iSHARES ESG GLOBAL BOND INDEX FUND

iShares by BlackRock

FUND UPDATE **31 May 2023**

Investment Performance (%)

	1 Mth	3 Mths	YTD	1 Yr	3 Yrs	5 Yrs	Since Incep
iShares ESG Global Bond Index Fund (Gross of Fees) (Class E)	-0.55	1.95	2.14	-2.89	-3.55	-	-1.90
Bloomberg Barclays MSCI Global Agg SRI Select ex-Fossil Fuels Index 100% AUD Hedged	-0.55	1.96	2.23	-2.87	-3.64	-	-1.91
Outperformance (Gross of Fees)	0.00	-0.01	-0.08	-0.02	0.09	-	0.02
iShares ESG Global Bond Index Fund (Net of Fees) (Class D)	-0.57	1.90	2.06	-3.08	-3.71	-	-2.12
Bloomberg Barclays MSCI Global Agg SRI Select ex-Fossil Fuels Index 100% AUD Hedged	-0.55	1.96	2.23	-2.87	-3.64	-	-1.91
Outperformance (Net of Fees)	-0.01	-0.06	-0.17	-0.21	-0.06	-	-0.21

Past performance is not a reliable indicator of future performance. Performance for periods greater than one year is annualised. Performance is calculated in Australian dollars and assumes reinvestment of distributions. Gross performance is calculated gross of ongoing fees and expenses. Net performance is calculated on exit-to-exit price basis, e.g. net of ongoing fees and expenses. Gross returns are provided for products offered to wholesale clients only who may be subject to differential fees. Please refer to the Fund's product disclosure statement for more information.

Performance Summary

Market Review

US

In May, U.S. debt ceiling negotiations dominated market sentiment throughout the month. Luckily, the U.S. debt ceiling deal, where U.S. President Biden and House Speaker Kevin McCarthy reached an agreement to lift the debt ceiling through to 2025 and avoid a technical default, that was passed with a few days left to spare. This removes near-term uncertainty and thrusts the market's focus back to the macro outlook with sticky inflation and a tight labor market. As a result, duration trended cheaper and the curve steadily flattened in May. The 10yr note traded in a 56bp intramonth range, finishing ~20bps cheaper from where we came into the month. As fears of a default gradually eased, mixed Fed rhetoric and stubbornly strong economic data ultimately helped catalyze the bear flattening.

During the May FOMC voted unanimously to raise rates 25 bps, moving the fed funds target range to 5.0-5.25%, in line with the median dot from their March SEP. When asked about the rate cuts priced by the market, Chair Powell said that it would not be appropriate to cut rates given the committee forecast for still elevated inflation at the end of the year. The Committee hinted at a pause in rate hikes for the June FOMC meeting when the statement removed mention of "some additional policy firming" being needed.

On the U.S. data front, we have seen some progress on moderating underlying inflation but there is still a ways to go. April Core CPI, released in May, rose 0.41% MoM, edging down YoY inflation back to 5.52% from 5.59%. Headline CPI climbed 0.37% mom in April, rebounding from 0.05% in March as the YoY rate inched down to 4.9% from 5.0%. Core services moderated to 0.36% MoM in April from 0.45% and the YoY rate slowed to 6.8% from 7.1%. As expected, OER and rents modestly rebounded but are averaging 0.5% mom over the past two months, down from its prior trend of 0.7%. Core goods rose 0.57% MoM in April, rebounding from 0.18% MoM in February and the YoY rate accelerated to 2.0% yoy from 1.5%. Apart from autos, which cooled 0.1% MoM, some major categories that saw gains were other goods rising 0.2% MoM, apparel and recreation goods up 0.3% mom, and medical

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goods and alcohol increasing 0.5% MoM. In terms of employment, the April payroll report, released in May, was consistent with a slowing labor market, but not a weak one. Total nonfarm payrolls rose 253K in April with downward revisions to prior months of 149K taking some of the shine off the report. Goods-producing employment rose 33K with support coming from construction and durable goods manufacturing. Employment in the more cyclical services sector, professional and business services, rose 43K, although temp help remained in contractionary territory with a decline of 23K. The unemployment rate fell 11 bps to 3.39% in April, the lowest level since May 1969. The overall labor force participation rate edged down 6 bps to 62.6%, pausing after starting off the year with a strong three-tenths improvement.

