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 October

Convertible securities finished higher in October, while equities and Investment grade 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.*

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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.^

Investment Grade Corporate Market Environment

The ICE BofA US Corporate Index returned -2.25%, underperforming the shorter-dated ICE BofA 1-10 Year US Corporate Index which returned -1.45%.**

Credit-quality subsector returns for the month**:

- AAA rated bonds: -3.34%
- AA rated bonds: -2.56%
- A rated bonds: -2.32%
- BBB rated bonds: -2.10%

Spreads narrowed to 86 bps from 92 bps, the average bond price fell to 93.58, and the market's yield rose to 5.22%.**

Gross new issuance for the period was USD 97.6 billion.^

The 10-year US Treasury returned -3.58%.^ The note's yield rose to 4.28% compared to 3.79% the prior month.^

Portfolio Review

Despite convertible market strength, equity and investment grade 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, and an airframe manufacturer executed a well-received capital raise. A cruise line reported better-than-expected earnings results, a major US bank guided for higher interest income, and a live entertainment company rallied on optimism around core business trends.

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 a residential solar provider traded lower on mixed quarterly results. 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 Industrials, Financials, and Materials, and decreased the most in Technology, Health Care, and Consumer Discretionary. 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.

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 October 2024 unless otherwise stated.

* Source: FactSet, as at 31 October 2024

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

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

Allianz Global Investors and Voya Investment Management have entered into a long-term strategic partnership, and as such, as of 25 July 2022, the investment team transferred to Voya Investment Management. This did not materially change the composition of the team, the investment philosophy nor the investment process. Management Company: Allianz Global Investors GmbH. Delegated Manager: Voya Investment Management Co. LLC ("Voya IM").

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