

Allianz Global Artificial Intelligence

Monthly commentary

Investment Objective

The Fund aims at long-term capital growth by investing in the global equity markets with a focus on the evolution of artificial intelligence 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.

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 basis points (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 on both a gross- and net-of-fees basis versus the blended benchmark (50% MSCI ACWI Index/50% MSCI World Information Technology Index). From a sector perspective, Information Technology and Financials were the largest relative contributors. The Health Care and Consumer Discretionary sectors were the largest detractors. Artificial intelligence (AI) infrastructure was the strongest performer given positive industry data points that remain constructive for our AI semiconductor and data centre-related holdings. AI applications was another outperformer with strength from companies with AI agent exposure. AI-enabled industries underperformed the blended benchmark because of our Health Care exposure.

Contributors

Morgan Stanley is a leading global financial services company with business segments that includes institutional securities, wealth management and investment management. The company reported strong better-than-expected earnings, with broad strength across segments. Morgan Stanley also highlighted that AI and technology investments helped drive new wealth management clients wins. We believe the company is well positioned to deliver products and services leveraging AI to enhance its various product offerings. Moreover, the company's earnings trajectory is also positioned to benefit from a recovery in capital markets, improved net interest income trends and controlled costs.

Datadog Inc. offers a monitoring platform that provides software engineers real-time observability across the entire technology and application stack. This platform enhances user experiences and avoids downtime through automated problem detection. Shares were higher as the spending environment for observability software experienced incremental improvements. Looking out, the company has an attractive growth trajectory given a large addressable market, Datadog's strong product offering, and the ongoing trend of digital transformation. Datadog is also a beneficiary of increased AI-stack workloads. The company has also integrated generative AI into its platform, including natural language prompts to surface intelligent insights from their observability data, generate key assets like tests and post-mortems and streamline incident response and remediation.

Detractors

Detractors include a vertically integrated solar manufacturer that specialises in the production of high-performance thin film-based solar photovoltaic panels. The company is implementing AI across its value chain to drive innovation, enhance efficiency and improve customer service. Shares were lower during the month as bookings slowed due to policy uncertainty. It remains well positioned to capture the growth potential of US utility scale solar. Also, the company has strong visibility with orders extending through 2027 and margins should trend higher as new projects get priced in at higher rates.

Among the largest detractors on a relative basis was Nvidia Corp. Although the stock was a meaningful position in the Fund, we were underweight relative to the benchmark. The benchmark had an average allocation of 11.50% during the quarter versus the Fund's average weight of 7.90%. Shares were higher during the period as Nvidia and other AI server companies provided positive commentary on the AI infrastructure investment environment. We still favour the company as one piece of a diversified exposure to the AI infrastructure opportunity. Cloud hyperscalers continue to add AI

compute capacity to meet large, unmet customer demand, while enterprises are also building out their own AI training capabilities to create new business applications and enhance employee productivity.

New Buys and Sells

New buys include a pharmaceutical company with drug franchises that includes oncology, diabetes and ventral nervous systems. The company's blockbuster obesity treatment is a key growth driver that has a large addressable market with strong momentum. It is also utilising AI to accelerate their drug discovery and development processes, including treatments for diseases with unmet medical needs.

We also bought a US financial services company. The company is positioned to benefit from a better regulatory backdrop and from Fed rate cuts that should yield a more favourable interest rate environment. It has been heavily investing in AI technologies, which should yield productivity enhancement and greater operation efficiency across areas that include fraud detection and personalised recommendations for customers.

Although we previously reduced the position in supplier of semiconductor manufacturing equipment, specifically machines for the production of chips through lithography, we ultimately exited the position given uncertainty regarding the spending intentions of key customers and potential additional US government export restrictions on equipment sold to China.

We also exited a data developer platform because of inconsistent performance over the past couple quarters. Further, we have been more concerned regarding competitive pressures, especially from a computer technology company, that is making it more challenging to migrate legacy workloads to the platform.

Market Outlook

We continue to have a constructive mid- to long-term outlook for equity markets given the earnings growth potential from continued AI innovation and adoption 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. We continue to maintain a balanced portfolio positioning for the upcoming Trump presidency, which should be similar to his past administration. 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 AI innovation in the years ahead.

As for what's next in the ongoing generative AI innovation wave, we expect the robust capital investments in "Phase 1" AI infrastructure to continue and the industry to enter the "Phase 2" AI applications wave that leverages this infrastructure to develop new generative AI capabilities in software to drive greater value and automation opportunities. We are also seeing early signs of "Phase 3" AI-enabled industries demonstrating effective use of generative AI. Many companies outside of the Technology sector are increasing investments in generative AI to train one's own industry-

specific model on its proprietary data or knowledge to compete better and innovate in the future. A backdrop of emerging AI beneficiaries underappreciated for their potential creates a significant opportunity for alpha generation in the years ahead.

AI infrastructure: The developments around generative AI and large language models further demonstrate that the demand backdrop for AI infrastructure companies should remain strong given the computing requirements for training complex AI models and subsequent inference needed for edge intelligence. More companies are now motivated to build out their own domain-specific generative AI capabilities through continuous training and refinement. As these launch for broad-based use, demand should also expand to networking and storage infrastructure to support the explosive growth in new AI workloads. Investment also appears to be expanding to smaller cloud providers, governments and corporations in more countries around the world, which should be supportive of the ongoing build-out of critical AI infrastructure in the coming years.

AI applications: A new wave of AI applications is emerging that infuse generative AI capabilities into their software to drive greater value and create more monetisation opportunities. Generative AI appears to be evolving into its next phase with the emergence of AI agents. These applications are customisable and run 24/7 and can mimic human decision-making capabilities. This can take a lot of costs out of businesses and dramatically improve productivity. As these AI agents roll out for broader distribution, AI applications companies can open up many new monetisation opportunities and create value for users.

AI-enabled industries: AI is helping to reinvent digital transformation, introducing new generative AI possibilities that can significantly boost productivity and reduce costs. As more processes go digital, the opportunity for AI to react to new information or unexpected changes can revolutionise every industry. Many companies in AI-enabled industries are increasing investments in generative AI to train one's own industry-specific model on its proprietary content or knowledge to compete better and innovate in the future. We are witnessing an increasing number of companies across Automotive, Consumer, Health Care and Finance sectors leveraging proprietary datasets that could yield differentiated AI models and applications that are difficult to replicate and can handle tasks better than general purpose AI. We believe this is just the tip of the iceberg as companies become more comfortable with AI's potential to drive greater efficiencies and automation across every part of their business.

Overall, we continue to believe we are at the very early stages of massive disruptive change brought about by advances in – and the deployment of – AI. We believe these changes will drive meaningful growth for companies that can take advantage and drive disruption within their respective industries. Our view is that the compounding effect from AI disruption will create massive opportunities for innovative companies across every sector. Stockpicking will be essential to capturing the benefits of this opportunity, especially in an environment characterised by disruption and change. As we have done since the launch of the Fund, we remain focused on identifying the companies that leverage AI to deliver the most shareholder value creation over the long term. Compared to the technology innovation ahead of us, humanity is still on day one of our journey through the AI revolution.

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