

Allianz Global Artificial Intelligence

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth by investing in the global equity markets with a focus on the evolution of artificial intelligence in accordance with environmental and social characteristics.

What Happened in December

Global equities pulled back in December following a strong rally in the prior month. For the US, markets were mixed amid a more hawkish outlook from the US Federal Reserve (Fed). Ongoing debates on President-elect Trump's policies and a narrowly averted government shutdown also introduced some uncertainty. The technology-heavy Nasdaq Composite Index held up relatively well due to positive headlines from mega-cap growth companies, while smaller cap stocks experienced more profit taking. European equities closed the month with flat returns. The weakness of the euro helped support the outlook for the region's exporters, although the threat of higher tariffs weighed on sentiment. While Asia equities were mixed overall, China stocks moved higher, buoyed by further signs that Beijing is taking steps to bolster economic growth.

As widely expected, the Fed cut rates by 25 basis points (bps) in December, but policymakers issued more cautious guidance for 2025, reducing the number of expected 25-bps cuts to two from four at the previous Federal Open Market Committee (FOMC) meeting. Concerns that progress against fighting inflation had stalled were cited for the change. It was mostly a different story in Europe, with the European Central Bank (ECB) cutting rates by 25 bps, while the Swiss National Bank reduced borrowing costs by 50 bps, its largest cut in nearly a decade. However, the Bank of England (BoE) kept rates on hold as inflationary pressures remained stubbornly high. The Bank of Japan (BoJ) also maintained its monetary stance.

Commodity prices were mixed. Oil prices, as measured by Brent crude, hovered around USD 72-73 per barrel for much of the month. While the Organisation of the Petroleum Exporting Countries Plus (OPEC+) nations voted to continue

production cuts in 2025, this was offset by concerns over the outlook for global growth. Gold mostly traded above USD 2,600 an ounce, remaining below the record high of almost USD 2,800 an ounce reached in late October.

From a sector perspective for the MSCI All Country World Index, performance was led by Consumer Discretionary and Communication Services, as mega-cap names held up better amid a mixed equity backdrop. The Materials and Health Care sectors were the top laggards over the period.

Portfolio Review

During the period, the Fund outperformed the blended benchmark (50% MSCI ACWI Index/50% MSCI World Information Technology Index). From a sector perspective, Consumer Discretionary and Information Technology were the largest relative contributors. The Industrials and Financials sectors were slightly offsetting. Artificial intelligence (AI) infrastructure was the strongest performer as our AI chip holdings reported better-than-feared earnings results. Both AI applications and AI-enabled industries pulled back during December, following strong returns in the prior month.

Contributors

The top relative contributor over the period was Broadcom Inc. The company designs, develops and supplies a broad range of leading semiconductor, enterprise software and security solutions. Shares outperformed during the period after the company reported solid earnings results and management articulated a materially larger-than-expected revenue opportunity for AI-related infrastructure in the next three years. Looking forward, the company is on track for meaningful acceleration in revenue and earnings growth driven by AI-related computing and networking programmes, software infrastructure and a recovery in its wireless semiconductor business.

Our position in electric vehicle (EV) producer Tesla Inc. was another contributor over the period. The stock continued its rally following the US presidential election results. Given Elon Musk's support for the Trump presidential election bid, the company stands to benefit under a friendlier regulatory regime and from a pro-business agenda. Looking forward, Tesla continues to have an ambitious innovation agenda, spanning EV, energy storage, autonomous driving and humanoid robots. We believe the company is making good progress on each of these agendas in ways that can unlock significant shareholder value in the future.

Detractors

Amongst the detractors is a supplier of building materials and construction services to professional contractors and housebuilders. The company uses AI, robotics and digital technologies to drive operational efficiencies. Shares were lower as higher interest rates weighed on housing activity and sentiment for the building products space. The company has been an organic market share gainer and consolidating smaller regional competitors. The management team has maintained financial discipline by returning cash to shareholders, while driving efficiency through AI.

Another detractor is an American energy company specialising in clean energy generation, primarily through its nuclear, wind and solar assets. Shares were lower alongside the rest of the Utilities sector, primarily from profit taking. The company is positioning itself to meet the growing energy demands from AI and digital infrastructure. The demand for data centre power is anticipated to drive significant growth in energy consumption. The anticipated rise in AI-driven electricity demand could lead to substantial power contracts with data centre operators over the coming years.

New Buys and Sells

We re-initiated a position in a technology conglomerate as the company's core search engine and advertising franchise continues to experience positive trends, while overall valuations remain relatively modest. Moreover, the company's recent AI announcements could drive better earnings growth. This included an upgraded generative AI chatbot, AI video generation models and an AI agent platform that allows enterprises to deploy agentic AI into their ecosystems.

