

Factsheet 30 April 2022

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 Reserve Bank increased the OCR by 50bps to 1.5% stating it was appropriate to continue to “tighten monetary conditions at pace”.
- Future guidance was light, however the RBNZ noted larger rise in the OCR now is consistent with the forward path for interest rates outlined in their February Statement.
- First quarter CPI came in at 1.8%, taking annual inflation to 6.9%. This is a miss on market expectations of 7.1%, but nonetheless a 32-year high.

Fund Highlights

- The fund is using a barbell strategy to benefit from higher future expected rates today while short positions are concentrated around upcoming Reserve Bank OCR review dates to reduce risk.
- Duration is actively managed with fund positions reflecting the likely path of the OCR over the coming months along with what is priced into security yields.
- The fund holds a range of securities including floating rate notes which provide some protection against a rising cash rate.

Performance

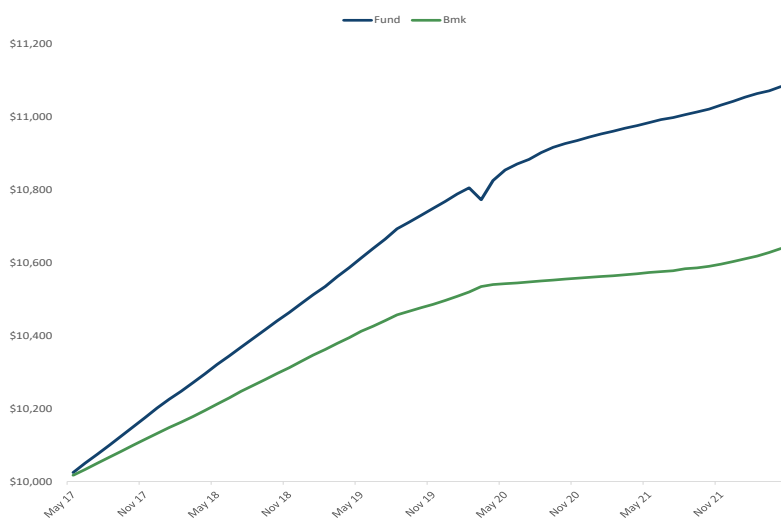
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale ¹	0.10%	0.26%	0.98%	1.54%	2.08%	2.97%
Benchmark ²	0.10%	0.27%	0.65%	0.78%	1.25%	2.06%
Retail ³	0.07%	0.19%	0.68%	1.22%	1.74%	
KiwiSaver ³	0.06%	0.16%	0.55%	1.16%		

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).

Five Year Cumulative Performance, \$10,000 invested^{1, 2}



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.

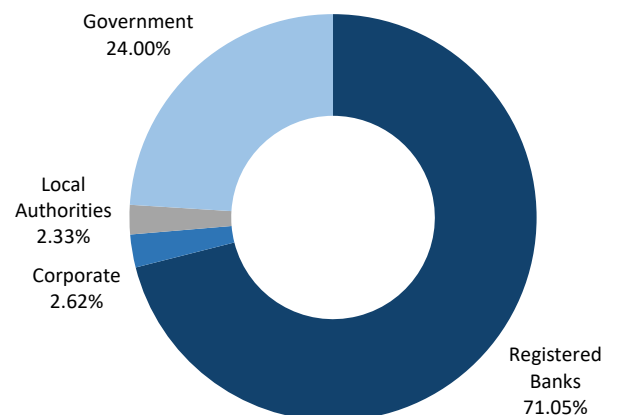
Overview

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.

