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 February

Markets were mixed in February, as investment grade bonds closed higher while equities and convertible securities finished lower. Q4 earnings momentum persisted, with approximately three-quarters of companies topping bottom-line consensus estimates, while corporate guidance remained mixed as managements await clarity around the new administration's policies. Except for a key manufacturing survey and unemployment, both of which were better than expected, economic data generally underwhelmed. Services, retail sales, consumer confidence, and select inflation measures missed estimates. Against this backdrop, the 10-year US Treasury yield fell sharply.

Equities Market Environment

The S&P 500 Index returned -1.30% for the month.*

Sector performance was mixed in February. Consumer Staples, Real Estate, and Energy were the top performing sectors, while Consumer Discretionary, Communication Services, and Industrials were the bottom performing sectors in the period.

Equity volatility was higher month to month with the VIX finishing at 19.63.*

Convertible Securities Market Environment

The ICE BofA US Convertible Index returned -1.99% for the month.^

Sector performance skewed negative in February. Telecommunications, Utilities, and Media outperformed, whereas Consumer Staples, Technology, and Industrials underperformed.

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

Monthly new issuance saw 8 issues priced, raising USD 5.3 billion in proceeds.^

Investment Grade Corporate Market Environment

The ICE BofA US Corporate Index returned +2.03%, outperforming the shorter-dated ICE BofA 1-10 Year US Corporate Index which returned +1.39%.**

Credit-quality subsector returns for the month**:

- AAA rated bonds: +2.60%
- AA rated bonds: +2.15%
- A rated bonds: +2.00%
- BBB rated bonds: +2.01%

Spreads widened to 88 basis points (bps), the average bond price rose to 94.19, and the market's yield fell to 5.13%.**

Gross new issuance for the month was USD 157.8 billion.^

The 10-year US Treasury returned +3.09%.^ The note's yield fell to 4.20% compared to 4.55% the prior month.^

Portfolio Review

The portfolio moved lower in the month as equity and convertible holdings offset strength in investment grade bonds.

Top contributors included Nvidia which reported a strong beat-and-raise quarter. Apple and an ecommerce conglomerate gained after announcing a strategic partnership. A health care real estate investment trust (REIT) advanced after boosting 2025 guidance, several pharmaceutical companies gained on strong long-term demand prospects, and a utility operator was higher on execution optimism of its long-term capital plan. The other top contributors were Wells Fargo, a cellular provider, and a consulting company.

Top detractors included Microsoft and an internet services company, both of which were impacted by weaker-than-expected cloud growth, as well as Amazon on cautious guidance. Delivery and margin concerns weighed on an electric vehicle manufacturer, and a semiconductor company consolidated strong 2024 gains. An alternative asset manager fell after forecasting near-term insurance business headwinds. The other top detractors were a health care provider on legal scrutiny, a software company with bitcoin exposure, and a cruise line operator that offered a conservative forecast.

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

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

Market Outlook and Strategy

Macro factors, including newly implemented tariffs and government efficiency initiatives, could weigh on consumer spending and delay corporate investment in the near term as households and companies await clarity around current and future policies. A growth slowdown would not be unexpected if these headwinds materialise. The recent increase in equity volatility likely reflects the possibility of downward revisions to short-term earnings growth estimates.

The US economy should continue to expand in 2025, supported by earnings growth, further US Federal Reserve (Fed) easing as inflation and the labour market continue to normalise, and the new administration's pro-US growth policies.

Apart from these factors, steady consumer spending, ongoing services sector expansion, continued fiscal spending, and improving productivity aided by the proliferation of artificial intelligence (AI) are growth tailwinds. Risk to the economy may increase if these trends weaken. Other considerations include tariff and immigration policies, geopolitical tensions, prolonged labour market softening, continued manufacturing contraction, and economic weakness outside of the US.

Against this backdrop, low- to high-single-digit returns in 2025 are possible for large-cap equities, convertible securities, and investment grade bonds. The equity market's path will not be linear, with bouts of volatility probable throughout the year. Given their defensive characteristics, investment grade bonds and convertible securities can mitigate market volatility better than equities.

The equity market could benefit from continued economic growth and accelerating or inflecting earnings from more companies. Secular growth themes, such as AI, lower taxes, increased mergers and acquisitions (M&A) activity, deregulation, productivity gains, and share buybacks are also catalysts. If either economic growth or earnings growth fall short of expectations, the equity market could be challenged. Valuations will continue to be debated.

US convertible securities have a favourable asymmetric return profile, providing upside participation potential when stock prices rise and downside mitigation when stock prices fall. The asset class may outperform the broad equity market if leadership broadens, and new issuance remains steady. USD 60-65 billion[#] of new issuance is expected in 2025 due to coupon savings demand, elevated refinancing needs, and a positive outlook for price appreciation among small- and mid-cap companies. Aside from diversification benefits, new issuance expands the opportunity set of investments with favourable terms and the desired risk/reward characteristics.

US investment grade corporate bond's risk/reward opportunity is favourable. Rising interest rates are a risk for high grade corporates, however the investment opportunity remains favourable given higher coupons and yields, and a positive fundamental outlook with limited default risk. The asset class trades at a discount to par, offering favourable total return potential and downside cushioning. If the 10-year US Treasury yield finishes 2025 near the lower bound of the expected range of 3.5-4.5%, the asset class return could exceed mid-single digits.

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 favourable annualised yields.

Collectively, these three asset classes can help provide a steady source of income and a favourable "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.

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All data are sourced from Allianz Global Investors dated 28 February 2025 unless otherwise stated.

* Source: FactSet, as at 28 February 2025

^ Source: BofA Merrill Lynch, as at 28 February 2025

** Source: ICE Data Services, as at 28 February 2025

Source: BofA Research, as at 28 February 2024