BlackRock Global Bond

Quarterly Investment Option Update

30 June 2022

Aim and Strategy

To generate capital and income return for investors seeking exposure to international fixed income markets, including Australia. The option aims to outperform the Bloomberg Barclays Global Aggregate Index (Australian dollar hedged) over rolling three-year periods. The option invests predominantly in international debt securities and foreign currency exposures. These include a broad universe of investment instruments, including fixed interest securities, mortgage securities, asset-backed securities, derivatives, repurchase agreements, stock lending and units in pooled investment funds.

Investment Option Performance

To view the latest investment performances for each product please visit amp.com.au/performance

Investment Option Overview

Investment Category	Global Fixed Interest
Suggested Investment timeframe	2 years
Relative risk rating	5 / Medium to high
Investment style	Core
Manager style	Single Manager

Asset Allocation	Benchmark (%)	Actual (%)
International Fixed Interest and Cash	100	100

Sector Allocation	%
Government	29.78
Corporate	34.33
Securitised	35.04
Other	0.86

Regional Allocation	%
UK	3.97
Europe (ex UK)	21.17
North America	57.23
Japan	2.82
Asia (ex Japan)	8.10
Other*	6.71

*includes EM exposure and Cash

Quality Allocation	%
AAA	34.34
AA	13.31
A	24.05
BBB	22.71
BB>	2.99
Not Rated/Cash	2.61

Portfolio Summary

After a strong 2021, risky assets struggled in the first quarter of 2022. Russia's invasion of Ukraine in February caused a global shock and markets tumbled as investors assessed the potential economic impact of the situation. Commodity prices soared to extreme levels given that Russia is a significant exporter of several key commodities, including oil, gas and wheat, exacerbating the surge in inflation as well as supply chain disruptions. At the start of this year, the narrative that inflation was transitory started to shift and over the quarter, central banks gradually became more hawkish and financial markets started to price in a faster pace of policy normalization. Developed market government bond yields edged sharply higher over the period, with US treasury yields seeing one of its worst selloffs on record. The extent of upward yield moves varied across markets and were less pronounced in Europe and the UK. Elsewhere, renewed Covid outbreaks in China led to lockdowns in some major cities with case numbers spiking to their highest levels since the beginning of the pandemic.

In the US, the Federal Reserve's (Fed) raised the target rate by 0.25% in March, as expected. The Fed made it clear that further increases will be appropriate and signaled a strong lean toward bringing inflation lower from current elevated levels, as it indicated a desire to move monetary policy into restrictive mode. The median dot plot showed seven hikes this year and four next year, with the policy rate rising to 2.8% in 2023 - above the neutral policy rate estimate of 2.4%. The Fed also indicated balance sheet runoff could commence at the next meeting, as it looks to reduce the size of its inflated $9 trillion balance sheet. Consumer sentiment worsened over the quarter in reaction to higher prices, hitting a low since 2011. However, the labour market appeared one of strength - the US added 431,000 jobs in March and the unemployment rate moved sizably lower from 3.8% to 3.6%, while average hourly earnings increased 5.6% year-on-year. Furthermore, February job openings moved back to their second highest level, reflecting labour market tightness.

In Europe, the European Central Bank (ECB) delivered a hawkish message, opting to taper asset purchases. The plan indicated €40 bn of net purchases in April, €30 bn in May and €20 bn in June, with net purchases potentially ending in Q3. President Christine Lagarde also left the door open to a first rate hike by the end of this year, that could arrive "some time after" the end of asset purchases. Separately, sentiment surveys in Europe following Russia's invasion of Ukraine reflected a downbeat assessment of economic conditions – the German ZEW survey collapsed a record 93.6 points to -39.3 in March, from 54.3 in February. Elsewhere, the Bank of England (BoE) raised rates twice over the quarter, aiming to curb inflation that it now expects to reach 8% in Q2, in part due to the Russia-Ukraine crisis. In addition, the Bank of Japan (BoJ) reaffirmed its dovish stance by opting to continue quantitative and qualitative easing plans, as well as yield curve control, with the aim to achieve a price stability target of 2%.

Developed market government bond yields shifted higher in response to hawkish signals from central banks. Yield increases were most notable at the short end, where yields are more sensitive to changes in monetary policy. The US 2-year treasury yield rose from 0.73% to 2.33% and the 10-year from 1.51% to 2.34%. The German equivalent rose from -0.62% to -0.07% and from -0.18% to 0.55% respectively. Corporate bonds delivered negative total returns and wider spreads. Spreads in the high yield market widened more than investment grade, however high yield saw less negative total return owing to higher income. Emerging market hard currency debt also underperformed over the period, while local currency debt was slightly more resilient. In currency markets, the strongest performers were the commodity-orientated Australian dollar and New Zealand dollar, while the Japanese yen hit a 7-year low (vs the US dollar). Commodities outperformed driven by higher energy prices, helped by tight inventory and supply risks, brent oil started the quarter at $87 a barrel and ended at $108 a barrel, with an intra-quarter peak of $128.

