Allianz Global Investors

Allianz

Flexi Asia Bond

Monthly commentary

- The Fund aims at long-term capital growth and income by investing in debt securities of Asian bond markets denominated in EUR, USD, GBP, JPY, AUD, NZD or any Asian currency in accordance with environmental and social characteristics. With the adoption of the Sustainability Key Performance Indicator Strategy (Relative) ("KPI Strategy (Relative)"), the Fund aims to achieve the reduction in greenhouse gas emissions ("GHG") of the Fund's portfolio which shall be at least 20% lower than that of its benchmark index within the same period ("Sustainability KPI").
- The Fund is exposed to significant risks of investment/general market, country and region, interest rate, creditworthiness/credit rating/downgrading, default, valuation, sovereign debt, emerging market, RMB debt securities, currency (such as exchange controls, in particular RMB), and the adverse impact on RMB share classes due to currency depreciation.
- The Fund is exposed to sustainable investment risks relating to KPI Strategy (Relative) (such as foregoing opportunities to buy certain securities when it might otherwise be advantageous to do so, and/or selling securities when it might be disadvantageous to do so or relying on information and data from third party ESG research data providers and internal analyses which may be subjective, incomplete, inaccurate or unavailable). The Fund focuses on the Sustainability KPI which may reduce risk diversifications and may be more volatile compared to broadly based funds. Also, the Fund may be particularly focusing on the GHG emission efficiency of the investee companies rather than their financial performance which may have an adverse impact on the Fund's performance.
- Investing in share class with fixed distribution percentage (Class AMf) is not an alternative to fixed interest paying investment. Investors should note that fixed distribution percentage is not guaranteed. The percentage of distributions paid by these share classes is unrelated to expected or past income or returns of these share classes or the Fund. Distribution will continue even the fund has negative returns and may adversely impact the net asset value of the Fund. Positive distribution yield does not imply positive return.
- The Fund may invest in high-yield (non-investment grade and unrated) investments and convertible bonds which may subject to higher risks, such as volatility, loss of principal and interest, creditworthiness and downgrading, default, interest rate, general market and liquidity risks and therefore may adversely impact the net asset value of the Fund. Convertibles may also expose to risks such as prepayment, equity movement and greater volatility than straight bond investments.
- The Fund may invest the assets in interest-bearing securities issued or guaranteed by a non-investment grade sovereign issuer (e.g. Philippines) and is subject to higher risks of liquidity, credit, concentration and default of the sovereign issuer as well as greater volatility and higher risk profile that may result in significant losses to the investors.
- The Fund may invest in financial derivative instruments ("FDI") which may expose to higher leverage, counterparty, liquidity, valuation, volatility, market and over the counter transaction risks. The Fund's net derivative exposure may be up to 50% of the Fund's net asset value.
- This investment may involve risks that could result in loss of part or entire amount of investors' investment.
- In making investment decisions, investors should not rely solely on this material.

Note: Dividend payments may, at the sole discretion of the Investment Manager, be made out of the Fund's capital or effectively out of the Fund's capital which represents a return or withdrawal of part of the amount investors originally invested and/or capital gains attributable to the original investment. This may result in an immediate decrease in the NAV per share and the capital of the Fund available for investment in the future and capital growth may be reduced, in particular for hedged share classes for which the distribution amount and NAV of any hedged share classes (HSC) may be adversely affected by differences in the interests rates of the reference currency of the HSC and the base currency of the Fund.

What Happened in September

September was a strong month as risk assets outperformed on the back of US Federal Reserve's (Fed) front -loaded easing cycle that began with a 50bps policy rate cut. In Asia, the market rally continued to gather pace, following positive headlines around China policy stimulus and subsequent monetary policy easing from People's Bank of China (PBoC). Asian credit (JACI composite) delivered 1.2% return in September. Year to date, Asian credit has delivered 7.1% in total return, driven by a good mix of tighter credit spreads (3.2%), as well as positive contribution for and treasury return (3.8%). Asian investment grade (IG) delivered 5.9% in total return, modestly ahead of JP Morgan US Liquid Index's (JULI's) 5.6% total return. Asian high-yield (HY) continued to report outstanding returns of 14.8%, significantly outperforming other HY markets.

