

# 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

- As widely expected, the Reserve Bank (RBNZ) delivered a 50bps hike taking the OCR to 3.0%.
- Rhetoric and statements from the RBNZ remain hawkish with the RBNZ clearly emphasizing it is “resolute” and determined to bring down inflation.
- Retail sales unexpectedly fell 2.3% in Q2 much weaker than the markets expectation of a 1.7% rise potentially suggesting the RBNZ is beginning to get some traction in slowing demand.

## Fund Highlights

- The fund holds a longer than benchmark duration position reflecting a view that cash rates will peak towards the end of 2022 or early 2023.
- Duration is actively managed with fund positions reflecting the likely path of the OCR over the coming months along with what is already 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

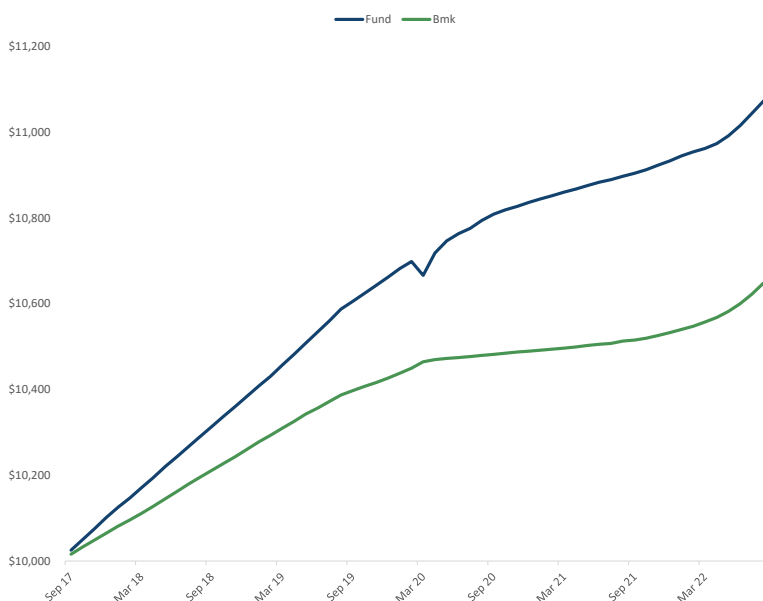
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale <sup>1</sup>	0.26%	0.74%	1.61%	1.50%	2.06%	2.92%
Benchmark <sup>2</sup>	0.24%	0.63%	1.29%	0.83%	1.27%	2.04%
Retail <sup>3</sup>	0.25%	0.66%	1.32%	1.19%	1.72%	
KiwiSaver <sup>3</sup>	0.23%	0.63%	1.19%	1.07%		

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).

## Five Year Cumulative Performance, \$10,000 invested<sup>1, 2</sup>



## 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.



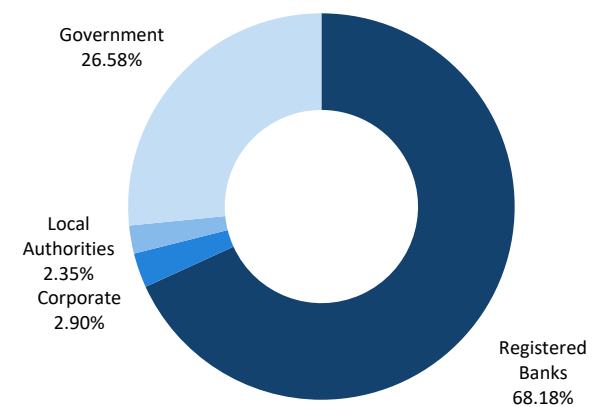
## Overview

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
NZ Tax Trading Co	13.92	AAA	30.0	Fund 97 days vs Benchmark 45 days
Tax Management NZ Limited	12.65	AA	29.7	
Cooperatieve Rabo U.A.	10.44	A	40.4	<b>Yield to Maturity</b>
ANZ Bank New Zealand	8.68			Fund (gross) 3.86% vs Benchmark 3.21%
Bank of New Zealand	8.11			

