Allianz Global Investors

Allianz

Flexi Asia Bond

Monthly commentary

Investment Objective

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 the Sustainability Key Performance Indicator Strategy (Relative). In this context, the aim is to outperform the sub-fund's Sustainability KPI compared to sub-fund's benchmark to achieve the investment objective.

What Happened in August

August was a volatile month with a big sell-off on risk assets in the first few days due to heightened recession fear but the market rebounded quickly and recovered most of the losses since then. Despite the elevated volatility, Asian credit (JACI composite) managed to deliver a decent 1.6% return in August. Investment grade (IG) credits returned 1.8% which was mainly coming from the favourable US Treasury movement while high yield (HY) also delivered a positive return of 0.5% thanks to the superior carry. Year to date, Asian credit delivered 5.9% in total return, driven by a good mix of spread return (2.7%) and treasury return (3.1%). Asian IG delivered 4.8% in total return, beating US IG's 3.8% total return, thanks to strong spread performance. Asian high-yield continued to report outstanding return of 12.7%, significantly outperforming other high-yield markets.

Asian IG spreads were stable on a month-on-month basis, despite the volatility during the month. In terms of sectors, perpetual bonds from Hong Kong issuers were the outperformers given the rate rally during the period with market pricing in 100% probability of rate cut in September. Indonesia and Philippine sovereign were also performing well with the expectation of the US Federal Reserve (Fed) cutting rates later this year and limited new supply within the space. New issue market for IG was less active but demand remained solid in August. Financials and China continued to be the major contributors to supply. Debut performance for the new issues were mainly driven by supportive US Treasury returns while spread returns were mixed.

Spreads for Asian HY tightened in August despite the market turmoil. delivering positive total returns , thanks to the decent carry and the supportive US Treasury returns. In terms of sectors, Property names experienced some sell-off in longer-dated names, likely driven by the weak data, and concerns that some of the state stimulus have not materialised. Nevertheless, the quality names continued to perform well in the secondary market, thanks to the strong shareholder background and their robust access to loan and bond markets. Outside China property, the two big sectors within Asian HY space, namely Macau Gaming and India Renewable, moved in line with the broader HY market, with divergence of performance among the names with higher quality names outperformed. The new issue market saw a few HY and non-rated new issuances, though the bulk of the issuance were by China local government financing vehicles (LGFVs) with limited liquidity in the secondary market. The actively traded non-rated new issuances were well-subscribed but secondary performance was disappointing given weak market sentiments.

Portfolio Review

The Fund returned positively, underperforming its benchmark for the month.

In August, the Fund dialled down the credit spread risk of the portfolio by reducing the large overweight in high yield bonds to a more manageable small overweight in high yield bonds. The cash proceeds are placed in fixed deposits while waiting for new issuances where activity stayed more muted, or better entry points in the secondary markets for investment grade bonds. In terms of duration, the Fund is keeping close to the benchmark as we approach the Federal Open Market Committee (FOMC) meeting in September. We are biased to go long duration ahead of FOMC as we are expecting a rate cut, but it seems like the market has already priced this. We await a better entry level to go long duration.

Market Outlook

With investors pricing in higher probability of a hard landing on US economy and political noises still hovering around, we expect volatility to remain in the markets over the near term. However, Asian credits should continue to benefit from the resilient credit fundamentals and supportive negative net bond supply for the rest of the year. With credit spreads staying at the tighter end of historical trading range and the decent performance of Asian credits year to date, we expect most of the return should come from carry in the near term. We continue to favour Asian high-yield over investment-grade for the better carry. That said, as certain sectors and corporates are navigating the downcycle, credit selection is still key to outperformance.

All data are sourced from Bloomberg and Allianz Global Investors, as at 31 August 2024 unless otherwise stated.