

ASIA FIX



A monthly brief on Fixed Income markets, sector performance, bond ETF flows and product trends

iShares Fixed Income Product Strategy

August 2024

July Market Highlights

Global Rates

In the US, July's FOMC meeting saw rates kept on hold again as expected, though the Fed gave a strong signal for a September rate cut following encouraging signs that inflation continues to move in the right direction. The bond market rallied, and 2Y and 10Y yields ended the month lower at 4.26% and 4.03% respectively. In Europe, the ECB held rates steady after a cut in June, following upside inflation surprises and downside growth news. Meanwhile in Asia, the BOJ surprised markets by raising interest rates to 0.25%, while providing guidance for further hikes ahead. 10Y JGB yields finished at 1.05%.

Credit

In the US, after a surge in IG credit spreads in June, spreads edged slightly downwards over July, tightening 1bp to end the month at 93bps. Meanwhile, US HY credit spreads widened 5bps to 314bps. In the region, Asia IG credit spreads hovered at previous levels, ending the month 3bps higher. Asia HY credit spreads continued to tighten, narrowing by 13bps.

Performance and yield level of key asset classes as of 2024/07/31

	Index	Total Return			Yield level		Spread level (bps) (credit only)	
		YTD	QTD	MTD	Jul-end	ΔMTD	Jul-end	ΔMTD
Aggregate	Global Aggregate	-0.49%	2.76%	2.76%	3.62%	-0.28%		
	US Aggregate	1.61%	2.34%	2.34%	4.64%	-0.36%		
	Japan FI, N-BPI	-3.05%	-0.10%	-0.10%	1.02%	0.05%		
Treasury & Agency	US Treasury	1.31%	2.19%	2.19%	4.19%	-0.38%		
	Agency MBS	1.63%	2.64%	2.64%	4.88%	-0.34%		
	China(CGB+PB)	4.68%	0.79%	0.79%	1.93%	-0.10%		
Credit (IG & HY)	US IG Corporates	1.89%	2.38%	2.38%	5.14%	-0.34%	93	-1
	US HY Corporates	4.58%	1.94%	1.94%	7.59%	-0.32%	314	5
	Asia IG, JACI IG	2.91%	1.30%	1.30%	5.17%	-0.18%	134	3
	Asia HY, JACI HY	12.14%	1.47%	1.47%	11.86%	-0.39%	657	-13
Emerging Markets	EM HC, EMBI GD	4.26%	1.87%	1.87%	8.18%	-0.23%	400	9
	EM LC, GBI-EM	-1.52%	2.27%	2.27%	6.37%	-0.22%	-	-

Source: Bloomberg, as of 31 July 2024. See notes at the bottom for indices used. Past performance is not a reliable indicator of current or future results and should not be the sole factor of consideration when selecting a product or strategy. Indices are unmanaged and one cannot invest directly in an index.

FX Hedging: FX Forward Premium or Cost as of 2024/07/31

FX Forward Premium or Cost is associated mainly with short-term interest rate differential between domestic and foreign currency (& currency basis). This impact can be positive or negative depending on the currency pair.

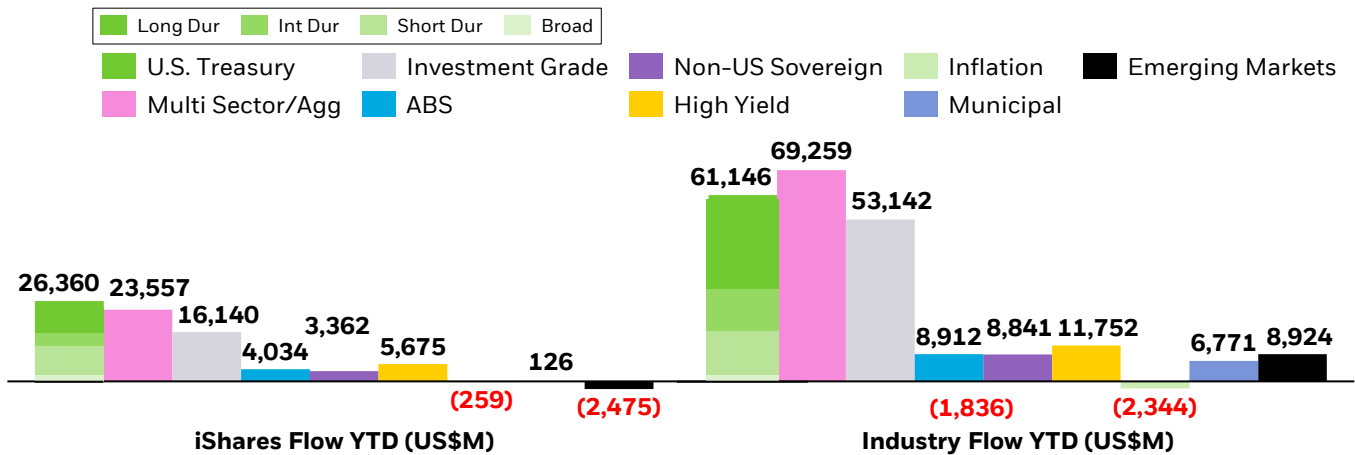
Currency to Hedge (Forward tenors: 3-month and 12-month, annualized)

