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 January

In January, US Treasuries traded sideways amid uncertainty about the US Federal Reserve's (Fed's) potential cutting cycle in March 2024. We anticipate a neutral stance from the Fed, maintaining reluctance to explicitly signal rate cuts and remaining data-dependent. The market is caught between positive growth fundamentals and an inflation outlook nearing target but not yet at its destination. Consequently, investment grade (IG) and high yield (HY) markets displayed performance divergence. The JP Morgan Asia Credit Index (JACI) composite declined by 0.4%, with JACI IG down by 0.8%, primarily driven by negative US Treasuries return, while JACI HY rose by 2.1%. On the supply side, the Asia credit primary market picked up in January, with about 31 new issues totalling approximately USD 17.8 billion printed. Most of the new issues performed well on debut, reflecting investor demand for bonds to deploy cash.

In Asia credit markets, JACI IG spread was hovering around a tight 10 basis point (bps) range, ending the month largely flat. Within Asian IG space, India and China outperformed, with spreads tightened 9 bps and 8 bps respectively, while Indonesia and Philippines underperformed, with spread widening 8 bps and 1 bps respectively. Positive rating actions on an issuer underpinned outperformance of India IG credits, with other credits generally mixed. In China, IG credits shrugged off weak equity performance, tightening 8 bps in January, mainly driven by BBB-rated Technology names and asset management companies (AMCs). AMCs suffered a volatile month, first trading down on negative rating actions, before rallying following news reports of potential ownership transfer of the AMCs to China Investment Corporation (CIC). Despite the lack of details, the reported reorganisation of the AMC sector is seen as integral to China's broader financial regulatory revamp, aiming to enhance efficiency, financial health, and governance for a strategic countercyclical role in economic and credit cycles.

Asia HY delivered a 2.7% return in January, significantly outperforming Global HY (+0.06%) and US HY (+0.02%). Among the countries, Pakistan and China were the key outperformers, returning 7.5% and 4.2% respectively, while Mongolia and Macau posted positive but lacklustre performance in comparison. In terms of sectors, Metals & Mining and Real Estate outperformed, with 7.8% and 6.1%. Pakistan performed well on the back of diminishing risks of a payment halt and expectation of further International Monetary Fund (IMF) engagement post-elections. As the upcoming 2024 maturity is expected to be comfortably repaid, the longer-dated maturity bonds are benefitting from rollover flows. Despite a weak equity backdrop, China HY credits delivered a broad-based rally. The China Property was, however, a notable exception, with outperformance interestingly driven by distressed names, which were lifted by rising expectations for further supportive measures, while the aggressive gapping up in price could also be attributed to lack of liquidity. While valuations remained tight, Indian Renewables also did well, supported by continuous positive credit trajectory.

Portfolio Review

The Fund returned positively (gross, USD).

Performance was primarily driven by our long spread positions via BBB and BB-rated credits. On the other hand, our underweight to CCC and below-rated names weighed on performance. We continue to be largely flat on duration, with a steepener bias while overweight spread beta. Over the month, we took profits on half of our 2v10-year curve steepener positions and looked for better re-entry points. We also added more BB-rated HY to beef up carry in the portfolio, given our positive view on Asian HY's total return potential this year, as default rate is expected to come down.

Market Outlook

Given the resilience in US economic growth and indications of a disinflationary path, we anticipate that Asia credit spreads can persist at lower levels for an extended duration. Our outlook for Asia credits remains optimistic, fuelled by the favourable conditions in the US and the increasing number of easing policy measures originating from China. Recent actions in China indicate a gradual shift towards more high-profile monetary easing and fiscal expansionary measures, deviating from the previous baseline.

In Asia IG, we anticipate continued sideways trading of credit spreads due to a limited supply. While IG spreads may appear tight, the positive lack of supply technical factor is likely to prevent significant widening, driven by investors deploying cash. Moreover, considering yields, Asia IG bonds remain attractive, particularly for BBB issuers, aligning with our preference for carry and yield.

On Asia HY, we hold a constructive view, expecting modest spread compression. The anticipated decline in Asia credit defaults contributes to our expectation of gradual spread tightening. Consequently, we advocate increasing allocations to the HY space. Within this segment, we express positivity towards India HY Renewables, driven by favourable policy tailwinds, alternative funding access, and attractive relative valuations compared to regional peers. That said, detailed credit selection counts.

The activity in the credit primary market has picked up, compared to December. The overall tone remains positive on both the supply and demand sides, with issuers achieving small new issue concessions. Looking ahead, supply is expected to remain elevated as issuers are poised to tap the market opportunistically in the coming weeks. As we navigate these market dynamics, our outlook reflects a strategic approach to capitalise on emerging opportunities, while remaining attentive to evolving economic conditions and policy developments.

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