Macquarie Investment Management

Macquarie Dynamic Bond Fund

Monthly report – 31 October 2020

Investment objective

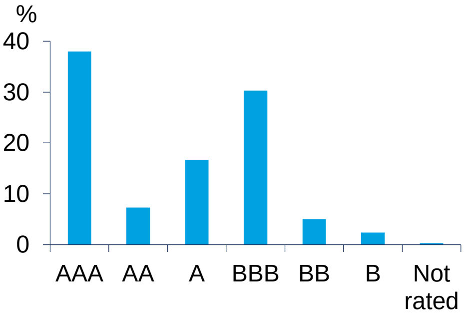
Aims to generate attractive returns by dynamically investing in global fixed income instruments. It aims to provide diversification against equity risk as well as capital growth and some income.

Key information

Fund details	
APIR code	MAQ0274AU
Inception date	30 September 2002
Fund size	$682.3m
Distribution frequency	Quarterly
Management fee*	0.614% pa
Minimum investment (Direct)	$20,000
Unit prices and spreads	**macquarie.com.au/unit_prices**

*Read the Product Disclosure Statement for more details on fees and costs.

Credit profile breakdown



Average credit rating: A+
Less than BBB includes residual exposure to issuers held through global investment grade allocation

Fund performance to 31 October 2020

	Total Fund return (gross)	Total Fund return (net)	Benchmark return	Total excess return (net)
1 month (%)	0.28	0.22	0.08	0.14
3 months (%)	0.58	0.42	0.13	0.29
1 year (%)	5.29	4.64	3.15	1.49
3 years (% pa)	5.76	5.12	3.41	1.71
5 years (% pa)	5.12	4.48	3.43	1.05
10 years (% pa)	5.75	5.10	4.80	0.30

Past performance is not a reliable indicator of future performance.
Total returns are calculated based on changes in net asset values and assumes the reinvestment of distributions.
Total net Fund returns are quoted after the deduction of fees and expenses. Due to individual circumstances, your net returns may differ from the net returns quoted above.
From 7 January 2019, the benchmark is Bloomberg Barclays Global Aggregate 1 to 10 years Index hedged to AUD. Prior to this, the benchmark was Bloomberg AusBond Composite 0+Yr Index. The performance information shown above is against the current benchmark. Further information in relation to the performance against the previous benchmark is available on request.

Asset allocation

	Fund (%)
Sovereign bonds[1]	45.1
Investment grade credit[2]	43.6
High yield	5.2
Emerging markets debt[3]	6.1

[1] Includes Australian government, Australian semi-government, supranational, global sovereign and cash
[2] Includes Australian and global investment grade credit
[3] May include holdings of sub-investment grade instruments

Fund statistics

Credit spread duration	2.7 years
Interest rate duration	4.1 years
Standard deviation[1]	2.9% pa
Yield to maturity[2]	1.5% pa

[1] Statistical measure of variance of Fund's post-fee monthly returns from its average post-fee return since inception used as gauge of volatility.
[2] Pre-fee return Fund would earn over next year based on current market conditions if there were no changes to interest rates or holdings of Fund. It is not an actual or estimated return.

Geographical exposure

	Interest rate duration[1] (%)	Credit spread duration[2] (%)
North America	47.4	43.9
Europe (ex UK)	3.9	17.2
UK	7.4	6.5
Australia/New Zealand	33.2	22.0
Japan	0.4	0.5
Others	7.7	9.9

[1] Calculated based on security's currency
[2] Calculated based on security issuer's currency

Fund highlights

There were three main themes colliding during October for financial markets to navigate. First, the virus. As the northern hemisphere countries returned to school and university in September, virus case counts began to rapidly rise. Surging cases were soon followed by rising hospitalisation and this factor was key in pushing governments to re-introduce restrictions. Across Europe and the UK, these new restrictions were not the full lockdown of earlier this year, but are still very significant, effectively closing most of the services sector for the coming month. Secondly, the US election loomed on the horizon. It is significant because expected fiscal stimulus has not been agreed ahead of 3 November and the outlook for fiscal policy is clouded by the potential complexity of the final result. Finally, Q3 economic data confirmed the sharp bounce in activity from the dire Q2 levels, but early data for Q4 suggests that activity is slowing, largely a result of the above themes.