Local Currency	3M		12M	
	USD	EUR	USD	EUR
JPY	-5.48%	-3.72%	-4.50%	-2.91%
KRW	-2.21%	-0.45%	-2.00%	-0.37%
AUD	-0.86%	+0.90%	-0.41%	+1.26%
CNY	-5.99%	-4.25%	-2.63%	-1.01%
SGD	-1.81%	-0.06%	-1.66%	-0.00%

Source: Bloomberg, as of 31 July 2024. Indices used: BBG Global Aggregate Index (USD, unhedged), BBG US Aggregate Index (USD), NOMURA BPI (JPY), BBG US Treasury Index (USD), BBG Agency MBS Index (USD), BBG China Treasury & Policy Bank Index (CNY), BBG US IG Corporate Index (USD), BBG US HY Corporate Index (USD), JP Morgan Asia Credit IG Index (USD), JP Morgan Asia Credit HY Index (USD), JP Morgan EMBI Global Diversified Index (USD), JP Morgan GBI-EM Index (USD, unhedged). Reference to the company name mentioned in this communications is merely for explaining the investment strategy, and should not be construed as investment advice or investment recommendation of those companies.

2024 July iShares Status Flow

- Global iShares Fixed Income ETF flows hit a 2-year high in July, gathering +\$21B of new assets**, the highest flow month since May 2022 during the consecutive rate hike period. US rates products led inflows +\$6.6B, followed by Investment Grade +\$5.2B, broad market +\$3.3B and High Yield +\$3B ETFs.
- In July, U.S. Treasury ETFs were the biggest contributor to flows across maturity buckets.** Driven by a combination of rate cut expectations in Q3 and an elevation in short-term UST yields, ultrashort ETFs including 0-3M and 0-1Y UST were particularly favored, bringing in +\$2.6B. Investors also allocated +\$2.3B to long term bonds, with the bulk of flows into 20Y+ UST.
- Within Credit, flows into IG were largely driven by trading vehicles.** iBonds fixed maturity ETFs added +\$942M, while floating rate bonds gathered +\$400M. Asset backed securities added +\$798M for the month, mostly into the MBS ETF.
- On riskier assets, High Yield gathered over +\$3B** in USD broad market and EUR HY Corporate bonds. **Hard currency EM ETFs saw +\$374M** of inflows as local currency exposures shed assets, while China and India government bonds were bright spots from a single country view, with the latter growing 27% in fund size over the past month.



Top/Bottom iShares Fixed Income ETF Sector Flows

Top 5 Exposures	MTD Flow (\$M)	% of AUM
Investment Grade - Broad	3,663	3%
Multi-Sector - Broad	3,271	2%
High Yield - Broad	2,861	5%
U.S. Treasury - Short Dur	2,634	3%
U.S. Treasury - Long Dur	2,305	3%
Top 5 Exposures Total	14,733	

Top 5 Exposures	YTD Flow (\$M)	% of AUM
Multi-Sector - Broad	24,913	14%
U.S. Treasury - Short Dur	9,366	10%
U.S. Treasury - Long Dur	8,357	11%
Investment Grade - Broad	7,747	7%
Investment Grade - Fixed	6,849	30%
Top 5 Exposures Total	57,231	

Bottom 5 Exposures	MTD Flow (\$M)	% of AUM
Investment Grade - Int Dur	(114)	-1%
Inflation - Short Dur	(74)	-1%
Convertible - Broad	(11)	-1%
Covered Bond - Int Dur	(11)	-2%
Non-U.S. Sovereign - Broad	(5)	0%
Bottom 5 Exposures Total	(215)	

Bottom 5 Exposures	YTD Flow (\$M)	% of AUM
CDS - Broad	(2,583)	-21%
Emerging Markets - Broad	(2,390)	-6%
Multi Sector - Short Dur	(924)	-8%
Inflation - Short Dur	(575)	-6%
Municipal - Short Dur	(352)	-4%
Top 5 Exposures Total	(6,824)	

Source: BlackRock, as of July 30 2024. Reference to \$ refers to USD.
iShares and industry ETF flows encompass globally listed products. 'Broad' categories reference blended maturity products.

