

# Nikko AM Income Strategy

Monthly Update 31 August 2024

Applies to the Nikko AM Income Fund.

## Market Overview

- Over the month the NZX50 (gross with imputation credits) increased 0.4% while the NZ Composite Bond Index advanced 0.91%. Cash provided a steady return of around 0.5%.
- The RBNZ surprised markets by delivering a 0.25% cut to the Official Cash Rate at their August meeting and projected further cuts in the OCR until it reaches 3.0% by late 2026 or early 2027.
- The June quarter CPI came in slightly below expectations at 0.4%, giving an annual increase of 3.3%.

## Fund Highlights

- The Income Fund increased by 0.8% over August as the bond market performed well, encouraged by the first of probably many rate cuts by the Reserve Bank.
- The interest rate sensitive property sector had a strong boost with Stride and Argosy advancing by more than 10% with Skellerup and Chorus also recording good month returns. Mercury, Scales and Meridian tailed the field.

## Distributions

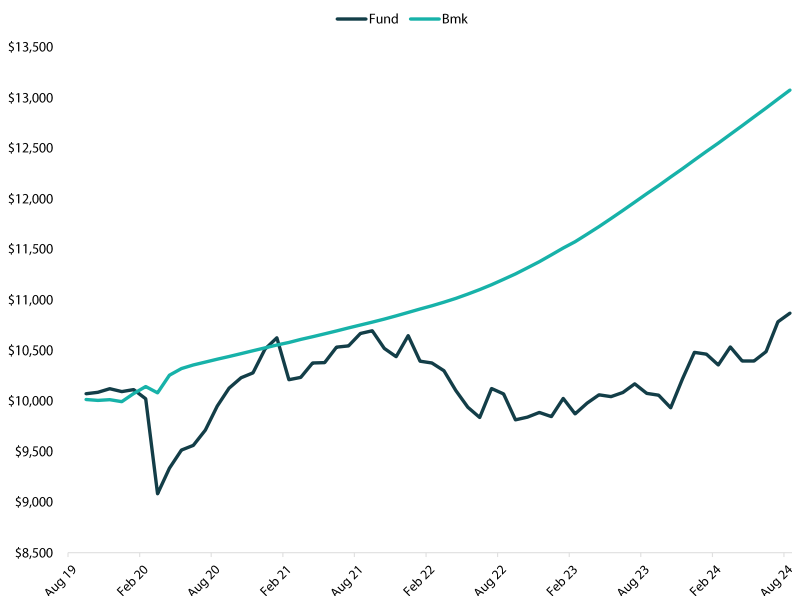
- The defined distribution rate (which is used to calculate the distribution you receive from the fund) is set at the start of each calendar year, based on the price of the fund at that point. The defined distribution rate for 2024 is 6.5%. This income will be distributed in four equal amounts each calendar 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)
<b>Retail<sup>1</sup></b>	0.79%	4.54%	7.87%	0.62%	1.68%	3.23%
<b>Benchmark<sup>2</sup></b>	0.69%	2.07%	8.51%	6.74%	5.51%	6.09%
<b>Market Index<sup>3</sup></b>	0.70%	4.35%	9.10%	1.22%		

- Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).
- Current benchmark: RBNZ Official Cash Rate +3.00% p.a.
- Current appropriate market index: 65% Bloomberg NZBond Credit 0+ Yr Index, 35% S&P/NZX 50 Gross Index.

