

Nikko AM NZ Bond Strategy

Monthly Update 30 November 2024

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

Market Overview

- Bond returns were positive as the move higher in yields following Trump’s Presidential victory began to unwind.
- The yield curve steepened slightly in shape as short-term rates had larger falls than longer maturities.
- There has been an increase in new bond deals to the market which has caused a modest widening in credit margins.

Fund Highlights

- The longer duration position was of benefit as interest rates moved lower delivering some modest capital gains.
- There was a reasonable amount of new bond issuance over the month, and we continue to add quality credit to maintain a higher yield.
- We expect the funds will continue to perform well over the medium term as the cash rate continues lower and carry-and-roll makes a larger contribution to returns with a positive shaped yield curve.

Performance

	One month	Three months	One year	Three years (p.a.)	Five years (p.a.)	Ten years (p.a.)
Wholesale¹	0.79%	0.52%	9.32%	2.46%	1.40%	3.76%
Benchmark²	0.57%	0.70%	8.04%	1.34%	0.22%	2.71%
Retail³	0.73%	0.35%	8.60%	1.81%	0.74%	3.02%

1. Returns are before tax and before the deduction of fees and including tax credits (if any).
2. Current benchmark: Bloomberg NZBond Composite 0+ Yr 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 fund aims to provide investors with regular income by constructing an actively managed investment portfolio of New Zealand bonds, deposits and cash with the potential for capital gain from New Zealand dollar fixed interest markets.

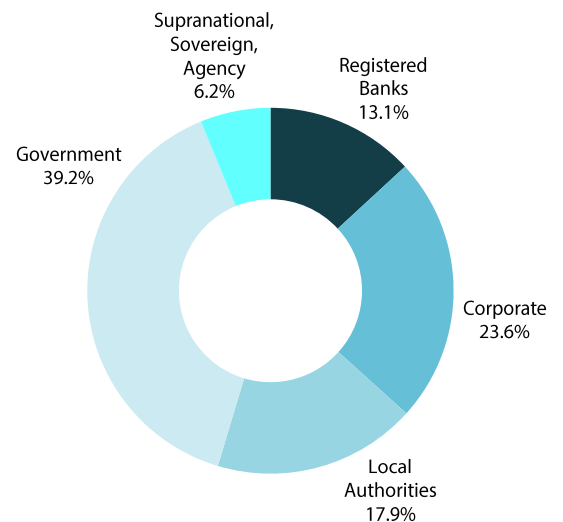
Objective

The fund aims to outperform the benchmark return by 0.60% 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 Corporate Issuers*	(%)
New Zealand Local Govt Funding Agency	9.54
Westpac New Zealand	7.97
Housing New Zealand	6.28
Bank of New Zealand	5.57
Kiwibank	5.09

* Excludes NZ central government

Credit Quality	(%)
AAA	63.41
AA	23.39
A	7.79
BBB	5.41

Green, sustainable and social bonds
21.09% of the fund
Duration
Fund 6.07 years vs Benchmark 4.75 years
Yield to Maturity*
Fund (gross) 4.63% vs Benchmark 4.20%

* Excluding the inflation component of government inflation linked bonds

Market Commentary

NZ bonds had a positive return for November as interest rates recovered lower in yield, unwinding some of the jump higher following Trump's Presidential victory. Fund performance was supported by a higher yield through quality credit and some modest capital gain with rates lower over the month.

In terms of sector performance, the fund's credit holdings continue to perform well. There has been some gradual widening of credit margins following an increase in supply, but over the medium term a higher yield should help support performance. The NZ yield curve has continued to steepen in shape with shorter rates having larger falls than longer maturity bonds. NZ governments generally performed better than swap with larger falls in yield. Interest rate moves for NZ government bonds were 1yr -13bps, 5yr -5.5 bps, 10yr -10bps, and the 2054 bond -4.5bps. NZ Swap rates were 1yr -2bps, 5 yr -2.5bps, 10yr -10bps, and 30yr -1bp.

The NZ bond market continues to remain reasonably well supported relative to global bonds with our market viewed a "safer bet" supported by a weaker economy, and a lower rates outlook. It is easier to have a higher conviction on the direction of short-term rates as these are more heavily influenced by the actions of the RBNZ and local economic outcomes that we expect should remain supportive with the cash rate moving lower. Longer maturity bonds look attractive in terms of a higher yield and potential for further modest capital gains. The caveat is longer bonds are more subject to the direction of offshore bond moves and there is greater uncertainty around growth and inflation outcomes in the US that could keep curves steeper.

We continue to like quality credit to maintain a higher yield and expect that carry-and-roll will make a larger contribution to returns going forward with the yield curve positive in shape. NZ government bonds have remained cheap relative to swap rates because of higher supply and where appropriate we hold an increased weighting to governments with the view that they will likely outperform swap products over the medium term.

Fund Commentary

The fund had a positive month returning 0.8% and outperformed its benchmark the Bloomberg Composite which returned 0.6%.

The key drivers of absolute and relative returns were the move lower in interest rates, and the fund's higher yield accrual from quality credit. The longer duration positioning was helpful as rates fell delivering modest capital gains. Credit margins have widened slightly (from previously tight levels) with more bond supply, but a gradual widening should benefit returns through a higher yield over the medium term. The fund has gradually increased its weighting to NZ government bonds as these have become cheap relative to swap with margins expanding as a function of greater supply. Whilst we see no imminent reason for these spreads to normalize, our holdings here provide protection should the government's financial position improve and its borrowing program fall.

We continue to favour adding quality credit to maintain a higher fund yield which has proved a consistent value add over time. We expect bonds can continue to perform well as cash rates are moved lower. The upward sloping yield curve will provide the fund with opportunity to execute a carry and roll strategy which should provide an additional contribution to future returns.

Key Fund Facts

Distributions		Hedging:	Any foreign currency exposure are hedged to NZD within operational range of 95%-105%	Strategy Launch:	October 2007
Wholesale:	Calendar quarter	Exclusions:	Controversial weapons	Strategy size:	\$654.1m
Retail:	Calendar quarter	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 .	Buy / Sell spread:	Click to view
Estimated annual fund changes (incl. GST)					
Wholesale:	Negotiated outside of unit price				
Retail:	0.65%, refer PDS for more details				

Compliance

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

Contact Us

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