AB Dynamic Global Fixed Income

Quarterly Investment Option Update

31 December 2018

Aim and Strategy

The strategy is designed for investors with higher risk tolerances and who want income returns exceeding Australian bank bill rates over the long term by investing in global debt and fixed income securities. It implements a global, multi-sector strategy investing in a broad range of fixed income securities. The strategy may hold corporate bonds, government bonds, asset-backed securities, mortgage-backed securities, closed and open-ended mutual funds (up to 5% of the assets)
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. 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.

Asset Allocation	Benchmark (%)	Actual (%)
Global Fixed	0	90.4
Aust. Fixed Interest	0	6.2
Cash	100	3.4

Sector Allocation	%
Global Sovereign	44.7
Investment Grade Corporates	30.8
Securitised	12.7
Emerging Markets	4.8
High Yield	3.7
Other (inc. Derivatives & Currency)	3.9

Regional Allocation	%
North America	40.0
Europe (excl. Great Britain)	23.1
Australia & New Zealand	8.6
Other (incl. Supranationals)	12.8
Great Britain	7.5
Japan	7.2
Latin America	0.8

Top Holdings	%
Canada 2% 09/01/2023	5.4
Australia 3.25% 04/21/2025	3.4
UST IFL 0.125% 04/15/2021	3.3
Japan IFL 0.1% 03/10/2026	3.2
UK Bond 2.5% 04/16/2020	2.0
International Finance Corp 3.25%	2.0
European Investment Bank 6.5%	2.0
International Bank for Recon. 5.25%	2.0
Germany IFL 1.75% 04/15/2020	2.0
UST IFL 1.25% 07/15/2020	1.9

Investment Option Performance

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

Investment Option Overview

Investment Category	Specialist Fixed Interest
Suggested investment timeframe	5 years
Relative risk rating	3 / Low to Medium
Investment style	Opportunistic

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 drove relative underperformance, as exposure to investment-grade and high-yield bonds in the eurozone and the US detracted. Sector/security selection within US inflation-linked bonds and commercial mortgage-backed securities (CMBS) also detracted. Country/yield-curve positioning offset some of these losses. Positioning in the US, Canada and Australia was positive while positioning in the eurozone was negative. Currency decisions were slightly positive for returns, although an overweight to the yen detracted.

Market commentary

Financial markets struggled in the fourth quarter as investors worried about reduced liquidity and the health of the global economy. Like most investors, the fund manager came into 2018 expecting a rougher ride. Global growth was strong, but the era of easy money was ending, suggesting the nearly uninterrupted rise in risk assets would end with it. Trade protectionism and other political threats also justified caution.

Investors were unnerved by signs of slowing global economic growth: economic data from China, Europe and Japan were below expectations in recent months, while falling oil prices heightened fears that global demand could decline. Making matters worse, the US Federal Reserve (the Fed) did not deliver the type of accommodative signal investors were hoping for when it raised rates in mid-December and telegraphed plans for two more hikes in 2019; markets were pricing in just one.

All in all, the period was dominated by a traditional “risk-off” environment as the year wound down. Credit spreads widened in the US and Europe, and the US yield curve flattened. The US 10-year Treasury yield finished the year at 2.68%, nearly 0.4% below where it began the fourth quarter and just 0.19% above where the two-year Treasury yield stood at year-end. The 10-year German Bund fell to 0.24% from 0.47% over the quarter.

Outlook

In 2019, the fund manager expect growth to remain positive but slow to a trend-like pace, as the macro backdrop points to a less favorable mix of growth and inflation. Downside risks continue to cloud the outlook in Europe and China, while global trade tensions still represent a significant concern. And this tableau is playing out with global debt levels elevated and central-bank balance sheets starting to shrink. In their view, central banks still have a vested interest in remaining accommodative and while they expect monetary conditions to tighten, it will likely be at a more gradual pace than the fund manager originally thought. The fund manager has lowered their GDP growth forecasts for 2019 a touch, now expecting global growth of 2.8%, emerging-market (EM) expansion of 4.5%, and developed-market growth of 1.7%.

Although the US economy is operating at full employment, and growth is above the noninflationary potential rate, market volatility is likely to slow the economy somewhat in the coming months. But considering how strong growth is, a modest slowdown should be welcomed, as it could temper the risk of eventual overheating or financial market imbalances that could jeopardize the expansion. Global factors, most notably the falling price of oil, pose downside risks to AB’s inflation forecasts and thus to their expectations for the Fed’s rate hike path through 2019. Politics remain an ever-present risk, with trade tensions and questions about the forward path of regulatory policy in focus. The fund manager has lowered their 2019 GDP growth forecast for the US to 2.0%.

In Japan, the fund manager now expects 2019 GDP growth of 1.2%, buoyed in part by further fiscal stimulus. CPI inflation is still far from the Bank of Japan’s 2.0% target. The central bank will likely maintain its quantitative and qualitative easing/yield-curve control program—designed to cap 10-year yields—through the year, though further tweaks are possible.

Availability

Product name	APIR
AMP Flexible Lifetime Super	AMP1997AU
AMP Flexible Super - Retirement account	AMP2022AU
AMP Flexible Super - Super account	AMP2027AU
CustomSuper	AMP1997AU
Flexible Lifetime - Allocated Pension	AMP2002AU
Flexible Lifetime Investment (Series 2)	AMP2036AU
SignatureSuper	AMP2007AU
SignatureSuper Allocated Pension	AMP2014AU
SignatureSuper Select	AMP2007AU

Contact Details

Web: www.amp.com.au
Email: askamp@amp.com.au
Phone: 131 267 (Mon. to Fri. 8:30am to 7:00pm AEST)

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