Allianz Global Investors

Allianz Global Equity Unconstrained

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth by investing in global Equity Markets to achieve a concentrated equity portfolio with a focus on stock selection in accordance with environmental and social characteristics.

What Happened in February

Global equities delivered mixed returns over February as markets struggled to navigate President Trump's deliberately disruptive and unpredictable agenda. Chinese stocks surged, boosted by strength in Technology companies. European shares also advanced, underpinned by growing optimism over a potential end to the war in Ukraine. In contrast, US and Japanese equities lost ground. At a sector level, defensive Consumer Staples companies were the best performing area in the MSCI All Country World Index, with Energy and Real Estate companies also faring well, while the Consumer Discretionary and Communication Services sectors suffered notable setbacks.

February brought growing signs that the US economy was slowing, with inflation expectations jumping due to President Trump's tariffs threats. Retail sales, consumer sentiment and home sales slumped in January and early indications showed services activity in February had contracted for the first time in more than two years. While the US Federal Reserve (Fed) indicated it was in no rush to cut rates, the European Central Bank (ECB) is expected to continue to reduce borrowing costs. Conversely, accelerating Japanese inflation increased the likelihood of another rate hike from the Bank of Japan (BoJ).

In currency markets, the Japanese yen strengthened as rising inflation increased speculation that the BoJ would continue to tighten monetary policy. The British pound also rose against the US dollar and the euro, bolstered by hopes that the UK may secure a trade deal with the US and better-than-expected economic data. Meanwhile, the euro closed the month little changed against the US dollar.

Oil prices eased over February, with Brent crude closing the month back below USD 73 a barrel as slowing US growth and the threat of a global trade war dampened the demand outlook. Gold rallied further, touching a fresh record high of USD 2,950 an ounce, amid robust demand for safe-haven assets.

Portfolio Review and Strategy

In February, the portfolio returned negatively.

Contributors

Monster Beverage was the largest positive contributor for the month. The company is one of the largest energy drink companies in the world, focused on the global non-alcoholic beverage market, with category leadership in energy drinks (92% of revenues, Monster Energy and Reign), strategic brands (6%, including NOS and Full Throttle), and alcohol beverages (2%, via The Beast Unleashed). Monster is expanding its market incrementally by investing in adjacent categories such as alcoholic beverages, coffee, hydration, and wellness drinks. Over 95% of its revenue comes from beverage sales, with strong global distribution through partnerships with major bottlers. After a difficult 2024, there were positive signs for the company in their Q4 reporting, with earnings and sales both above consensus estimates. There was a small increase in US sales after consecutive quarters of contraction, with international growth accelerating strongly. This suggests that Monster continues to gain share in the growing global energy drinks market and it remains the most significant long-term growth driver for the company.

A US insurance broker also provided positive returns for February. We believe that insurance brokers are superior businesses to the insurance carriers as they take no underwriting risk, no investment/credit risk, and have no exposure to natural catastrophes (which are rising in both frequency and severity due to climate change). This leads to lower volatility in year-to-year profitability. Customer loyalty for the brokers is high, with retention rates of 90%+, and both the property and casualty (P&C) brokerage and reinsurance brokerage markets are highly consolidated. The increasing levels of sophistication in insurance packages also means increasing demand for brokers. Q4 results reported at the end of January showed healthy organic growth in both brokerage and risk management. Adjusted earnings per share (EPS) growth was strong, primarily due to expanding margins. Guidance was also positive with organic growth for brokerage to be in the 6-8% range for 2025.

Detractors

A US managed care organisation was the biggest detractor to performance in February. The company is the most diversified, combining a top tier top-tier health insurer, pharmacy benefit manager, provider, and health analytics franchise. It serves 76 million Americans through these products. The share price fell towards the end of the month as the Wall Street Journal reported that the US Department of Justice (DOJ) had launched an investigation into the company's billing practices within their Medicare Advantage (MA) program and whether company practices lead to diagnoses that generate extra payments within the MA plans they manage. The area of concern revolves around the process of risk-adjusted coding, where Medicare providers are compensated in line with the risk of the population they cover. This process should provide cover to a wider range of beneficiaries and prevent organisations "cherry picking" only low risk members at the expense of sick, marginalised or lower income groups. In response, the company stated "we are not aware of the launch of any new activity as reported by the Journal., but rather a long standing investigation over two years, under the prior DOJ" and "the government regularly reviews all MA plans to ensure compliance and we consistently perform at the industry's highest levels on those reviews". We will continue to closely monitor news flow in the coming months.

After a positive start to the year, Thermo Fisher, the largest company in the scientific tools sector, gave back most of its January gains. Offering a comprehensive range of analytical instruments, software, services, consumables, and reagents, its diverse customer base includes biopharma (42%), academic (19%), clinical and diagnostic (23%), industrial (14%), and applied science (2%) sectors. The company has a strong focus on innovation and is geographically expanding into high-growth markets. In terms of quality, it is typically highly cash generative with strengths in capital allocation and boasts a 10-year earnings compound annual growth rate (CAGR) of over 16% as of 2022, prior to post-pandemic effects. The company's Q4 results were solid but guidance remains cautious on a gradual recovery of their end markets. The focus on US health care spending, government efficiencies and potential tariffs weighed on the stock as investors speculated on potential impacts. Although Thermo does have exposure to US government and academic spending, revenues are relatively small and tariff impacts are limited, with the majority of Chinese production destined for local markets. The company remains a core holding within the portfolio with the potential for solid EPS growth in the coming years.

Market Outlook

While a "soft landing" for the US economy remains the most probable scenario, recent economic data suggest that strong growth and persistent inflationary pressures could challenge expectations for a smooth transition. Additionally, uncertainty surrounding President Trump's economic and geopolitical policies is adding complexity to both the economic outlook and the trajectory of Fed monetary policy normalisation.

At the same time, US equity valuations remain comfortably above their longer-term averages despite the recent relative weakness. Earnings growth expectations for the Technology sector appear especially optimistic and this disconnect between valuations and broader economic risks could contribute to increased market volatility. In this environment, risk-aware investors may seek diversification in more attractively valued markets.

There are already signs of increased capital flows into European equities since January, where select companies with global business models remain resilient despite weaker regional macroeconomic conditions. Furthermore, potential US diplomatic efforts, particularly regarding Russia-Ukraine negotiations, could improve investor sentiment, supporting a more stable business climate and stimulating capital expenditures.

Despite ongoing political and economic uncertainties, corporate earnings remain robust for now, historically supportive of equity markets and our portfolios. We were pleased with our companies' Q4 and H2 results overall, although in the recent rotation, value-oriented areas of the market such as Banks, Weapons and Consumer Staples are currently shining even brighter. Much like heat came out of the US market recently, this may not be enduring.

Within our portfolios, we invest predominantly in market leading, often global businesses. Our companies offer pricing power, critical products and services, and are heavily integrated into production processes and information technology (IT) infrastructure, offering resilience in a trade war scenario. In Europe, we have plenty of construction exposure which could benefit from a potential rebuild of Ukraine, not to mention the general recovery of semiconductors anticipated later this year and medtech which can benefit both our European and global portfolios. While there are considerable political uncertainties, corporate earnings should remain robust for now, and healthy corporate earnings are usually favourable for our fundamentally focused strategies.

All data are sourced from Bloomberg and Allianz Global Investors as at 28 February 2025 unless otherwise stated.

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