

# Enhanced Cash Fund

Investor Factsheet for the quarter ended 30 September 2024

	Quarter Performance	1 year	Since Inception
Gross Fund Return*	1.87%	6.69%	6.46%
S&P/NZX Bank Bills 90-Day Index	1.43%	5.81%	5.79%
<b>Out/under performance</b>	<b>0.44%</b>	<b>0.88%</b>	<b>0.68%</b>

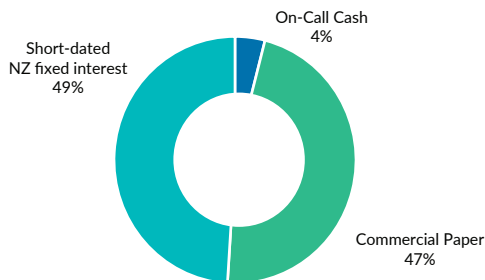
## Key Fund Facts as at 30 September 2024

Fund Name	Enhanced Cash Fund	Risk Indicator	<span style="border: 1px solid black; border-radius: 50%; padding: 2px;">1</span> <span style="border: 1px solid black; border-radius: 50%; padding: 2px;">2</span> <span style="border: 1px solid black; border-radius: 50%; padding: 2px;">3</span> <span style="border: 1px solid black; border-radius: 50%; padding: 2px;">4</span> <span style="border: 1px solid black; border-radius: 50%; padding: 2px;">5</span> <span style="border: 1px solid black; border-radius: 50%; padding: 2px;">6</span> <span style="border: 1px solid black; border-radius: 50%; padding: 2px;">7</span>
Inception Date	07/06/2023	Market Index	S&P/NZX Bank Bills 90-Day
Fund Value (NZD)	\$43,064,032	Yield to maturity <sup>1</sup>	5.31%
Unit Price	\$1.0810	Duration (years) <sup>2</sup>	0.33

## TARGET ASSET ALLOCATION



## SECURITY TYPES FOR THE QUARTER



## The fund in its macro context

The September quarter was resoundingly positive for investors with exposure to New Zealand fixed interest securities, providing capital gains to investors as interest rates fell. The New Zealand dollar two-year swap rate fell -1.39% over the quarter while the 10-year swap rate fell -0.61%.

Driving these falls in interest rates were both domestic and overseas factors. Here at home, the Reserve Bank of New Zealand (RBNZ) conducted a 'dovish pivot' back in July, setting the market up for imminent cuts to the Official Cash Rate (OCR). This first cut duly came at the August Monetary Policy Statement with a 0.25% cut signalling an official start to the easing cycle. A subsequent cut of 0.50% backed up the RBNZ's dovish outlook.

The United States Federal Reserve (the Fed) also kick-started its easing cycle over the quarter with a 0.5% cut to the policy rate in August. As a result, the United States also saw falling rates, albeit less significant than here, with the US two-year treasury rate down -0.28% over the month and down -1.07% over the quarter.

## Portfolio Attribution

For the quarter to 30 September the Enhanced Cash Fund delivered a gross return of 1.87% outperforming the fund's market index return of 1.43%.

For the four quarters to 30 September the Enhanced Cash Fund delivered a gross return of 6.69% significantly outperforming the fund's market index return of 5.81%.

The fund's duration began the quarter at around 0.5 years, which provided capital gains to the fund over the last three months as interest rates moved lower. The fund's yield of 6.0% at the beginning of the quarter was also a contributor to outperformance, representing a significant premium to the OCR.

Credit spreads on commercial paper moved lower over the quarter, which all else equal was a small positive for performance, however it leads to a lower starting yield going forward. The average spread on A2 rated Commercial paper tightened from 29bps in June, to 15bps in September.

\* 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.

<sup>1</sup> Portfolio yield to maturity is the weighted average yield to maturity of the securities within the fund.

<sup>2</sup> Portfolio duration is the weighted average modified duration of the securities within the fund.

## Portfolio position and conviction

We continue to believe that we have seen the peak in interest rates for this cycle and that short-term rates will continue to move lower over the next year. At the end of September, the fund's duration was 0.3 years, which we consider to be a relatively 'short' duration position for the fund. This positioning reflects that there is already significant easing priced into interest rates - the Overnight Indexed Swap (OIS) market is pricing an OCR below 4% by February next year and an OCR around 3% by the end of 2025. As such, our current preference is to keep duration short and focus on attractive opportunities in the credit sector.

In the fixed interest portion of the portfolio, we continue to hold close-to-maturity corporate bonds for the attractive yields on offer. Many of these bonds mature in the next three to six months, meaning any exposure to changes in credit spread is very minimal. Additionally, we have been building positions in Floating Rate Notes (FRNs) of high-quality corporates. We like FRNs at this stage in the cycle as they have very little exposure to interest rate movements (given the coupon on these bonds resets frequently).

Our latest move has been to sell out of some of our fixed-rate bank bonds which had been trading on yields well above 5% and are now trading below 4% (significantly below the current OCR). We have rotated those proceeds into 2025 New Zealand Government Inflation-Indexed bonds which we expect to provide a stronger return for lower credit risk (the New Zealand Government is AA+-rated).

## Conclusion

We believe there is substantial opportunity for active management of cash and cash equivalents and short-dated New Zealand fixed interest. The peak in the interest rate cycle has provided strong capital gains returns to the portfolio over the last 12 months. As active managers our focus now shifts from maintaining duration to earning a quality premium over the cash rate via credit spreads. However, on any unjustified (in our view) increases in interest rates we will look to lengthen duration again.

## FUND CREDIT BREAK-DOWN

Credit profile <sup>3</sup>	%
AAA	0%
AA (+ to -)	32%
A (+ to -)	25%
BBB (+ to -)	43%

<sup>3</sup> Where an issue is not rated we have used the Issuer rating. Where both are unrated we have assigned an internal rating.

## TOP 10 FUND HOLDINGS AT QUARTER END

Security	Weight
Precinct Properties NZ Ltd 4.42% 27/11/2024	6.8%
Powerco Ltd 4.67% 15/11/2024	6.5%
Property for Industry Limited 4.59% 28/11/2024	5.2%
Port of Tauranga CP 01/10/2024	4.6%
NZ Local Govt Funding Agency Ltd CP 15/10/2024	4.6%
Transpower New Zealand CP 07/11/2024 0%	4.6%
Meridian Energy Limited CP 20/11/2024	4.6%
Westpac New Zealand 1.439% 24/02/2026	4.5%
Rabobank FRN 16/06/2025	3.5%
Genesis Energy Limited 5.0% 03/04/2025	3.5%
<b>Major holdings as % of total portfolio</b>	<b>48.5%</b>

## 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.

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.
- New Zealand fixed interest and cash investors have historically been rewarded for credit more 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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