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 March

Asian credits performed well in March again. Returns were supported by interest accrual, lower US Treasury yields and spread compression for both investment grade (IG) and high yield (HY) credits. In March, JACI composite returned 1.1%, with the IG sub-index returning 0.9% and HY bonds returning 1.8%. Year-to-date, JACI composite has delivered 1.4% total return, mainly driven by the firm 6.8% total return of Asia HY credits.

JACI IG delivered a positive performance in March, in line with other regional markets – US and Europe IG, in USD terms. Stable fundamentals, attractive yields and limited supply had supported further compression of Asia IG credit spreads by 7 basis points (bps). Within Asian IG, all sectors provided positive returns. Following the smooth elections in February, Indonesian sovereign and quasi-sovereigns were amongst the top contributors for the month. Hong Kong Financials also performed well as demand for new issues was strong and led to repricing of the existing curves. In China, the National People's Congress meeting was a non-event as the major policy targets such as gross domestic product (GDP) growth and budget deficit were in line with expectations. March was also an eventful month for global central banks as the Bank of Japan (BoJ) ended the negative interest rate and yield curve control policies, while the Swiss National Bank was the first G10 central bank to cut rates. The new issue market picked up in March with diversified supply across sectors and countries amounting to USD 10.8 billion, bringing year-to-date supply to USD 40.6 billion. Supply was well absorbed although issuers tried to price close to or even tighter than the secondary curve.

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Asia HY registered its fifth consecutive month of positive returns, outperforming Global HY (1.2%) and US HY (1.1%) once again. Pakistan and Sri Lanka sovereigns were the key contributors to performance, given their significant presence within the HY index and positive developments over the month. Pakistan reached an agreement on the second and final review with the International Monetary Fund (IMF) on the IMF's USD 3 billion standby arrangement, having met all the targets set by the IMF. It was also announced that Pakistan and the IMF would commence negotiations in April for a new bailout programme. Sri Lanka saw progress on their debt restructuring as they drew close to finalising a six-year moratorium on debt with the Paris Club and India. Sri Lanka also reached a staff-level agreement with the IMF on the second review of the four-year Extended Fund Facility.

Macau Gaming performed well in March. Results for Q4 2023 were decent from a credit point of view, comfortably above breakeven levels, although below equity market expectations for some names. At the sector level, year-to-date gross Gaming revenue was more than 65% above Q1 2023. While valuations are tighter now, carry is still attractive and stable for the sector. The Chinese Real Estate sector also presented idiosyncratic opportunities, with the sector seeing modest positive returns. Within the sector, investors rotated towards the higher quality issuers as issuers reported earnings and sales at the national level remained weak. Given the rotation within the sector, some Chinese Real Estate issuers were among the top contributors for the month at the issuer level. The new issue market was active for Asia HY. Given the expected negative net supply for the year and strong investor demand, most deals were well absorbed. Hong Kong Additional Tier 1 bonds (AT1s) repriced tighter after a well-subscribed new issue, while there was even a short-dated Chinese Industrial new issue that was significantly oversubscribed.

## Portfolio Review

The Fund gained from the higher spread beta and duration as credit spreads continue to grind tighter. Our overweight in BBB and BB, while underweighting AAA, AA and A, delivered performance. Although the overweight in duration contributed, the 5-year versus 30-year US Treasury (UST) curve steepener detracted as the UST curve flattened instead. In terms of sector allocation, our overweight in Financials and Industrials, and our underweight in sovereign and quasi-sovereign, contributed positively.

We extended our long duration when UST 10-year yield reached 4.3%, while keeping the steepener bias. Although credit spreads remain at tight levels, we expect the positive technicals factor will argue against a large spread sell off. The all-in yield of the bonds continues to provide attractive carry for the portfolios.

## Market Outlook

Asia credit markets have performed well at the composite level on a year-to-date basis. We expect this to continue given favourable growth and inflation dynamics in the region, well-positioned credit cycle, as well as strong market technicals with expected negative net supply. While Asia IG spreads are fair at best, total yield level remains attractive versus historical average and should continue to attract buyers into the market. Limited supply in Asian IG space will limit the extension of spread widening should global risk sentiment turn. We do not see any near-term catalyst for aggressive spread widening and 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. The 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 still key to outperformance.

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

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