The US 10-year Treasury opened at 3.43% and increased throughout the month, closing 22bps higher in yield at 3.65%. US rates stayed in range until mid-May, when debt ceiling negations and approaching X date began to dominate market sentiment. This was further exacerbated by market awakening of sticky inflation, making rate cuts this year unlikely. The 2yr yield sharply repriced to 4.56% at one point, before ending May at 4.40%. The 10yr note pushed higher, but at a smaller magnitude, bringing the 2s10s curve to a monthly low of -76bps. The 5s30s curve flattened by 8bps, reaching 13bps at month end.

Eurozone

Rates markets finished the month almost unchanged although this hid material moves intramonth with volatility remaining elevated. Initially impacted by the resilience of inflation in the UK, European duration markets sold-off with 10-year German yields rising above 2.50%. These moves were subsequently reversed after inflation data in Europe demonstrated prices rose slower than analyst expectations.

The next ECB meeting is on the 15th June with close to 25bps of tightening priced by the market. Thereafter, expectations are for one more hike (bringing the deposit rate to 3.75%) with rates held at these levels for the remainder of 2023. Comments by ECB members were deemed to support this with Executive Board member Fabio Panetta advising "we have not yet reached the final destination, but we are not far from it". In addition, whilst President Lagarde admitted inflation is still too high there was an admission with regards future hikes that "we need to continue climbing, but not as rapidly".

The evolution of inflation markets dominate rate expectations with European data suggesting inflation is falling at a quicker pace than analyst expectations. Rising at the slowest pace since the invasion of Ukraine, inflation was 6.1% in May, down from 7% in April and lower than expectations of 6.3%. Core inflation (stripping out volatile food and energy components) fell from 5.6% to 5.3% although these moves were assisted by subsided public transport tickets in Germany. Forward looking gauges including manufacturing price setting expectations suggest further downside whilst improvement in supply chains and further falls in commodities are additional tailwinds for this theme to continue.

Despite a recent downgrade and uncertainty over future action from another agency, French and German sovereign spreads contracted through May. Periphery countries also performed with spreads between Italian and German bonds (10 year) reaching 180bps (170bps year to date low) although noticeable outperformer was Greece. Recently upgraded to BB+ from Fitch and approaching investment grade status, spreads tightened by almost 50bps in May and now trade at 140bps over Germany, 40bps lower than Italy.

In other markets, dominating themes centred around the US debt ceiling and underperformance of UK gilts. Uncertainty concerning the former saw yields on 1 month treasury bills rise above 6% as investors attached a premium to liabilities maturing close to the perceived 'X' date (day in which US could no longer meet its financial obligations). Subsequently resolved, investor focus will now turn to anticipated volume of treasury bill issuance and thereafter the speed at which the maturity profile of these new issues is increased. In the UK, sticky inflation data saw expectations for further tightening from the Bank of England increase. Gilt yields reached levels witnessed during the LDI crisis in September 2022 although slower pace of change ensured markets functioned as expected.

UK

Even with three bank Holidays for the month of May the UK gilt market managed to experience significant volatility – alongside a twelfth consecutive rate hike by the Bank of England (BoE), Inflation again beating expectations, GDP coming in well below estimates and a poor Manufacturing PMI print. Macro was largely the story for the month while credit was incredibly muted compared to the moves seen in gilt yields, with 10yr Gilt yields rising over 70bps at one point to reach levels only seen during the LDI crisis last autumn. To give the volatility context, Gilt yields moved over 50bps across the curve this month briefly surpassing their US equivalents. The market is now pricing another 100bps of rate hikes by the BoE, after inflation beat expectations for the third month in a row. Similar to last month the data continues to prove the BoE is unlikely to cool tightening anytime soon.

The start of the month saw BoE's Monetary Policy Committee (MPC) hike rates 25bps to 4.5% in a 7-2 vote, in line with expectations as inflation continued to surprise to the upside in both core and headline components. UK GDP shrank by -0.3% MoM yet was in line with expectations YoY at 0.2% growth and 0.1% QoQ growth. Manufacturing PMI hit a 3-month low of 47.8 while Services PMI was the highest it's been in a year at 55.9. The month's biggest economic print was inflation, core at 6.8% YoY vs expected 6.2% and headline 8.7% YoY vs expected 8.3%. Good prices have started to fall but a tight labour market has fueled wage growth putting added pressures on domestic prices. The market now prices four additional 25bps interest rate hikes by the BoE as the sharp drop in wholesale energy prices has taken much longer than expected to feed through to consumers.

