

Nikko AM NZ Cash Strategy

Monthly Update 31 May 2024

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

Market Overview

- As widely expected, the Reserve Bank kept the OCR on hold in its May Monetary Policy Statement.
- Markets were caught off guard by the statement’s decidedly hawkish tone, with key surprises including a higher OCR track, along with an explicit call out of the “possibility of increasing the OCR”.
- In sympathy with the Reserve Bank’s statement, markets rapidly reduced bets that OCR cuts would occur in 2024.

Fund Highlights

- The fund holds a longer than benchmark duration position reflecting a view that the RBNZ’s hiking cycle is complete.
- We are looking to maintain a long duration position; however, this may be tempered should markets price cuts at a too rapid pace.
- Credit quality remains high and is expected to perform well in the face of a recession.

Performance

	One month	Three months	One year	Three years (p.a.)	Five years (p.a.)	Ten years (p.a.)
Wholesale¹	0.55%	1.61%	6.50%	3.96%	3.06%	3.24%
Benchmark²	0.48%	1.42%	5.80%	3.47%	2.38%	2.47%
Retail³	0.53%	1.54%	6.20%	3.66%	2.75%	2.89%
KiwiSaver³	0.52%	1.52%	6.16%	3.55%	2.66%	

1. Returns are before tax and before the deduction of fees and including tax credits (if any).
2. Benchmark: Bloomberg NZBond Bank Bill Index. No tax or fees.
3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

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, Senior Fixed Income Manager.

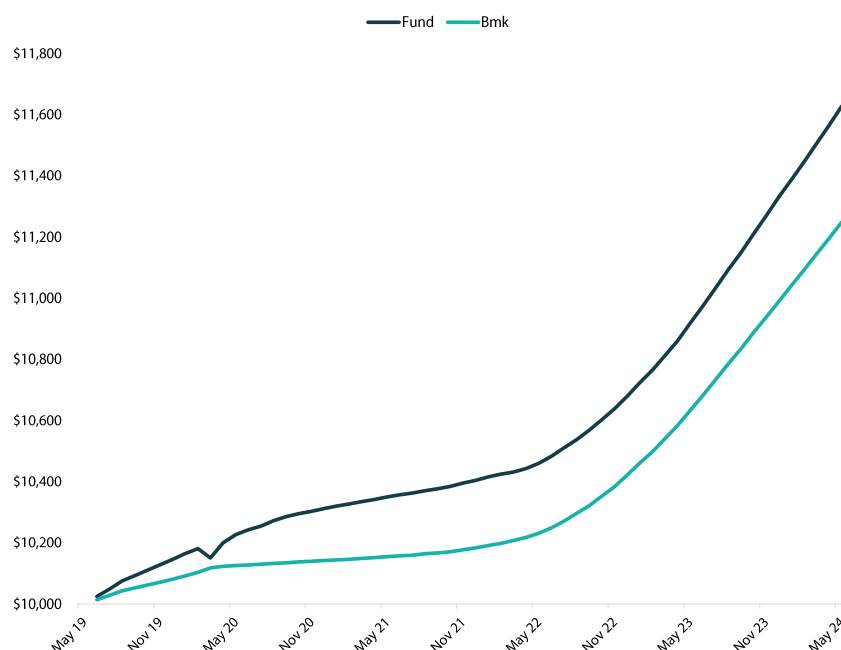
Overview

The strategy aims to generate income by constructing an actively managed investment portfolio of short-term deposits and bonds whilst preserving capital value.

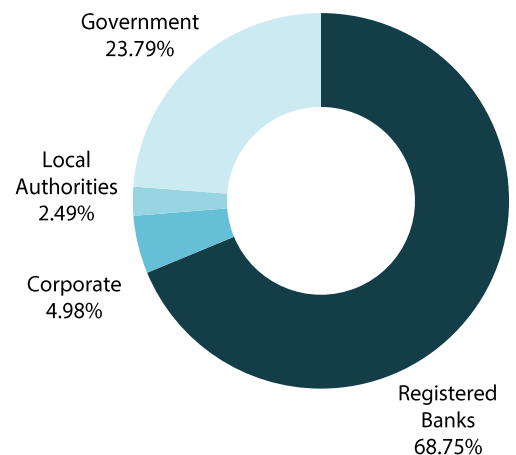
Objective

The fund aims to outperform the benchmark return by 0.20% per annum before fees, expenses and taxes over a rolling three-year period.

