ALLIANCEBERNSTEIN®

FIVE QUESTIONS FOR FIVE YEARS

AB DYNAMIC GLOBAL FIXED-INCOME FUND

Global financial markets have experienced plenty of challenges during the five years since AllianceBernstein (AB) launched the AB Dynamic Global Fixed-Income Fund in Australia. We put five questions to Portfolio Manager, John Taylor**, about how the Fund has performed and what lies ahead.**

Q: WHAT WERE THE MARKET HIGHS AND LOWS FOR THE LAST FIVE YEARS AND HOW DID YOUR FUND RESPOND TO THEM?

Key events during this period were a sustained sell-off in credit in the second half of 2015 and, of course, the Brexit referendum result in mid-2016.

Investors in 2015 were worried about the economic slowdown in China and the collapsing oil price, which weighed heavily on equity markets before spilling over into credit. Spreads in general performed poorly and anything commodity-related underperformed massively.

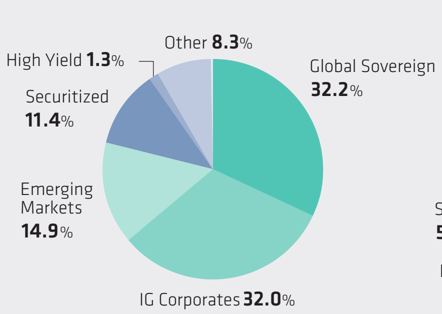
We already had significant exposure to higher-quality bonds and we owned Japanese yen; and the portfolio was relatively light on credit. Then, towards the end of first-quarter 2016, spreads showed signs of stabilising and we pivoted towards commodity-related credits and emerging-market debt, which had also suffered a lot.

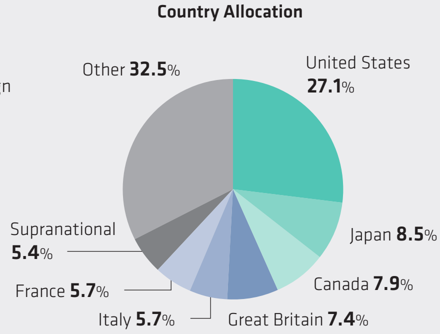
This meant that we delivered stability when credit spreads deteriorated and performed well when they began to recover again.

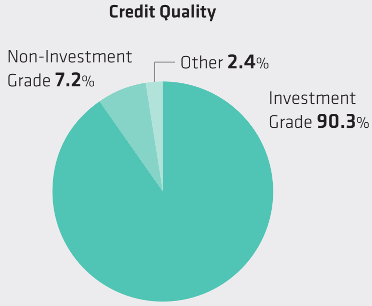
The uncertainty in the run-up to the Brexit referendum was a challenge which we addressed by hedging tail risks. We did this in three ways.

John Taylor
Co-Head of European Fixed Income and Director of Global Multi-Sector
John is a member of the Global Fixed Income, UK and European Fixed Income and Absolute Return portfolio-management teams. He joined the firm in 1999 as a fixed-income trader and was named in Financial News' "40 under 40 Rising Stars in Asset Management" in 2012.

FUND COMPOSITION (% OF ASSETS)







One was to have a short position in sterling, which we put on in the days just before the vote. The market had fully priced-in a victory for the Remain side, and we felt that it wasn't sufficiently discounting the possibility of a vote for Leave.

The second hedge was to buy inflation-linked gilts. The rationale was that, if Leave were to win, the pound would fall quite quickly, adding to inflationary pressure. That would have worked well for short-dated, inflation-linked gilts. There was virtually no downside to the transaction because, if Remain won, the implications for the gilts would have been neutral.

Thirdly, we bought protection by going short on some of the UK retail credits which, in the event of a Leave vote, would have to deal with higher import costs caused by the weaker pound and with the negative impact on UK economic growth. All three hedges worked well for us.

ALL THREE HEDGES WORKED WELL FOR US

Q: TO WHAT EXTENT DID THE FUND'S PERFORMANCE VALIDATE THE INVESTMENT THESIS BEHIND IT?

DGFI is a global, multi-sector fund unconstrained by market benchmarks, so it's really designed to go anywhere and do anything. That gives it enormous flexibility, which is what paid off so well during the credit sell-off, when we were able to position for a recovery in spreads by adding investment-grade commodity-related credit, general high-yield credit and various forms of emerging-market debt. For example, if you look at the European and US high-yield markets during late 2015 and 2016, they were generating returns of around minus 5 per cent while returns for DGFI were positive, at around 50 basis points.

Q: IF YOU COULD GO BACK FIVE YEARS, IS THERE ANYTHING YOU WOULD HAVE DONE DIFFERENTLY IN TERMS OF MANAGING THE FUND?

Looking back, I think we probably underestimated the impact that quantitative easing (QE) would have globally and in Europe, in terms of the size of the programmes and their longevity, and the extent to which they benefited fixed-income returns and helped to reduce volatility. With the benefit of hindsight, we could have increased all the positions in our portfolio—duration and credit—because, as it turned out, there wasn't that much volatility to worry about.

