AB Dynamic Global Fixed Income

Quarterly Investment Option Update

30 September 2021

Aim and Strategy

The strategy may hold corporate bonds, government bonds, asset-backed securities, mortgage-backed securities, closed and open ended mutual funds (including AllianceBernstein (AB)funds) and bank loans located anywhere in the world, including developed and emerging countries. Up to 40% of the strategy's assets may be higher risk and rated below investment grade and up to 5% of the investment's assets may be invested in mutual funds.The strategy intends to hedge to Australian dollars most of the foreign currency exposures of its debt and fixed income securities, however up to 10% of the strategy's net asset value may be exposed to the risks and returns of international currencies.

Derivatives may be used to manage risk exposures, invest cash and gain or reduce investment and currency exposures. Derivatives will not be used for leveraging or gearing purposes.

Investment Option Performance

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

Investment Option Overview

Investment Category	Specialist Fixed Interest
Suggested Investment timeframe	5 years
Relative risk rating	6 / High
Investment style	Opportunistic
Manager style	Single Manager

Asset Allocation	Benchmark (%)	Actual (%)
Global Fixed Interest	N/A	86.2
Aust. Fixed Interest	N/A	11.5
Cash	N/A	2.3

Sector Allocation	%
Investment Grade Corporates	36.9
Global Sovereign	29.4
Emerging Markets	10.9
Securitised	10.6
High Yield Credits	10.5
Other (inc. Derivatives & Currency)	1.7

Regional Allocation	%
North America	44.0
Europe (excl. Great Britain)	22.6
Australia & New Zealand	14.3
Other (incl. Supranationals)	8.3
Great Britain	6.3
Latin America	3.1
Japan	1.4

Top Holdings	%
Australia Bond 5.75% 07/15/2022	4.4
Canada Housing Trust No. 1 1.95% 12/15/25	4.2
Italy .95% 09/15/2027	4.2
Australia Bond 4.25% 04/21/2026	2.0
US Treasury Note 0.75% 01/31/2028	1.8
Australia Bond 2.75% 06/21/35	1.5
Australia Note 1% 12/21/2030	1.4
New Zealand Bond (Senior) 2.75% 04/15/2037	1.2
New Zealand Note 2.75% 04/15/2025	1.0
Australia I/L Bond 3% 09/20/2025	1.0

Portfolio Summary

It remains important for fixed-income investors to be selective given tightening financial conditions. Rising trade tensions and tighter financial conditions signpost a step down in the pace of global growth.

Investment Option Commentary

Sector/security selection contributed to relative outperformance. The allocations to investment-grade and high-yield credit added, as the accommodative posture by developed-market (DM) central banks created the backdrop for the continuation of investor demand for higher-yielding assets. Exposure to credit risk–transfer securities (CRTs) also contributed, driven by several different factors which include strong technical without much issuance, a solid performance in risk assets and strong fundamentals. Further boosting returns was the exposure to eurozone inflation-linked securities as breakevens continued to widen over the period.

Currency positioning was positive as the short position in the Brazilian real contributed the most, as the currency posted negative return, while the long positions in the Indian rupee, South African rand and New Zealand dollar added to performance. However, this was offset somewhat by the short positions in the Indonesian rupiah, Swiss franc and the long position in Norwegian krone.

Country yield-curve positioning was negative, mostly the result of the modest duration position in the Brazilian duration which had a negative impact on performance as yields rose over the period. Long duration position in the US detracted as yields rose over the month amid the US Federal Reserve's (the Fed's) tapering discussions and rising concerns about inflation which outweighed signs of moderating global growth.

Market Commentary

During the quarter, as the global growth recovery continued and the coronavirus delta variant began to peak, numerous crosscurrents impacted fixed-income markets. Transitory inflation expectations were questioned as inflation prints were higher than expected. In addition, challenges in China from its property sector and the ongoing debt-ceiling debate in the US contributed to investor uncertainty. Interest rates were volatile—declining early in the period over growth concerns surrounding the delta variant as well as a number of technical factors—then rising for the remainder of the quarter, driven mostly by inflation and central bank tapering headlines.

DM central banks appear to be approaching policy normalization, while inflation is more pervasive and persistent than many had anticipated. The Fed indicated that tapering of its asset purchase program is imminent, and the dot plot revisions pointed to an increase in the number of Federal Open Market Committee members who expect that it may be appropriate to raise short-term rates next year. At the same time, the BoE hinted that a modest tightening of monetary policy may be necessary to meet its inflation target before the asset purchase program ends. The European Central Bank (ECB) signaled a "moderately lower" pace of asset purchases in the fourth quarter, and its pandemic emergency purchase programme (PEPP) is set to expire in March 2022. Still, bond purchases under the APP are expected to continue for the foreseeable future. Over the quarter, among 10-year government bonds, yields rose the most in the UK and Canada, up 31 and 12 basis points (b.p.), respectively. Yields rose by modest amounts in the eurozone, US and Japan, and were 4 b.p. lower in Australia.

