

Nikko AM NZ Cash Strategy

Monthly Update 31 August 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

- The Reserve Bank surprised markets with a 0.25% cut to the Official Cash Rate.
- The August OCR cut is likely to be the first of many with the RBNZ projecting a low point of 3% by late 2026 or early 2027.
- In response to the OCR cut the 90-day Bank Bill rate fell by 0.24% and 1-year swap rates fell by 0.33%

Fund Highlights

- The fund holds a longer than benchmark duration position reflecting our view that the RBNZ's hiking cycle is complete and a prolonged easing cycle has started.
- 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 | 0.52% | 1.60% | 6.51% | 4.44% | 3.23% | 3.29% |
| Benchmark² | 0.47% | 1.43% | 5.79% | 3.92% | 2.58% | 2.52% |
| Retail³ | 0.48% | 1.51% | 6.19% | 4.13% | 2.92% | 2.95% |
| KiwiSaver³ | 0.48% | 1.50% | 6.16% | 4.03% | 2.82% | |

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.

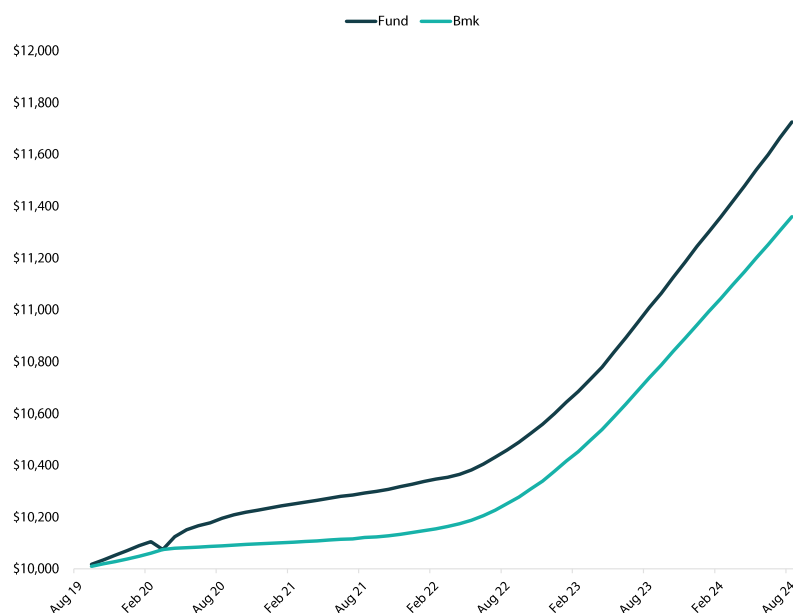
Overview

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

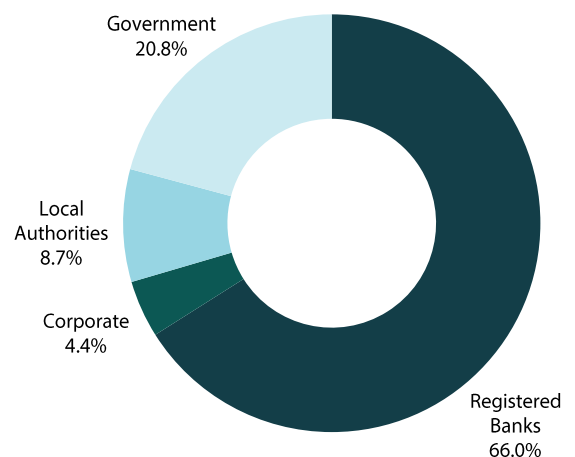
Objective

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 |
|------------------------|-------|---------------|-------|--|
| Westpac New Zealand | 11.50 | AAA | 26.17 | Fund 90 days vs Benchmark 45 days |
| Tax Management NZ | 10.53 | AA | 29.99 | Portfolio Yield (YTM with FRN yield to next reset date) |
| NZ Tax Trading Co | 10.30 | A | 43.85 | Fund (gross) 5.91% vs Benchmark 5.29% |
| Kiwibank | 8.93 | | | |
| Cooperatieve Rabo U.A. | 8.87 | | | |

Market Commentary

August was an eventful month for the cash and short-term fixed interest market with a strong rally occurring in response to the Reserve Bank starting their cutting cycle earlier than the market was anticipating. Over the month, in response to the OCR cut, the 90-day Bank Bill rate fell by 0.24% to 5.22%, the 1-year swap rate fell by 0.33% to 4.47% and the 6-month Bank Bill rate declined by 0.32% to 4.95%.

After a long 15 month pause in the OCR at an elevated 5.5% the Reserve Bank indicated the time was right for an easing cycle to begin. The Bank is signalling a progressive move in the OCR to a low point of 3% late in 2026 or early 2027. The market is pricing in a more aggressive easing path and near term there is risk the market could be disappointed with the timing and magnitude of rate cuts. We think the NZ economy is very weak and there is the possibility of a 50-bps rate cut at some stage, investing for the medium-term outlook we do expect longer rates have room to move lower particularly if the cash rate ends below 3%.

The overall positive is the start of the easing cycle will be welcomed by households and the business sectors alike who have until recently been despondent about future prospects. The most recent survey of business opinion has seen a boost in optimism, and we expect consumer confidence to also improve, especially if mortgage costs fall further, but it could take some time to reinvigorate consumer spending and growth. One of the key takeaways from the August MPS was the RBNZ's change as to where they see the balance of risks, and their assessment of the NZ economy was a lot more negative than the May MPS update. The RBNZ communicated a more forward-looking stance and that they now have confidence that inflation is slowing. The RBNZ's growth forecasts have been revised down significantly, incorporating negative growth in both Q2 and Q3, and CPI inflation is expected to be in the 1-3% band next quarter but the near-term outlook is lower due to lower tradable inflation.

Fund Commentary

The fund performed well in August returning 0.52% outperforming its benchmark the 90-day Bank Bill Index which returned 0.47%.

The fund's duration position ended the month at 90 days, 45 days longer than benchmark. This long duration position positively contributed to fund performance over August as short maturity rates fell by approximately 30 bps. The market is pricing a more aggressive rate cut profile than the RBNZ forecast pricing implies over the coming year with the cash rate around 4% in Feb 25. We agree the NZ economy has slowed significantly and there is the possibility of a 50-bps rate cut at some stage, but the magnitude and timing of cuts will remain tied to the inflation and economic data going forward.

In terms of investing the yield curve is inverted with the OCR at 5.25% and 1-year swap at 4.40%. We want to maintain a higher yield on the fund balanced against locking in higher rates for longer through investing out to one year. Fortunately, the fund is able to invest at levels higher than the bank bill or swap rates through adding quality credit. We will continue to look for opportunities to maintain and add duration positions on any backups in yield however remain cautious given markets high expectations for OCR cuts.

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: \$1,128m Buy / Sell spread: 0.00% / 0.00% |
|---|--|---|

Compliance

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

Contact Us

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

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