

# Nikko AM Global Bond Strategy

Monthly Update 29 February 2024

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

## Market Overview

- Ongoing strength in the US economy, as reflected by a resilient labour market and signals from January PMI surveys, alongside improving sentiment across Europe, boosted risk assets over February.
- Sovereign bond yields fluctuated as financial markets pulled back expectations for the timing of central bank rate cuts, with government bonds exiting February 1.9% lower.
- We continue to expect central banks to cut policy rates this year – albeit later than initially expected.

## Fund Highlights

- Returns were negative for the month with the fund slightly behind its benchmark.
- Underperformance was driven by Duration and Government/Swaps selection strategies, respectively. Meanwhile, Corporate selection strategy contributed to excess returns.

## Performance

	One month	Three months	One year	Three years (p.a.)	Five years (p.a.)	Ten years (p.a.)
<b>Wholesale<sup>1</sup></b>	-0.95%	2.49%	6.41%	-1.71%	1.65%	3.44%
<b>Benchmark<sup>2</sup></b>	-0.70%	2.16%	5.12%	-2.04%	0.64%	2.86%
<b>Retail<sup>3</sup></b>	-0.65%	1.77%	5.36%	-2.40%	0.80%	2.51%

1. Returns are before tax and before the deduction of fees and including tax credits (if any). Based on actual calendar periods.
2. Benchmark: Bloomberg Barclays Global Aggregate Index, hedged into NZD. No tax or fees.
3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any). Based on change in unit price.

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



## Investment Manager

Nikko AM NZ uses Goldman Sachs Asset Management Australia Pty Ltd (GSAM) for the management of global fixed interest assets. Established in 1988, GSAM is one of the world's leading asset managers. The Goldman Sachs Asset Management Global Fixed Income Team managed over US\$690 billion of global fixed income and currency assets (as at 30th September 2022).

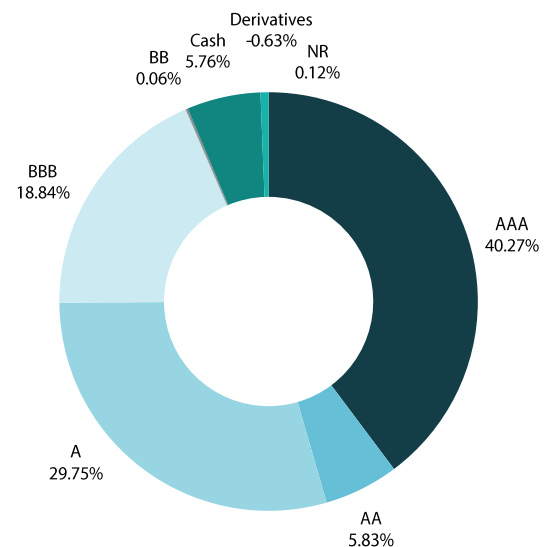
## Overview

The Strategy aims to provide investors with regular income by constructing an actively managed investment portfolio of permitted investments, with the potential for capital gain from global fixed interest markets.

## Objective

The strategy aims to outperform the benchmark return by 1% per annum before fees, expenses and taxes over a rolling three-year period.

## Credit Quality



Sector Allocation (% of fund)	Fund	Index	Duration
<b>Governments</b>	20.24%	44.22%	Fund 6 years vs Benchmark 6.58 years
<b>Agency</b>	5.82%	7.90%	<b>Yield to Maturity</b> Fund (gross) 5.67% vs Benchmark 5.27%
<b>Collateralised &amp; MBS</b>	36.91%	11.56%	
<b>Credit</b>	27.37%	20.49%	
<b>Emerging market debt</b>	4.52%	15.82%	
<b>Cash, derivatives, other</b>	5.13%	0.00%	

\*Includes deferred settlements

## Market Commentary

Ongoing strength in the US economy, as reflected by a resilient labour market and signals from January PMI surveys, alongside improving sentiment across Europe, boosted risk assets over February. Global investment grade (IG) spreads tightened by 4bps while US high yield spreads narrowed by 32bps. By contrast, sovereign bond yields fluctuated as financial markets pulled back expectations for the timing of central bank rate cuts, with government bonds exiting February 1.9% lower.

We continue to expect central banks to cut policy rates this year – albeit later than initially expected. In addition, we think the recent rise in US Treasury yields, driven by resilient economic data and US Federal Reserve (Fed) pushback of early rate hikes, is likely temporary. We believe that yields will fall even as the Fed cutting cycle begins, albeit likely at higher levels than expected at the beginning of 2024. Ongoing disinflation alongside strong growth will still allow for insurance rate cuts given disinflation progress is the Fed's primary focus.

Elsewhere, robust technical dynamics dominated spread sectors such as the IG corporate credit market over the month. Despite a record pace in supply year-to-date, spreads remained anchored. Alongside soft-landing, much so no-landing sentiment, a strong risk-on tone in equity markets (which was supportive for spreads), strong demand driven by attractive yields and expectations that yields will fall as policy eases, drove spreads narrower.

We still see value in maintaining balanced portfolios that draw income from high-quality assets like IG credit and securitized sectors (where we remain overweight), and protection from government bonds (higher yields have strengthened the potential for bonds to protect portfolios against recession risks). Moreover, we reduced exposure to agency mortgage-backed securities (MBS) over the month due to tepid demand caused by higher rate volatility and ahead of an upcoming seasonals.

## Fund Commentary

The portfolio underperformed its benchmark over the month. This was driven by our Duration and Government/Swaps selection strategies. By contrast, our Corporate selection strategy contributed to excess returns.

Detraction of our Duration strategy was driven by our forward steepener and directional underweight positions on US rates. Upside surprises in labour market and inflation data, as well as markets pushing back expectations for the Fed cutting cycle, led to flattening of the US yield curve and a spike in yields across the curve. Our position on the 7-year node of the US yield curve, where we were overweight, particularly underperformed.

Our Government/Swaps selection strategy also underperformed. This was driven by our US and European steepener positions. In Europe, the number of interest rate cuts priced to end-2024 also fell, front-end yields rose, and longer-maturity bonds outperformed shorter-dated counterparts. This saw the European yield curve flatten, challenging our position. Meanwhile, our Corporate selection strategy contributed to excess returns. This was driven by our preference to be overweight the short-to-intermediate part of the IG corporate curve. Over the month, 1-3 and 3-5 year portions of the IG curve tightened by 6bps and 8bps, respectively. Our down-in-quality bias among IG corporates also contributed.

## Key Fund Facts

<b>Estimated annual fund charges (incl. GST)</b>		<b>Hedging:</b>	All investments will be hedged to New Zealand dollars within an operational range of 98.5% - 101.5%.	<b>Strategy Launch:</b>	October 2008
<b>Wholesale:</b>	Negotiated outside of the unit price. 0.80%, refer to PDS for more details.	<b>Exclusions:</b>	Controversial weapons.	<b>Strategy size:</b>	\$564.3m
<b>Retail:</b>		<b>Restrictions:</b>	Thermal coal mining and extraction, oil tar sands extraction, tobacco stocks and fossil fuels. For more information, please refer to the Statement of Investment Policy and Objectives (SIPO) on our website <a href="https://www.nikkoam.co.nz/invest/retail">https://www.nikkoam.co.nz/invest/retail</a> .	<b>Buy / Sell spread:</b>	0.00%/0.00%
<b>Distributions:</b>					
<b>Wholesale:</b>	Calendar quarter				
<b>Retail:</b>	Calendar quarter				

## Compliance

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

## Contact Us

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