

Factsheet 31 January 2023

NIKKO AM INCOME STRATEGY

Applies to: Nikko AM Income Fund (retail).

Market Overview

- Equity markets continued to see high levels of volatility in individual company performances from month to month. In general companies and industries that are sensitive to rising interest rates have performed poorly over the past year however as the trend towards higher rates is fading these sectors may perform better as the year progresses. The property sector falls into this grouping and continues to be under pressure from rising interest rates and downward property valuations.

Fund Highlights

- The Fund benefited from strong bond and equity markets over January and delivered a positive start to the new year.

Distributions

- The defined distribution rate (which is used to calculate the distribution you receive from the fund) is set at the start of each calendar year, based on the price of the fund at that point. The defined distribution rate for 2023 is 5.5%. This income will be distributed in four equal amounts each calendar quarter, based on the price at 1 January 2023.

Performance

	One month	Three months	One year	Three years (pa)	Five years (pa)	Ten years (pa)
Retail ¹	1.82%	1.89%	-3.55%	-0.29%	0.91%	3.32%
Benchmark ²	0.60%	1.73%	5.53%	4.56%	5.00%	6.34%
Market Index ³	2.56%	3.37%	-0.44%			

1. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

2. Current benchmark: RBNZ Official Cash Rate +3.00% p.a.

3. Current appropriate market index: 62.5% Bloomberg NZBond Credit 0+ Yr Index, 30% S&P/NZX 50 Gross Index, 7.5% Alternatives exempt.

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

Change of investment strategy 01/07/2020



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.

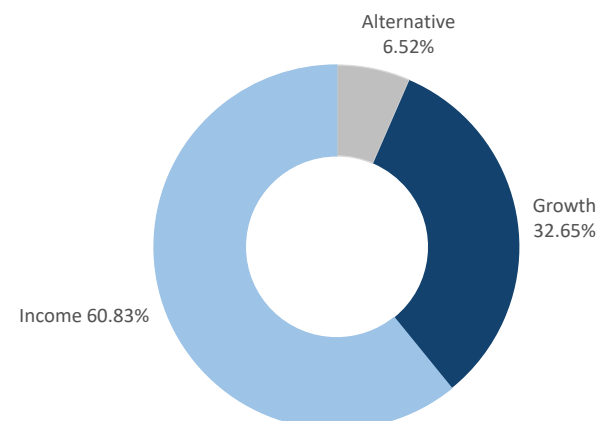
Overview

The strategy aims to provide investors with regular income from an actively managed investment portfolio. The fund invests in NZ fixed interest, Australasian equities and property. Equities with a good dividend stream and a focus on growing value over time are selected as an attractive alternative to fixed income securities. Equity selection is determined by the NZ investment team.

Objective

The objective of this fund is to outperform the RBNZ Official Cash Rate by 3.00% p.a. over a rolling three-year period before fees, expenses and taxes. Prior to June 2020, the objective and strategic asset allocation of fund were materially different. From 1 July 2020 these were amended to include equities.

Asset Allocation



Top 5 Fixed Income Issuers*	(%)	Duration*	Top 10 Equities	(%)	(%)
Westpac New Zealand Ltd	7.67%	Fund 3.57 years	Heartland Group	3.30%	Chorus Limited 2.24%
ASB Bank Ltd	4.35%	Yield to Maturity	Skellerup Holdings Limited	3.07%	Works Finance Nz Ltd 2.22%
Kiwibank Ltd	3.53%	Fund (gross) 5.54%	Spark New Zealand Ltd	2.99%	Stride Stapled Grp Npv 2.17%
Contact Energy Ltd	3.50%		Infratil Limited	2.73%	EBOS Group Ltd 1.86%
Liberty Finance	3.20%		Contact Energy	2.49%	Meridian Energy Ltd 1.71%

*Includes cash holdings.

Fund Commentary

The Fund benefited from strong bond and equity markets over January and delivered a positive start to the new year.

The S&P/NZX 50 Gross Index advanced 4.3% over the month and the bond sector gained 1.7% as measured by the Bloomberg Corporate Bond Index. Interest rates fell globally as investors started to anticipate central banks slowing the pace of cash rate rises, expectations of the peak in cash rates also reduced. How long cash rates will stay high before the tightening cycle starts to be partially reversed is the next question to be answered.

Equity markets continued to see high levels of volatility in individual company performances from month to month. In general companies and industries that are sensitive to rising interest rates have performed poorly over the past year however as the trend towards higher rates is fading these sectors may perform better as the year progresses. The property sector falls into this grouping and continues to be under pressure from rising interest rates and downward property revaluations. The fund owns 14 companies in its equity portfolio, over the month nine increased in price and five declined. Looking at the performance of some individual equity names in the fund Genesis, Mercury Energy and Scales were standouts, after a strong run EBOS Group fell over the past month as did Spark, Stride Property and Argosy. NZ bond yields have likely peaked after retreating from the highs seen late last year. The fund’s duration has varied around benchmark to modestly long which resulted in a good outcome over the past month.

Business and consumer confidence surveys remain weak and economic data has shown signs of softening, but there is still reasonable uncertainty in terms of how “sticky” inflation will be and how tight monetary conditions will impact the economy. This will determine how long rates need to stay at restrictive levels. The steeply inverted yield curve complicates the decision on yield curve positioning as there is no term interest rate premium to compensate the fund going longer in duration. NZ bonds can generate reasonable returns over the year ahead as there is plenty of yield available through purchasing three-to-five-year bonds rather than going longer on an inverted yield curve. An inverted yield curve indicates bond investors expect recessionary economic conditions to emerge and cash rates to fall. Should this occur mid-term bonds could provide strong returns over the coming year. The Option Fund was up strongly over the month. Bond yields moved through a small number of option strike levels however the strong levels of income ensured the return over January was satisfactory.

We continue to believe investors should seek income from a diverse range of sources. Bond rates are looking attractive and even though most equity prices have fallen over the past year we believe the environment remains acceptable for equities although we concede catalysts for new growth remain elusive and an economic slowdown looks inevitable. The Income Fund remains invested in a range of NZ companies listed on the NZX that pay a consistent level of dividends or who have the likelihood of doing so in the future. In addition to the fund receiving a steady stream of dividend income, we expect that over time the industry sectors and business models adopted by these companies should be rewarded by a steady or rising share price.

Key Fund Facts

Distributions	Estimated annual fund charges (incl. GST)
Distributions for this fund are defined annually and are effective for the calendar year. The defined rate is gross of tax. Distributions are not a taxable event. Tax will be deducted (refunded) at 31 March and on full or partial withdrawals.	0.80%, refer PDS for more details
Hedging	Buy / Sell
All investments will be in New Zealand dollars	spread: \$4.7m
	Click to view
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 .	Strategy size
Exclusions: Securities that conduct activities listed on the Schedule to Cluster Munitions Prohibition Act 2009. Tobacco manufacturers.	Strategy Launch
	October 2007

Compliance

The fund complied with its investment mandate and trust deed during the quarter, except that an error has been identified in the Option Fund where the value of specific options were incorrectly accounted for in the net asset value of the fund on certain days. We are working through the details and will advise the affected clients when the impact analysis is complete later in January.

Contact Us

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