Schroder Fixed Income

Quarterly Investment Option Update

31 March 2021

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/performance

Investment Option Overview

Investment Category	Fixed Interest
Suggested Investment timeframe	3 to 5 years
Relative risk rating	5 / Medium to High
Investment style	Core
Manager style	Single Manager

Asset Allocation	Benchmark (%)	Actual (%)
Aust. Investment Grade	100%	68.7%
Cash & Equivalents	0%	17.3%
Global Investment Grade	0%	-0.3%
Australian High Yield	0%	8.3%
Global High Yield	0%	6.1%

Sector Allocation	%
Government	21.3
Semi-Government	17.0
Supranational/Sovereigns	7.1
Corporates	23.4
Subordinated	4.9
Collateralised	5.3

Quality Allocation	%
AAA	29.7
AA	17.8
A	7.8
BBB	25.4
Below BBB	3.6
Not Rated	0.6

Top Holdings	%
AUSTRALIA (COMMONWEALTH OF) 2.75 21-NOV-2028 Reg-S	3.6
AUSTRALIA (COMMONWEALTH OF) 0.25 21-NOV-2024 Reg-S	3.0
NEW SOUTH WALES TREASURY CORPORATI 2.0 08-MAR-2033	1.9
AUSTRALIA COMMONWEALTH OF (GOVERN 2.0 21-AUG-2035 Reg-S	1.8
AUSTRALIA (COMMONWEALTH OF) 2.25 21-MAY-2028 Reg-S	1.5
TREASURY CORPORATION OF VICTORIA 1.5 10-SEP-2031	1.5
AUSTRALIA (COMMONWEALTH OF) 2.75 21-NOV-2027 Reg-S	1.5
WESTERN AUSTRALIAN TREASURY CORPOR NONDMUNI 3.0 21-OCT-2026	1.4
AUSTRALIA (COMMONWEALTH OF) 2.75 21-MAY-2041 Reg-S	1.4
AUSTRALIA (COMMONWEALTH OF) 1.75 21-JUN-2051 Reg-S	1.3

Investment Option Commentary

The Schroder Fixed Income Option delivered a positive relative return in the March quarter. This continued to highlight a year of very strong positive performance.

The Manager materially shifted the portfolio in anticipation of higher yields. In late 2020 and early 2021 they reduced interest rate duration by about two years, increased allocations to inflation-linked bonds and also trimmed credit exposures, particularly to those markets where spreads are most vulnerable to rising yields. More recently, the Manager has have increased the portfolio's duration and reduced their inflation exposure, locking in good profits on these trades. However, they remain cautiously positioned. The Manager expects the next few months to be volatile as strong activity and inflation data challenge central bank commitments to keep rates at zero for several more years. The Manager is well prepared to manage through the risks ahead, and believe fixed income is becoming more valuable again at higher yields.

Market Commentary

Equity markets overcame initial concerns around higher bond yields and rallied through March, being supported by a strong outlook for corporate earnings and the US congress giving final approval to Biden's $1.9 trillion fiscal support package. The fiscal package is roughly equivalent to 9% of US GDP and has seen growth estimates for the US revised up to around 6% for 2021. Australian growth has also been revised higher, though to a smaller degree, with expectations of 4% growth for the year. US bond yields continued to rise through March driven by the prospect of higher growth and inflation, while yields in other core markets fell moderately through the month. US Federal Reserve Chair Powell has stressed that a pick up in inflation is expected, but is likely to be transitory rather than structural. On the data front, the US ISM index posted another strong reading, while global property markets also performed strongly. Locally, property prices increased by 2.8% over the month, while Sydney prices had their strongest monthly increase in 33 years, rising by 3.7% through March.

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Global equities returned 4.2% in local currency terms through March, while the Australian market underperformed with a return of 2.4%. The style rotation towards value continued, with value equities outperforming growth equities by about 5% in the month, though growth has still outperformed over a one year timeframe. Emerging market equities had a negative return over the month, 1.5% in USD terms (mostly due to a negative return in Chinese equities), as a stronger US dollar and a slower than expected vaccine rollout weighed on sentiment. Over the quarter, growth assets performed strongly, with Australian equities returning 4.3% and global equities returning 6.2%. US 10 year treasury yields increased by 0.34% through March to end the month at 1.74%, while Australian 10 year treasury yields moved in the opposite direction, falling by 0.13% to end the month at 1.79%. Similarly, longer end bond yields also fell in Germany and Japan by 0.03% and 0.06% respectively over the month. Over the quarter, Australian and US 10 year treasury yields both increased by approximately 0.8%. Credit spreads also diverged during March, with high yield spreads continuing to compress, global investment grade relatively flat, and Australian investment grade spreads moderately wider.

Outlook

The Manager holds a strong cyclical view. However, they believe markets have already priced in quite a lot of our expectation, and they are also less certain on the structural story. The Manager believes bond yields will continue to move higher in Q2 as global growth booms and inflation starts to materialise, however they have moderated and modified our positions. For much of the March quarter, the Manager was running a larger short duration position in the US, however they recently halved this position with yields now materially higher, especially in longer dated maturities. They have also taken profit on their US inflation-linked positions. The Manager is still looking for higher yields, but whereas the first phase of this bond yield rise was driven by lifting inflation expectations and higher term rates, they expect the next phase will see markets questioning the commitment of central banks to remain on hold – and intermediate and short end yields do not look prepared for this.

Corporate spreads have largely been undisturbed by the recent rise in bond yields as markets focus on growth and positive earnings trajectories – in fact, spreads are now tighter than where they started the year. However, while the improvement in corporate fundamentals is undoubtedly good news, given that spreads have already compressed to historically tight levels the Manager does not think they will compress too much further. As a result, they made strategic reductions in credit exposure over the past three months, primarily in global investment grade credit, but also in Australian investment grade bonds and mortgages. In addition, in anticipation of an increase in market volatility and uncertainty about the central bank response to much stronger data, they have also introduced a tactical short position in US high yield credit.

Availability

Product Name	APIR Code
AMP Flexible Super - Super	AMP1505AU
AMP Flexible Super - Retirement	AMP1376AU
CustomSuper	AMP1288AU
Flexible Lifetime - Super	AMP1288AU
Flexible Lifetime - Allocated Pension	AMP1295AU
Flexible Lifetime - Investments (Series 2)	AMP2040AU**
SignatureSuper	AMP1302AU
SignatureSuper - Allocated Pension	AMP1309AU

**Closed to new and existing investors

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