

Allianz Europe

Equity Growth Select

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth by investing in European equity markets with a focus on growth stocks of large market capitalisation companies in accordance with environmental and social characteristics.

What Happened in March

European equities moved lower over March but held up better than US shares. President Donald Trump's withdrawal of US military aid to Ukraine and comments signalling faltering US commitment to The North Atlantic Treaty Organisation (NATO) and European security initially weighed on sentiment, but shares recovered after the German Parliament agreed to relax its debt brake. The landmark debt reform bill will unleash hundreds of billions of euros for defence and infrastructure spending. However, European markets stumbled further towards month end on heightened uncertainty in the run-up to the president's self-dubbed "Liberation Day" of sweeping tariffs on 2 April. At a sector level, Consumer Discretionary and Information Technology shares fell the most, while Utilities and Energy were the only sectors to post gains.

The flash HCOB eurozone composite purchasing managers' index (PMI) ticked up slightly to 50.4 in March from 50.2 in February. Services activity slowed modestly but remained in expansion territory, while the manufacturing PMI rose from 47.6 in February to 48.7 in March, a 26-month high. Inflation in the eurozone eased to 2.3% in February from 2.5% in January. The European Central Bank (ECB) cut its key interest rate by 25 basis points (bps) to 2.5%, as expected, and slashed its gross domestic product (GDP) growth outlook by 0.2% to 0.9% for 2025 in light of the worrying trade tariff backdrop and economic uncertainty.

German equities declined in March but outperformed the broader European market, despite stumbling towards month end in the run-up to President Donald Trump's self-dubbed "Liberation Day" of sweeping tariffs on 2 April. German lawmakers approved a landmark debt brake reform deal proposed by the country's Chancellor-in-waiting Friedrich Merz. The historic vote will change the German Constitution and ease borrowing limits in order to fund higher defence and security spending, as well as the creation of a EUR 500 billion infrastructure fund. Germany's ZEW Indicator of

Economic Sentiment soared to 51.6 points in March from 26 points in February, the highest level in over two years, on optimism surrounding fiscal policy.

UK equities fell modestly over the month amid continued economic and geopolitical uncertainty, weakening further into month end in the run-up to President Donald Trump's self-dubbed "Liberation Day" of sweeping tariffs on 2 April. The UK economy unexpectedly shrank by 0.1% in January, following a rise of 0.4% in December. The Office for Budget Responsibility halved its 2025 growth outlook to 1%, while the chancellor's Spring Statement outlined welfare cuts, boosted defence spending and warned of tax hikes to come. The Bank of England (BoE) kept rates on hold at 4.5% at its March meeting, despite a slight easing in the annual rate of inflation.

Performance Review

The Fund fell in March, underperforming the benchmark and the broader MSCI Europe. Optimism initially surrounded Europe, with Friedrich Merz's "whatever it takes" plan to unleash defence spending and overhaul German infrastructure set to usher in the largest economic stimulus since the fall of the Berlin Wall. The ECB cut rates by 25 bps to 2.5% as expected, but signalled that they may slow the pace of rate cuts in future. Despite all the new local market stimulus, US tariff and recession fears eventually dominated sentiment. The withdrawal of US defence support for Ukraine further added to risk aversion.

The best performing European stocks were generally weapons manufacturers and their associated suppliers, with many banks also remaining steadfast. The risk-off mood meant the best performing sectors were Utilities, Insurance, and Energy, while Consumer Discretionary and Information Technology lagged. Overall, these market dynamics led to a significant outperformance of Value over Growth by 6.7% (MSCI European indices), creating a challenging environment for our sharply growth-oriented strategy.

The top active contributor was a high-quality chocolate producer (Consumer Staples and reporting well lately), while the worst active contributor was a hotel group (high US exposure and leisure spend concerns). We are engaging with our companies individually on tariff impact and remain confident in their relative market-leading positions pricing power, cost and technological advantages, product and service criticality, network effects, and supply chain flexibility to help mitigate impact.

Top contributors

Stock of a high-quality chocolate producer gained almost 3%, being a highly attractive Consumer Staple in a risk-off oriented market. Its financial year (FY) 2024 organic sales growth was just shy of 8%, slightly below expectations, however margin exceeded 16%. This is impressive with cocoa prices reaching record highs earlier this year, rising over 150% year-on-year. To deal with extreme cocoa costs, peers shrunk product and reduced cocoa content. Conversely, the company maintained its high standards, cut costs and took market share. Volume and promotional data remain mixed, but it is an "affordable luxury", evidenced by its execution of pricing power recently. Management have guided for similar 7-9% organic growth in 2025 with further margin expansion.

Stock of a mining (80% of sales), construction and demolition equipment maker enjoyed a 10% boost this year, with the company helpfully linked to the infrastructure stimulus and potential Ukraine rebuild opportunity. Its Q4 beat on orders, sales and adjusted earnings before interest, taxes, depreciation, and amortisation (EBITDA) was also well received by investors, even if margins were slightly soft due to transitory factors. Our longer-term, structural investment case is defined by ageing equipment, and the need to electrify and automate, to reduce emissions and meet climate targets.