Giving credit where credit is due

As July sees record monthly flows in fixed income, fund flows into credit ETFs in particular have been gaining momentum, even as credit spreads continue to tighten on the back of a (still) resilient-than-expected economy. We see investors looking to credit ETFs for their liquidity benefits in navigating episodes of market volatility, as can be seen through average daily volume (ADV) and % share of largest credit ETFs traded. (left table)

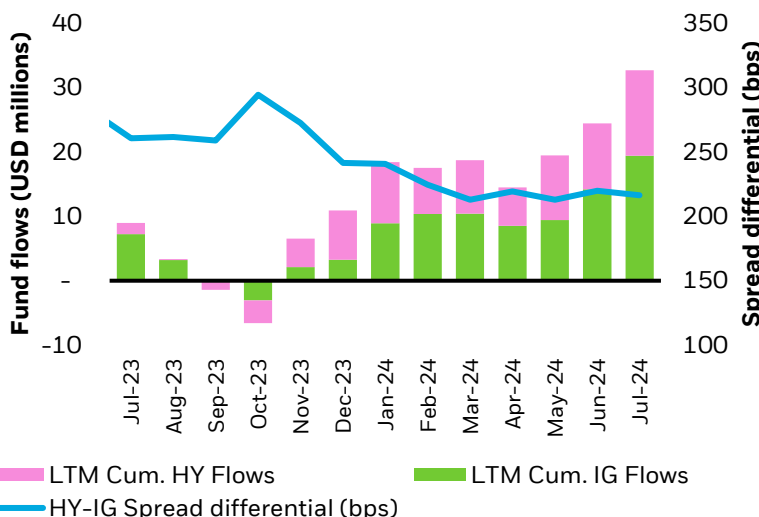
The right chart shows, on a relative basis, that **high quality fixed income (green)** continues to attract more flows this year as investors turn more constructive in putting on quality duration trades and positioning for Fed rate cuts. That said, **high yield (pink)** did see +\$3B inflows, predominantly in US Broad HY (as mentioned in pg2). The AUM of the top 2 largest US HY ETFs have both increased over the past year, yet the AUM gap has significantly narrowed – signifying how investors are broadening out their use cases when allocating to US HY.

Credit ETFs see increasing trading volumes over the last few years

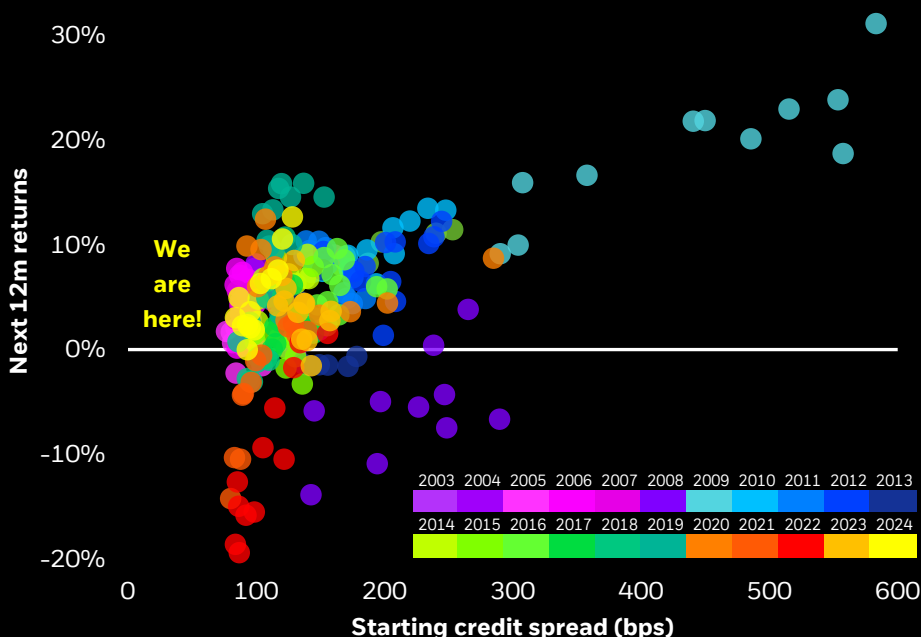
Year	IG ETFs		HY ETFs	
	Top 20 ADV (\$bn)	Top 3 share	Top 20 ADV (\$bn)	Top 2 share
2018	1.4	80%	2	88%
2019	1.9	83%	2.7	92%
2020	3.1	87%	4.5	87%
2021	3.3	84%	3.8	83%
2022	4.3	88%	5.7	84%
2023	4.1	85%	4.6	84%
2024*	4.8	89%	4	84%

Source: J.P.Morgan, Bloomberg, 31 July 2024. *Refers to YTD. Chart on the right from BlackRock, 31 July 2024. Based on iShares fixed income ETF flows. HY-IG spread differential reference to OAS levels for BBG US Corporate and US Corporate HY Total Return Indices.