Investment Option Commentary

The Fund underperformed its benchmark over the quarter driven by the Fund's credit and emerging market strategies.

Within credit strategies, the main detractors were the Fund's overweight allocations to securitized assets, predominantly through US CMBS in February. The Fund's overweight to USD and EUR denominated investment grade industrials, select high yield names, as well as USD denominated investment grade financials further detracted from performance. Negative performance was partially offset by the Fund's underweight allocation to EUR investment grade financials and utilities and the Fund's overweight exposure to US ABS within securitized assets.

Emerging market strategies posted negative returns over the quarter, led by the Fund's overweight allocation to emerging market hard currency debt. The Fund's modest long in the Russian ruble detracted in February, as did the overweight to Mexico and Indonesia and local currency government bonds. This was partially offset by the Fund's overweight to China local currency government bonds and its long position in the Mexican peso.

Macro rates strategies ended the period with positive returns, driven by the Fund's underweight exposure to US, which added consistently over the period. The Fund's underweight exposure to Germany, Italy, France, and UK duration also added. In addition, the Fund's yield curve positioning in Canada and Australia added, as did its overweight exposure to US inflation-linked bonds. Positive performance was partially offset by the Fund's yield curve positioning in the US, Germany, and the UK, as well as its overweight to Spain, Greece, Australia and Canada duration. Furthermore, the Fund's underweight to UK inflation-linked bonds and overweight exposure to eurozone inflation-linked bonds detracted, as did its underweight to Japan duration.

The Fund's developed market active currency positions posted modestly positive returns, with the main contributor being its short euro position. In addition, the Fund's short position in the Swedish krona and Japanese yen added to performance, while its long position in the US dollar and short in the Canadian dollar detracted.

Outlook

The Ukraine war has aggravated inflation pressures and put central banks across the globe in a difficult position. Blackrock expects central banks to quickly normalize their policy stance, with rates rising from historically low levels. However, trying to contain inflation might be costly to growth and employment and it will be difficult for central banks and governments to cushion the negative growth shock.

In the US, the recent solid growth of payrolls checked the box for the Fed in its drive toward fighting inflation - although the inflation-drivers today are largely supply-driven shocks exacerbated by the war in the Ukraine and particularly the impact on energy markets, and more recently on food/fertilizer supply.

Consequently, in defining the line on monetary policy, the Fed looks clearly committed in reaching at least policy neutrality, if not potentially policy rate levels beyond that point. Blackrock thinks the Fed will make at least one – and maybe two – 50 basis point rate hikes by the June FOMC meeting, which could even include an inter-meeting hike. This does not surprise us as it would build in some room to adjust policy easier in the future - if necessary - and would help suppressing inflationary conditions. However, going much further on tightening, including reducing liquidity within the system, could create instability in the market.

In terms of portfolio positioning, when deciding the asset allocation, amidst so much uncertainty around economic growth, inflation, policy and geopolitics, it does not help that market liquidity is being challenged. For these reasons, Blackrock thinks that the economy is not in calm waters yet. Blackrock believes in holding a large allocation in cash for now and that interest rates could still go higher from here – although a lot of the "heavy lifting" has already been done.

Still, as the market reprices to account for tighter policy, investment opportunities should arise and particularly in higher quality assets, there are now areas that look much more attractive. In fact, after an incredible re-pricing, front-end sovereign and higher-quality credit assets are offering very unique carry profiles, especially relative to their volatility, with some tangible portfolio benefits as these high-quality assets should perform well during adverse market shocks.

To conclude, as assets become more attractive, Blackrock are ready to deliberately deploy some of the cash that they have stored over the last year, but they are not in a rush to do so. Blackrock thinks that the next couple of months will provide more clarity on the economy and on policy, which will help them navigate this challenging environment.

Availability

Product name	APIR
SignatureSuper*	AMP1113AU
SignatureSuper Allocated Pension*	AMP1142AU
SignatureSuper Term Pension*	AMP1142AU
Flexible Lifetime – Investments (Series 1)**	AMP1116AU
Flexible Lifetime – Investments (Series 2)**	AMP1403AU

* Closed to new investors
** Closed to all investors

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