AXA Investment Managers

For professional clients only
November 2024
Monthly Perspectives
Fixed Income



# Global Strategic Bonds strategy

# Bonds budgets and central banks

- Rising government bond yields have led to a moderation in global fixed income markets
- Tight credit spreads ensure healthy interest costs for refinancing in corporate credit markets
- Developed market employment data shows mixed signals
- The US election dominated news flow, with policy uncertainty pushing yields higher

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## What's happening?

- After a decent run of strong returns in fixed income markets positive returns in global fixed income were almost universally negative in October. Spreads remained supportive throughout the month, but government bond yields rose driving markets lower. The exception to this was European High Yield which outperformed and was the only positive performing fixed income asset class.
- In the US, payrolls, and employment data were stronger than expected. Headline CPI easing by 0.1% less than expected to 2.4%, and core inflation rose to 2.7% compared to the expected 2.4% and despite a run of softer labour market data, October's payrolls showed a surprise 240k gain, nearly 100k above estimates. Conversely jobless claims rose the most in more than a year by 33k to 258k, likely some of this though can be attributed to disruption from hurricane Helene. US Treasury Yields rose across the curve, and market expectations for further rate cuts this year were adjusted. The rise in treasury yields may also be linked to uncertainty surrounding the US Election.

| Strategy in focus – representative account (31/10/24) | |
|---|---|
| Assets under management | **$632 m** |
| Duration | **5.91 years** |
| Yield[1] | **5.59%** |
| Running yield[1] | **4.79%** |
| Spread to government[2] | **184 bps** |
| Number of holdings | **253** |
| Launch date | **11/05/2012** |

| Net performance – representative account (USD)[3] | **Cumulative** | **Annualised** |
|---|---|---|
| One month | **-1.46%** | **-** |
| One year | **12.89%** | **12.89%** |
| Three years | **-2.24%** | **-0.75%** |
| Five years | **5.61%** | **1.10%** |
| Ten years | **26.42%** | **2.37%** |

Source: AXA IM as at 31/10/2024. The data is based on a representative account that follows the Global Strategic Bonds strategy. **Past performance is not a reliable indicator of future results**. Performance calculations are net of fees, based on the reinvestment of dividends.

- UK unemployment dropped to 4.0%, the lowest in three months, but other employment measures indicated more slack. Vacancies and PAYE declined, and average weekly earnings fell to 4.9% from 5.1% in the three months to September, the lowest since June 2022. UK CPI for the month was 1.7%, below expectations and the 2.0% BoE target. Services inflation also slowed to 4.9% from 5.6%. The UK budget took centre stage, with bond investors expecting fiscal tightening to prompt more aggressive BoE monetary policy easing. However, the Office for Budget Responsibility (OBR) suggested limited positive impact on growth and hinted at slightly higher bank rates and inflation. The UK budget also included additional spending commitments, leading to higher gilt yields across the curve.

- In October, the ECB, the only one of the three major central banks to meet, lowered rates for the third time this year. On October 16th, the Governing Council cut rates by 25bps, bringing the policy rate down to 3.25%. The cut was not surprising given weak economic releases for some of the eurozone's main economies. Wage growth across the 20-nation area, previously an inflationary concern, is still elevated but is now slowing more rapidly than expected. September's inflation prints for the region dipped to 1.7% from 2.2% the previous month.

- Despite negative returns from rising all in yields, credit market spreads narrowed in October. This was supported by the global trend of lower interest rates, leading to reduced future interest costs for companies, and positive supply and demand dynamics across credit markets. The extent to which UK Gilts and US Treasuries sold-off in October offset any spread tightening in UK and US credit markets, however European government bonds did not sell-off to the same extent and European spreads outperformed meaning European Investment Grade and European High Yield were the top performing fixed income asset classes in October returning -0.2% and +0.7% respectively.

## Portfolio positioning and performance

- **Defensive (26%):** During the month, we made minimal adjustments to the defensive risk bucket of the strategy. However, due to the mark-to-market effect of rising yields, the overall allocation decreased by c.1%. One trade we executed was reducing our exposure to longer-dated US Treasuries. This did not impact our overall duration exposure, which remains at around 6 years. Although we still favour US curves, which account for over half of our duration exposure, we added 0.7 years of duration risk to the UK as we believe it has underperformed and UK curves are attractively valued. At the end of the month, our duration stood at 2.9 years to the US, 1.8 years to the UK, and 1.1 years to Europe.

