

New Zealand Fixed Interest Fund

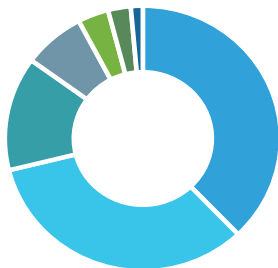
Investor Factsheet for the quarter ended 31 March 2024

	Quarter Performance	1 year	3 years*	5 years*	Since Inception*
Gross Fund Return**	0.40%	6.02%	0.40%	1.71%	5.11%
Bloomberg NZBond Composite 0+ Yr Index ¹	0.25%	5.01%	-0.07%	1.21%	4.87%
Out/under performance	0.15%	1.01%	0.47%	0.50%	0.24%
Tracking error	n/a	0.48%	0.45%	0.90%	0.94%
Information ratio	n/a	2.13	1.05	0.56	0.26
Sharpe ratio	n/a	0.07	-0.60	-0.12	0.76

Key Fund Facts as at 31 March 2024

Fund Name	New Zealand Fixed Interest Fund	Risk Indicator	1 2 3 4 5 6 7
Inception Date	26/06/2008	Market Index	Bloomberg NZBond Composite 0+Yr
Fund Value (NZD)	\$152,707,991	Unit Price	\$1.9280
Yield to maturity ²	5.10%	Annual Fund Charge (ex-GST)	0.75%
Duration (years) ³	4.55		
Average credit quality ⁴	AA		

INVESTMENT BY SECTOR



● NZ State Owned Enterprises, 1.40%	● Supranationals, 2.66%
● Local Authority Stock, 3.62%	● Cash and cash equivalents, 7.29%
● LGFA Securities, 13.88%	● Corporate Investment, 33.29%
● NZ Government Stock, 37.86%	

The fund in its macro context

For the March 2024 quarter we saw investments in domestic fixed interest and local equities generally deliver small positive returns.

For fixed interest investors, in our view, the major theme continues to be around inflation and the timing of an easing in monetary policy; the last vestiges of inflation are proving difficult to stamp-out. We also note geo-political concerns with several armed conflicts around the globe adding to investor anxiety.

Portfolio attribution

For the quarter to 31 March 2024 the New Zealand Fixed Interest Fund delivered a gross return of 0.40% marginally outperforming the fund's market index return of 0.25%.

For the four quarters to 31 March 2024 the fund delivered a gross return of 6.02%, comfortably outperforming the fund's market index return of 5.01%.

As longer-dated interest rates and bond yields have fallen over the last two quarters our strategy of increasing duration by selling shorter-dated corporate bonds and buying longer-dated New Zealand Government bonds has meant the fund has delivered significant capital gains. We are an active investment manager and calibrate portfolio construction to our assessment of prevailing economic conditions is consistent with our investment philosophy.

Portfolio position and conviction

We believe domestic inflation peaked some time ago and that the Reserve Bank of New Zealand (RBNZ) will have the confidence to begin reducing its Official Cash Rate (OCR) towards the middle or end of this year. This is earlier than the RBNZ's forecast, where it predicts the first OCR cut towards the middle of next year.

* Annualised

** Gross Fund Returns are calculated before deduction of taxes and fund charges but after deduction of trading expenses and including imputation credits where applicable. Market index returns do not have any deductions for fund charges, trading expenses or tax.

¹ For periods prior to July 2023 the market index/benchmark return is the S&P/NZX Investment Grade Corporate Bond Index.

² Portfolio yield to maturity is the weighted average yield to maturity of the securities within the fund.

³ Portfolio duration is the weighted average modified duration of the securities within the fund.

⁴ Average credit quality is the weighted average (using a linear scale) credit rating of the securities held within the fund. Where an issue is not rated, we have used the issuer rating. Where both the issue and issuer are unrated, we have assigned an equivalent internal rating.

The extreme market volatility that has plagued investors over recent years is likely to continue in our view. We expect interest rates to fall further and while the initial impetus is a positive news story – falling inflation – we see the next driver as something more sinister, an economic recession.

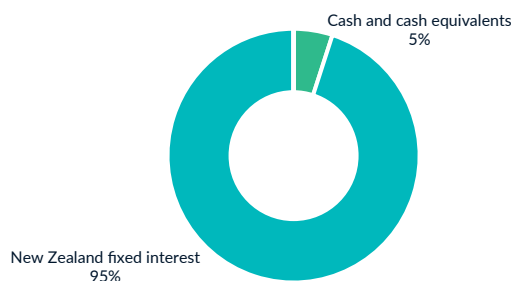
Therefore, we are positioning the New Zealand Fixed Interest Fund by continuing to buy New Zealand Government bonds funded by the sale of lower credit quality non-Government bonds, a pragmatic approach to mitigating the risk of security default. In addition, we intend to increase portfolio duration from 4.55 years as at the end of March to somewhere approximating 5 years over the next month or so; the goal here is to position the portfolio for further capital gains as and when the OCR is cut.

Conclusion

The portfolio has performed as constructed, delivering capital gains as term interest and bond yields have fallen over the last two quarters.

This is consistent with our philosophy and investment style because as an active investment manager we will have preference for investment exposures that match our assessment of the prevailing economic conditions. Falling inflation matched with an economic recession mean we are rationing our non-Government bond exposures and increasing portfolio sensitivity with “hard duration” or long-dated New Zealand Government bonds.

TARGET ASSET ALLOCATION



TOP 10 FUND HOLDINGS AT QUARTER END

Security	Weight
ANZ transactional bank account	7.3%
New Zealand Government 3% 20/04/2029	6.1%
Westpac New Zealand 1.439% 24/02/2026	5.5%
New Zealand Government 15/05/2032 2.00%	3.8%
New Zealand Government 14/04/2033 3.5%	3.7%
New Zealand Government 4.50% 15/05/2030	3.3%
New Zealand Local Government Funding Agency Ltd 15/04/2027 4.50%	3.2%
Dunedin City Treasury 1.93% 18/04/2028	2.9%
New Zealand Government 15/05/2028 0.25%	2.8%
New Zealand Government 1.5% 15/05/2031	2.7%
Major holdings as % of total portfolio	41.3%

Investment Philosophy and Thesis

Octagon is an active investment manager. Our investment philosophy focuses on developing a repeatable process that systematically looks for short-to-medium term inefficiencies in market pricing of securities with a solid economic basis and a good management team to deliver long term, measurable alpha.

Octagon builds its fixed interest and cash portfolios based on several investment philosophies, namely:

- That the risk free rate oscillates around the neutral cash rate as the regulator implements monetary policy.
- Historically investors in New Zealand fixed interest and cash have been rewarded for credit better than duration.
- Successful research can identify attractive investment opportunities within the credit sector.
- New Zealand fixed interest and cash markets provide multiple sources for alpha generation from; duration, yield curve positioning, sector and security selection and secondary market trading.
- New Zealand Fixed Interest and Enhanced Cash funds are both core strategies not unreasonably constrained by benchmarks.

Portfolio Manager



Craig Alexander
Head of Fixed Interest and ESG

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