And investors continue to roll deep in credit despite tightening credit spreads...



Yet historically tighter credit spreads have on average delivered positive returns over the subsequent 12 months...



Source: BlackRock, 31 July 2024. 2024 YTD returns are based on cumulative returns up till 31 July 2024 instead of next 12m returns. Reference to BBG US Corporate Total Return Index. The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results.

What may (not) surprise most is that **tighter credit spreads may not mean limited room for returns**. Historically, deeply negative 12m returns from a position of tight spreads can be attributed to mainly two key market events: 2008 GFC and COVID-19 crisis. In both cases, there were sharp duration sell-offs on top of credit spreads widening.

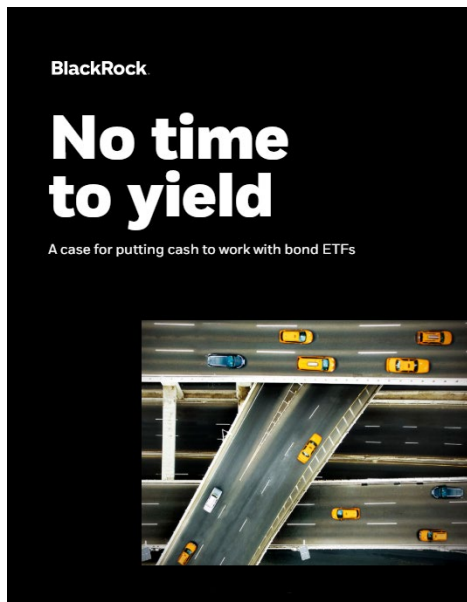
Year-to-date for 2024, spread assets have largely performed (marked in **yellow**) while returns in duration assets were broadly marginal.

Decade-high levels of all-in yields are expected to drive bond returns through rest of the year. The ability to stay nimble by picking points on the yield curve, i.e. at the intermediate portion, could balance both credit and duration risk, while optimizing for potential price appreciation, liquidity and current yields.

To find out more about credit ETFs, contact your iShares representative.

No Time to Yield

A case for putting cash to work with bond ETFs



Last year, our whitepaper **“The Great Yield Reset”** discussed the generational opportunity for investors to rethink their portfolios with a greater focus on fixed income.

In our latest paper **“No Time to Yield”**, we highlight our updated expectation that global bond ETFs will reach US\$6 trillion in AUM by 2030. We discuss the opportunity within bonds and why investors may want to consider moving now to capture decades-high yields, get cash off the sidelines, and employ efficient, precise tools such as bond ETFs in this new market regime.

As investors take a more dynamic approach to asset allocation, we believe bond ETFs are among the most powerful tools within the investor tool kit to navigate this market environment.

The timing of potential interest rate cuts may be uneven worldwide, but the message is clear: Don't wait.

Source: BlackRock, “No Time to Yield”, as of April 2024.
There is no guarantee that any forecasts made will come to pass.

Key themes we discuss in this piece:

1

Time to put cash to work and capture higher rates

Yields are higher today than they have been in years. If inflation indicators continue to fall, the time of elevated cash rates may be drawing to a close.

2

Investors are choosing bond ETFs in record numbers, but they have room to do more

Many investors are still significantly underweight to fixed income, with a 22% average allocation, based on total global industry AUM, far below the “60/40” portfolio allocation often referenced in balanced portfolio discussions.

3

Now is the time to move

Even with ongoing volatility in economic data and bond markets, we believe it's time for investors to move because, historically, the market has tended to price in rate actions before they occur.

Index Your Bonds with Asia Credit

Asia bond markets definitely have a part to play in the next leg of growth in index and ETF adoption. As investors continue to move beyond the “active versus passive” debate, constant product innovation will offer increasingly precise sources of potential returns, and help lead more investors to embrace bond index building blocks alongside high conviction active strategies in pursuit of optimal portfolio outcomes.

In this Asia-focused **“Index Your Bonds”** paper, we spotlight iShares Asia Credit exposures, provide insights on how they are managed in practice, and discuss how innovations such as ESG integration will make indexing an integral part of investing in Asia fixed income.



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