

Capital Group Global High Income Opportunities Hedged (AU)

Market review

- The fourth quarter was host to a continued “risk on” market environment, with lower-rated, riskier segments of fixed income markets delivering the strongest results as investors sought out higher yielding assets. However, investor sentiment was somewhat tempered by news out of the UK of a more contagious strain of the COVID-19 virus.
- U.S. fixed income markets posted another quarter of gains, boosted by the rollout of COVID-19 vaccines, passage of an economic stimulus bill, and some clarity around the U.S. election. The Fed left interest rates at near-zero at its December meeting, and pledged to continue buying government-backed debt for the foreseeable future.
- Elsewhere, both local currency and U.S. dollar-denominated emerging markets debt rose. US dollar-denominated debt, as measured by the J.P. Morgan EMBI Global Index¹, gained 5.5% in US dollar terms. Meanwhile, local currency debt, as measured by the J.P. Morgan GBI-EM Global Diversified index², climbed 9.6% in US dollar terms. With very low yields in developed markets, investors flocked to higher yielding government debt in places such as Mexico and South Africa. In currency markets, the South African rand appreciated the most against the U.S. dollar.
- The high yield market, as represented by the Bloomberg Barclays US High Yield 2% Issuer Cap index returned 6.4% over the quarter in US dollar.³

Portfolio review

- For the three months ended 31 December 2020, Capital Group Global High Income Opportunities Hedged (AU) returned 7.5%⁴ before fees, while the index returned 6.4%.⁵ Net of fees, the fund returned 7.3%.⁶ Over a one-year period, the fund returned 8.4%⁴ before fees and 7.5%⁶ after fees, compared to the index’s return of 4.0%⁵.
- **Areas that helped the portfolio in Q4⁷**
 - **Mexican local currency and hard currency sovereign bonds**

Mexican local currency bonds offer relatively high real yields, scope for policy easing, and a well-supported currency. Meanwhile, the hard currency bonds have been supported by an improving external outlook, helped by US fiscal stimulus and hopes for a vaccine.
 - **Indonesian local currency sovereign bonds**

The Indonesian rupiah appreciated almost 6% relative to the US dollar over the quarter, helping returns for the local currency bonds. Subdued inflation should continue to provide support to Indonesian local currency bonds.
- **Areas that hurt the portfolio in Q4⁷**
 - **Argentine hard currency sovereign bonds**

Argentina defaulted on its sovereign debt repayments in 2020, resulting in capital outflows. It has also been suffering from double-digit inflation, a weak fiscal position and the impact of the COVID-19 lockdown.

- **Frontier Communications (integrated telecom services)**

The heavily indebted US telecoms group entered Chapter 11 in early 2020, but is widely expected to exit from that early in 2021. The company owns significant fibre assets across the US and our analyst sees potential for growth in that area as well as scope for meaningful de-leveraging.

Outlook

The portfolio continues to have a modest tilt towards emerging market debt.

High yield

- Managers maintain a cautious stance given rich valuations but continue to have strong issuer credit convictions and are still finding relative value opportunities.
- In particular, they added to their holdings of Ford Motor Company. It is a high-quality, prime auto lender with a proven business model in downside scenarios. The company's bonds have been large beneficiaries of the Fed's bond buying programmes and our analyst views them as a core, liquid BB holding within a high yield portfolio. Managers reduced positions in Owens & Minor and PetSmart.

Emerging market debt

- Portfolio managers increased holdings in Indonesian and Mexican local currency bonds. Owning Indonesian local currency duration is relatively attractive given the yield on the local currency bonds relative to the country's policy interest rate. Mexico has pursued austerity to help counter the economic impact of the pandemic. It could also continue to benefit from greater optimism around the global economic recovery as well as low interest rates in developed markets.
- Portfolio managers also reduced positions in the Dominican Republic and Brazil.

Markets have recovered significantly since the height of the crisis experienced in the first quarter of 2020. Portfolio managers have reduced the overall risk profile of the portfolio as a result. They stand ready, however, to adopt a more risk-on stance should volatility re-emerge and assets reprice again. They continue to maintain a cash buffer to deploy into new issues and/or relative value opportunities.

Stock returns are total returns as shown in local currency terms, unless otherwise stated. Sources: Capital Group, Barclays Capital, JPMorgan

¹ JPM EMBI Global Total Return. Source: JPMorgan

² JPM GBI-EM Global Diversified Total Return. Source: JPMorgan

³ Bloomberg Barclays US Corporate High Yield 2% Issuer Capped Index. In US dollar terms. Source: Bloomberg Barclays

⁴ Returns are before management fees and expenses, in Australian dollar terms. Source: Capital Group

⁵ 50% Barclays Capital U.S. Corporate High Yield 2% Issuer Capped Index hedged to AUD, 20% JPMorgan Emerging Markets Bond Index Global hedged to AUD, 20% JPMorgan Global Bond Index - Emerging Markets Global Diversified in USD hedged to AUD, 10% JPMorgan Corporate Emerging Markets Bond Index Broad Diversified hedged to AUD. Sources: Barclays Capital, JPMorgan

⁶ Returns are net of fees at maximum management fee, in Australian dollar terms. Source: Capital Group

⁷ Data reflects absolute contributions to GHIO returns, in US dollar terms

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