Allianz Global Investors

Allianz Select Income and Growth

Monthly commentary

Investment Objective

The Fund aims at long term capital growth and income by investing in investment grade corporate Debt Securities and Equities of US and/or Canadian Equity and Bond markets.

What Happened in July

Equity, convertible, and investment grade bond markets finished higher in July despite a tangible increase in volatility. The Q2 earnings season got off to a solid start with most companies exceeding top- and bottom-line estimates and year-over-year earnings growth approaching double digits. Cost controls, operating efficiencies, increasing capital expenditures and steady consumption factored into better-than-expected results. Corporate management outlooks varied, however. Economic reports were also mixed. Q2 gross domestic product (GDP) growth, retail sales, and monthly payrolls surpassed forecasts, and inflation gauges continued to ease. Conversely, manufacturing remained in contractionary territory, home sales missed estimates, and weekly jobless claims moved higher. Against this backdrop, the US Federal Reserve (Fed) kept interest rates unchanged at the July Federal Open Market Committee (FOMC) meeting, but Chair Jerome Powell noted if economic data continues on its current path, “a reduction in our policy rate could be on the table as soon as the next meeting in September”.

Equities Market Environment

The S&P 500 Index returned +1.22% for the month.*

July saw a rotation in sector leadership, with Real Estate, Utilities, and Financials the top performing sectors in the period, while Communication Services, Technology, and Consumer Discretionary were the bottom performing sectors.

Equity volatility was higher month-to-month, finishing at 16.36.*

Convertible Securities Market Environment

The ICE BofA US Convertible Index returned +1.93% for the month.^

Convertible securities were positively impacted by rising stock prices.

Most sectors closed higher with Materials, Energy, and Utilities outperforming, while Consumer Staples, Technology, and Transportation underperformed.

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

New issuance saw 5 issues priced, raising USD 2.0 billion in proceeds.^

Investment Grade Corporate Market Environment

The ICE BofA US Corporate Index returned +2.36%, outperforming the shorter-dated ICE BofA 1-10 Year US Corporate Index which returned +1.99%.**

Credit-quality subsector returns for the month**:

- AAA rated bonds: +2.59%
- AA rated bonds: +2.36%
- A rated bonds: +2.37%
- BBB rated bonds: +2.36%

Spreads widened to 97 basis points (bps) from 96 bps, the average bond price rose to 93.62, and the market's yield fell to 5.22%.**

Gross new issuance for the period was USD 120.3 billion.^

The 10-year US Treasury returned +2.88%.^ The note's yield fell to 4.05%, compared to 4.37% the prior month.^

Portfolio Review

Top contributors in the period included Apple and a major electric vehicle (EV) manufacturer, both of which rallied after providing better-than-expected read-throughs on production and demand. An aerospace company reported a beat-and-raise quarter driven by strong free cash flow, an industrial conglomerate outperformed across all business segments and appointed a well-received new CEO, and a cellular tower REIT boosted its outlook for organic growth in several key end markets. Holdings in software, residential solar, and consumer finance all gained after reporting earnings growth that exceeded expectations. A utility operator and a clean energy company were also top contributors.

Top detractors included technology companies capitalising on secular trends around artificial intelligence (AI) and cloud migration, including Microsoft, Amazon, and a technology conglomerate, as well as several semiconductor companies led by Nvidia. A medical device manufacturer sold off on declining procedure volumes, and competitive concerns pressured a pharmaceutical company. The other top detractors in the period were a restaurant chain and a design software holding company.

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

Exposure increased in Industrials and Real Estate, and decreased the most in Health Care, Technology, and Consumer Discretionary. Covered call option positioning increased month-over-month.

Market Outlook and Strategy

2023's economic momentum has carried over into 2024. Economic tailwinds include a healthy labour market, steady consumption, government spending, elevated household net worth, an end to the rate hike cycle, and accelerating earnings. Economic headwinds include persistent inflation, restrictive monetary policy, prolonged yield curve inversion, less personal savings, and US/international political risks, among others.

US equity valuations reside near long-term averages. Visibility around 2024 and 2025 earnings, US dollar and Treasury market stabilisation, and an end to the rate hike cycle could be positive developments for stocks. Any equity market volatility will present opportunities for active managers to take advantage of better prices in attractive investments.

US convertible securities should continue to provide benefits to investors, including an attractive asymmetric return profile and potentially lower volatility relative to the equity market. The shift in the universe's composition exiting 2022 remains largely unchanged heading into 2024. Many securities offer attractive current yields and exhibit defensive characteristics given lower deltas and closer proximities to bond floors. This dynamic may allow for greater downside protection if equity volatility rises. If the prices of underlying stocks advance, convertible securities could be positioned to participate in the upside. Lastly, higher debt financing costs should draw issuers to the convertible market for coupon savings. As a result, new issuance is expected to increase materially year-over-year.

US investment grade corporate bond's risk/reward opportunity is also compelling. Rising interest rates are a risk for high grade corporates, however the investment opportunity remains attractive given higher coupons and yields, and a positive fundamental outlook with limited default risk. The asset class trades at a discount to par, offering compelling total return potential and downside cushioning.

A covered call options strategy can be utilised to help 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 help 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.

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

* Source: FactSet, as at 31 July 2024

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

** Source: ICE Data Services, as at 31 July 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.