Factsheet 31 January 2021

NIKKO AM NZ BOND STRATEGY

Assets are held in the Nikko AM Wholesale NZ Bond Fund. The Nikko AM NZ Bond Fund (retail) invest in units in the wholesale fund, which the commentary refers to.

Market Overview

- The NZ yield curve steepened over the month as interest rates moved higher.
- Credit margins continue to be well supported due to demand / supply dynamics.
- Bond markets have had some larger moves while liquidity has been limited.

Fund Highlights

- Fund returns were negative over the month as interest rates moved higher in yield. The fund performed reasonbly well in comparison to benchmark despite rising rates.
- NZ credit holdings continued to perform well.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale[1]	-0.35%	-2.27%	5.17%	6.25%	5.59%	6.40%
Benchmark[2]	-0.41%	-2.52%	2.80%	4.78%	4.20%	4.99%
Retail[3]	-0.42%	-2.45%	4.41%	5.47%	4.81%	

1. Returns are before tax and before the deduction of fees.
2. Current benchmark: Bloomberg NZBond Composite 0+ Yr Index. No tax or fees.
3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

Portfolio Manager

Fergus McDonald,

Head of Bonds and Currency

Fergus is responsible for the investment of the Bond, Cash and Currency mandates. Fergus has been actively involved in the NZ financial markets since 1981. The portfolio management team for the domestic fixed income funds includes Ian Bellew, Fixed Income Manager and Matthew Johnson, Fixed Income Manager.

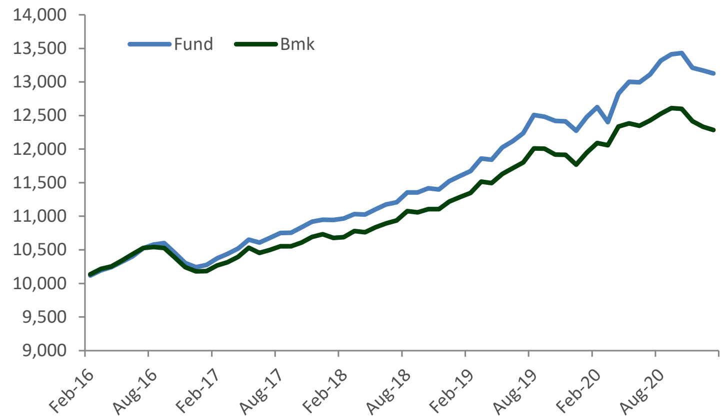
Overview

The fund aims to provide investors with regular income by constructing an actively managed investment portfolio of New Zealand bonds, deposits and cash with the potential for capital gain from New Zealand dollar fixed interest markets.

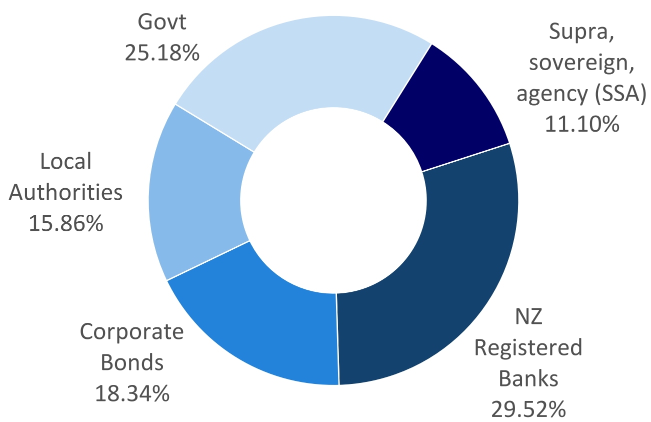
Objective

The fund aims to outperform the benchmark return by 0.60% per annum before fees, expenses and taxes over a rolling three year period.

Five Year Cumulative Performance, $10,000 invested[1&2]



Asset Allocation



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Nikko Asset Management

Top 5 Corporate Issuers*	(%)
NZ Local Govt. Funding Agency	10.84
Kommunalbanken	8.06
Kiwibank	5.22
Westpac Bank	5.11
Housing New Zealand	5.09

*excludes central government

Credit Quality	(%)
AAA	11.87
AA	59.84
A	24.21
BBB	2.65
BB	1.43

Duration
Fund 5.87 years vs Benchmark 5.27 years

Yield
Fund (gross) 0.96% vs Benchmark 0.75%

Market Commentary

The returns from NZ bonds were negative for January as interest rates continued to move higher and further steepened the upward slope of the yield curve. NZ longer maturity bonds have continued to perform poorly as positive economic sentiment, and thin market liquidity has exacerbated the moves higher in yield.

The best performers were credit holdings and in general, shorter maturity bonds which were less impacted by rising yields. NZ government bonds and in particular swaps have suffered with swap spreads having larger moves higher in yield, as sell flows have dominated with little buying interest.

NZ bonds now look a lot cheaper on both an absolute basis and relative to offshore markets, so far there has been little respite in the sell-off higher in yield. At month end the 3-year government bond finished 1 basis points lower, the 10-year finished 13 basis points higher in yield, and the 2041 bond was 15 basis points higher in yield. Funds with longer duration positioning than benchmark had a larger negative contribution from duration, but on the positive side investing in longer maturity bonds with a steep yield curve helps build a higher portfolio yield relative to benchmark. This should help add value over time, and with yields now higher the prospects for future returns from bonds look better.

We believe the best strategy is to focus on positioning the funds to outperform over the medium to long term. The fund's relative duration position has shortened and is moderately longer than benchmark. Positioning the fund with a higher yield than benchmark and buying quality credit should continue to support returns.

Looking forward, the NZ cash rate and shorter maturity bonds are likely to remain at low levels for some time, however longer-term rates are more difficult to predict. The current market consensus is that yield curves will likely continue to steepen as the world recovers from the negative impacts of the virus as vaccines get distributed, and the large amounts of stimulus support economic recovery. In counterbalance to expectations for higher interest rates, we have already had a reasonable move higher and steeper in NZ yield curves, and market positioning is vulnerable to some disappointment if the recovery is delayed.

Fund Commentary

The fund marginally outperformed the Bloomberg NZ Bond Composite benchmark over the month. The main driver of negative returns was the rise in interest rates and the fund's longer duration positioning. Credit holdings and inflation linked bonds did continue to perform well in comparison to swaps and government bonds.

Key Fund Facts

Distributions

Wholesale fund: Calendar quarter
Retail fund: Calendar quarter

Estimated annual fund charges (incl. GST)

Wholesale: Negotiated outside of unit price
Retail: 0.70%, refer PDS for more detail

Hedging

All investments will be in New Zealand dollars

Buy / Sell spread

Click to view

Strategy size

$399.4m

Strategy Launch

October 2007

Compliance

The wholesale fund complied with its investment mandate and trust deed during the month.

Contact Us

www.nikkoam.co.nz | nzenquiries@nikkoam.com