In China, policymakers announced significant market supportive measures to boost market sentiments The government first announced its' intention to recapitalize the 6 state-owned Chinese banks, with an estimated RMB 1 trillion of capital injections. If confirmed, this would mark the first time since the global financial crisis (GFP) that China's largest state-owned banks will be re-capitalized. Policymakers also announced various stimulus measures for the real estate sector, with a comprehensive package of policy measures and stimulus that exceeded market expectations. Outside of China, the Australian Prudential Regulation Authority (APRA) released a proposal that would see additional Tier 1 (AT1) phased out such that regulatory capital requirements will be met with common equity and Tier 2. This measure would be supportive of the Australian AT1 sector.

Asian IG spreads tightened over September, on the back of the sentiment boost from the Fed and Chinese policymakers. For top gainers, China technology was the strongest outperformer. IG sovereigns in Philippines and Indonesia, and Malaysia quasi-sovereigns also outperformed given their long duration profile.

In a similar note, Asian HY also delivered strong returns of 1.8% for September, with both Treasury and credit spread movements driving gains. Within HY, China and China real estate led gains, followed by Sri Lanka and Pakistan Sovereigns, which was driven by their respective idiosyncratic situations. China HY industrials also benefitted from the optimism in real estate, rallying in tandem.

In Sovereign HY space, election noise in Sri Lanka drove market volatility higher, though the bond market subsequently ended the month in positive territory. Sri Lanka authorities had secured an agreement in principle (AIP) with the international and local bondholders' group. This reduced concerns about the need to re-negotiate the structure of the current proposal. Newly elected President Anura Kumara Dissanayake (AKD) had also signaled his willingness to be pragmatic and not abandon the International Monetary Fund (IMF) deal. Over in Pakistan, the IMF announced that they have approved a USD 7bn loan for Pakistan under the Extended Fund Facility to support its economy. The initial USD 1bn will be disbursed immediately, with the remaining amount to be released over the next 3 years.

Portfolio Review

The Fund outperforming its benchmark for the month.

The Fund had reduced its allocation to HY from the previous month, retaining a small overweight that supported higher carry contribution. Over the month, we traded tactically on duration from the short side but remained largely neutral on overall portfolio duration. We picked up some high yield during the volatile periods and this contributed as these bonds rebounded.

Outlook and Positioning

As the Fed begin their rate cutting cycle, these positive sentiments would flow into the bond markets. Although Fed easing cycle is widely anticipated, the more aggressive Fed cut suggest that the policy makers are determined to ensure a soft landing and avoid any hard landing scenario. With this soft-landing backdrop, it should be overall positive for credits. One potential source of volatility would the upcoming US elections. As we proceed closer to the election, rhetoric from both US presidential candidates could possibly lead to knee-jerk reaction to the financial markets. Therefore, we must remain vigilant on this front.

Within Asia, we remain sanguine about Asia credit with all the positive headlines from China. As market sentiment continue to be buoyant and excited by the new policy supports from China, we think that credit spreads can continue to grind tighter.

However, we do feel that most of the returns from Asia credits would likely come from lower rates and yield carry, which would still be decent.

In the Asian IG, credit spreads should continue to benefit from strong demand despite lower yields. Improving IG credit quality reflected in continued positive rating actions, is also supportive, despite regional growth risks. For these reasons, we continue to expect IG spreads to remain relatively resilient going into year end. We would also focus on risk optimization in anticipation of higher volatility due to uncertainty on political noises and risk aversion behavior going into year end. We maintain a long-spread bias and position in the shorter end.

We continue to favour Asian HY given the wider credit spreads and stable to improving fundamental outlook. Given the strong performance of the asset class, prudent credit selection is increasingly important for outperformance.

Connect with Us | **hk.allianzgi.com** | **+852 2238 8000** | **Search more** Allianz Global Investors

Like us on Facebook **安聯投資 – 香港**

Connect on LinkedIn **Allianz Global Investors**

Subscribe to YouTube channel **安聯投資**