Factsheet 31 July 2021

NIKKO AM INCOME STRATEGY

Applies to: Nikko AM Income Fund (retail).

Market Overview

- New Zealand's economic activity has surpassed pre-COVID levels and therefore the COVID inspired cut in the Official Cash Rate from 1% to 0.25% over 2020 can expect to be taken back, perhaps rising to 1.5% in 2023 where rises should top out.
- Even though the NZ economy has recovered well and the outlook for a global economic recovery is looking promising, even with the rise in the COVID Delta variant, short-term rates will stay low compared to past tightening cycles.

Fund Highlights

- The Income Fund returned 0.12% over July. Returns from long term bonds were strong however short-term interest rates increased resulting in losses for short term bonds.
- Five of the thirteen equity holdings gained in value with the best performers being Argosy and Stride Property, both advancing around 4%, Infratil was the laggard falling 5%. Meridian remains the smallest exposure and Heartland the largest.
- The combined return from all sectors delivered a modest positive return illustrating the benefit of holding a diverse portfolio of assets.

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 2021 is 3.0% p.a. This income will be distributed in four equal amounts each calendar quarter, based on the price as at 1 January 2021.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Retail[1]	0.12%	1.62%	8.58%	2.26%	2.77%	4.58%
Benchmark[2]	0.27%	0.81%	3.25%	5.03%	4.28%	7.10%
Market Index[3]	-0.20%	-0.52%	2.15%			

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, 7.5% S&P/NZX 50 Gross Index, 7.5% Alternatives exempt.

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.

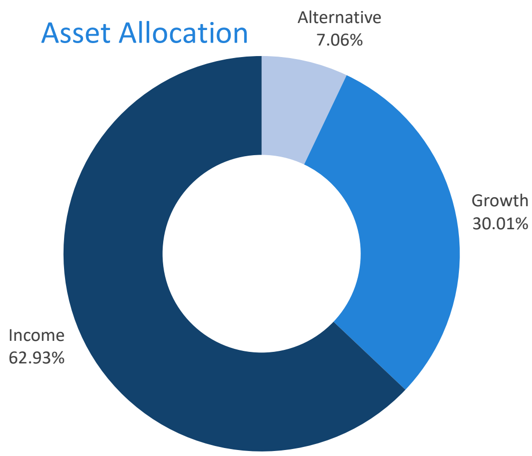
Objective

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 these were amended to include equities.

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

Change of investment strategy 01/07/2020

Asset Allocation



Top 5 Fixed Income Issuers*	(%)
NZ Local Govt Funding Agency	6.20
Westpac New Zealand Ltd	6.09
Bank of New Zealand	5.84
Infratil Ltd	5.13
Kiwibank Ltd	4.45

Duration*
Fund 4.70 years
Yield to Maturity
Fund (gross) 2.11%

Top 10 Equities	(%)		(%)
Heartland Group	3.13	Works Finance NZ Ltd	2.24
Spark New Zealand Ltd	3.00	Argosy Property Ltd	2.08
Skellerup Holdings Ltd	2.88	Mercury NZ Ltd	2.02
Stride Stapled Group	2.87	Infratil Ltd	1.83
Contact Energy Ltd	2.46	Scales Corporation Ltd	1.78

*Applies to the portfolio of directly held fixed income assets only.

Fund Commentary

The Income Fund returned 0.12% over July. Returns from long term bonds were strong, however short-term interest rates increased resulting in losses for short term bonds. The Income Fund's equity holdings delivered a mixed bag of results with the equity sector delivering a small negative return. The combined return from all sectors delivered a modest positive return illustrating the benefit of holding a diverse portfolio of assets. Longer term bonds performed strongly as NZ long term interest rates followed global trends and decreased. The fall in rates occurred as investors seem to agree with central banks' views that any rise in inflation is likely to be transitory and will not become a significant problem. In addition, it now seems the global economic growth spurt may also be transitory as the emergence of the Delta COVID variant knocks investor sentiment. Longer term interest rates have already risen a lot since reaching their low points in September and October last year. In contrast, the rates on shorter term bonds have started to rise in anticipation of a rise in the Official Cash Rate, with the first increase possibly occurring as early as August 2021. Even though the next move in the OCR is up we expect the increase in cash rates will be modest, perhaps peaking at 1.5% in 2023.

The share portfolio of the Income fund fell by around 0.35% over July. Five of the thirteen holdings gained in value with the best performers being Argosy and Stride Property, both advancing around 4%, Infratil was the laggard falling 5%. Meridian remains the smallest exposure and Heartland the largest.

We continue to believe that even though the NZ economy has recovered well and the outlook for a global economic recovery is looking promising, even with the rise in the Delta variant, short-term rates will stay low compared to past tightening cycles. New Zealand's economic activity has surpassed pre-COVID levels and therefore the COVID inspired cut in the Official Cash Rate from 1% to 0.25% over 2020 can expect to be taken back and perhaps rise to 1.5% in 2023 where rises should top out. With the prospect of interest rates remaining low relative to historical levels we continue to believe it is appropriate for investors to seek income from more diverse sources than the interest rate market alone. Even though some equity prices have fallen we believe the growth environment remains attractive but economic growth is unlikely to accelerate from current levels and possibly fall back as new catalysts for growth remain elusive. This means the Income Fund will remain invested in a range of NZ companies listed on the NZX that pay an acceptable 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.

The bond sector of the fund is invested primarily in medium to longer duration assets. We are happy to have exposure to longer term assets as the Official Cash Rate looks likely to remain low over the next year or two, and longer term rates have already risen significantly in response to the strong economic recovery. For further sustained rises in long term yields to occur, new sources of growth and inflation need to emerge. This may happen as the labour market is tight, however we have difficulty seeing significant risks to the upside as the housing market is cooling, the boarders remain closed and export prices will have difficulty pushing higher from here.

The managers of the fund continue to look for opportunities to add value and income. Low and stable short term interest rates represent both a threat and an opportunity. High levels of liquidity in the banking system have left many investors looking for a home for their money which gives them an opportunity to earn more than bank deposits. This search for income is likely to be an enduring theme for the next few years.

Key Fund Facts

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.

Estimated annual fund charges (incl. GST)

0.80%, refer PDS for more details

Hedging

All investments will be in New Zealand dollars

Buy / Sell spread:	Strategy size	Strategy Launch
Click to view	$4.8m	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. Tobacco manufacturers.

Compliance

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

Contact Us www.nikkoam.co.nz | nzenquiries@nikkoam.com