

Factsheet 31 December 2021

NIKKO AM NZ BOND STRATEGY

Assets are held in the Nikko AM Wholesale NZ Bond Fund. The Nikko AM NZ Bond Fund (retail) invest in units in the wholesale fund, which the commentary refers to.

Market Overview

- The NZ yield curve flattened in shape over December.
- Credit margins have widened modestly over the quarter however we expect credit holdings will perform well with little supply expected until the end of the NZ holiday period.
- The pipeline of new bond issuance appears to have slowed into year end.

Fund Highlights

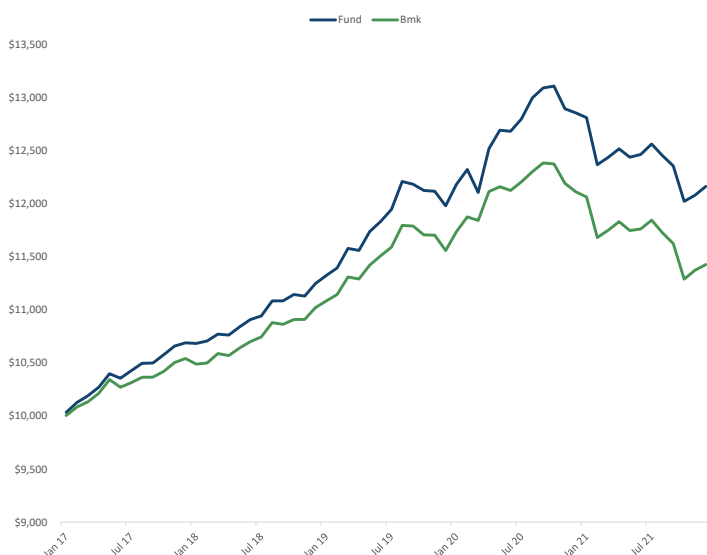
- NZ Bond Fund returns were positive over the month, but negative over the quarter as interest rates increased over the month of October.
- The fund has a modest long duration position.
- The outlook for credit remains supportive and maintaining a higher fund yield should benefit returns.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale ¹	0.69%	-1.56%	-5.40%	2.64%	4.00%	4.74%
Benchmark ²	0.48%	-1.70%	-5.67%	1.21%	2.71%	3.28%
Retail ³	0.64%	-1.72%	-6.01%	1.92%	3.26%	3.92%

1. Returns are before tax and before the deduction of fees.
2. Current benchmark: Bloomberg NZBond Composite 0+ Yr 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.

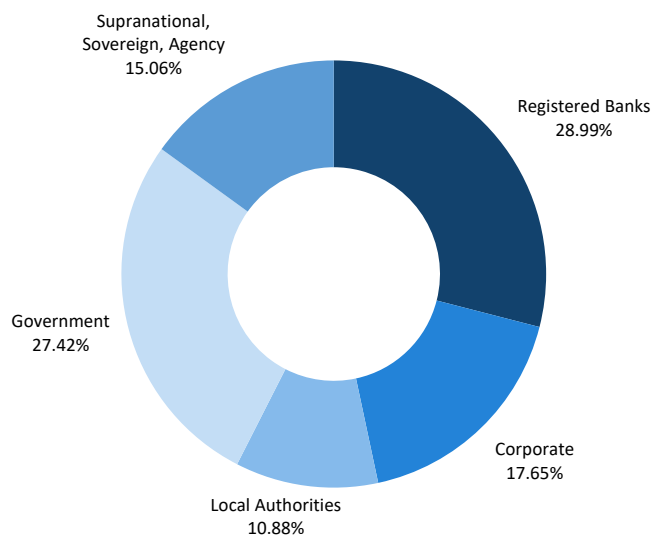
Overview

The fund aims to provide investors with regular income by constructing an actively managed investment portfolio of New Zealand bonds, deposits and cash with the potential for capital gain from New Zealand dollar fixed interest markets.

Objective

The fund aims to outperform the benchmark return by 0.60% per annum before fees, expenses and taxes over a rolling three-year period.

Asset Allocation



Top 5 Corporate Issuers*	(%)	Credit Quality	(%)	Duration
Housing New Zealand Ltd	7.99	AAA	55.0	Fund 5.41 years vs Benchmark 5.34 years
Kommunalbanken AS	6.72	AA	21.3	Yield to Maturity
Westpac New Zealand Ltd	6.11	A	19.5	Fund (gross) 2.40% vs Benchmark 2.28%
China Construction Bank	5.15	BBB	2.8	Green, sustainability and social bonds
Kiwibank Ltd	4.88	BB	1.4	15.55% of the fund

*excludes NZ central government

Market Commentary

The NZ bond market had a mixed quarter. Increased concern over inflation was the catalyst for rates to jump much higher in October, and rising rates in offshore bond markets and poor liquidity exacerbated the move higher. November was positive following some pricing reassessment lower after the November update from the Reserve Bank. The bank acknowledged the strength of the economy, in particular strong employment and inflation has caused them to increase their OCR projections. However, interest rates subsequently fell as the market had already priced in a lot more interest rate increases than the considered steps approach the bank discussed. December was a positive month with short term rates finishing a little higher in yield while long term rates were lower. The NZ yield curve remains very flat in shape. NZ interest rate moves were reasonably volatile over December following offshore moves and with reduced liquidity locally. With no local data the US bond market that remains open through our holidays will likely be an important influence on the direction of rate moves.

From a sector perspective shorter maturity NZ swaps rates marginally outperformed similar maturities of NZ government bonds while longer maturities underperformed as swap spreads widened. Credit margins have widened modestly over the quarter however we expect credit holdings will perform well with little supply expected until the end of the NZ holiday period. The supply/demand dynamics have been supportive of NZ credit for some time, but we have a preference to sell bonds that look expensive in terms of margin and replace with bonds that offer better value and should prove more defensive if we get an increase in supply in 2022. In terms of sector allocation, we have a preference to invest in quality higher yielding credit as bonds priced as a margin over swap will most likely outperform low yielding government bonds over the medium term. This has at times proved challenging when government bonds have a better month as some benchmarks have a large component of government bonds. The reduced issuance of government bonds going forward, and the possibility of NZ government bonds being included in some offshore benchmark indices is something we are mindful of. In terms of direction from here yield curves have become very flat with cash rates increases priced in, liquidity has at times been challenging; inflation may remain elevated over the medium term, balanced against an elevated degree of uncertainty in a COVID world. The fund is positioned close to benchmark, and we have been mindful of investing in the better/safer parts of the yield curve should rates rise.

Fund Commentary

The fund's modest long duration position was a positive over the past month as longer maturity bonds performed better than shorter maturities. However, over the quarter the longer than benchmark position was a drag on performance as rates lifted strongly over October. We let this long position reduce into year-end to reduce risk as often the first quarter of the New Year is quite volatile in terms of interest rates moves. Fund performance was in line with the Bloomberg NZ Bond Composite benchmark. Yield curve positioning, credit and inflation linked bonds all adding to performance relative to benchmark.

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:	0.65%, refer PDS for more detail
Hedging		Buy / Sell spread	Strategy size
All investments will be in New Zealand dollars		Click to view	\$392.1m
Strategy Launch			
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 quarter.

Contact Us

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