

Nikko AM Income Strategy

Monthly Update 31 January 2024

Applies to the Nikko AM Income Fund.

Market Overview

- The S&P/NZX 50 Gross (with imputation credits) Index returned 0.87% over January.
- The bond sector as measured by the Bloomberg NZ Bond Composite Index fell 0.60% as longer-term rates increased after a strong period of performance.

Fund Highlights

- The Income Fund fell slightly over the first month of the new year. After strong equity and bond market performance over November and December perhaps a period of calm to reflect upon the outlook for markets was to be expected.
- The fund's equity portfolio did not perform as well as the Index as it does not have exposure to strong performers such as A2 Milk which advanced close to 12% over the month.
- Cash and short-term bonds were the best performing parts of the fixed income market as they held their value as the Official Cash Rate remained unchanged.

Distributions

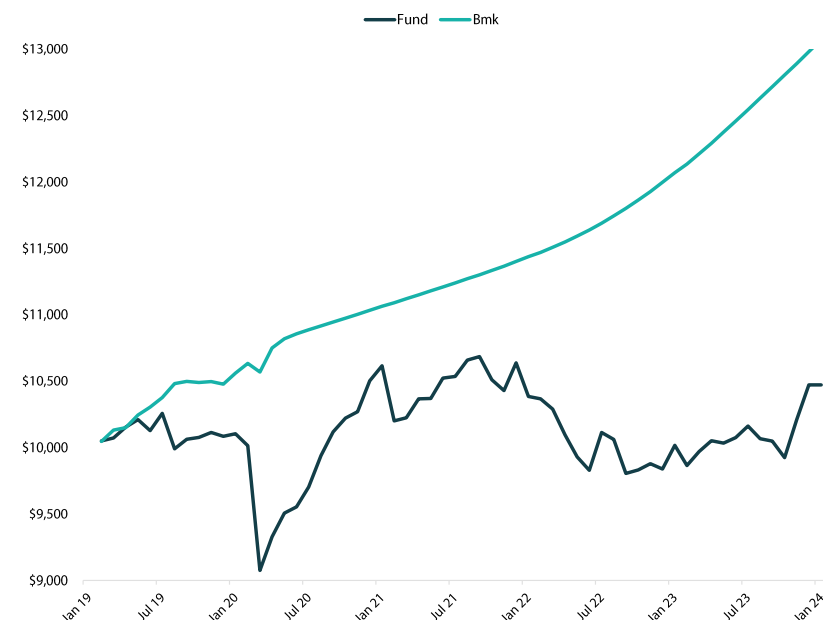
- The defined distribution rate (which is used to calculate the distribution you receive from the fund) is set at the start of each calendar year, based on the price of the fund at that point. The defined distribution rate for 2024 is 6.5%. This income will be distributed in four equal amounts each calendar quarter, based on the price on 1 January 2024.

Performance

	One month	Three months	One year	Three years (pa)	Five years (pa)	Ten years (pa)
Retail¹	-0.16%	5.34%	4.37%	-0.51%	0.89%	3.31%
Benchmark²	0.70%	2.08%	8.30%	5.72%	5.51%	6.17%
Market Index³	0.18%	6.29%	3.76%	-0.73%		

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%.

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, Senior Fixed Income Manager and Matthew Johnson, Fixed Income Manager.



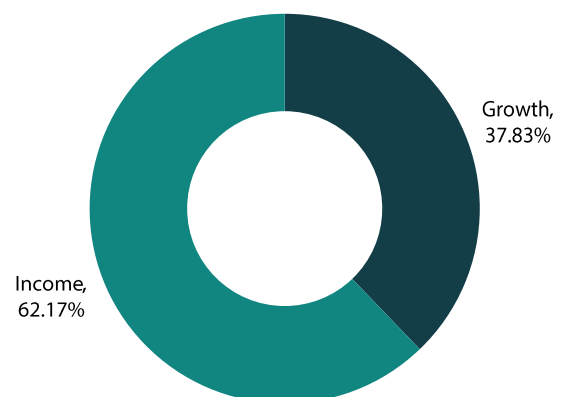
Overview

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 Income Issuers*	(%)	Duration	Top 10 Equities	(%)	(%)	
ANZ Bank New Zealand	10.43	Fund 3.35 years	Spark New Zealand	3.20	Contact Energy	2.91
Westpac New Zealand	7.89	Yield to Maturity	Bank Of New Zealand	3.19	Meridian Energy	2.68
Kiwibank	5.13	Fund (gross) 5.94%	Works Finance NZ	3.17	Skellerup	2.51
Powerco	4.89		Chorus	3.10	Heartland	2.38
TR Group	4.25		Infratil	3.06	Kiwibank	2.02

*Includes cash holdings.

Fund Commentary

The Income Fund fell slightly over the first month of the new year. After strong equity and bond market performance over November and December perhaps a period of calm to reflect upon the outlook for markets was to be expected. Top of mind is the topic of when Central Banks will feel comfortable enough to reduce cash rates in response to a lower inflation outlook and by how much. The interest rate outlook is likely to be important for the near-term performance of long-term bond rates and equities. A degree of anticipation of rate cuts seems to be already priced into markets. If rate cuts aren't delivered in the time frames expected by markets a period of disappointment and market weakness can be expected.

The S&P/NZX 50 Gross (with imputation credits) Index returned 0.87% over January. The fund's equity portfolio did not perform as well as the Index as it does not have exposure to strong performers such as A2 Milk which advanced close to 12% over the month. The bond sector as measured by the Bloomberg NZ Bond Composite Index fell 0.60% as longer-term rates increased after a strong period of performance.

Longer term interest rates continued to follow trends in international markets. NZ 10-year rates followed US Treasury yields higher as the US Federal Reserve seems to be in no rush to reduce rates. They noted in a recent statement that it does not expect it will be appropriate to reduce rates until it has gained greater confidence that inflation is moving sustainably toward 2%. The Fed is unlikely to reach that level of confidence by the time of their March meeting. Even though US inflation has fallen dramatically Governor Powell is of the opinion more data confirming the downward trend is required.

Cash and short-term bonds were the best performing parts of the fixed income market as they held their value as the Official Cash Rate remained unchanged. The best guess is that the RBNZ will hold the OCR until at least August before gradually cutting. The exact timing and extent of the cuts will depend upon inflation continuing to fall in a sustainable manner.

If markets get impatient with Central Bank inaction and interest rates move higher, we believe it will represent a buying opportunity as the general trend in rates is down however the timing of this occurring is uncertain.

The fund's equity portfolio performed well over the month with 9 of the 14 holdings increasing in value however there was a wide variation in performance of individual names. EBOS, Infratil, Argosy, Spark and Mercury all saw solid gains above 2% while Skellerup and Heartland trailed the field.

We continue to believe investors should seek income from a diverse range of sources. Looking ahead over the medium term a lower rate environment should be supportive for both bond and equity returns. 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 dividend income, we expect 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

Estimated annual fund charges (incl. GST)	0.80%, refer PDS for more details.	Hedging:	All investments will be in New Zealand dollars.	Strategy Launch:	October 2017
Exclusions:	Controversial weapons.	Distributions:	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.	Strategy size:	\$3.2m
Restrictions:	Adult entertainment, gambling, fossil fuels, alcohol stocks, tobacco stocks. For more information please refer to the Statement of Investment Policy and Objectives (SIPO) on our website https://www.nikkoam.co.nz/invest/retail .			Buy / Sell spread:	Click to view

Compliance

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

Contact Us

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