Around 85% of the company's underground offering is now available as electric, with superior batteries to peers, although adoption is still in the early stages. Electric equipment offers higher margins, also on servicing.

Stock of a laboratory testing services company held steady through March, gaining around 2%. Its FY 2024 results largely met its own guidance and investors' expectations on revenues and adjusted EBITDA. Sales arrived about 2% above consensus, driven by the life division, where the company took market share in Europe and benefitted from strong per- and polyfluoroalkyl substances (PFAS) testing in North America. Management anticipates mid-single digit organic revenue growth in 2025, plus potential revenues from acquisitions, and a higher margin. Answering to the last remaining short-seller allegations, an independent cash audit confirmed their FY 2023 cash balance and system integrity. A shareholder meeting in late April will discuss related parties' transactions, concluding this baseless event.

Top detractors

The hotel group mentioned previously reported on FY 2024 with few surprises, given the availability of high frequency industry data and its stable, high margins. Revenue increased 7%, driven by 3% revenue per available room (REVPAR) growth and 4.3% net unit growth (in USD). Earnings before interest and taxes (EBIT) also lifted 10.3%, while earnings per share (EPS) was up 15% due to share buybacks. The company has meaningful US exposure, and with recession fears circling, the stock sold slid -18% in March. We continue to appreciate the company for its high single-digit growth in fee revenue expected from REVPAR and net unit gains, where its new hotel pipeline is up 10% year-on-year. Its valuation is now below 20x (12-month forward price-to-earnings ratio (P/E)) and looks compelling versus companies with comparable economics and risk profiles.

A payments company was the star of the earnings season show, with volume growth rising from 27% in Q3 to 29% in Q4. Net revenue growth accelerated from 20% in Q3 to 23% in Q4. EBITDA margin also ramped up from 46% in H1 to 53% in H2 as the rapid headcount expansion of 2023 annualised. The strong results combined with 2025 guidance for an acceleration in net revenue growth and further expansion in EBITDA margin versus 2024. The stock rallied over 20% year-to-date until the tech selloff and recession concerns erased these gains. The runway for growth remains, with less than a third wallet share on the digital side and below 40% in unified commerce, a major growth lever where volumes also accelerated from 33% in Q3 to 36% in Q4.

A semiconductor manufacturer had been under dual headwinds of high automotive and China exposure, leading to several FY guidance cuts through 2024 and a relatively low valuation. In a welcome pivot, the company's FY Q1 results surprised positively. Q1 revenues beat consensus by 6.5%, although the stronger USD was a key driver, also lifting sales guidance from "down low single digits" to now "flat to up". The margin guide was unchanged given trade tariff uncertainty, the key factor reducing the stock -14% in March. The CFO met with us in our Frankfurt office last month. They anticipate the trough in automotive-related demand and inventory correction is passing, and have achieved several new design wins, in China and in Germany.

Market Outlook

The sweeping US tariffs announced in April mark a significant escalation in global trade tensions, introducing a material headwind to global growth and sentiment. Tariffs of this scale will pressure supply chains, raise costs, and likely prolong the current period of elevated market volatility. While the risk of recession has undoubtedly risen, particularly if retaliatory measures broaden, history shows that companies that are structurally well positioned can often adapt.

We have faced similar challenges before, albeit at lower intensity: during the US-China trade war of 2018-2019, global markets corrected sharply but had fully recovered by mid-2019. Companies with strong balance sheets, pricing power,

and adaptability managed to outperform, and many diversified their production. Some firms even benefitted from reshoring and supply chain investment. While near-term pressure on consumer sentiment and corporate margins is likely, particularly in the US, historical precedent suggests that quality businesses with structural growth drivers tend to navigate these environments relatively well.

Importantly, recent comments from the US administration that tariffs may be wound back for countries offering a “phenomenal” deal, and that “the tariffs give us great power to negotiate,” suggest that a path towards negotiation remains open. If no further escalation occurs, the announced tariffs could represent the maximum impact, though significant supply chain adjustments will still be necessary. Non-tariff measures, however, will complicate negotiations and prolong uncertainty, which markets tend to dislike.

Although unlikely to offset the severity of these tariffs, greater international cooperation among allied countries and accelerated reshoring efforts could help create new demand drivers over time.

Against this backdrop, our high quality, structural growth strategy naturally promotes holdings that are fundamentally resilient, with continued earnings growth key to driving stock prices as tariffs evolve – and potentially dissolve. Many of our companies are leaders in essential industries, have pricing power, asset-light models, or domestic market exposure that help buffer against external shocks. Several are also aligned with long-term secular trends such as reshoring, energy transition, and automation, which are likely to be reinforced as global supply chains regionalise.

After three years of derating, valuations for most of our European companies have fallen to, or below, their 10-year historical averages, meaning much of the current uncertainty is already reflected in prices. A lot of heat has also left our global stocks. While we intend to remain vigilant to downside risks, we are also focused on selectively adding to high-quality companies where short-term dislocations create long-term opportunities. We believe our disciplined approach and focus on quality businesses positions us well to navigate this period of heightened uncertainty.

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sg.allianzgi.com

+65 6438 0828

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