The accommodative posture by DM central banks created the backdrop for the continuation of investor demand for higher-yielding assets. DM high-yield corporate bonds posted positive returns and outperformed DM government bonds. Investment-grade DM corporate bonds were down in absolute terms but in line with duration-matched treasuries. Within emerging markets (EM), corporate bonds had positive returns, EM sovereign debt trailed, and EM local-currency bonds underperformed the most as the US dollar gained on most DM and EM currencies during the period. Securitized assets were mixed, with CRTs and collateralized loan obligations (CLOs) delivering positive returns while returns in the commercial mortgage-backed securities (CMBS) varied.

Outlook

Global growth expectations have shifted markedly in recent months from widespread optimism and upside risks to a more sober assessment of the economic outlook. There is also concerned that global supply-chain dislocations could be more pervasive and persistent than expected. So, while the GDP forecasts have not changed very much, the relative stability of the estimates masks an important change in the narrative surrounding growth risks and inflation. Of particular concern to is the specter of a more challenging growth and inflation mix and a less certain outlook for monetary policy—one in which the only choices available to central banks may be quite difficult ones.

For now, the view is that inflation is likely to fall back next year. But upward pressure on prices has already been less transitory than expected, perhaps hinting at a more fundamental shift in inflation dynamics. How central banks respond will depend on their tolerance for higher inflation and the extent to which inflation expectations are well anchored. That is likely to mean greater dispersion among yields in DM countries. But the key focus for investors remains the US Federal Reserve (the Fed). As things currently stand, the fund does not expect a US rate hike until 2023. But rapid tapering would in theory leave the door open for an earlier rate move, giving investors something else to be distressed about. The longer-term outlook is clouded by strong secular trends, including populism and insular trade protectionism. Deglobalization will likely continue as countries and economic blocs attempt to create independence in areas including medical equipment and supplies, batteries, semiconductor chips and rare earth minerals. Resolution of trade conflicts remains elusive while geopolitical trade pacts are in flux.

The fund manager has trimmed the global GDP estimate from 6.1% to 5.9%, based on lowered estimates of DM and EM GDP growth of 5.2% and 6.9%, respectively. There is also an expectation of lower global growth of 4.2% in 2022 as economies normalize. Both forecasts are well above the precrisis trend of about 3.0%. Global manufacturing continues to be in expansion, according to the J.P. Morgan/IHS Markit Manufacturing PMIs, which held steady in September at 54.1.

In the US, robust policy support means that 2021 is likely to be the best year for GDP growth in nearly 40 years. As these policy measures fade in 2022, the fund manager expect growth to moderate but remain above the long-term trend. Consumer demand has rebounded very quickly in tandem as the US economy has reopened, with the supply side of the economy struggling to keep up. Those challenges have been more persistent than expected, in part because the coronavirus delta variant continues to have global impact on supply chains that have not rebooted as quickly as forecast. The resulting imbalance between supply and demand has pushed prices higher, but there is the belief that most of the pricing pressures are transitory and that inflation should decelerate in 2022. If the fund manager is correct, this will allow the Fed to remain accommodative across the forecast horizon. But if price pressures spill over into higher inflation expectations, the Fed may have to respond more quickly than it anticipates or the fund manager had anticipated. The fund doubts that the Fed will raise rates next year since there is no urgency for the Fed to act. The IHS Markit manufacturing sector PMIs moderated from 61.1 to 60.5 in September, mostly due to material shortages and supply-chain bottlenecks. Given the impact of the delta variant and supply-chain disruptions, the fund has lowered the US GDP forecast for this year to 6.1%.

Availability

Product Name	APIR Code
AMP Flexible Super - Super	AMP2027AU
AMP Flexible Super - Retirement	AMP2022AU
CustomSuper	AMP1997AU
Flexible Lifetime - Super	AMP1997AU
Flexible Lifetime - Allocated Pension	AMP2002AU
Flexible Lifetime - Investments (Series 2)**	AMP2036AU
SignatureSuper	AMP2007AU
SignatureSuper Select	AMP2007AU
SignatureSuper - Allocated Pension	AMP2014AU

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