

Schroder Fixed Income

Quarterly Investment Option Update

31 December 2019

Aim and Strategy

To obtain exposure to a range of domestic and international fixed income assets with the objective of outperforming the Bloomberg AusBond Composite 0+Yr Index, whilst delivering stable absolute returns over time. The option adopts a Core-Plus investment approach whereby a core portfolio comprising of Australian investment grade bonds (including government, semi-government, supranational and corporate bonds) is complemented by investments in a diverse range of global and domestic fixed income securities. The targeted result is a defensive strategy which is broadly diversified with low correlation to equity markets.

Investment Option Performance

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

Investment Option Overview

| | |
|---------------------------------------|------------------|
| Investment Category | Fixed Interest |
| Suggested Investment timeframe | 3 to 5 years |
| Relative risk rating | 3/ Low to medium |
| Investment style | Core |
| Manager style | Single Manager |

| Asset Allocation | Benchmark (%) | Actual (%) |
|-------------------------|---------------|------------|
| Aust. Investment Grade | 99.99% | 82.46 |
| Cash & Equivalents | 0% | 4.55 |
| Global Investment Grade | 0% | 4.23 |
| Australian High Yield | 0.01% | 8.24 |
| Global High Yield | 0% | 0.52 |

| Sector Allocation | % |
|--------------------------|-------|
| Cash & Equivalents | 3.86 |
| Government | 8.64 |
| Semi-Government | 24.63 |
| Supranational/Sovereigns | 21.51 |
| Corporates | 29.80 |
| Subordinated | 3.71 |
| Collateralised | 7.85 |

| Quality Allocation | % |
|--------------------|-------|
| AAA | 47.86 |
| AA | 17.78 |
| A | 5.76 |
| BBB | 21.37 |
| Below BBB | -0.45 |
| Cash & Equivalents | 7.67 |
| Not Rated | 0.02 |

| Top Holdings | % |
|---|------|
| QUEENSLAND TREASURY CORPORATION GOVTGUAR 3.25 21-JUL-2026 | 3.21 |
| INTERNATIONAL BANK FOR RECONSTRUCT 2.8 13-JAN-2021 (SENIOR) | 2.15 |
| NEW SOUTH WALES TREASURY CORP NONDMUNI 5.0 20-AUG-2024 | 1.92 |
| TREASURY CORP OF VICTORIA NONDMUNI 5.5 17-DEC-2024 | 1.79 |
| AUSTRALIA (COMMONWEALTH OF) 4.5 21-APR-2033 Reg-S | 1.77 |
| NEW SOUTH WALES TREASURY CORP NONDMUNI 2.75 20-NOV-2025 | 1.74 |
| AUSTRALIA (COMMONWEALTH OF) 3.75 21-APR-2037 Reg-S | 1.67 |
| TREASURY CORPORATION OF VICTORIA GOVTGUAR 3.0 20-OCT-2028 Reg-S | 1.64 |
| NEW SOUTH WALES TREASURY CORPORATI NONDMUNI 3.0 20-APR-2029 Reg-S | 1.43 |
| AUSTRALIA (COMMONWEALTH OF) 3.0 21-MAR-2047 Reg-S | 1.39 |

Investment Option Commentary

Over the December quarter, the Schroder Fixed Income strategy returned -1.21% (before fees), as bonds gave up some of their gains from earlier in the year, ahead of the benchmark by 0.11% (before fees). Over the year, the strategy returned a robust 7.94% (before fees), above the benchmark by 0.68% (before fees).

Over the quarter, the Fund earned additional income versus the benchmark through its high quality credit allocations, which also benefited from further spread contraction, while the Fund's inflation linked bond and yield curve steepening exposures also added value. Over a year, the Fund's relative outperformance has been driven by a combination of long duration and yield curve positioning, and moderately constructive allocations to higher quality credit.

The Fund shifted positioning in the quarter to reflect reduced concern over downside growth risks, and indeed some prospect of modest global reflation. In rates, the Fund reduced duration and introduced yield curve steepening positions, while maintaining its inflation linked exposure. In the Fund's credit allocations, it added to its Australian investment grade credit, high yield and mortgages overweight position, trimmed its US high yield short and added a new exposure to emerging market debt.

Market Commentary

Risk assets continued to rally through December as trade tensions eased and manufacturing indicators showed tentative signs of an improvement. There was a 'phase one' deal between the US and China which meant that US tariffs on Chinese goods set for December 15 were no longer implemented. Market sentiment was further bolstered by more positive manufacturing Purchasing Managers' Indices (PMIs) at a global level, though the alternative Institute for Supply Management (ISM) figures from the US were less supportive. In the UK, the Conservative Party was re-elected, paving the way for some form of a Brexit deal to be reached in the future. The pound rallied following the election, though has since given back most of its initial gains. On the policy front, the Federal Open Market Committee (FOMC) reaffirmed the current monetary policy stance as being appropriate, with the Fed dot forecasts implying that policy will be on hold for the immediate future. Domestically, the property market continued its rebound, but Q3 growth figures remained soft and other economic indicators showed mixed signals, resulting in the RBA maintaining a dovish stance.

Global equities returned 2.4% in local currency terms, while the Australian market underperformed, posting a loss of 2.2%. Over the last quarter, all major equity markets delivered positive returns, with emerging markets performing particularly well, having returned almost 12% in USD terms over the last 3 months. Global government bond yields moved higher during December and over the fourth quarter. In the US, 10-year yields increased by 0.14% during the month and 0.25% over the quarter, to end December at 1.92%. Australian bonds followed a similar trend with the 10-year yield rising by 0.34% and 0.35% over the month and quarter respectively, to end December at 1.37%. Yields also rose by 0.18% in Germany and by 0.06% in Japan through the month. Credit spreads across global investment grade, high yield and emerging market debt all tightened over the month, as well as the quarter.

Outlook

and with a lower probability for strong beta returns to continue alongside the low level of yields, the Manager is now positioned to capture some of the relative opportunities between countries. The Manager has also shifted to a yield curve steepening view in the US – driven by the Fed either easing more or staying on hold while the global reflation story plays out.

The Manager still favours Australian investment grade credit – including both corporate bonds and AAA-rated RMBS – to access high quality income. In the low yield world it will be a challenge to sensibly balance income generation with efficient risk management, and the Manager is looking for ways to effectively diversify both income and risk sources. The Manager has recently made allocations to US mortgages and to emerging market debt, as this helps diversify traditional interest rate and corporate credit risk, and are exploring several other opportunities.

The Manager continues to avoid global high yield credit, which is most vulnerable to growth and earnings disappointment and potential for defaults, given its current tight spread, and like owning longer-term inflation linked bonds in both the US and Australia as inflation expectations are depressed. Overall the portfolio retains its high-quality focus, and remains predominantly tilted towards Australian exposure, though Schroders are additionally seeking to capture several relative opportunities and seek new sources of return and diversification. The Manager believes it is well-positioned for a more challenging 2020 return environment and expect actively-managed fixed income to continue to be a valuable portfolio holding in this environment.

Availability

| Product name | APIR |
|---|-----------|
| AMP Flexible Lifetime Super | AMP1288AU |
| AMP Flexible Super - Retirement account | AMP1376AU |
| AMP Flexible Super - Super account | AMP1505AU |
| CustomSuper | AMP1288AU |
| Flexible Lifetime - Allocated Pension | AMP1295AU |
| Flexible Lifetime Investment (Series 2) | AMP2040AU |
| SignatureSuper | AMP1302AU |
| SignatureSuper Allocated Pension | AMP1309AU |

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