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 March

Equity, convertible, and high yield markets advanced in March. With the Q4 earnings season winding down, investors focused on economic data and monetary policy. The labour market remained healthy, the services sector stayed in expansionary territory, and consumer sentiment increased. In contrast, the manufacturing sector contracted, and some inflation measures were higher than anticipated. The US Federal Reserve (Fed) kept rates unchanged at March's Federal Open Market Committee (FOMC) meeting, with Chair Jerome Powell suggesting policy easing "at some point this year".

Equities Market Environment

The S&P 500 Index returned +3.22% for the month, marking the fifth consecutive month of gains.*

The market broadened with all 11 sectors finishing higher. Energy was the best performing sector, followed by Utilities and Materials. Consumer Discretionary was the worst performer, followed by Real Estate and Information Technology.

Equity volatility was lower month-to-month, finishing at 13.01.*

Convertible Securities Market Environment

The ICE BofA US Convertible Index returned +2.32% for the month.^

Convertible securities were positively impacted by rising stock prices and credit spread tightening.

Most sectors finished higher with Energy, Consumer Discretionary, and Industrials outperforming, while Materials, Transportation, and Telecom underperformed.

Below-investment grade issues outperformed investment grade issues. Total return (balanced) issues outperformed yield alternative (busted) and equity sensitive issues.

New issuance increased month-over-month with 17 issues priced, raising USD 10.4 billion in proceeds.^ March's monthly volume was the largest in three years.

Investment Grade Corporate Market Environment

The ICE BofA US Corporate Index returned +1.19%, outperforming the shorter-dated ICE BofA 1-10 Year US Corporate Index which returned +0.90%.**

Credit-quality subsector returns for the month**:

- AAA rated bonds: +1.22%
- AA rated bonds: +1.05%
- A rated bonds: +1.11%
- BBB rated bonds: +1.28%

Spreads narrowed to 94 basis points (bps) from 100 bps, the average bond price increased to 92.59, and the market's yield fell to 5.41%.**

Gross new issuance decreased month-over-month to USD 143.8 billion.^

The 10-year US Treasury returned +0.63%.^ The note's yield fell to 4.21%, compared to 4.24% the prior month.^

Portfolio Review

The portfolio was positively impacted by strength across risk assets and safe havens.

Top contributors were led by semiconductor holdings, including a technology company that designs graphics processing units which unveiled a new artificial intelligence (AI) processor, and a memory chip manufacturer that reported a beat-and-raise quarter. An industrial conglomerate gained on potential spin-off benefits, and a technology conglomerate was higher on AI licensing agreement headlines. A major US bank and an insurance company advanced on margin improvement optimism. An energy producer was higher alongside crude oil and a clean energy company traded up on power consumption forecasts. Other contributors included Amazon and a financial exchange.

Top detractors were led by companies navigating slower end markets for electric vehicles (EVs) and consumer electronics. Multiple software positions underperformed on sales growth fears and production outlook concerns weighed on an airframe manufacturer. A railroad operator, a payment processing company, and a technology company also underperformed.

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

Exposure increased the most in Consumer Staples, Communication Services, and Materials, and decreased the most in Consumer Discretionary, Technology, and Industrials. Covered call option positioning increased month-over-month.

Market Outlook and Strategy

2023's economic momentum has carried over into 2024. Economic tailwinds include low unemployment, steady consumption, government spending, waning inflation, a stabilising manufacturing sector, an end to the rate hike cycle, and accelerating earnings. Economic headwinds include continued restrictive monetary policy and quantitative tightening, less 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 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.

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

* Source: FactSet, as at 31 March 2024

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

** Source: ICE Data Systems, as at 31 March 2024