- to long-term outlook for agency MBS valuations remains sensitive to discussion around a tapering in the Fed's balance sheet. The May FOMC minutes stated that most policymakers expect to announce a change in the Fed's reinvestment policy later this year. Primary market activity in asset-backed-securities (ABS) has already surpassed last year's total by 36%, with \$105bn of issuance year-to-date. Activity in 2016 was dominated by auto ABS, which accounted for almost half of issuance, while this year's issuance is largely due to credit card ABS.

The fund is underweight agency MBS. GSAM expect spreads to trend wider amid a pick-up in interest rate volatility, the impending Fed tapering of agency MBS reinvestments and increased supply into the summer home buying season. Within the sector, and predominantly in Ginnie Mae securities, the fund is underweight lower coupon securities and overweight higher coupons. GSAM expect the Fed to announce a change in its reinvestment policy in September, and in line with the recent FOMC statement, GSAM expect tapering to be capped at levels that would limit the size of a reduction in the Fed's balance sheet in any given month. GSAM believe Federal Family Education Loan Program (FFELP) ABS offer attractive spread with strong credit protection and remain among the most compelling sectors in securitized products. GSAM are also positive on collateralized loan obligations (CLOs) and residential mortgage credit, particularly legacy non-agency MBS which benefits from negative net supply and improving collateral performance.

Compliance

The Fund complied with its investment mandate during the month.