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



Sector Allocation



Top 5 Issuers	(%)	Credit Rating	(%)	Duration
Tax Management NZ	12.68	AAA	23.79	Fund 85 days vs Benchmark 45 days
Westpac New Zealand	11.98	AA	31.35	Portfolio Yield (YTM with FRN yield to next reset date)
NZ Tax Trading Co	11.10	A	44.86	Fund (gross) 6.25% vs Benchmark 5.59%
Kiwibank	8.85			
ASB Bank	6.11			

Market Commentary

The Reserve Bank kept the OCR on hold in its May Monetary Policy Statement. Whilst this decision was widely expected, the statement's decidedly hawkish tone and forecasts caught markets off guard. Key surprises included actively considering the "possibility of increasing the OCR" and an OCR track that was not only higher, but also deferred the timing and extent of rate cuts. Adding to this higher for longer theme the RBNZ increased its assessment of the neutral OCR level to 2.75%, a 25bps increase from its last assessment.

Going into the meeting, markets were looking for a softening of the Reserve Bank's tone along with statements acknowledging the relationship between current monetary policy settings and the string of weak domestic economic data. The Reserve Bank continues to ignore the mayday calls from economic data, resolutely focusing on the need for lower inflation with Governor Orr going as far as stating in an interview following the MPS that the RBNZ "can't start to ease before inflation hits 2%". This disconnect of market expectations and the statement's tone resulted in a rapid reassessment of the timing and extent of OCR cuts – notably 1-year swap increased from a pre MPS low of 5.35% to end the month at 5.50%, much unchanged from its April level.

Whilst we have some sympathy with the RBNZ taking a conservative stance its current positioning seems disjointed from economic data and the large lags inherent in monetary policy transmission. There is an element of jawboning to the RBNZ's stance, rather than a hike being a central tactic it is more likely the RBNZ is attempting to present a hard line to push back against markets over enthusiastically pricing cuts before the data truly turns. This aside, risks of an economic capitulation rise each meeting where the OCR remains at highly contractionary emergency levels. We continue to view the next move in the OCR as likely to be down and view backups in yield as opportunities to add duration.

Fund Commentary

The fund performed well in May returning 0.55% outperforming its benchmark the 90-day Bank Bill Index which returned 0.48%.

Despite the RBNZ surprising markets with a hawkish statement, 90-day bills were much unchanged as pre MPS OCR cut expectations were centred around November as the most likely date, some five months away. Conversely, in the lead up to the MPS 1-year swap had fallen 15bps to a low of 5.35%, these falls were then entirely reversed in sympathy with the RBNZ's higher for longer stance ending the month much unchanged at 5.5%. With 1-year swap at a similar level to the OCR we expect some opportunities to add duration over the coming months. The OCR is at highly contractionary emergency levels and economic impacts are very apparent, the longer it remains at these emergency levels, the greater the risk the economy capitulates. The RBNZ faces some difficult decisions in the year ahead as lag continues to build, despite the RBNZ considering the "possibility of increasing the OCR" we view this as jawboning and expect the next move in the OCR is likely to be down.

Key Fund Facts

Distributions Wholesale: Calendar quarter Retail: Calendar quarter KiwiSaver: Does not distribute Estimated annual fund changes (incl. GST) Wholesale: Negotiated outside of unit price Retail: 0.30%, refer PDS for more details KiwiSaver: 0.30%, refer PDS for more details	Hedging: All investments will be in New Zealand dollars Exclusions: Controversial weapons 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 .	Strategy Launch: October 2007 Strategy size: \$969.8m Buy / Sell spread: 0.00% / 0.00%
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Compliance

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

Contact Us

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