Allianz Global Investors

Allianz Income and Growth

Monthly commentary

- The Fund aims at long-term capital growth and income by investing in US and/or Canadian corporate debt securities and equities.
- The Fund is exposed to significant risks of investment/general market, company-specific, creditworthiness/credit rating/downgrading, default, valuation, asset allocation, country and region, emerging market, interest rate, currency (such as exchange controls, in particular RMB), and the adverse impact on RMB share classes due to currency depreciation. The Fund's investments focus on US and Canada which may increase concentration risk.
- 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 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, particularly if such HSC are applying the IRD Neutral Policy.

What Happened in December

Equity, convertible, and high yield markets finished lower in December. The Federal Reserve cut its benchmark interest rate by 25 basis points to a range of 4.25-4.50%. However, the central bank also updated its summary of economic projections for 2025, decreasing its forecast for further interest rate cuts and employment, while increasing its forecast for real gross domestic product (GDP) growth and inflation. On the economic front, nonfarm payrolls, small business optimism, and consumer sentiment rose, and inflation measures were generally in line with estimates. On the other hand, regional manufacturing gauges missed expectations. Against this backdrop, the 10-year US Treasury yield rose, pressuring risk assets and core fixed income.

Equity and Option Market Environment

The S&P 500 Index returned -2.38% for the month.*

Sector performance was mixed in December. Communication services, consumer discretionary, and information technology were the top-performing sectors, while materials, energy, and real estate were the bottom-performing sectors in the period.

Equity volatility was higher month to month with the VIX finishing at 17.35.*

Convertible Market Environment

The ICE BofA US Convertible Index returned -3.98% for the month.^

Nearly all sectors finished lower in December. Transportation, telecommunications, and industrials outperformed, whereas materials, energy, and technology underperformed.

Below-investment grade issues outperformed investment grade issues. Yield-oriented (busted) issues outperformed total return (balanced) and equity sensitive issues.

Monthly new issuance saw 19 issues priced, raising USD 11.7 billion in proceeds to bring the full-year total to USD 84.7 billion. ^

High-Yield Bond Market Environment

The ICE BofA US High Yield Index returned -0.43% for the month.^ BB, B, and CCC rated bonds returned -0.65%, -0.32%, and +0.19%, respectively.^

Spreads widened to 292bp from 274bp, the average bond price fell to 95.48, and the market's yield rose to 7.65%.

Industry performance skewed lower with telecoms, transportation, and media outperforming, while cable, real estate, and energy underperformed.

Trailing 12-month default rates finished the period at 1.47% (par) and 1.02% (issues). **

Monthly new issuance saw 17 issues priced, raising USD 11.5 billion in proceeds to bring the full-year total to USD 288.8 billion. **

Portfolio Review

The portfolio was negatively impacted by weakness across risk assets.

Top contributors in the period included a multinational technology company and a major US electric vehicle manufacturer. Two technology companies capitalizing on secular trends around artificial intelligence and cloud migration – were also notable contributors, along with several semiconductor companies. An airframe manufacturer outperformed on production optimism, and a commercial airline rallied after boosting earnings guidance.

Top detractors in the period included a software company with bitcoin exposure and several healthcare-related holdings facing regulatory uncertainty. Multiple positions settled lower, consolidating strong year-to-date gains, such as a multinational corporation and technology company, an aerospace company, a specialty Real estate investment trust (REIT), and a power management company. The other top detractors were a home improvement retailer navigating interest rate headwinds and a clean energy company expected to benefit from higher power prices and demand.

All option positions expired below strike and the portfolio was able to retain the set premiums.

Exposure increased the most in financials, consumer staples, and utilities, and decreased the most in health care, real estate, and consumer discretionary. Covered call option positioning increased month over month.

Outlook and Strategy

The US economy should continue to expand in 2025, supported by earnings growth, further Fed easing as inflation and the labor market continue to normalize, and the new administration's pro-US growth policies.

Apart from these factors, steady consumer spending, ongoing services sector expansion, continued fiscal spending, and improving productivity aided by the proliferation of artificial intelligence are growth tailwinds. Risk to the economy may increase if these trends weaken. Other considerations include tariff and immigration policies, geopolitical tensions, prolonged labor market softening, continued manufacturing contraction, and economic weakness outside of the US.

Against this backdrop, mid- to high-single-digit returns in 2025 are possible for large-cap equities, convertible securities, and high-yield bonds. The equity market's path will not be linear, with bouts of volatility probable throughout the year. Given their defensive characteristics, high-yield bonds and convertible securities can mitigate market volatility better than equities.

The expected range of annual returns for large-cap equities is 5-10%. The market could benefit from continued Fed easing, economic growth, and accelerating or inflecting earnings from more companies. Secular growth themes, such as artificial intelligence, lower taxes, increased mergers and acquisitions (M&A) activity, deregulation, productivity gains, and share buybacks are also catalysts. If either economic growth or earnings growth fall short of expectations, the equity market could be challenged. Valuations will continue to be debated.

US convertible securities have an attractive asymmetric return profile, providing upside participation potential when stock prices rise and downside mitigation when stock prices fall. The asset class may outperform the broad equity market if leadership broadens, and new issuance remains steady. USD 60-65 billion of new issuance is expected in 2025 due to coupon savings demand, elevated refinancing needs, and a positive outlook for price appreciation among small- and mid-cap companies. Aside from diversification benefits, new issuance expands the opportunity set of investments with attractive terms and the desired risk/reward characteristics.

The US high-yield market, yielding over 7%[1], is expected to deliver a coupon-like return in 2025 with upside possible. As a result, the asset class continues to offer equity-like returns but with less volatility. The market's attractive total return potential is a function of its discount to face value and higher coupon, which also serves to cushion downside volatility. Credit fundamentals are stable, near-term refinancing obligations remain low, and management teams continue to exercise balance sheet discipline. Increased M&A activity and deregulation could also have a positive market impact. In this environment, new issuance is expected to remain elevated, the default rate should stay below the historical average of 3-4%, and spreads can remain tight.

A covered call options strategy can be utilised to generate premium income. In periods of elevated or rising equity volatility, premiums collected may translate into more attractive annualised yields.

Collectively, these three asset classes can provide a steady source of income and a compelling "participate and protect " return profile.

The Income and Growth strategy is a client solution designed aim to provide high monthly potential income, the potential for capital appreciation, less volatility than an equity-only fund.

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Source: Allianz Global Investors dated 31 December 2024 unless otherwise stated.

*Source: FactSet, as at 31 December 2024.

^Source: BofA Merrill Lynch, as at 31 December 2024.

**Source: J.P. Morgan, as at 31 December 2024.

[1] Source: ICE Data Services; data as at 31 December 2024.

Allianz Global Investors and Voya Investment Management entered into a long-term strategic partnership on 25 July 2022, upon which the investment team transferred to Voya Investment Management. This did not materially change the composition of the team, the investment philosophy nor the investment process. Management Company: Allianz Global Investors GmbH. Delegated Manager: Voya Investment Management Co. LLC ("Voya IM").

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