Allianz Global Investors

Allianz European Equity Dividend

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth by investing in companies of European equity markets that are expected to achieve sustainable dividend returns in accordance with the Sustainability Key Performance Indicator Strategy (Absolute). In this context, the aim is, at least, a year-on-year improvement pathway on the sub-fund's weighted average Sustainability KPI to achieve the investment objective.

What Happened in March

Global equities moved higher over March, further bolstering already strong year-to-date returns. Sentiment was lifted by signs of improving economic momentum in Europe and China, as well as by central bank indications that rate cuts were likely to start in the summer. At a sector level, Energy companies advanced the most, followed by Materials stocks, while Consumer Discretionary was the weakest. Global bonds gained as central banks appeared to be less concerned about the possibility of a resurgence in inflation than many had feared. The largest downward movement in yields was seen in Europe, particularly in the UK where 10-year yields dropped around 25 basis points (bps) after UK inflation fell more than expected. Elsewhere, the yield on the 10-year German Bund fell 10 bps to 2.3%, while the 10-year US Treasury yield declined 5 bps to 4.2%. The Swiss National Bank became the first major central bank to lower rates this cycle. Japan was the exception with bond yields rising slightly after the Bank of Japan (BoJ) finally ended its below-zero interest rate policy. The US dollar, euro and British pound strengthened against the Japanese yen. While the BoJ increased borrowing costs for the first time since 2007 and ended its yield curve control policy, it stressed that borrowing costs would not rise sharply until inflation expectations were anchored at its 2% target. Commodity prices rallied. Oil prices moved higher, closing the month around USD 87 a barrel (Brent crude), given the ongoing conflicts in Ukraine and the Gaza strip, as well as the increased attacks in the Red Sea. Gold prices also advanced, touching a fresh high of more than USD 2,200 an ounce.

Portfolio Review

It was mostly a less volatile month compared to markets over the last year, and the MSCI High Dividend Yield Index returned a similar level to the broader MSCI. Similarly, last month government bond markets were steady. For example, German 10-year Bunds mostly yielded between 2.3% and 2.4% across the month. The strongest rises in equity markets came from the Banks sector which rose by 11% in euro and the Energy sector, with a 7% return. With tensions high in the Middle East, benchmark oil prices remained above USD 80 which is a profitable price for the European oil and gas producers. The Banking sector saw a general move higher as profitability is strong, with only Swedish banks dropping over concerns there for the property market. Transportation was one of the few sectors to decline over the month. Results and news in shipping and deliveries were disappointing, as weak European industrial production has been reducing demand for shipping and related services. Hence, it is not unusual to see a short-term reaction in shares that have previously risen strongly. Conversely, the holdings in the Financials sector were again a strong positive. The large weighting in Banks was a key contribution as the sector rose broadly, whilst stock selection in Insurers was again a positive. We reduced some large positions in stocks that had given strong returns previously, for example in the Insurance sector. We also reduced certain Consumer companies, such as a clothing retailer. Strong results helped the shares to climb to an all-time high and so it was prudent to moderate one of the largest holdings in the Fund given the higher valuation of the shares. Our principal focus is owning quality and financially sound companies; waiting until opportunities arise when we can buy them at attractive valuations, so they offer dividend yields ahead of the overall market.

Market Outlook

The overall outlook for the equity markets still appears favourable. US growth remains healthy, and high labour demand in particular is encouraging. At the same time, there are more and more signs of an improvement in sentiment in Europe. Meanwhile, the Chinese government has announced ambitious new growth targets and will probably implement stimulus measures to achieve them. Importantly, Chinese leaders have recently emphasised that the country plans to become a top technology provider. Corporate earnings have recently been convincing overall. As long as earnings growth is stable, market participants should remain optimistic even in the face of new record highs. It is clearly positive that the stock market uptrend in the US is now more broadly-based and no longer driven only by the Technology sector. With many equity valuations quite high, the markets may be vulnerable to setbacks if the earnings trends and/or the economic environment deteriorate significantly. The leading international central banks have successfully dampened market participants' expectations about the timing and size of rate cuts. Money market participants currently expect the US Federal Reserve (Fed) and the European Central Bank (ECB) to take the first rate steps towards mid-year. From our vantage point, the combination of moderate to low growth, slower inflation and relatively high interest rates in the developed economies for some time to come should support the fixed income markets. From a risk/return vantage point, high-quality bonds appear particularly attractive at the current rate level. At the same time, high yield spreads have narrowed. As a result, the high yield segment appears vulnerable to a potential downturn in economic activity. Careful selection is therefore particularly important in this market segment, as the financial situation of the individual issuers may play a key role.

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