

Nikko AM Global Bond Strategy

Monthly Update 31 October 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

- October was a lacklustre month for global bonds as market participants recalibrated their expectations for US Federal Reserve (Fed) policy amid uncertainty around the US Presidential election and its implications on inflation and monetary policy.
- The European Central Bank (ECB) implemented its third 0.25% rate cut in the current cycle, a move widely expected given further weakening of activity, wage and inflation data.
- Japanese bond yields followed the upward global trend with the 10-year yield topping 0.97% for the first time since July, with political uncertainty also contributing to the move higher.

Fund Highlights

- The portfolio underperformed its benchmark over October.
- Underperformance was driven by our Duration and Government/Swaps selection strategy.
- Among our strategies, our Corporate selection strategy was the best performer.

Performance

	One month	Three months	One year	Three years (p.a.)	Five years (p.a.)	Ten years (p.a.)
Wholesale¹	-1.85%	0.44%	10.78%	-0.56%	0.93%	3.30%
Benchmark²	-1.48%	0.69%	9.39%	-0.99%	0.04%	2.60%
Retail³	-1.84%	0.77%	10.22%	-1.30%	0.26%	2.42%

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

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.

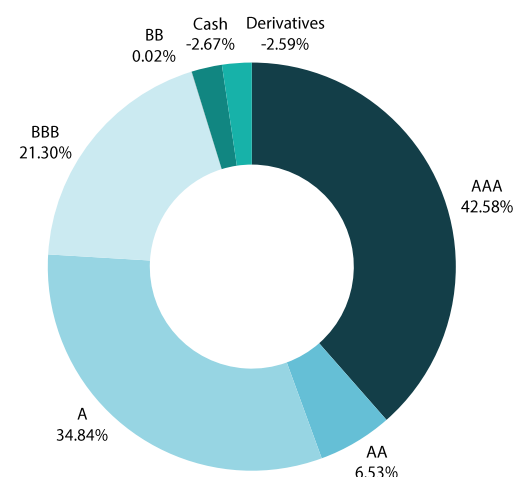
Objective

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

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



Credit Quality



Sector Allocation (% of fund)	Fund	Index
Governments	29.96%	44.35%
Agency	5.10%	7.80%
Collateralised & MBS	40.08%	11.26%
Credit	26.01%	20.42%
Emerging market debt	4.12%	16.17%
Cash, derivatives, other	-5.26%	0.00%

*Includes deferred settlements

Duration
Fund 6.32 years vs Benchmark 6.51 years
Yield to Maturity
Fund (gross) 5.56% vs Benchmark 4.75%

Market Commentary

October was a lacklustre month for global bonds as market participants recalibrated their expectations for US Federal Reserve (Fed) policy amid uncertainty around the US Presidential election and its implications on inflation and monetary policy. 2-year US Treasury yields spiked by 54bps while the US dollar gained by 3.2%. Additional catalysts perturbed selloffs in other developed market (DM) government bond markets. In the UK, concerns around the fiscal implications of the first Labour party budget saw 10-year UK Gilts selloff by 50bps and the spread between UK Gilts and German Bunds widen. Elsewhere, upside surprises in Euro area data led to underperformance into month-end. Lastly, Japanese bond yields followed the upward global trend with the 10-year yield topping 0.97% for the first time since July, with political uncertainty also contributing to the move higher.

The European Central Bank (ECB) implemented its third 0.25% rate cut in the current cycle, a move widely expected given further weakening of activity, wage and inflation data. Elsewhere, despite no policy changes at the Bank of Japan's (BoJ) policy meeting, the central bank reiterated data dependency, especially amid a policy easing Fed. In early November, the Fed cut the federal funds rate by 0.25%, from 4.75-5% to 4.5-4.75%, while the Bank of England (BoE) delivered its second rate cut in this cycle, lowering the policy rate from 5% to 4.75% due to reduced risks of inflation persistence.

Credit markets were not immune to the weakness experienced among sovereign bonds. Emerging market (EM) debt underperformance was mainly driven by a stronger US dollar. By contrast, investment grade (IG) spreads remained contained, with spreads narrowing - supported by strong demand. Securitized credit spreads also tightened across the board.

We are focussed on three key investment themes: dialling up duration, earning income amid the ongoing expansion and going global. In our view, extending duration can protect against growth risks and capture upside in sovereign bonds considering global monetary easing. We also think income can be earned from corporate bonds and securitized sectors in an environment categorised by healthy consumer spending and central banks easing to elongate the expansion. Lastly, given central bank actions vary in pace and likely destinations, we are vigilant of relative-value opportunities across interest rates. In all cases, active security selection is essential.

Fund Commentary

The portfolio underperformed its benchmark over the review period. This was driven by our Duration and Government/Swaps selection strategy. Among our strategies, our Corporate selection strategy was the best performer.

Detraction from our Duration strategy was driven by our US steepener position. Short-dated US Treasury yields spiked higher as markets adjusted their estimates for Fed rate cuts given strong US data coupled with expectations of inflationary pressures in event of a Republican victory for the US Presidential election. This challenged our position.

Our Government/Swaps position also underperformed. This was driven by our European steepener position as short-end European yields ultimately ended the month 13bps higher, driven by upside surprises in Eurozone GDP and inflationary data at the end of the month.

Corporate selection returns were neutral against the benchmark. This was driven by our bias for the IG curve to steepen and bias towards BBB-rated credits. The US IG curve steepened by around 3bps over the month, while BBB-rated spreads tightened by around 10bps, on lighter supply, as well as positive third quarter earnings reports.

Key Fund Facts

Estimated annual fund charges (incl. GST)		Hedging:	All investments will be hedged to New Zealand dollars within an operational range of 98.5% - 101.5%.	Strategy Launch:	October 2008
Wholesale:	Negotiated outside of the unit price.	Exclusions:	Controversial weapons.	Strategy size:	\$713m
Retail:	0.80%, refer to PDS for more details.	Restrictions:	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 https://www.nikkoam.co.nz/invest/retail .	Buy / Sell spread:	0.00%/0.00%
Distributions:					
Wholesale:	Calendar quarter				
Retail:	Calendar quarter				

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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