- **Intermediate (25%):** The strategy's overall exposure to the intermediate risk bucket stayed consistent in October. However, we reduced our exposure to the US automotive sector and shifted to several higher quality Financial Services and Banking credits. We believe the automotive sector is encountering significant challenges such as the transition to electric vehicles and the continuation of disrupted supply chains.

- **Aggressive (49%):** Exposure to the strategy's aggressive risk bucket increased by 1% during the month. Our European High Yield exposure had a positive mark-market effect which contrasted with Emerging Market Debt and US High yield where the sell-off in government bonds saw these two asset classes cheapen up. We took advantage of this by purchasing more high conviction US Yield high names in Telecommunications, Financial Services and Healthcare.

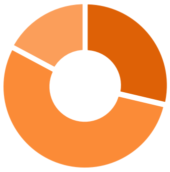
## Outlook

- After a very strong period for fixed income, it has been little surprise to many that markets tempered during October, our core view though remains for a global soft landing with no recession, lower inflation, interest rates to move back towards a more neutral level with curves to steepening.
- The increase in yields in October was driven by policy uncertainty leading up to the US election, some risk premium related to the path towards more neutral monetary policy, and a string of geopolitical events. With relatively flat yield curves, the move to lower yields is expected to be more significant at shorter maturities. Therefore, we believe that having duration exposure through shorter-dated bonds is preferable to taking on risk at the long end.
- Growth slowing with no recession will continue to be supportive for credit where the real driving factor is the sizeable reduction in future interest costs – a weakening of consumer demand may be more of a concern for share prices as opposed to credit fundamentals. In addition, corporate balance sheets remain generally healthy and the relatively low default levels lead us to view current spread levels as fair, especially in high yield asset classes.
- Escalation in the middle east conflict and potentially overdone market reaction to Beijing's stimulus mean we are optimistic but cautious on emerging markets. Emerging Market Debt continues to be in favour, so our view is that the asset class could continue to surpass people's low expectations.

| Strategy breakdown | |
|---|---|
| Defensive | 25.7% |
| Intermediate | 24.8% |
| Aggressive | 49.4% |
| **Total** | **100%** |

| Defensive breakdown | 25.7% |
|---|---|
| US Government Bonds | 8.6% |
| Core Europe Government Bonds | 8.4% |
| Inflation-Linked Bonds | 4.1% |
| Cash | 4.7% |

| Intermediate breakdown | 24.8% |
|---|---|
| US IG Credit | 9.2% |
| Euro & Sterling IG Credit | 15.7% |



| Aggressive breakdown | 49.4% |
|---|---|
| Emerging Markets (HC 14.2%/LC 0%/FX 0%) | 14.2% |
| US High Yield | 26.8% |
| European High Yield | 8.5% |

| Derivatives breakdown | 10.4% |
|---|---|
| Bond Futures | 17.5% |
| Credit Default Swaps | -7.1% |

## Credit rating breakdown

| Category | Rating | Total |
|---|---|---|
| Defensive | Cash | 4.7% |
| | AAA | 3.3% |
| | AA | 17.8% |
| | Total | 25.7% |
| Intermediate | AA | 0.6% |
| | A | 7.9% |
| | BBB | 16.4% |
| | BB | 0.0% |
| | Total | 24.8% |
| Aggressive | AA | 0.0% |
| | A | 0.5% |
| | BBB | 2.2% |
| | BB | 20.7% |
| | B | 17.5% |
| | CCC & below | 8.6% |
| | Not rated | 0.0% |
| | Total | 49.4% |
| **Total** | | **100%** |

(1) Yield figures quoted will vary in the future and are not guaranteed. Yield calculated to maturity, assuming next call date, using local currency yields.
(2) Average credit spread relative to government bonds.

(3) Representative account has been selected based on objective, non-performance-based criteria, including, but not limited to the size and the overall duration of the management of the account, the type of investment strategies and the asset selection procedures in place. Therefore, the results portrayed relate only to such accounts and are not indicative of the future performance of such accounts or other accounts, strategies and/or services described herein. In addition, these results may be similar to the applicable GIPS composite results, but they are not identical and are not being presented as such. Account performance vary based upon the inception date of the account, restrictions on the account, along with other factors, and may not equal the performance of the representative accounts presented herein. The performance results for representative accounts are net of all fees and reflect the reinvestment of dividends or other earnings.

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