# 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 February

Despite a big sell-off in the US Treasuries (UST) at the beginning of February, Asian credit spreads managed to tighten throughout the month, more than offsetting the UST sell-off, thanks to continuously robust performance from Asia high yield (HY), as well as the resilience of Asia investment grade (IG) credit. In February, the JP Morgan Asia Credit Index (JACI) – Composite managed to stay afloat with 10 basis points (bps) in total return, lifted by 2.2% total return from Asia HY. Year-to-date, JACI has delivered 40 bps in total return, mainly driven by the strong total return of 4.9% from Asia HY. For IG, the JACI IG spread tightened 12 bps, not enough to cushion UST sell-off, resulting in a slightly negative 20 bps in total return. Nonetheless, JACI IG outperformed JP Morgan US Liquid Index (JULI) IG and EUR IG in both total return and spread return terms, thanks to its lower duration exposure and stronger technicals. The new issue market in February remained quiet with activities mainly from regional financial institutions.

In Asia credit markets, higher total yield helped attract buyers into Asia IG over the month, despite the slightly negative return for the IG segment. Within Asia IG, Indian IG corporates spread continued to show strong momentum for compression, mainly led by continuous repricing in the credits of a transport and utility infrastructure company. China IG spreads also enjoyed a decent rally on the back of buoyant Chinese New Year travel and consumption data, as well as the bigger-than-expected 25-bps loan prime rate (LPR) cut during the month. Indonesia's no-surprise presidential election result gave investors more clarity and visibility in policy continuity, which supported resilience in Indonesian IG spreads. Towards end of the month, Hong Kong's annual budget announcement with property relaxation measures have lifted HK property sentiments, leading to spread compression in Hong Kong IG property names.

In contrast, Asia HY had another month of strong performance, up 2.2%, significantly outperforming global HY (+1.5%) and US HY (+30bps). The stellar performance was mainly led by the sovereigns (ie, Pakistan and Sri Lanka), and China HY. Asian HY additional tier 1 bonds (AT1s) also had a good month, led by Southeast Asia (SEA) and Hong Kong banks, after better-than-expected earning results. The rest of the Asia HY market was jogging along, while most SEA corporates released satisfactory earnings.

For Pakistan, the election earlier in the month caused some volatility in bonds, which was then quickly reversed after news on two major political parties having agreed to form a coalition government. Moreover, reports of the country having met International Monetary Fund (IMF) conditions for further funding drawdown, coupled with prospects for new funding, have further lifted bond prices. Sri Lanka USD-denominated bonds also did well this month on the back of the release of the long-waited restructuring proposal for its USD bonds after months without progress.

The China HY rally was again largely broad-based, lifted by better equity performance. Industrial names have had a strong run year-to-date, with some bonds repricing from HY of over 20%, down to low to mid-teens. China Real Estate bonds also rallied after the LPR cut, which was viewed by the market as being property supportive. Interestingly, this month China HY property names continued to outperform the IG part of the sector.

An interesting development this month is the reopening of HY new issue markets, with decent new issue debut performance, indicates that there are sufficient liquidity waiting to be put to work in this region.

## Portfolio Review

The Fund (class AM USD) returned negatively at -0.33%, largely in line with its benchmark of 0.09%[1].

The Fund continued to reap the gains from higher spread beta while duration dragged both total and relative performance. Our decision to have large overweight in BB-rated credits and underweight in A- and AA-rated credits were the biggest positive allocation contributors to performance, while our underweight in lower-quality party of the credit curve dragged. In terms of sector allocation, our overweight to Financials and underweight in Quasi-sovereigns have contributed positively, while idiosyncratic exposure in Real Estate partially offset the allocation effect.

We continue to be slightly long duration with a steepener bias while maintaining a long-carry position and long-HY allocation. Nonetheless, as HY has significantly outperformed year-to-date, we are looking to rebalance our HY beta exposure by reducing some outperforming sectors such as Financials and reducing idiosyncratic exposures.

## Market Outlook

Notwithstanding any near-term rebalancing activities after Asia credit market's outperformance year-to-date against other credit markets, we expect Asia credit spreads to remain largely resilient, given favourable growth and inflation dynamics in the region, well-positioned credit cycle, as well as strong technicals. Moreover, shifting policy landscape in China reduces tail risk that could otherwise have been exacerbated by further downward spiral of growth.

While Asia IG spreads are fair at best, total yield level remains attractive versus history average and should continue to attract buyers into the market. Limited supply in Asia IG space will limit the extension of spread widening, should global risk sentiment turn. We continue to like the carry in Asia IG credits.

Asia HY has outperformed other credit markets year-to-date by a large margin and remains reasonably attractive considering its higher rating composition. Favourable credit cycle of most of the sectors in Asian HY space gives us comfort to build our core holdings with stable carry, while normalisation of default rate in China offers spread compression and credit repricing opportunities. That said, as certain sectors and corporates are navigating the downcycle, credit selection in those sectors is key to outperformance.



All data are sourced from Bloomberg and Allianz Global Investors, as at 29 February 2024 unless otherwise stated. Global High Yield refers to ICE Global High Yield Index (HW00), US High Yield refers to ICE US High Yield (H0A0). Country and Sector performance listed in the market review section is based on Bloomberg PORT's figures.

[1] Source: Allianz Global Investors/IDS GmbH. Performance is shown based on AM USD share class. Fund performance is calculated in the respective fund currency with net income and dividends reinvested.