Allianz Global Investors

Allianz Japan Equity

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth by investing in Japanese equity markets in accordance with environmental and social characteristics.

What Happened in June

Japanese equities made further modest gains in June despite protracted trade talks between Tokyo and Washington and geopolitical risks in the Middle East. The impact of Trump's tariffs has contributed to a notable deterioration in business sentiment. Japanese exports fell by 1.7% in May compared with the same period last year, the sharpest fall in eight months, as businesses struggled to navigate an uncertain trade backdrop. More positively, the flash estimate of the au Jibun Bank Japan composite purchasing managers' index (PMI) rose to 51.4 in June, up from May's reading of 50.2.

Core inflation rose to 3.7%, driven higher by surging rice prices. With the cost of the nation's politically sensitive staple grain doubling in a year, Prime Minister Shigeru Ishiba has promised a slew of measures to ease voter dissatisfaction about soaring food prices and low wage growth after the ruling party suffered its worst result at the Tokyo local elections ahead of Upper House elections. The Bank of Japan (BoJ) held rates steady at 0.5% at its June meeting and also announced a slowdown in unwinding its balance sheet in order to reduce volatility in the Japanese government bond market.

In terms of sectors, Communication Services and Information Technology sectors outperformed due to the strong performance of gaming and artificial intelligence(AI)-related stocks. On the other hand, Consumer Discretionary and Health Care sectors lagged due to uncertainty around the US trade situation.

JUNE 2025

Portfolio Review

The Fund lagged the benchmark TOPIX index in June, mainly due to negative sector allocations effects as a result of a slight overweight exposure in Consumer Discretionary and underweight in Information Technology.

At a stock level, a precision tools maker especially for the semiconductor production industry, and an electrical equipment manufacturing company, developing and manufacturing power and telecommunication systems products – both AI-related names - continued to outperform given expectations for structural earnings growth. In addition, other high-growth names such as a medical statistics data services provider, and a video game company also contributed positively. On the other hand, not holding a manufacturer of semiconductor testing devices and electronic measuring instruments in the Technology sector impacted performance.

Pharmaceutical stocks also underperformed, reflecting uncertainty around the US healthcare industry given the policy objective of reducing the cost of drugs drastically. We expect to maintain an overweight position in one of the leading Japanese pharmaceutical companies considering the balance between medium-term earnings growth opportunity and its attractive valuation.

Market Outlook

While previous concerns regarding tariffs have eased somewhat, nonetheless there are still significant uncertainties. High inventory levels accumulated prior to the tariff policy change, for example, and the growing uncertainty in international trade which could restrain capital expenditure (capex) and production represent potential risks. The full impact of the tariff announcements on corporate performance and the real economy may only emerge with a lag of several quarters. Despite this, we believe that structural drivers remain in place for a more positive, longer-term outlook. In particular, the combination of inflation as well as ongoing governance reforms should contribute both to improved earnings as well as a greater focus on shareholder value.

The spring wage negotiations (Shunto) have concluded with another year of more than 5% headline wage growth, which should help improve consumption going forward. In addition, the BoJ is expected to maintain interest rates at current levels for the time being given global uncertainty and downside risks to the economy. The current exchange rate (JPY 140-145/USD) is already factored into companies' forward guidance.

Over recent years, 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. The unwinding of cross-shareholdings is also progressing and represents a positive trend.

Under these circumstances, we aim to maintain a balanced portfolio, combining growth stocks with higher earnings visibility as well as selective value-oriented stocks with potential positive catalysts, such as turnaround prospects and an improvement in shareholder returns. The portfolio also has relatively close-to-benchmark sector positioning, so that stock selection is expected to be the consistent driver of returns.

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All data are sourced from Allianz Global Investors and Bloomberg as of 30 June 2025 unless otherwise stated.