Allianz Global Investors

Allianz US Short Duration High Income Bond

Monthly commentary

Investment Objective

The Fund aims at long-term income and lower volatility by investing in short duration high yield rated corporate debt securities of US bond markets in accordance with environmental and social characteristics.

What Happened in January

High yield bonds finished higher in January. The Q4 earnings season got off to strong start. About one-third of the way through, nearly 80% of S&P 500 companies have surpassed bottom-line estimates with the index on pace to deliver double-digit (year-over-year) earnings growth for a fifth consecutive quarter. Geopolitical developments were volatile surrounding Venezuela, Greenland, and Iran, though markets broadly looked through the noise. Economic data underscored a resilient backdrop with firm labour and services indicators, offset by softer consumer confidence and weak housing activity. The US Federal Reserve (Fed) held rates steady as expected and markets priced in roughly 50 basis points (bps) of cumulative cuts by year-end. Additionally, President Trump nominated Fed Governor Kevin Warsh as the next head of the central bank. Against this backdrop, markets saw large rotations – including into cyclicals and small caps – and the 10-year US treasury yield rose to 4.26%.*

The ICE BofA US High Yield Index returned +0.48% for the month.*

Credit-quality subsector returns for the month*:

- BB rated bonds: +0.50%
- B rated bonds: +0.50%
- CCC rated bonds: +0.25%

Spreads widened to 288 bps from 281 bps, the average bond price rose modestly to 98.09, and the market's yield rose to 7.12%.*

Industry performance was mostly higher as Energy, Telecoms, and Chemicals outperformed, while Packaging/Paper, Technology, and Services underperformed.

Trailing 12-month default rates finished the period at 1.97% (par) and 1.40% (issues).^ The upgrade/downgrade ratio was steady at 1.1.^

Monthly new issuance saw 41 issues priced, raising USD 30.0 billion in proceeds.^ High yield funds reported estimated net flows of -USD 1.3 billion.^

Portfolio Review

Industries contributing the most to performance were Energy, Support-Services, and Retail. Strength in Energy was primarily attributable to an issuer in petroleum refining, with additional contribution from issues in midstream logistics. Within Support-Services, an issuer in building products drove performance. Multiple issues from an automotive retailer had a positive impact on performance in Retail.

Financial Services and Technology were the sole detractors from performance in the period. Within Financial Services, a payments issuer was the primary source of weakness. A financial data software company detracted the most from performance in Technology.

Liquidity remained in focus to pay distributions, meet redemptions and to take advantage of reinvestment opportunities. Transactions in the period included new purchases in Passenger Airlines and Oil & Gas Storage & Transportation, and a complete sell in Cable & Satellite.

Market Outlook

2026 US economic growth could surpass that of 2025. Potential tailwinds include stimulus from the One Big Beautiful Bill Act (OBBBA – tax cuts/refunds and capital spending acceleration), foreign direct investment from overseas, continued monetary policy easing (including the recently announced asset purchase programme), and steady consumption. Reshoring activity, less regulation, expanding credit, and a rebound in consumer and business confidence are also potential drivers. Improvements in the housing and/or manufacturing sectors could aid growth as well. Key economic risks include heightened geopolitical tensions and elevated fiscal deficits globally. Additionally, if unemployment and/or inflation rise sharply, the odds of an economic slowdown increase.

In an environment where changes in the labour market and prices are more muted, the Fed can continue to target a neutral policy position. Currently, market odds suggest additional interest rate cuts to a range of 3.00-3.25% – a level that is consistent with the Fed's median, longer run projection of 3%.

The US high yield market, yielding more than 7%**, offers equity-like returns but with less volatility. The asset class is expected to deliver another year of coupon-like returns in 2026. The market's attractive total return potential is a function of its discount to face value and higher coupon, which also serves to cushion downside volatility. Credit fundamentals are stable, near-term refinancing obligations remain low, and management teams continue to exercise balance sheet discipline. Additionally, the market's credit quality composition has improved. In this environment, new issuance is expected to remain steady, spreads can stay tight, and the default rate should continue to reside below the historical average.

Longer-duration issues are the most likely to be impacted by high and volatile rates, but the overall high yield market should have a dampened response due to its larger coupon relative to other fixed income alternatives. As a result, US high yield bonds contribute from both a diversification and a relative performance perspective, offering a very compelling yield opportunity.

The strategy remains an attractive fixed income solution without taking excess credit risk, the shorter maturity puts securities first in line to repayment at par, and the Fund lessens price volatility that may be highly amplified in passively managed strategies.

All data are sourced from Allianz Global Investors, S&P Dow Jones Indices and FactSet, dated 31 January 2026 unless otherwise stated.

* Source: BofA Merrill Lynch, as at 31 January 2026

^ Source: J.P. Morgan, as at 31 January 2026

** Source: ICE Data Services, as at 31 January 2026

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