Asset Allocation



Top 5 Issuers	(%)	Credit Quality	(%)	Duration
Tax Management NZ Ltd	11.97	AAA	24.0	Fund 90 days vs Benchmark 45 days
NZ Tax Trading Co	11.59	AA	39.5	
Westpac New Zealand Ltd	10.44	A	36.5	
Bank of New Zealand	9.59			Yield to Maturity
ANZ Bank New Zealand	8.24			Fund (gross) 2.48% vs Benchmark 1.73%

Market Commentary

From a markets standpoint the one certainty of April was the OCR needed to increase, however views were split on how much. The RBNZ hiked by 50bps stating a “stitch in time” approach of increasing the OCR by more now, rather than later, would have the best chance of heading off rising inflation expectations. The RBNZ also noted that this larger OCR move was “consistent with the forward path for interest rates outlined in their February Statement”, implicitly hinting that doing more now may lessen the need to continue to hike beyond levels previously forecast in February.

Markets were initially unruffled by the RBNZ decision to implement a larger OCR increase having gone into the meeting day pricing some 0.43% of OCR increases, seeing the Reserve Bank’s move as entirely reasonable given current inflation and employment conditions. However, as the month progressed the trend of increasing interest rates resumed with markets rapidly moving to price another 50bps OCR increase for May whilst at the same time somewhat disregarding the “stitch in time” analogy in respect to the terminal OCR level for this hiking cycle. Looking to terminal OCR pricing, we note that an OCR near 4% is now priced by February of 2023. This pace and level of OCR increase may be somewhat muddled by market flows. The swap market particularly for terms of 1 and 2 years continues to see strong pay side interest from banks on the back of high levels of mortgage fixing whilst at the same time the level of fixed receivers continues to be limited. The lack of receivers is multi-faceted, we see a couple of key drivers, firstly, receivers continue to be concerned at the level of hawkishness from the Reserve Bank and secondly international investors are likely focusing on global geopolitical tensions and larger portions of their portfolio rather than the nuances of the economy and central bank of a small south pacific nation. It is hard to see this situation reversing until these factors abate, this leads us to believe 1-year swap pricing will continue to decouple from actual market expectations of the OCR over the coming months. This may present investment opportunities with the next key reference point the Reserve Bank’s May monetary policy statement where we expected to see an updated OCR path and forward guidance released.

Fund Commentary

The fund marginally outperformed in April returning 0.104% versus its 90 day bank bill index which returned 0.102%. The fund has been implementing a barbell investment strategy, with short positions concentrated around the upcoming Reserve bank meeting dates complemented with some longer positions to take advantage of higher rates offered for tenor. Performance of our barbell has been well balanced performing roughly in line with the benchmark. On one hand longer positions have detracted performance with 1 year swap increasing some 110bps over the past two months, the fastest bimonthly rate of increase since the bond rout of 1994. Whilst conversely, the short leg of our barbell has performed strongly with 1 month and 2-month bank bill rates increasing an impressive 55bps and 60bps respectively over the same time. Complementary to our short leg we decreased our overall duration position in April by some 20 days as it became apparent a 50bps increase was a real possibility. Overall we remain comfortable with our barbell strategy continue to see potential for outperformance over time. We gain comfort in this strategy from the level of slope available in the term and credit curves out to 1 year and the level of terminal OCR priced with markets pricing near 4% by February 2023 a level above neutral (low to mid 2s) and where we see peak (low 3s). Finally, we also note that 1 year swap rates are likely decoupled from actual OCR expectations which may present opportunities over the coming months.

Key Fund Facts

Distributions		Estimated annual fund charges (incl. GST)		
Wholesale fund:	Calendar quarter	Wholesale:	Negotiated outside of unit price	
Retail fund:	Calendar quarter	Retail:	0.30%, refer PDS for more details	
KiwiSaver fund:	Does not distribute	KiwiSaver:	0.45%, refer PDS for more details	
Hedging		Buy / Sell spread	Strategy size	Strategy Launch
All investments will be in New Zealand dollars		0.00% / 0.00	\$905m	October 2007
Restrictions				
Adult entertainment, gambling, fossil fuels, alcohol stocks, tobacco stocks. For more information please refer to the Statement of Investment Policy and Objectives (SIPO) which can be found on our website https://www.nikkoam.co.nz/invest/retail .				
Exclusions				
Securities that conduct activities listed on the Schedule to Cluster Munitions Prohibition Act 2009.				

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

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