

Allianz

Yield Plus Fund

Monthly commentary

- The Fund aims at long-term income and enhanced return by investing directly and indirectly in global interest bearing securities.
- The Fund is exposed to significant risks which include investment/general market, investing in other underlying collective investment schemes and exchange traded funds, asset allocation, sovereign debt, creditworthiness/credit rating/downgrading, counterparty, interest rate changes, valuation, volatility and liquidity, and currency.
- 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.

What Happened in December

Global equities slid as the euphoria of Trump's decisive election victory faded and the US Federal Reserve (Fed) issued a more hawkish outlook for interest rates in 2025. The tech-heavy Nasdaq Composite Index held up relatively well due to ongoing interest in mega-cap growth stocks, but the broad-based S&P 500 Index lost ground as sentiment was knocked by the Fed more hawkish rate projections for 2025.

Global bonds sold off as investors became less optimistic on the Fed's willingness to cut rates in 2025. Having started the month around 4.2%, the yield on the 10-year Treasury bond climbed sharply, closing the month near a seven-month high of 4.6%, as the month's Federal Open Market Committee (FOMC) meeting revealed policymakers had reduced the number of rate cuts they expected in 2025.

As widely expected, the Federal Reserve cut rates by 25 basis points (bps) in December, but policymakers issued more cautious guidance for 2025, reducing the number of expected 25-bps cuts to two from four at the previous FOMC meeting. Concerns that progress against fighting inflation had stalled were cited for the change. It was mostly a different story in Europe, with the European Central Bank (ECB) cutting rates by 25 bps. The Bank of Japan (BoJ) also maintained its monetary stance.

Portfolio Review

The Fund generated a negative return over December.

During December, total exposure to fixed income investments has been slightly reduced. We have mainly reduced allocation to corporate bonds and increased short duration government bonds. Within risky assets, we have maintained our equity exposure, with some rotation out of developed markets to Asian equities.

Outlook and Strategy

Donald Trump's return to the White House will probably be a turning point for both the US economy and the financial markets. Additional fiscal stimulus and deregulation should fuel growth in the US and support riskier assets at least in the short term. At the same time, the regional gap in terms of growth, inflation and interest-rate trends looks set to widen. US equities remain attractive due to the "Trump effect", but we are well aware that their valuations are high in a historic comparison. In contrast, European equity valuations appear favourable, and the ECB might opt for larger rate cuts than the Fed because euro-area growth will likely remain low. In China, domestic stimulus and reforms of the private pension system might give the market a stronger lift than currently expected. Overall, we remain optimistic for equity investments, but expect volatility to increase, particularly as market participants learn more about the potential impact of the new US policies – above all immigration and tariffs – on inflation and global supply chains. The dynamic market environment, pronounced regional divergences and persistent geopolitical uncertainties will probably require an active approach to portfolio management.

During his second term of office, Donald Trump will probably increase government spending and cut taxes. These measures will lift the growth outlook for the US. We expect US growth to exceed that of other developed economies in 2025. However, the generous fiscal policy may boost US inflation again. That is why we think that the Fed will stop its rate-cut cycle in the first half of 2025 and keep the Fed funds rate near 4%. In the euro area, growth looks set to remain subdued against the background of political paralysis, sluggish productivity growth and low consumer confidence. In response, the ECB may reduce its deposit rate below the neutral level of 1.75% during the coming quarters. As the yield differential grows and rate trends diverge, opportunities on the government bond market are increasing. We continue to expect a steepening of the yield curve in Europe and the US. From our vantage point, it makes sense to take an active approach in bond portfolio management. In view of the different developments in the individual economies, we recommend targeted duration positioning combined with relative value trades across regions, currencies and maturities.

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Source: from Bloomberg and Allianz Global Investors and as at 31 December 2024 unless otherwise stated.

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