Principal®

Principal Global Investors Funds

Global Sukuk Fund

I Class November 2024

Market Review

US Treasury (UST) market initially weakened across the board in November, with yields moving higher, after Donald Trump's sweeping win in the US presidential election was met with mixed reactions. The new Republican government is expected to implement fresh rounds of policies, ranging from tariffs, tax cuts, and immigration crackdowns, to boost economic growth and reduce dependencies on cheap foreign imports and labour. Benchmark 10-year UST yields surged by 22bps from 4.28% at end-October to touch an intra-day high of 4.50% on 15th November. Nevertheless, sentiment in the US Treasury market turned positive with 10-year UST yields rallying 33bps lower to close the month at 4.17% (m-o-m 11bps lower), anchored by mixed US economic data. The US Fed delivered a smaller 25bps interest rate cut at the November FOMC meeting, taking it to the 4.50%-4.75% range, with US Fed Chairman Jerome Powell emphasizing that the results of the recent presidential election would have no "near term" impact on US monetary policy. The UST yield curve shifted lower and bull flattened, with the shorter 2-3-year yields falling by 2-4bps, while the longer 5-30-year yields sinking by 11-14bps.

In early November, 10-year UST yields initially fluctuated lower from 4.28% at-end October amid generally weaker than expected US economic data, before rising 20 bps higher to 4.48% on 6th November, following Donald Trump's victory in the US presidential election. In October, nonfarm payrolls plunged from 223,000 in September to 12,000, far below consensus expectations of 100,000, reflecting lingering impacts from hurricanes in the Southeast US and strikes at Boeing Co., as well as manufacturing job cuts. Despite this, unemployment rate held up at 4.1% in October, while average hourly earnings rose from the revised 3.9% in September to 4.0% y-o-y in October (consensus 4.0%, m-o-m rose from 0.3% to 0.4%), driven by hiring in health care and government, while other sectors softened due to weather-related disruptions. Meanwhile, ISM manufacturing contracted further from 47.2 in September to 46.5 in October (consensus 47.6), dragged down by a decline in production and shrinking inventories. On the other hand, ISM services unexpectedly expanded from 54.9 to 56.0 (consensus 53.8), marking its fastest pace in over two years, quelled by a pickup in hiring.

On 6th November, Donald Trump's sweeping win in the US presidential election, was greeted with both optimism and trepidation by the markets. Trump is poised to implement fresh rounds of policies ranging from tariffs, tax cuts, and immigration crackdowns, to boost economic growth and reduce dependencies on cheap foreign imports and labour. While Trump's first administration featured similar policies and resulted in a boost to corporate profits, these measures, if implemented in the current post-pandemic recovery environment, raised concerns of rekindling inflation. At the FOMC meeting on 7th November, the US Fed unanimously cut its interest rate by 25bps, bringing it to the 4.50%-4.75% range; moving at a less aggressive pace than before, albeit continuing its efforts to right-size the monetary policy. Fed Chairman Jerome Powell commented that the economy has made significant progress towards the Fed's dual-mandate goals of maximum employment and stable prices, and even if GDP growth runs stronger-than-expected, policy rates will still remain on a path towards neutral. The labor market remains in solid condition, inflation has eased substantially from its peak and is on a sustainable path towards the Fed's 2.0% goal. The Fed is committed to maintain the economy's strength by returning inflation to the 2.0% goal while supporting maximum employment. He also added that the results of the recent presidential election would have no "near term" impact on US monetary policy. In response, UST 10-year yields rallied 20bps lower, back to the 4.28% level.

In mid-November, UST yields continued to be pressured higher, with 10-year UST yields surging back up 22bps higher to 4.50%, as investors braced for the potential outcome of President Trump's second administration. On the same note, several US Fed officials reiterated their mounting uncertainty over the neutral rate due to the recent structural changes in the economy which requires more time to be fully assessed. Sentiment was also dampened by stronger than expected US economic data, particularly the stickiness in inflation and hefty upward revisions of retail sales data. In October, US headline CPI stayed firm at 0.2% m-o-m (consensus 0.2%, y-o-y up from 2.4% to 2.6% vs. consensus 2.6%), while core CPI also remained sticky at 0.3% m-o-m (consensus 0.3%, y-o-y maintained at 3.3% and matching consensus), as prices of used cars and hotel rates climbed, possibly reflecting damage and evacuation orders from Hurricane Helene and Milton. In addition, airfares continued to rise, and healthcare costs surged. Meanwhile, US retail sales shrank from 0.8% in September to 0.4% m-o-m in October, primarily attributed to sales increase in electronics and appliance stores, followed by auto sales.

Nevertheless, 10-year UST yields reversed course and plunged 33bps lower to close the month at 4.17%, on the back of mixed US economic data. In November, the final University of Michigan Sentiment survey surprisingly worsened from 73.0 in October to 71.8 (consensus 73.9), suggesting deep divisions among Republicans and Democrats on the path for the economy following Trump's presidential election win. The short-term inflationary expectations remained at 2.6% in November, while long-term inflationary expectations inched higher from 3.1% to 3.2% in November (consensus 3.1%). New home sales slumped from 738,000 in September to 610,00 in October (consensus 725,000), as two hurricanes hit the Southeast and affordability challenges continued to weigh on buyers. Hurricanes Helene and Milton, which tore through parts of the Southeast, impeded sales in the nation's biggest housing region and dragged down overall sales. Meanwhile, the second reading of 3Q24 US GDP remained solid at 2.8%, largely powered by a broad-based increase in consumer spending and steady business investment. In line with this, US Fed preferred gauge of inflation accelerated in October, further supporting policymakers' more cautious approach to lowering interest rates. In October, headline PCE inflation rose from 2.1% in September to 2.3% y-o-y (consensus 2.3%, m-o-m stayed firm at 0.2%), while core PCE inflation ticked higher from 2.7% to 2.8% y-o-y (consensus 2.8%, m-o-m maintained at 0.3%).

