Allianz Global Intelligent Cities Income

Monthly commentary

Investment Objective

The Fund aims at long-term income and capital growth by investing in global equity and bond markets with a focus on companies whose business will benefit from or is currently related to evolution of intelligent cities and connected communities in accordance with the Sustainability Key Performance Indicator Strategy (Relative). In this context, the aim is to outperform the Sub-Fund's Sustainability KPI compared to Sub-Fund's benchmark to achieve the investment objective.

What Happened in October

Global equities mostly ended October lower. Japanese stocks were a rare bright spot, advancing on hopes of higher government spending after the ruling Liberal Democratic Party lost its parliamentary majority for the first time in 15 years. Elsewhere, however, early gains were more than offset by a weak close to the month. US stocks lost ground over October. Shares trended higher for much of the month, with the Nasdaq Composite Index hitting a fresh high as mega-cap technology stocks returned to favour, before slumping on the final trading day of the month. While the race for the White House remains neck and neck, a handful of swing states will likely decide the election result.

Global bonds sold off, with yields rising sharply in the US as polls indicated Donald Trump was likely to win November's presidential election. The former president has promised to hike import tariffs substantially, while tax cuts are likely to further swell the fiscal deficit. The yield on the 10-year US Treasury bond rose 50 basis points (bps) over the month to close just below a 4-month high of 4.30%. On a global basis, corporate bonds outperformed government debt, with high yield debt faring better than investment grade securities.

With economic data continuing to indicate a soft landing for the US economy and a solid jobs market, expectations grew that the US Federal Reserve (Fed) may slow the pace of its rate cuts. In Europe, the European Central Bank (ECB) lowered interest rates by 25 bps, marking its third cut of this year. The People's Bank of China (PBoC) also reduced its 1- and 5-year loan prime rates by 25 bps. The rates are used as a reference point for most loans and mortgages in China.

Oil prices initially surged past USD 80 per barrel after Iran launched hundreds of rockets at Israel, sparking fears that Israel may retaliate by attacking Iranian oil facilities. However, oil prices subsequently retreated, closing the month around USD 73 per barrel, after Israel's response focused on military targets and Tehran signalled it would take a measured response to these strikes. Gold prices surged to a fresh record high of almost USD 2,800 an ounce amid ongoing geopolitical tensions and as investors evaluated political risks ahead of the US presidential election.

From a sector perspective for global equities, as measured by the MSCI All Country World Index, performance was led by Financials. The favourable interest rate backdrop and strong earnings were tailwinds for the sector. Communication Services was the only other sector with positive absolute returns. The Materials and Consumer Staples sectors were the top laggards over the period.

Portfolio Review

During the period, the Fund outperformed its custom benchmark (70% MSCI All Country World Index + 30% ICE BofAML US Corporate & High Yield Index).

On a single security basis, our positions in Celestica Inc. (equity, electronic manufacturing services), Digital Realty Trust Inc. (equity, other specialised REITs), and an internet infrastructure solutions company (equity, internet services and infrastructure) contributed to performance. In contrast, our positions in a semiconductor manufacturing equipment supplier (equity, semiconductor materials and equipment), a supply chain management software company (equity, application software), and an ecommerce company (equity, broadline retail) detracted from performance.

From a sector perspective, Real Estate and Information Technology were the top absolute contributors, and Health Care and Industrials were the top absolute detractors over the period.

Outlook

We continue to have a constructive mid-to-long term outlook, given the earnings growth potential over the coming years. However, we could see higher market volatility in the near term as markets digest the outcome of the US elections, potential shifts in some policies and timing of future rate cuts by the Fed. For the upcoming Trump presidency, we continue to maintain a balanced portfolio positioning across our equity, convertible and fixed income holdings. Overall corporate earnings have been relatively resilient year-to-date, although there have been pockets showing some softness given the lag effect of higher rates. As we have done in periods of volatility, we will opportunistically look to upgrade select names and add to our highest conviction ideas to better position the portfolio for improved performance.

Since inflation is now moving towards the Fed's target of 2% and employment conditions have moderated, the central bank is now in a more comfortable spot to normalise policy. The Fed started its cutting campaign by reducing the federal funds rate by 50 bps, with more reductions expected in the coming months. Since the risk of inflation has abated, the Fed has greater latitude to pursue its goal of maximum employment. An easier monetary backdrop should be constructive for the economy to regain its footing, but it may take time for effects to take hold. We remain optimistic in the resiliency of the US economy, corporate earnings growth and innovation in the years ahead.

We continue to maintain a balanced portfolio of innovative companies with profitable business models, strong management teams, as well as unique products and services that should help navigate the current environment better. Ongoing policy support like the US Infrastructure Investment and Jobs Act, European Green Deal and other stimulus proposals from around the world should help provide more funding over the coming years to improve our cities and fight climate change. Ongoing secular trends, which include the electrification of transportation, energy transition to clean and renewable power, and decarbonisation of industrial infrastructure, provides additional tailwinds for the modernisation of cities around the world.

As cities get smarter, they become more liveable and more responsive – and today we are seeing only a glimpse of what technology could eventually do to significantly improve the quality of life in urban environments. As an example, we continue to see advances in technology around Internet of Things (IoT – sensors and devices connected by networks to computing systems). IoT has enormous potential to advance how smart cities work. Research on big data and analytics from massive streams of real-time data is being applied to numerous initiatives. The resulting work can transform cities by improving infrastructure, creating more efficient and cost-effective municipal services, enhancing public transportation, reducing traffic congestion and keeping citizens safe and more engaged in the community.

Citizens and businesses will benefit from improvements in air quality, convenience, cost, energy provision, health care, safety, traffic, waste management and more. The growth of intelligent cities should only accelerate over the coming years and their potential is limitless. We are excited about the investment opportunities presented and believe our research-driven, bottom-up process is the most effective means to capture the value generated as we build a better future.

All data are sourced from Allianz Global Investors and Bloomberg as of 31 October 2024 unless otherwise stated.