Factsheet 31 January 2021

NIKKO AM NZ CASH STRATEGY

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

Market Overview

- The New Zealand economy continues to perform well in response to the stimulus packages adopted over the past year.
- Unemployment numbers dropped and the inflation rate increased closer to the Reserve Bank's targets.
- The 90-day Bank bill rates edged up a couple of points from 0.27% to 0.29%, however credit spreads remain at record lows.

Fund Highlights

- The fund holds a portfolio of high quality credits which are expected to perform well in an environment of low and stable short term interest rates.
- With a longer than benchmark duration position the fund's yield to maturity is enhanced over its benchmark benefiting from slope in the credit curve.
- Returns are likely to moderate over the coming months as proceeds from maturities are reinvested at current prevailing market interest rates.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale[1]	0.08%	0.24%	1.53%	2.32%	2.64%	3.35%
Benchmark[2]	0.02%	0.07%	0.52%	1.34%	1.68%	2.34%
Retail[3]	0.04%	0.16%	1.22%	1.95%	2.29%	
KiwiSaver[3]	0.03%	0.13%	1.07%			

1. Returns are before tax and before the deduction of fees.
2. Benchmark: Bloomberg NZBond Bank Bill 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.

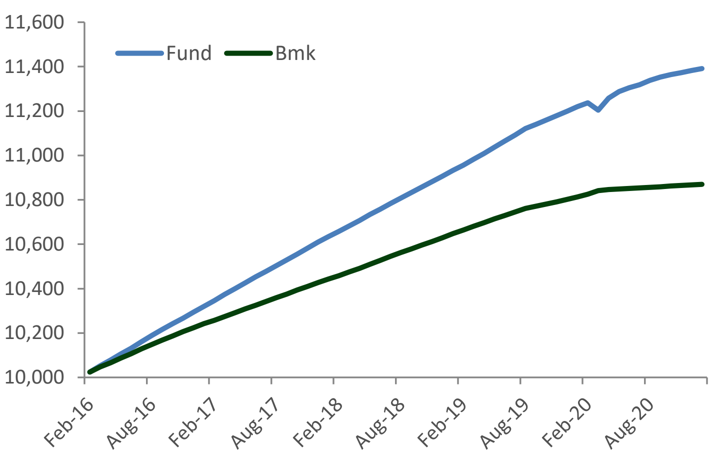
Overview

The strategy aims to generate income by constructing an actively managed investment portfolio of short-term deposits and bonds whilst preserving capital value.

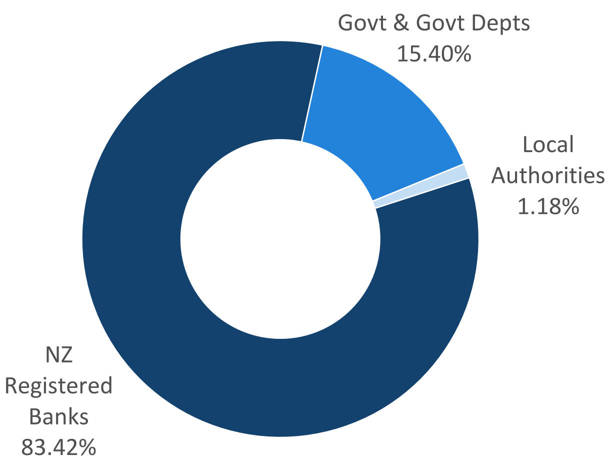
Objective

The fund aims to outperform the benchmark return by 0.20% per annum before fees, expenses and taxes over a rolling three year period.

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



Asset Allocation



Top 5 Issuers	(%)
Westpac	16.67%
ANZ Bank	13.99%
Rabobank	13.39%
ASB Bank Limited	9.63%
NZ Tax Trading	9.30%

Credit Quality	(%)
AAA	-
AA	56.87
A	43.13

Duration
Fund 100 days vs Benchmark 45 days

Yield
Fund (gross) 0.92% vs Benchmark 0.27%

Market Commentary

New Zealand's strong economic recovery from the COVID inspired recession has seen investors attention swing from the possibility of a negative official cash rate to how and when the Reserve Bank might start to unwind its monetary policy stimulus.

The market now no longer expects the RBNZ to cut the cash rate again with the majority of forecasters expecting the cash rate to remain at 0.25% over 2021. New Zealand's V shaped recovery has seen GDP return to pre-COVID levels already, December quarter CPI inflation numbers came in higher at 0.5% compared to expectations of 0.2% and in early February a report on the labour market revealed unemployment dropped from 5.3% to 4.9%. With inflation higher and unemployment lower than the Reserve Bank was expecting, the bank finds itself much closer to achieving its monetary policy objectives than it thought it would be at this point in the economic cycle. That said we believe it is much to soon to be contemplating the RBNZ hiking rates. One area that continues to vex central bankers and politicians alike is house price increases. Macroprudential tools such as the re-introduction of LVRs are likely to be the policy of choice in this area rather than the blunt tool of interest rates so we do not believe strong house price growth will engender an interest rate response until LVRs are well entrenched. Another factor keeping bank deposit rates low is the Reserve Bank's Funding for Lending Programme (FLP) which became available for drawdowns on December 7 with $1.04 billion drawn over the month with the interest rate linked to the OCR. To put this drawdown rate and size into context, drawdowns can be made any time in the next two years as required and the total size of the FLP program is estimated to be between $20b and $30b. The FLP will be amongst the cheapest funding sources for banks with the only cheaper funding source coming from call accounts generally paying a rate of 0%. These funding dynamics should see interest rates for all other funding sources come under pressure until the FLP is near fully drawn. Despite the presence of the FLP, 90-day bank bill rates edged up a couple of points to 0.29% at month end. With interest rates so low this movement up in bank bill rates will provide a negative drag on returns of securities priced over bank bills such as commercial paper and registered deposits, however we can see little reason for these increased rates to persist. There is logically little reason for bank balance sheets to pay up for bank bill funding when they can draw on the FLP at the OCR rate of 0.25%.

Given these various events, we expect short interest rates will continued to be anchored around their current levels. The possibility of the RBNZ cutting the OCR remains, however, the odds of this occurring has significantly reduced considering improving domestic economic data, sizeable monetary and fiscal support already in place and the roll out of a COVID vaccine globally. From here, it is likely any cuts to interest rates would need to be preceded by another March style lockdown.

Fund Commentary

The fund performed well in January returning 0.08% outperforming the 90 day bank bill index which returned 0.02%. The fund holds a longer than benchmark duration position which provides a yield enhancement over the index with benefits accruing primarily from the slope of the credit curve. Recent data shows the NZ economy has been more resilient than expected and has recovered from the impact of the COVID lockdown earlier in 2020. This strong performance, if maintained, could lead to rising interest rates for longer tenors however the RBNZ is operating very accommodative monetary policy - the OCR is at a record low of 0.25%, a quantitative easing program is in place and now the Funding for Lending Program is available for drawdown. These initiatives are likely to see short rates anchored around current levels over the next year. In this environment we expect short term interest rates will be stable and the fund's long duration position to perform well.

Key Fund Facts

Distributions

Wholesale fund:	Calendar quarter
Retail fund:	Calendar quarter
KiwiSaver fund:	Does not distribute

Hedging

All investments will be in New Zealand dollars

Estimated annual fund charges (incl. GST)

Wholesale:	Negotiated outside of unit price
Retail:	0.32%, refer PDS for more details
KiwiSaver:	0.45%, refer PDS for more details

Buy / Sell spread	Strategy size	Strategy Launch
0.00% / 0.00	$846.4m	October 2007

Compliance

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

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