Allianz Global Investors

Allianz China A-Shares

Monthly commentary

Investment Objective

The Fund aims at capital growth over the long term by investing primarily in the A-Shares equity markets of the People's Republic of China ("PRC").

What Happened in April

The Fund outperformed the benchmark in April. Stock selection in the Information Technology and Materials sectors were the key contributors.

At a single stock level, a top contributor was Zhongji Innolight. The company makes optical transceivers that allow high levels of data to be transmitted quickly across a network. These play an important role in areas such as the development of artificial intelligence (AI) applications, especially in data centres where high speed data transmission is required. Innolight delivered a good set of results during the month and should continue to benefit from rising AI-driven demand.

Conversely, a top detractor was a leading semiconductor equipment producer. Q1 results were slightly below expectations, partly due to higher levels of research and development (R&D) expenses as the company continues to invest heavily in future growth projects. It has been gaining market share given its technological edge over other equipment players in China and in the longer term should benefit from the increased localisation of semiconductor production.

Portfolio Strategy and Outlook

China equities have continued their good run since Chinese New Year. Both onshore and offshore markets have notched up gains of more than 15% (USD) since early February.

APRIL 2024

The improved market performance is due to a number of factors. First, the decision in January to mobilise the "national team" through significant buying of onshore exchange-traded funds (ETFs) provided a significant confidence boost. The Q1 results season has also been reassuring with a number of high profile "beats". While top-line growth has generally been muted as expected, tighter control of costs has fed through into improved bottom-line profitability.

Alongside the improved earnings picture has been a notable increase in dividend payouts. These have been spurred by a recent regulatory push, but from a fundamental perspective there certainly appears to be room to increase dividends. The overall dividend payout ratio of around 30% is relatively low in a global context, despite the high levels of cash on many corporate balance sheets.

Enhancing shareholder returns was a key feature of the once-a-decade guidelines – known as the "Nine Measures" – issued by China's State Council in April. The 2024 Nine Measures concentrate mainly on improving the quality of capital markets in areas such as stricter regulation of initial public offerings (IPOs) through higher thresholds, more forceful de-listing mechanisms, better shareholder returns, enhancing investor protection through improved disclosure and encouraging long-term institutional equity ownership.

One particular area the measures address is the high level of equity issuance, which has long been a headwind for China markets. Mainland China and Hong Kong's combined stock market capitalisation has surged in the past two decades from less than USD 1 trillion in 2003 to currently around USD 14 trillion. Much of this has come about as a result of IPOs and secondary issuance. In contrast, the level of share buybacks, especially in onshore markets, has been quite limited.

The amount of equity issuance has declined significantly in 2024 while share buybacks have picked up. If this is the start of a more structural change which eases the earnings drag from equity dilution – combined with higher levels of share buybacks and dividend payouts – then the scene may be set for a more favourable balance of equity demand and supply going forward.

There was quite limited portfolio activity last month. We initiated a new position in a low-cost airline, which is expected to benefit both from a pick-up in travel activity and customers trading down in search of lower prices. The portfolio continues to have relatively close-to-benchmark sector allocations. At month-end, the largest sector overweight is Industrials (+3.9%), while the largest underweight is Health Care (-3.7%).

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All data are sourced from Bloomberg and Allianz Global Investors as at 30 April 2024 unless otherwise stated.

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