AMP Australian Bond

Quarterly Investment Option Update

30 September 2015

Aim and Strategy

To provide a total return (income and capital growth) after costs and before tax, above the UBS Composite Bond (All Maturities) Index on a rolling 12 month basis. The portfolio invests primarily in Australian government bonds and credit securities and may also invest in global fixed income securities, and derivatives in global fixed income markets, which may also include a small exposure to emerging markets. Exposure to global fixed interest securities will principally be hedged back to Australian dollars.

Investment Option Performance

To view the latest investment performances please visit www.amp.com.au

Availability

Product name	APIR
AMP Flexible Lifetime Super	AMP0343AU
AMP Flexible Super - Retirement account	AMP1319AU
AMP Flexible Super - Super account	AMP1449AU
AMP Growth Bond	AMP1188AU
CUSTOM SUPER	AMP0343AU
Flexible Lifetime - Allocated Pension	AMP0590AU
Flexible Lifetime - Term Pension	AMP0890AU
Flexible Lifetime Investment	AMP1048AU
Flexible Lifetime Investment (Series 2)	AMP1388AU
Investment Linked Deferred Annuity	AMP0753AU
Investment Linked Single Premium	AMP0088AU
Investment Linked Single Premium	AMP0130AU
METCASH SUPERANNUATION PLAN	AMP0343AU
MultiFund Flexible Income Plan	AMP0356AU
SignatureSuper	AMP0738AU
SignatureSuper Allocated Pension	AMP1128AU

Investment Option Overview

Investment category	Fixed Interest - Enhanced Fixed Interest
Suggested investment timeframe	2 years
Relative risk rating	Low - Medium
Investment style	Active

Asset Allocation	Benchmark	Range (%)
Global Bonds	100	95-100
Cash	0	0-5

Top 10 Securities	%
AUSTRALIAN GOVERNMENT	17.97
QUEENSLAND TREASURY CORP	11.10
NEW S WALES TREASURY CRP	5.74
TREASURY CORP VICTORIA	3.90
INTL BK RECON & DEVELOP	3.79
WESTERN AUST TREAS CORP	3.71
Australia & New Zealand Banking Group Ltd	2.81
Westpac Banking Corp	1.92
LLOYDS BANK PLC	1.57
INTER-AMERICAN DEVEL BK	1.53

Credit Exposure	%
AAA	45.50
AA	18.13
BBB	16.99
A	14.10
Cash	4.57
Sub Investment Grade	0.83
Not Rated	-0.11

Performance summary

- The Fund underperformed its benchmark in the September quarter but yielded a positive return. Bond yields fell slightly over the quarter as risks surrounding China added to the attractiveness of risk-free assets.
- Credit positioning was the main detractor from returns as volatility increased and spreads widened.

The Reserve Bank of Australia maintained the official cash rate at 2.00% over the quarter, however the market has factored in an expected rate cut next year.

Investment Option Commentary

The Fund underperformed its benchmark in the September quarter. Credit positioning was the main detractor from returns as volatility increased and credit spreads widened due to concerns about anticipated policy action by the US Federal Reserve, China's growth outlook and the continued fall in commodity prices.

At the start of the September quarter we shifted to a long duration bias on a tactical basis as economic data started to show signs of slowing momentum, commodity prices resumed their downtrend and risks surrounding China continued to build. We added to this position throughout August as global economic data and market sentiment continued to deteriorate. Late in the quarter, market volatility increased substantially due to a combination of poor share market sentiment and further risks surrounding China and commodities. In the US, however, economic data continued to be robust, and in some sectors of the economy, even accelerated. We continued to have a long duration bias for the remainder of the quarter. However, the position was quite modest as valuations were relatively unattractive. Duration positioning added to overall performance for the quarter.
We still like the higher income for corporates compared to government bonds and supranationals, and remain overweight credit risk relative to the benchmark, although we did reduce credit exposure. The supranational and government sectors have been used to fund the credit overweight.

In terms of spread performance at the sector level, exposures to real estate, semi-governments and consumer discretionary outperformed over the quarter, while allocations to materials, utilities and energy detracted the most from returns. Overall portfolio hedges in credit default swap indices lifted overall performance. At the issuer level, the top performers were overweight positions in International Bank for Reconstruction and Development, APT Pipelines and DBNGP Finance. Underperformers were commodities-related overweight positions in Glencore Australia Holdings, Kinder Morgan and Santos Finance.

In terms of portfolio activity, over the quarter the Fund participated in primary issues from SABMiller, Westpac, Lloyds Bank and Apple. This was funded by reducing positions in BHP Billiton, Caterpillar, Toyota and Direct TV, as well as financial exposures BNP Paribas, Bank of America and Goldman Sachs in the secondary market. The Fund also added bought protection position in the iTraxx Australia and US CDX investment grade credit derivative contracts to protect against anticipated near-term credit risk volatility within the Fund, particularly the higher-beta offshore exposures. Overall credit risk within the portfolio was therefore reduced over the quarter to keep the fund in line with a moderating macro credit score, but continues to be at a modest overweight relative to the benchmark.

Market commentary

Over the September quarter bond yields fell slightly as risks surrounding China, particularly in relation to the volatility in the stock market, added to the attractiveness of risk-free assets. Negotiations between Greece and the Eurozone had raised concerns; however these abated in August as a near-term resolution was reached. US economic data also started to stabilise and inflationary pressures on average showed steady improvement, which led the US Federal Reserve to adjust its rhetoric more towards monetary policy tightening. At the end of the quarter, the dovish surprise at the September Federal Open Market Committee meeting saw bond yields reassert their downtrend. Australian bond yields followed their global counterparts and displayed a similar dynamic as foreign investors reduced their Australian bond portfolio weightings.

Outlook

Global factors are likely to cause Australian bond yields to move higher. After a disappointing start to 2015, the US should record solid 2% to 3% real economic growth for the remainder of 2015. This should warrant the US Federal Reserve starting to raise interest rates by the end of 2015. This is a key negative for global bond yields. However, we also expect better growth outcomes in Europe and Japan in 2015 as aggressive policy stimulus and currency weakness have a positive impact. While China is expected to see solid growth of 6.8% in 2015, there are stronger growth prospects for India and Asia given recent monetary policy stimulus. These better growth outcomes in the US, Europe and Asia should see a mild acceleration in global growth which would warrant higher global sovereign bond yields this year.

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