

# Allianz Income and Growth

## Monthly commentary

### Investment Objective

The Fund aims at long-term capital growth and income by investing in United States of America ("US") and/or Canadian corporate debt securities and equities.

### What Happened in October

Convertible securities finished higher in October, while equities and high yield bonds closed lower. The Q3 earnings season got off to a strong start, with most companies exceeding top- and bottom-line estimates and year-over-year earnings growth approaching double digits. Management commentary has been focused on positive credit conditions, strong artificial intelligence (AI) demand, favourable advertising traction, mixed consumer demand, China headwinds, and industrials/auto-related softness. On the economic front, the Q3 gross domestic product (GDP) growth was above trend, consumer confidence rose, employment data was balanced, and core inflation increased modestly. Against this backdrop, futures markets pared back rate cut expectations to 25 basis points (bps) for the November Federal Open Market Committee (FOMC) meeting, driving Treasury yields higher.

### Equities Market Environment

The S&P 500 Index returned -0.91% for the month.\*

Most sectors fell in October. Financials, Communication Services, and Energy were the top performing sectors, while Health Care, Materials, and Real Estate were the bottom performing sectors in the period.

Equity volatility was higher month-to-month with the VIX finishing at 23.16.\*

## Convertible Securities Market Environment

The ICE BofA US Convertible Index returned +0.84% for the month.^

Sector performance was mixed with Materials, Consumer Discretionary, and Technology outperforming, while Consumer Staples, Utilities, and Health Care underperformed.

Investment grade issues outperformed below-investment grade issues. Equity sensitive issues outperformed total return (balanced) and yield-oriented (busted) issues.

New issuance saw 7 issues priced, raising USD 9.6 billion in proceeds.^

## High-Yield Bond Market Environment

The ICE BofA US High Yield Index returned -0.55% for the month.^

Credit-quality subsector returns for the month^:

- BB rated bonds: -0.89%
- B rated bonds: -0.45%
- CCC rated bonds: +0.62%

Spreads narrowed to 288 bps from 303 bps, the average bond price fell to 95.72, and the market's yield rose to 7.51%.^

Most industries finished lower with Telecoms, Cable, and Transportation outperforming, while Packaging/Paper, Health Care, and Real Estate underperformed.

Trailing 12-month default rates finished the period at 1.39% (par) and 0.79% (issues).\*\*

New issuance saw 39 issues priced, raising USD 27.2 billion in proceeds.\*\*

## Portfolio Review

Despite convertible market strength, equity and high yield market weakness weighed on the overall portfolio.

Top contributors in the period were led by several semiconductor companies, including Nvidia that are seeing strong AI demand growth. A software company with bitcoin exposure advanced alongside the cryptocurrency. An alternative asset manager gained on mergers and acquisitions (M&A) news, an airframe manufacturer executed a well-received capital raise, several cruise lines reported better-than-expected earnings results, and a major US bank guided for higher interest income.

Top detractors in the period included Apple and Microsoft, both of which consolidated year-to-date gains, and several pharmaceutical holdings that declined on earnings-related concerns. An aerospace company fell despite raising guidance, and an automotive components manufacturer traded lower on production uncertainty. A health care diagnostics company expected to benefit from improving bioprocessing demand also underperformed. Other top detractors in the period were issues in financial services and clean energy.

Most option positions expired below strike and the portfolio was able to retain the set premiums.

Exposure increased the most in Financials, Materials, and Industrials, and decreased the most in Health Care, Technology, and Consumer Staples. Covered call option positioning decreased month-over-month.

### Market Outlook and Strategy

The easing cycle has begun, with the US Federal Reserve (Fed) cutting interest rates by 50 bps in September as inflation normalises and the labour market softens.

Apart from an accommodative shift in monetary policy, potential economic tailwinds include steady consumption, continued government spending, improving productivity, increasing capital expenditures, and the proliferation of AI. Risk to the economy may increase if these trends weaken. Other potential headwinds include escalating geopolitical tensions, prolonged labour market softening, deteriorating consumer sentiment, and continued manufacturing contraction.

In the short term, US equity volatility could increase due to labour disputes, foreign conflicts, and US elections. Over the intermediate term, the equity market could move higher on continued Fed easing and economic expansion, secular growth drivers, such as AI, and accelerating earnings growth or an earnings inflection from more companies. If economic growth or earnings growth fall short of expectations, the equity market could be challenged.

US convertible securities have an attractive asymmetric return profile, providing upside participation potential when stock prices rise and downside mitigation when stock prices fall. Higher debt financing costs have drawn issuers to the convertible market for coupon savings, resulting in accelerated new issuance at favourable terms and an expanded investment opportunity set with the desired risk/reward characteristics. While a change in market leadership is not certain, a sustained broadening of the equity market could be a positive development for the asset class.

The US high yield market, yielding over 7%<sup>^</sup>, offers the potential for equity-like returns but with less volatility. The market's attractive total return potential is a function of its discount to face value and higher coupon, which also serves to cushion downside volatility. Credit fundamentals are stable, near-term refinancing obligations remain low, and management teams continue to exercise balance sheet discipline. Given these factors, the default rate has been below the long-term average with expectations for it to trend towards the historical average in 2025. Regarding credit spreads, they can stay tight for many years. This was the case in the mid-1990s and 2000s – periods like today when high yield balance sheets were healthy and defaults were low, the economy was stable, and interest rates were elevated.

A covered call options strategy can be utilised to generate premium income. In periods of elevated or rising equity volatility, premiums collected may translate into more attractive annualised yields.

Collectively, these three asset classes can provide a steady source of income and a compelling “participate-and-protect” return profile.

The Fund is a client solution designed to provide high monthly income, the potential for capital appreciation, and less volatility than an equity-only fund.

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All data are sourced from Allianz Global Investors dated 31 October 2024 unless otherwise stated.

\* Source: FactSet, as at 31 October 2024

^ Source: BofA Merrill Lynch, as at 31 October 2024

\*\* Source: J.P. Morgan, as at 31 October 2024

^^ Source: ICE Data Services, as at 31 October 2024

Allianz Global Investors and Voya Investment Management (Voya IM) have entered into a long-term strategic partnership, and as such, as of 25 July 2022, the investment team transferred to Voya IM and Voya IM became the delegated manager for this fund. AllianzGI continues to provide information and services to Voya IM for this investment through a transitional service agreement.

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