

Macquarie Dynamic Bond Fund

Monthly report – 31 July 2023

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.

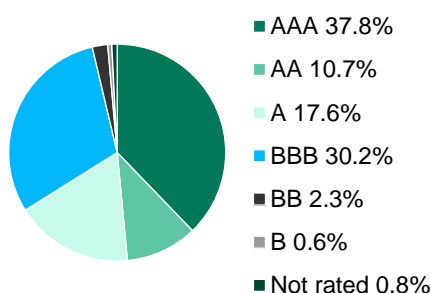
Key information

Fund details

APIR code	MAQ0274AU
Inception date	30 September 2002
Fund size	\$1,021.2m
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 July 2023

	Total Fund return (gross)	Total Fund return (net)	Benchmark return	Total excess return (net)
1 month (%)	0.68	0.63	-0.04	0.67
3 months (%)	-1.48	-1.63	-0.75	-0.88
1 year (%)	-1.30	-1.90	-3.60	1.70
3 years (% pa)	-1.95	-2.55	-3.98	1.43
5 years (% pa)	1.71	1.08	0.17	0.91
10 years (% pa)	3.04	2.41	2.47	-0.06

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 24 August 2021, the Bloomberg Barclays fixed income benchmark indices were rebranded as the "Bloomberg Indices". As a result, the "Bloomberg Barclays Global Aggregate 1 to 10 years Index hedged to AUD", was renamed "Bloomberg Global Aggregate 1 to 10 years Index hedged to AUD."

From 1 January 2023, the benchmark is the Bloomberg Global Aggregate Index (Hedged to AUD). Prior to this, the Fund had different benchmarks. The Benchmark return and Total excess return (net) information shown above is based on the current benchmark. Over certain periods, these returns may be materially higher than the returns against the previous benchmarks. Further information about the performance of the Fund against the previous benchmarks is available on request.

Asset allocation

	Fund (%)
Sovereign bonds [^]	43.1
Investment grade credit*	51.6
High yield	1.6
Emerging markets debt [^]	3.7

[^]Includes Australian government, Australian semi-government, supranational, global sovereign and cash

*Includes Australian and global investment grade credit

[^]May include holdings of sub-investment grade instruments

Fund statistics

Credit spread duration	2.6 years
Interest rate duration	5.2 years
Standard deviation [^]	3.5% pa
Yield to maturity*	4.9% pa

[^]Statistical measure of variance of Fund's post-fee monthly returns from its average post-fee return since inception used as gauge of volatility.

*Pre-fee returns 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 [^] (%)
North America	59.2
Europe (ex UK)	8.5
UK	12.9
Australia/New Zealand	20.9
Japan	-7.1
Others	5.6

[^]Calculated based on security's currency

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Fund highlights

The Fund covered some of its underweight Japanese govt bond position after the Bank of Japan announced some changes to its Yield Curve Control policy. Overall interest rate risk remained reasonably steady as duration was trimmed in core holdings such as US Treasuries and Australian government bonds. The Fund added to yield curve steepening positions over the month as the global central bank tightening policy reaches its latter stages.

The Fund's credit positions contributed to performance versus the benchmark for July. Amongst credit sectors, security selection within investment grade was a key contributor, as were emerging markets holdings due to tighter spreads in all risk markets. Amongst individual issuers, Australian and global financials were amongst the largest contributors (Morgan Stanley, Westpac and NAB, amongst others), as the global banking sector rebounded strongly after lagging for several months. Amongst underperformers, AT&T modestly detracted, as reports of lead sheathing on some of the company's legacy wireline network added uncertainty to the picture – we remain very comfortable with the long-term fundamentals of the issuer.

The Fund made small changes to credit exposure over the month, adding modestly to global issuers to maintain yield in an ongoing uncertain environment. The Fund further added to Agency MBS securities, with spreads on these sectors remaining at the upper end of historical ranges, which continue to offer attractive yields with very strong fundamental credit quality. The Fund also added credit downside protection via options, which we believe provides low-cost and positive-asymmetric protection for the portfolio, in the case of a meaningful sell-off in the coming months. We continue to expect opportunities to add to credit positions over time - but at higher spread levels, given the likelihood of economic weakness in the medium term.

Market overview

The market narrative with regard to the economic outlook has evolved toward a belief that a soft landing for the economy can be achieved, while inflation gradually eases back toward target. Risk markets have embraced this narrative, with equities surging, led by the US (S&P500 +3% in July and +10% since end May), and credit spreads tightening (IG -16bp in EUR and -10bp in USD, HY -23bp and Emerging Markets -35bp). The inflation data is clearly slowing, again led by the US, as supply pressures continue to dissipate, and slower demand gradually quells pricing power. The economic data is more mixed, but where the broader resilience of the service sector stands in stark contrast to the manufacturing sector which is in recession in most countries. Perhaps the biggest surprise has been the resilience of the labour market, where the slowdown has slowed hiring but not leading to large job losses.

Central banks, on the other hand have yet to be convinced of this 'goldilocks' outcome on growth and inflation. Certainly, policy rates have been tightened faster and more significantly than any time since the 1970s, yet many central banks continue to push rates higher. Hopes (from markets) for a 'pause' are ever present but this belief was put to the sword several times already in this cycle. Part of the problem is that governments have been reluctant to wind back spending despite the passing of the pandemic crisis. Thus, monetary policy is carrying more weight to slow growth and pull inflation back to target. For bond markets, lower inflation should be good news for lower yields but the upward pressure on short term yields from central bank tightening has created a negative carry environment that is proving difficult to fight.

Outlook

The battle lines of debate have been drawn, are you in the recession camp or the no recession camp. Consensus for a long time has been convinced recession would be inevitable, sustained yield curve inversion never gets it wrong? Yet long and variable lags are difficult to live through even if the inevitable ends up becoming true.

The big surprise in 2023 has been fiscal spending, which has remained more persistent than expected, underpinned by large increases to benefits and salaries and support for the Ukraine war effort. As fiscal spending feeds directly into the economy it has underpinned the jobs market, household incomes and therefore spending. The impact of monetary tightening is gradual and importantly felt differently between countries depending on lending practices. That said, higher rates are a drag on growth but for households and business there can be winners (e.g. savers) and losers (e.g. borrowers). Key for the economy is when this is accompanied by a tightening of lending conditions, which is taking place, the combination of monetary over-tightening and excessive tightening of credit conditions has resulted in recession every time in the past.

Our base case outlook remains for a cyclical recession, similar to 2001, acknowledging that hard landing risks have reduced in recent months. Our highest conviction view this year has been for inflation to fall, highlighting the possibility of a dip into deflation, remains on track. This is key for our position to add duration into each back up in the bond market. Risk markets remain very tightly priced, and therefore vulnerable to weaker growth emerging through the second half of this year. In addition, the environment of monetary over-tightening and tightening credit conditions also signals risk for potential financial dislocation, such as experienced with US Regional Banks earlier in the year. History guides that risky assets do not tend to react significantly until evidence of a downturn or financial risk become clearly evident. We therefore maintain a strategically constructive view on duration and cautious of risk markets, recognising that the pathway ahead is potholed by a high level of uncertainty.

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

Important information

Macquarie Investment Management Australia Limited ABN 55 092 552 611 AFSL Licence 238321 is the issuer of units in, and responsible entity of the Fund. Macquarie Investment Management Global Limited ABN 90 086 159 060 AFSL 237843 is the investment manager of the Fund.

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