Japan

JGB yields declined in shorter-than 5yr zone, but rose in longer-than 7yr zone. 10Yr yield ended the month 4bp higher at 0.43%.After the Fed raised interest rates by 0.25% as expected at the beginning of the month, there was a strong belief in the markets that the rate hike cycle was over, but then strong economic indicators and hawkish comments from some FOMC members led to volatility in the major foreign bond markets toward the end of the month. One the other hand, the domestic bond market remained within a relatively narrow range.

The overall inflation ex-perishable food was +3.4% YoY in April, and remained above the central bank's 2% target for thirteenth straight month as food prices continued to be high. The unemployment rate remained relatively low at 2.6% in April.

Risk Characteristics

	Fund	Benchmark
Average Maturity (Years)	8.55	8.68
Modified Duration (Years)	6.86	6.82
Norminal Yield (%)	3.61	3.63
Convexity	0.85	0.86

Top 10 Issuers (%)

	Weight (%)
UNITED STATES TREASURY	19.7
JAPAN (GOVERNMENT OF)	12.6
UNIFORM MBS	9.3
CHINA PEOPLES REPUBLIC OF (GOVERNMENT)	5.8
GOVERNMENT NATIONAL MORTGAGE ASSOCIATION 2	2.9
ITALY (REPUBLIC OF)	2.8
UK CONV GILT	2.8
FRANCE (REPUBLIC OF)	2.5
GERMANY (FEDERAL REPUBLIC OF)	2.3
SPAIN (KINGDOM OF)	1.8

Top 10 Issuers held by ESG score

	ESG Score
AKZO NOBEL NV	10.0
ASSICURAZIONI GENERALI SPA	10.0
BUNGE LIMITED FINANCE CORPORATION	10.0
COMPAGNIE GENERALE DES ETABLISSEMENTS MICHELIN SCA	10.0
COUNCIL OF EUROPE DEVELOPMENT BANK	10.0
CRH FINANCE DAC	10.0
DANONE SA	10.0
DNB BANK ASA	10.0
DNB BOLIGKREDITT AS	10.0
EMD FINANCE LLC	10.0

Quality

	Fund %	Benchmark %
Aaa	43.7	43.8
Aa	13.9	13.9
A	29.6	27.9
Baa	13.0	12.7
Ba	0.0	0.0
NR	-0.2	1.7

Maturity Exposure

	Fund %	Benchmark %
< 5	42.14	41.59
5 - 10	33.34	33.54
>= 10	24.52	24.87

Country Exposure

	Fund %	Benchmark %
US	41.44	41.57
Japan	13.21	13.17
China	5.96	5.95
Germany	4.54	4.50
France	5.35	5.19
UK	4.48	4.30
Italy	3.21	3.06
Canada	3.41	3.45
Other	18.41	18.81

ESG Sector Score

	Fund	Benchmark
Treasuries	6.15	6.16
Government Related	6.49	6.42
Corporates	5.67	5.52
Securitized	5.39	5.38

ESG Score Breakdown

	Fund	Benchmark
Environmental	5.38	5.28
Social	6.75	6.74
Governance	6.29	6.31

Green Bonds Exposure

	Fund %	Benchmark %
Green Bonds	0.10	0.03

About the Fund

Investment Objective

The Fund aims to match the return of the Bloomberg Barclays MSCI Global Aggregate SRI Select ex-Fossil Fuels index (AUD hedged) before fees less interest withholding taxes and the cost of currency hedging.

Fund Strategy

The strategy seeks to match the distribution of the risk-and-return factors of the index through a "stratified sampling" approach. This approach breaks the index into "cells" of securities that have similar factors of risk and return and then build a portfolio to match these cells. The factors we consider are interest-rate risk, credit risk and specific (security) risk.

Should be considered by investors who ...

- Seek broad exposure to global bonds.
- Seek a fund that uses a stratified-sampling approach so returns match those of the global bond market before fees and before the cost of currency hedging.
- Have a long term investment horizon.

Fund Details

iShares ESG Global Bond Index Fund (Class E)	
APIR	BLK2319AU
Fund Size	523 mil
Buy/Sell Spread	0.10%/0.10%
Tracking Error (3 Years p.a.)	0.15%

iShares ESG Global Bond Index Fund (Class D)	
APIR	BLK4636AU
Management Fee	0.20%

^ The actual inception of the Fund is 1 August 2019.

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