

Allianz

Japan Equity

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth by investing in equity markets in Japan.

What Happened in September

The Japanese equity market declined in September, due mainly to shifting speculations regarding the Liberal Democratic Party's (LDP's) leadership election. The TOPIX Index (total return) closed with a modest decline of 1.53% (in Japanese yen terms).

The Bank of Japan (BoJ) kept rates on hold at its September Monetary Policy Meeting (MPM), signalling that the economy would likely continue to grow above its potential rate "as a virtuous cycle from income to spending gradually intensifies". Policymakers also called for vigilance to upside inflation risks but warned against creating too much market expectation of future rate hikes.

Mr. Ishiba becomes Japan's new Prime Minister on 1 October. He called a general election to be held on 27 October in an effort to consolidate the increasingly polarised LDP. He is said to support higher corporate taxes and is not expected to resist the BoJ's plans to raise interest rates.

In terms of sectors, Consumer Staples outperformed due to the strong performance of food and toiletry companies. The Industrials sector also outperformed, driven by China-related gains buoyed by the announcement of the largest stimulus package since the pandemic. On the other hand, Health Care and Utilities sectors underperformed instead.

Portfolio Review

The Fund underperformed the benchmark TOPIX Index in September, mainly due to negative stock selection in Health Care and Materials.

At the individual stock level, a pharmaceutical company underperformed due to missing expectations on the endpoint for hormone receptor-positive/HER3 negative breast cancer trials. Shin-Etsu Chemical also underperformed on the back of concerns over a softening polyvinyl chloride (PVC) market driven by a slowdown in the US housing market, as well as a weakening semiconductor market. On the other hand, quality/growth stocks such as a medical statistics data services provider and a sportswear company outperformed, mainly due to steady fundamentals.

Market Outlook

Notwithstanding the recent market volatility, we have a constructive longer-term view on the Japan equity market outlook. We are encouraged by the resilience of the Japan market since the extreme volatility in early August and believe that structural drivers remain in place for a more positive outlook. In particular, the combination of higher inflation as well as ongoing governance reforms should contribute both to improved earnings as well as a greater focus on shareholder value.

Over the last year, the Tokyo Stock Exchange (TSE) has initiated reforms to improve corporate governance by requiring companies to focus on capital management and returns on invested capital. This addresses a key criticism often made about corporate management in Japan, especially the high levels of cash held on company balance sheets during a period of very low interest rates.

It is notable that the level of dividend payouts and share buybacks in Japan has increased in recent years. During the financial year 2023/2024 results period, for example, the announcement of share buybacks in Japan reached record levels. The unwinding of cross-shareholdings is also progressing and represents a positive trend.

As Mr. Ishiba says he will follow the direction of the previous administration and the details of his own policies are still undecided, there will be no change in our investment strategy.

Under these circumstances, we aim to maintain a balanced portfolio between defensive and cyclical stocks. We are maintaining a combination of growth stocks with high earnings visibility and value stocks with potential positive catalysts, such as turnaround prospects and an improvement in shareholder returns. The portfolio also has a relatively close-to-benchmark sector positioning, so that we expect stock selection to be the main driver of returns.

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