Allianz Global Investors

Allianz Dynamic Asian High Yield Bond

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth and income by investing in high yield rated debt securities of Asian bond markets.

What Happened in October

Asian credit markets corrected in October, moving in step with the steep rise in US Treasury rates, as expectations for policy rate cuts were tempered down following the continued strong economic data released in the US. In contrast, China announced further stimulus measures that boosted broad market sentiments. Amidst this backdrop, Asian credit (JP Morgan Asia Credit Index composite) gave up some of its previous gains, correcting 1.0% in October. Investment grade (IG) credits suffered the bulk of the US Treasury correction – declining 1.3% over the month despite tighter IG credit spreads. High yield (HY) credits outperformed, delivering positive returns of 1.1%, driven by their high carry and tighter HY credit spreads, while the short duration nature of the asset class mitigated the negative Treasury impact. Year-to-date, Asian credit has delivered 6.1% in total return, with performance driven mainly by spread return (+4.1%) and to a smaller extent, Treasury return (+1.9%). Asian HY continued to be the stellar outperformer, with an outstanding return of 16.0%, significantly outperforming other regional HY markets.

Asian HY delivered another month of firm performance, with credit spreads tightening by 58 basis points (bps), which more than compensated for the spike in US Treasury rates. Most market sectors were in positive territory, with Sri Lanka and China clearly dominating the gainers.

In Sri Lanka, the market was buoyed by better developments on the political front as the new government continued to be more pragmatic than initially feared. The country also announced that the long awaited USD 12.5 billion sovereign debt exchange will be launched as early as November, with the aim of completion by Q4. This would allow Sri Lanka to climb out of default sooner than expected.

The China Real Estate sector also saw strong gains as Chinese authorities announced further policies that demonstrated their resolve to stabilise the sector and broader economy. The Ministry of Finance initially announced broad measures to reduce housing inventory, capitalise state-owned enterprise (SOE) banks and alleviate local government debt. This was followed by subsequent news from the Chinese government that a sum of at least RMB 10 trillion over the next few years was being considered. Further measures were also announced, which included widening of the "whitelist" of housing projects eligible for financing, removal of more home purchase and sale restrictions, as well as reduced mortgage and down payment rates. The Ministry also highlighted in a statement that the bottoming out of the property market has begun.

Portfolio Review

The Fund returned positively, underperforming its benchmark.

The Fund's overweight exposure to the China Real Estate sector was a positive contributor to relative performance, as the sector was buoyed by additional support measures announced by the Chinese government on support measures. Macau detracted slightly from performance due to profit taking after a strong run. Security selection was again the major positive driver of active returns.

Market Outlook

Major global central banks excluding Japan have begun their respective rate cut cycles. While the terminal rates are still data-dependent and evolving, the downward trajectory in rates is clear and supportive for credits as an asset class. In the short to medium term, the key event risk is the US elections and the potential changes to policies.

Within Asia, we remain sanguine about Asian credit with the continued positive headlines from China. As market sentiment continues to be buoyant and excited by the new policy support from China, we think that credit spreads can continue to grind tighter. However, we do feel that most of the returns from Asian credits would likely come from lower rates and yield carry, which is still decent.

On Asian HY credits, we continue to favour Asian HY, given the wider credit spreads, as well as stable to improving fundamental outlook. Asian HY is also relatively more idiosyncratic and less prone to geopolitical concerns. Given the strong performance of the asset class, prudent credit selection remains key for outperformance.

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