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



## 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.



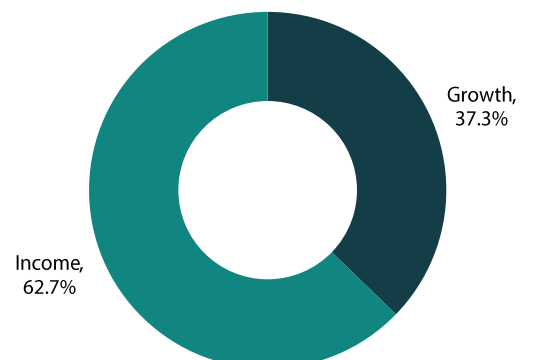
## Overview

The strategy aims to 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	(%)	(%)	
Westpac New Zealand	8.37	Fund 3.83 years	Infratil	3.66	Meridian Energy	2.62
ANZ Bank New Zealand	6.67	<b>Yield to Maturity</b>	Chorus	3.32	Skellerup Holdings	2.58
Powerco	4.91	Fund (gross) 5.22%	Bank Of New Zealand	3.15	Heartland	2.46
Kiwi Property	4.18		Works Finance NZ	3.08	Spark New Zealand	2.16
Auckland International Airport	3.60		Contact Energy	2.63	Kiwibank	2.06

\*Includes cash holdings.

## Fund Commentary

The Income Fund increased by 0.8% over August as the bond market performed well, encouraged by the first of probably many rate cuts by the Reserve Bank. The NZ equity market was modestly positive as company results indicated many businesses are struggling to combat the country's recessionary environment. Over the month the NZX50 (gross with imputation credits) increased 0.4% while the NZ Composite Bond Index advanced 0.91%. Cash provided a steady return of around 0.5%.

Markets continue to focus on the words and actions of the Reserve Bank of NZ and influential central banks such as the US Federal Reserve for signs of when and by how much cash rates will be cut. The RBNZ did surprise markets by delivering a 0.25% cut to the Official Cash Rate at their August meeting and projected further cuts in the OCR until it reaches 3.0% by late 2026 or early 2027.

The NZ economy remains weak and inflation pressures are falling. The June quarter CPI came in slightly below expectations at 0.4%, giving an annual increase of 3.3%. When the large 1.8% September 2023 increase is replaced by a much more modest number later this year, CPI inflation should be within the RBNZ's speed limit of between 1% and 3% before quickly heading to the 2% mid-point. The RBNZ now seems to be anticipating inflation moving back to target rather than waiting for confirmation that it has. This change in view perhaps explains the RBNZ bringing forward the timing of rate cuts, especially as weak economic activity is likely to continue before staging a recovery over 2025.

The Federal Reserve is also turning more dovish as Governor Powell all but told markets that rate cuts are on the table in September. If the Fed does move it increases the likelihood of the RBNZ continuing on their measured pace of cuts. Equity markets also seem to be taking the lead from interest rate markets with downward trajectory of interest rates lifting the animal spirits of equity investors. If cash rates move significantly lower over the next year or two, we would expect bond rates to follow but not to the same extent. We are also aware that large falls in cash rates are already priced into markets so any disappointment could see some retracement in prices/yields however if this does occur it could represent a good buying opportunity.

The S&P/NZX 50 Gross (with imputation credits) Index increased by 0.4% over August and there continued to be a wide variance in stock returns. The interest rate sensitive property sector had a strong boost with Stride and Argosy advancing by more than 10% with Skellerup and Chorus also recording good month returns. Mercury, Scales and Meridian tailed the field.

The bond sector as measured by the Bloomberg NZ Bond Composite Index increased 0.91%. Longer-term bonds continued to be the best performing part of the fixed income sector. Bonds have performed well as inflation pressures globally and locally are decreasing and more central banks join the rate cutting cycle.

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

<b>Estimated annual fund charges (incl. GST)</b>	0.80%, refer PDS for more details.	<b>Hedging:</b>	All investments will be in New Zealand dollars.	<b>Strategy Launch:</b>	October 2017
<b>Exclusions:</b>	Controversial weapons.	<b>Distributions:</b>	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.	<b>Strategy size:</b>	\$3.2m
<b>Restrictions:</b>	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 <a href="https://www.nikkoam.co.nz/invest/retail">https://www.nikkoam.co.nz/invest/retail</a> .			<b>Buy / Sell spread:</b>	<a href="#">Click to view</a>

## Compliance

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

## Contact Us

[www.nikkoam.co.nz](http://www.nikkoam.co.nz) | [nzenquiries@nikkoam.com](mailto:nzenquiries@nikkoam.com)

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