We exited the remaining small position in a health benefits company as profitability outlook appears to have deteriorated over the next year. Also, we sold our remaining position in a workflow management software maker. We previously reduced the name at higher prices as shares were approaching our intermediate-term price target. We decided to exit the position as management recently provided some cautious commentary on their near-term growth trajectory.

Market Outlook

We maintain a positive outlook for equity markets in 2025, though markets may have periods of volatility due to concerns over stickier inflation, the implementation of Trump's fiscal policies, subdued global growth and slower interest rate cuts. The Fed looks to be in a comfortable spot balancing inflation with economic stability and should continue its path towards rate cuts, albeit at a more gradual pace. An easier monetary policy backdrop should be constructive for pockets within the US economy to regain its footing and drive more broad-based growth.

We believe the upcoming Trump administration represents an evolution of policy, with a net positive effect on AI innovation. Trump recognises the US leads in AI and wants to maintain that leadership. A less regulated and business-friendly environment should be conducive for more AI investment and capital markets activity. However, companies heavily reliant on an overseas supply chain in some countries may face greater uncertainty. It remains to be seen how much tariffs and other restrictions could impact certain industries, but overall should be manageable. A wide range of capital is fuelling the AI investment backdrop, including venture capital, private equity, self-funding from larger technology companies and the start of an AI initial public offering (IPO) cycle.

From an innovation perspective, progress with AI development is accelerating as more powerful capabilities become readily available from the robust "Phase 1" infrastructure buildout. We are beginning to enter "Phase 2" where new generative AI use cases and application adoption drive significant benefits over the coming years. Our analysis suggests that investments in AI could lower the marginal costs of operations, much like the information technology (IT) revolution did. Furthermore, the advanced features of AI-enhanced products or services can drive new levels of productivity, cost savings and revenue opportunities across industries in "Phase 3". Given the transformative potential of AI investments, we believe profit margins may not simply hold steady but could in fact grow, supporting valuations for innovative companies that are investing now to disrupt the status quo.

AI infrastructure: Spending on AI infrastructure should continue to be robust over the next several years as more powerful AI data centres are built around the globe. Nvidia's upcoming Blackwell AI chips provide up to a 30 times performance increase compared to the previous generation and more hyperscalers are designing custom AI chips to meet their unique specific needs. This is driving demand for new data centre architectures that can handle the higher power, cooling, space and networking requirements. Overall demand for generative AI training remains durable as more companies across the ecosystem are rushing to build better foundational models or fine tune other models. Growth in AI inference systems is also expanding to process and respond to new data in real time and support applications that require low latency and high reliability at the edge of the network. Newer reasoning engines require more "think time" to yield better results, driving additional workload demand.

AI applications: Generative AI applications are evolving into their next phase with the emergence of AI agents. Unlike AI copilots designed to answer a single question, AI agents have decision engines that allow them to operate autonomously and complete complex tasks. AI agents can be easily customised to handle repetitive tasks and have human-like decision making capabilities to adapt to different situations. This can create a new level of automation and dramatically cut costs and improve productivity. We believe there will be an upcoming surge of new generative AI-infused applications across many areas of consumer and enterprise workflows over the next several years, driving more investment opportunities.

AI-enabled industries: AI continues to open up new possibilities to drive true industry transformation across every industry. Many companies in AI-enabled industries are increasing investments in generative AI to train one's own industry-specific model on its proprietary content or knowledge to compete better. In Health Care, the application of AI could dramatically speed up the time for drug discovery, accelerate clinical trials and dramatically improve the efficacy of medical devices. Within Financial Services, there are companies with significant volumes of data related to transactions, customer interactions and research. This allows for the creation of AI solutions to enhance operational efficiency, improve fraud detection and personalise client service. There are similar opportunities within Automotive, Consumer, Industrials, Energy and even Mining. We think this is only the beginning as innovative companies embrace AI to enhance efficiency, lower costs, launch new products, take market share and drive higher levels of profitability.

We are still in the early innings of the AI era. Despite significant advancements, there is a lot more potential to be unlocked in the future. The industry is rapidly evolving, with major investments and innovations continuing to drive progress towards artificial general intelligence, possibly within the next decade. AI is becoming more integrated into various fields, from finance to health care to humanoid robotics. It is an exciting time, and we are likely to see even more transformative changes in the coming years.

Our view remains that the compounding effect from AI disruption will create opportunities for innovative companies across every sector. We believe that stockpicking will be essential to capturing the benefits of this opportunity, as today's AI winners may change in the future in an environment characterised by rapid change and disruption. We remain focused on identifying the companies that can best leverage AI to deliver the most shareholder value creation over the long term.

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