During October, these events combined to create some volatility, with risk initially rallying before paring back gains while government bond yields moved higher, which steepened yield curves. This volatility was not uniform across countries. In rates, rising US Treasury yields notably underperformed European government bonds, where yields fell over the month. In credit, US investment grade (IG) spreads outperformed European IG. Spreads narrowed modestly in the high beta sectors of high yield and emerging markets.

The Fund delivered a positive return in October. The Fund's holdings of credit securities added meaningfully to performance over the month, with IG credit contributing to both sector rotation and security selection. Small positions in high yield and emerging markets also added to returns through positive security selection outcomes. The Fund added some new high yield bonds and emerging markets exposures over the month, while trimmed exposures to IG credit that had performed well and offered limited upside from here.

Credit markets were overall stronger in October, driven by the strong supply-demand technicals and reflecting the direct central bank support underpinning IG credit in particular. The demand for credit globally has remained strong as investors continue to search for yield. Retail inflows to bond funds and exchange-traded funds generally remained strong, while insurance companies continued to be strong buyers of global corporate credit. New corporate issuance was low, in part due to the beginning of the Q3 earnings season in the US and a considerable amount of corporate funding already complete earlier this year. Thus, credit spreads have tightened even as macroeconomic news deteriorated and virus cases escalated. The higher yielding parts of the market was softer toward the end of the month, and several higher beta issuers were forced to pull new deals from the USD market due to unattractive pricing or lack of demand for most high-risk credits, though most of the IG and broader credit markets remained well supported.

The Fund's overall duration was reduced in October to levels slightly below its strategic target. This reduction was largely in Australian government bonds after yields fell in response to the Reserve Bank of Australia indicating in the November meeting that it is likely to provide further monetary stimulus to the economy. Allocations to European and UK bonds increased as we expect the tightening of restrictions to further undermine growth in coming months and expect to see higher market pricing of central bank policy response by both the European Central Bank and Bank of England. The Fund's exposure to US Treasuries remained modest and was focused in the 5 year part of the curve.

Outlook

The US presidential vote remains undecided at the time of writing but it appears that Congress will remain unchanged, with the House led by the Democrats and the Senate by the Republicans. This situation implies that hopes for clear and decisive fiscal stimulus can be unlikely, though further support measures are likely to be put in place. This plays into a cautious outlook for economic growth with the coronavirus still with us.

The recent economic data is showing a very strong rebound in activity during Q3, following the dramatic plunge that had taken place during the second quarter. It is becoming clear that China in particular, but also other Asian/southern hemisphere countries that followed a virus eradication approach, are returning toward pre-COVID normal more quickly. In contrast, Europe and the UK are already looking vulnerable to a double-dip recession as the virus grip is proving particularly severe. The US seems to be delicately treading a middle path, on one hand dealing with surging virus cases but so far managing to avoid the pull towards broader and more restrictive measures. That said, the northern hemisphere is facing seasonal risk (the winter) on top of the already vulnerable situation. In addition, the bias in the early Q4 data suggests that growth is already slowing and that the overall services sector will remain compromised for some considerable time. There continues to be a steady drip of optimism on vaccine development, but it is still too early for this to be built into outlook assumptions, particularly as there are likely to be significant logistical delays to wide deployment.

In the meantime, policy makers continue to give considerable support to the economy. Prospects are that further monetary easing will be deployed in the coming months, with focus on the European Central Bank and the Bank of England to follow the easing announced this week by the Reserve Bank of Australia. While this is likely to be welcomed by financial markets, the real benefit to economic activity is likely to be modest. Fiscal policy is now seen as the key to igniting economic activity. But as this is subject to politics, its deployment is much less certain. Europe agreed to significant stimulus in July, but by delaying deployment until January economic activities have suffered. Talks in the US are for significant stimulus, but Congress and the White House cannot agree on how much or where to spend. The key uncertainty therefore is: will this become clearer after the election?

In summary, we believe the 'lower for longer' environment is likely to continue to characterise fixed income investment for a considerable period. As we expect central bankers to maintain highly supporting policies, financial markets should be underpinned, but pocketed by periodic volatility as the real economy tries to navigate the very difficult months ahead.

Macquarie Dynamic Bond Fund

Monthly report – 31 October 2020

For more information speak to your financial adviser, call us on 1800 814 523, email mim.clientservice@macquarie.com or visit macquarie.com