At the time, however, there appeared to be good reasons for not doing this, and they were mainly to do with valuations. German bond yields, for example, were about 100 basis points below what we regarded as fair value, and that was entirely because of QE.

You could argue that we were placing too much emphasis on a fundamental valuation framework at a time when the market was under the influence of such a strong technical factor, but it's fundamentals to which markets ultimately revert. You can see this from the investments that have started to underperform as QE has been unwound. People are now much more worried about Italy, for example, because there's less QE now to support Italian sovereign debt.

Q: LOOKING AHEAD, WHAT ARE THE MAJOR INVESTMENT RISKS AND OPPORTUNITIES THAT YOU SEE FOR THE FUND?

Volatility is likely to increase and, for a fund like DGFI, that's a risk and an opportunity. This will be partly the result of a reduction in QE and the effects of quantitative tightening as the US Federal Reserve winds down its balance sheet, but populism will be a big factor, too.

It's going to be with us for a long time. We've seen how it's given rise to surprising political developments such as Brexit and Donald Trump winning the 2016 US Presidential election, and how these upsets caused volatility in financial markets. Historically, the policies of populist governments tend to be inflationary, and that's something we're positioned for. Minimum wages around the globe are already rising and to some extent that's a populist phenomenon, as people are pushing back against how much profits have been going to shareholders over the years and how workers have suffered as a result.

Populism is also helping to reverse the trend to globalisation, and the US-China trade war is part of the evidence for that.

VOLATILITY IS LIKELY TO INCREASE: THAT'S A RISK AND AN OPPORTUNITY

Q: HOW ARE YOU POSITIONING THE PORTFOLIO IN VIEW OF THIS OUTLOOK?

We're positioned for structurally higher inflation, with 10 to 15% of the portfolio in inflation-linked bonds globally. We're also positively positioned in Italy because we feel that the sell-off in Italian spreads, which had been driven by the populist coalition, has been overdone and we can see the potential for some spread tightening. It's important to note that a bond market doesn't necessarily become un-investable just because the country it's in has a populist government. That's where the flexibility of the DGFI fund is so important. At times the market is going to panic just like any other, and that creates an opportunity to step in and position oneself advantageously.

At the same time, we haven't abandoned the traditional building blocks of the portfolio. We still have a big focus on owning short-term maturities in the better-quality end of the credit market to generate income, and balancing that exposure with high-yielding, high-quality government bonds. With that solid arrangement behind us, we try to use sell-offs in other markets to add even more value to performance.

FUND PERFORMANCE (%)

As of June 30, 2019

	Gross Fund Returns	Total Returns	Growth Returns	Distribution Returns	Benchmark Returns*
1 Month	0.79	0.75	(0.41)	1.16	0.13
3 Months	1.71	1.57	0.40	1.17	0.45
1 Year	4.85	4.30	2.35	1.95	1.97
2 Year	3.32	2.75	1.20	1.55	1.88
3 Year	3.53	2.92	0.45	2.47	1.86
4 Year	4.02	3.39	0.47	2.92	1.95
Since Inception†	4.00	3.36	0.95	2.41	2.09

* Benchmark: Bloomberg Ausbond Bank Bill Index
† Fund inception: June 2, 2014.

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FUND COMPOSITION DISCLOSURE

Numbers may not sum due to rounding. The Fund seeks to control risks and enhance returns through currency management. The Fund intends to hedge to Australian dollars most of the foreign currency exposures of its debt and fixed income securities, however up to 10% of the Fund's net asset value may be exposed to the risks and returns of international currencies. The Fund is currently 98.5% hedged to Australian dollars.

The Fund may invest up to 40% of its assets in lower rated, higher yielding non-investment grade debt and fixed income securities as rated by a credit rating agency ("CRA"). Debt and fixed income securities that are rated below investment grade are commonly referred to as "junk bonds". They are considered to be more speculative in nature and subject to a greater risk of loss of principal and interest income than investment grade securities. Investment grade rated assets, on the other hand, are those which, in the opinion of a CRA, are more likely to meet their financial commitments. Ratings assigned by a CRA are merely the opinion of that CRA about the likelihood of the issuers of the rated securities to meet their debt obligations when they fall due or the likelihood of loss in the event of a default of the issuer of the rated securities. Credit ratings used by the Investment Manager are intended for use by wholesale clients, and should not be relied upon by retail clients when making a decision about the product offered in the Fund's PDS. Ratings should not be taken to be an indication of investment merit or a recommendation to buy, sell or hold any particular investment. There are inherent limitations with credit ratings; future events and developments cannot be foreseen and credit ratings may change over time due to, among other things, a change in the financial condition of the issuer. The investment manager may use credit ratings of securities as an input into security selection alongside the investment manager's own screening, research and risk management processes.

PERFORMANCE FIGURES

In Australian Dollars. Numbers may not sum due to rounding. The Total, Growth and Distribution Returns of the Fund are net of fees and costs and do not allow for tax or inflation. Performance is calculated using the relevant end of month Exit Prices and assumes that income is re-invested and that the investment is held for the full period. The performance figures are historical and past performance is not necessarily an indication of future performance. The information above may change.

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