Allianz Global Floating Rate Notes Plus

Monthly commentary

Investment Objective

The Fund aims to capture income from a global universe of floating-rate notes. The Fund seeks potential long-term capital growth in accordance with the Sustainable and Responsible Investment Strategy (SRI Strategy).

What Happened in September

In September, global investment grade corporate spreads tightened -2 basis points (bps) to 100 bps (USD unchanged at 92 bps, EUR +1 bps to 117 bps, and GBP +1 bps to 121 bps) versus government bonds and generated +35 bps of excess returns. During September the US Federal Reserve's (Fed's) 50-bps rate cut provided a boost to markets pushing equity markets to highs and causing credit spreads to tighten. The cut was much anticipated albeit higher than expected with Powell cooling any market speculation that this was the new normal but a "recalibration" towards target rates. Meanwhile, in the UK, the Bank of England (BoE) held interest rates at 5% after consumer price index (CPI) remained a bit stickier than expected in August but indicated it may lower rates again as soon as November. In China, economic stimulus announcements led to the best week for Chinese equities since 2008, with the CSI 300 up +15.7%. The People's Bank of China (PBoC) introduced several measures including a cut in the required reserve ratio and a reduction in the reverse repo rate, alongside mortgage rate cuts and relaxed rules for second-home purchases. Additionally, the Chinese Politburo has vowed to intensify fiscal efforts, which should support the property sector and boost domestic consumption.

Lower rates could prove to be supportive for some industries, namely the Real Estate sector. The sector has performed strongly over the month and with future funding costs on the decline, we would expect good performance from the sector over the next few quarters. Risks have risen in the eurozone area as weak purchasing managers' indices (PMIs, 48.9 versus 50.5 expected) have raised questions on the economic strength of the region as both Germany and France reported flash PMIs below 50. Elsewhere in the region, weak demand, especially from China, has led to profit warnings from some of the auto companies causing for further concerns in the region.

Turning to primary, in the US there was record issuance of USD 179.8 billion, taking the year-to-date total in excess of USD 1.35 trillion, surpassing the USD 1.2 trillion yearly estimates and is over 30% above the same point last year. In Europe, this month's issues stood at EUR 103 billion, seeing a sharp rebound in almost all asset classes and has only been surpassed by September 2019 and 2021, with year-to-date issuance now at the EUR 800 billion mark.

Portfolio Review

The Fund generated positive gross return in September, slightly ahead of its cash reference index, secured overnight financing rate (SOFR). Positive absolute performance was generated by attractive underlying yields inbuilt within the Fund, with SOFR at 4.96% by the end of the period.

Portfolio activity was somewhat limited in September with overall portfolio risk remaining broadly unchanged, while we remained focused on alpha generation through issuer and sector selection, as well as harvesting new issue premiums. Of note was our addition of a global bank's short call, seasoned, preferreds that offer an attractive yield in our view.

We also used the outperformance of a streaming media company's USD denominated paper as an opportunity to switch into the issuer's EUR paper, reversing the switch performed in July. The trade helps illustrate the advantages of the global, multi-currency nature of the Fund's investment universe, and cross currency benefits of the approach.

We note that we are increasingly cautious on the Automotive sector, given the continued challenges of the sector associated with deteriorating demand, shifting Chinese consumer spending preferences (towards domestic demand), and structural challenges associated with the shift to battery electric vehicles (BEVs). However, we believe that the Fund remains well positioned in the context, with a preference for issuers focused on the Truck sector (such as a heavy-duty truck manufacturer), higher quality issuers (such as a Japanese carmaker), or issuers with more limited exposure to China (such as a US automobile manufacturer).

Outlook

The strong technical support of elevated all-in yields remains in place despite the 50-bps rate cut in September, in our view. Additionally, we note that the rate cutting cycle should lead to switching out of money market funds, which we expect to be supportive for the credit positioning of the Fund.

We continue to think that the floating rate note space is attractive and have seen continued demand for floating paper associated with the inverted yield curve.

We consider the global corporate market to be at fair value, as the market is pricing in strong fundamentals across the majority of sectors, as evidenced by the recent earnings season, but also discounting future growth concerns. Generally, we continue to favour financial issuers given the benefits associated with the elevated interest rate environment and attractive valuations relative to industrial issuers, while acknowledging the recent compression make this less attractive, at the margin. Consistent with this, we prefer moving up the capital stack in Financial issuers. Additionally, we continue to like the defensive nature of US regulated Utilities.

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All data are sourced from Bloomberg Barclays, Bloomberg and Allianz Global Investors as of 30 September 2024 unless otherwise stated.