### Market Commentary

As widely expected in its August Monetary Policy Statement (MPS) the Reserve Bank delivered a fourth consecutive 50bps hike taking the OCR to 3%. The RBNZ’s statement and rhetoric remain strongly hawkish, with the RBNZ comfortable in continuing to tighten “at pace” and remaining “resolute” in its commitment to bring inflation back towards 1-3%. The RBNZ’s statement also included several other items of note – a revised OCR track more front-loaded with a marginally higher peak; comments suggesting the neutral level of interest rates might be higher than expected and a reference to the challenge increased government spending may bring. With the hike widely expected our focus and that of the markets were around clues as to the RBNZ’s next move and where it sees peak OCR. Here, key in the quantitative realm was the updated OCR track. The track was moved marginally upward and further front-loaded from its May MPS state. Peak is now seen at 4.1% vs 3.9% - this move representing an increased predisposition to hike rather than a meaningfully higher peak OCR, keeping in mind that historically the RBNZ moves the OCR in multiples of 25bps. In our view this track combined with the statement and comments made at the post MPS press conference where Governor Orr repeated a reference to 4% now strongly suggest we will see two further 50bp hikes by year end. This set of potential hikes are consistent with the RBNZ’s desire to tighten “at pace” especially when one considers the longer than usual gap between OCR review meetings that occurs over year end (~13 weeks vs the more typical ~7weeks). By getting to where it arguably sees peak OCR by November the RBNZ effectively buys itself more time to review the impact of its actions on inflation and the economy before having to make further decisions.

In its quest to tame inflation one of the areas the RBNZ has been at pains to point out is it needs to reduce demand. Governor Orr has made comments to this extent on multiple occasions, most recently of note at the Jackson Hole conference (an annual gathering of central bankers from around the world). Here Orr pointed out that the RBNZ “needs very low consumption” and in reference to Q2s weak retail sales (down 2.3%) stated this “not a surprise” but rather is a “good signal that monetary policy is biting”, we tend to agree and expect the impact of monetary policy to continue to grow in this area over the coming months. In this same interview Orr also stated he expects there will be at “least another couple of rate hikes” but then the RBNZ will be in a position where it can be “data driven”. Further affirming this Orr stated the RBNZ is “watching for signs” where it “can be confident” it is “slowing the economy”, and this is being reflected in “inflation expectations”. In this regard Orr stated “We’re seeing the beginning of that quite strongly” and that he feels “confident” the RBNZ is “on top of it.” All this supports our belief we are nearing the end of the hiking cycle.

### Fund Commentary

The fund performed well in August returning 0.26% outperforming its benchmark the 90-day Bank Bill Index which returned 0.24%. Over August 90-day bank bills increased 0.325% to end at 3.465% whilst 1-year swap rates increased a more substantial 0.47% to end at 4.20%. The increase in 90-day bank bills is largely as one would expect given a continuation of 50bps hikes at each RBNZ meeting, whilst 1-year rates reflect a reasonable view on where terminal OCR levels might reach. It now looks increasingly probable that we are entering the tail end of this hiking cycle with the RBNZ suggesting it sees a peak OCR around ~4% potentially as soon as November. Further to this there are tentative signs that the impact of monetary policy is beginning to have a meaningful impact in the real economy with Q2 retail sales falling 2.3% (vs market expectations of a 1.7% rise). From here on the RBNZ will be watching for signs that reinforce its view that monetary policy is having a meaningful impact on economic activity and inflation expectations. With the focus increasingly moving to the timing of the end of the hiking cycle vis-à-vis the size of the next hike running a longer duration position will become increasingly logical. We are continuing to look for opportunities to maintain or lengthen our longer than benchmark duration position where pricing sufficiently compensates for a peak OCR level in the low 4%.

### Key Fund Facts

<b>Distributions</b>		<b>Estimated annual fund charges (incl. GST)</b>	
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
<b>Hedging</b>		<b>Buy / Sell spread</b>	<b>Strategy size</b>
All investments will be in New Zealand dollars		0.00% / 0.00	\$858m
<b>Strategy Launch</b>			
October 2007			
<b>Restrictions:</b> 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 <a href="https://www.nikkoam.co.nz/invest/retail">https://www.nikkoam.co.nz/invest/retail</a> .			
<b>Exclusions:</b> 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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