Brent crude oil prices initially rose in November, from 73.16/bbl at end-October to reach USD 76.24/bbl on 5th November, amid production hike delay by the OPEC+, tropical storms as well as heightened worries over the potential escalation of the Israel-Hezbollah conflict. Brent prices subsequently fell to USD 70.72/bbl, before closing the month at 72.94/bbl (0.30% lower m-o-m), as sentiment was dampened by continued weakness in China's economic data but supported by signs of easing tension in the Israel-Hezbollah conflict.

In early November, Brent prices edged higher from USD 73.16/bbl at end-October to reach USD 76.24/bbl on 5th November, amid OPEC+ decision on output hike, tropical storms threatening oil production as well as concerns over an escalation in the Israel-Hezbollah conflict. On 4th November, the OPEC+ alliance agreed to delay its December production increase until early next year due to an impending glut. Tropical Storm Rafael is threatening disruptions at US offshore oil and natural gas platforms, with its path on target to affect about 1.7 million barrels a day of daily output. Furthermore, a second Trump administration is expected to be more welcoming to the US shale industry and more skeptical of renewables, pushing Brent prices higher.

Nevertheless, Brent crude prices subsequently fell to USD 70.72/bbl on 13th November, as China's anemic consumer inflation data and further deterioration in factory-gate prices, continued to trouble the market. Following this, the OPEC alliance slashed its oil demand growth forecasts for this year and the next four consecutive months as it belatedly recognized a slowdown in China, the world's second largest crude oil importer. However, according to OPEC, global oil consumption will increase by 1.8 million barrels a day, which is equivalent to a 107,000 bpd less than previously forecasted after data from across Asian nations such as China and India, as well as Africa, went below expectations. Meanwhile, OPEC+'s leadership may take consolation from the improving performance of some members that have lagged in implementing their output cutbacks. For example, Khazakstan reduced its production by 292,000 bps to 1.29 million bpd in October, touching slightly below its quota, demonstrating that the country has made a start on the additional curbs it pledged as compensation for previous overproduction. On the contrary, the International Energy Agency (IEA) reported that global oil markets face a surplus of more than 1 million bpd next year as Chinese demand continues to wane, cushioning oil prices against the turmoil in the Middle East region. The IEA added that oil consumption in China, the powerhouse of world markets for the past two decades, has contracted for six straight months and this year's growth will only be at 10% of the growth rate seen in 2023.

Towards month-end, Brent crude oil prices initially rose again to USD 75.41/bbl on 22nd November, as simmering geopolitical tensions in Russia-Ukraine and Israel-Iran, outweighed weakening crude demand. The Russia-Ukraine conflict has rapidly intensified following months of bloody attrition, with the use of longer-range missiles by both sides. Meanwhile, Iran announced that it will increase its nuclear fuel-making capacity after it was censured by the UN's International Atomic Energy Agency. Nonetheless, Brent prices settled the month lower at USD 72.94/bbl (0.30% lower m-o-m), amid signs of easing tension in the Israel-Iran conflict and China's electric vehicles (EV) boom threatening demand for oil. On 26th November, Israel reached a deal for a 60-day ceasefire with the Lebanese militant group, Hezbollah, after weeks of talks mediated by the US. President Joe Biden said that all sides had agreed to a ceasefire that would "end the devastating conflict between Israel and Hezbollah", adding that the US, Egypt, Qatar and Turkiye will make a fresh push for a ceasefire between Israel and Hamas. Meanwhile, according to official statistics, China's sales of EV and hybrids have in fact reached a tipping point, a trend that is poised to send appetite for transport fuels into a decline that may have a major impact on the oil market. The more rapid-than-expected uptake of EVs has shifted views among oil forecasters at energy majors, banks and academics in recent months. Unlike in the US and Europe, where peaks in consumption were followed by long plateaus, the drop in demand in China is expected to be more pronounced.

Fund Review

The Fund outperformed the Dow Jones Sukuk index return by 45bps in November, with returns of 0.43% compared to the index return of -0.02%. Year to date, the Fund outperformed the index by 310bps, with returns of 3.30% compared to index returns of 0.20%.

Portfolio Outlook and Strategy

In October, Saudi's Minister of Economy and Planning announced that the non-oil sector now accounts for 53% of Saudi's GDP. Private investment in the non-oil sector has surged by 70%, and the non-oil economy has grown 20% since the gov unveiled its reform plans. In 1H24, 184 companies such as PepsiCo and Deloitte relocated their regional headquarters to Saudi, while investment licenses jumped by 50%.

Meanwhile, Dubai approved its largest ever government budget for 2025-2027, featuring record-breaking revenues of Dh302 billion and planned expenditures of Dh272 billion. Around 46% of the spending will be allocated to infrastructure investments and related construction projects including the Al Maktoum international airport development and the new Blue metro line. The remaining 30% will be utilized for social development; 18% on security, justice, and safety sector; and the remaining 6% on supporting the public services sector.

While the overall outlook for fixed income remains positive amid expectations of further US rate cuts, the fixed income market may continue to fluctuate in the near term amidst mixed economic data releases, and as investors priced in expectations that Trump's second presidency may result in higher inflation and slower rate cuts. Any retracement in yields may present opportunity for an attractive re-entry level, as the US Fed is widely expected to continue cutting rates in 2024 and 2025.

Risk Considerations

Investing involves risk, including possible loss of principal. Past Performance does not guarantee future return. All financial investments involve an element of risk. Therefore, the value of the investment and the income from it will vary and the initial investment amount cannot be guaranteed.

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