Allianz Global Investors

Allianz Hong Kong Equity

Monthly commentary

- The Fund aims at long-term capital growth by investing in equity markets in Hong Kong.
- The Fund is exposed to significant risks of investment/general market, country and region, emerging market (such as Mainland China), company-specific, and RMB (such as exchange controls), and the adverse impact on RMB share classes due to currency depreciation.
- The Fund may invest in the China A-Shares market directly via the Stock Connect or other foreign access regimes and/or other permitted means and/or indirectly through all eligible instruments and thus is subject to the associated risks (including quota limitation, change in rule and regulations, repatriation of the Fund's monies, trade restrictions, China market volatility and uncertainty, potential clearing and/or settlement difficulties, change in economic, social and political policy in PRC and Mainland China tax risks).
- The Fund may invest in financial derivative instruments ("FDI") which may expose to higher leverage, counterparty, liquidity, valuation, volatility, market and over the counter transaction risks. The Fund's net derivative exposure may be up to 50% of the Fund's net asset value.
- This investment may involve risks that could result in loss of part or entire amount of investors' investment.
- In making investment decisions, investors should not rely solely on this material.

Note: Dividend payments may, at the sole discretion of the Investment Manager, be made out of the Fund's capital or effectively out of the Fund's capital which represents a return or withdrawal of part of the amount investors originally invested and/or capital gains attributable to the original investment. This may result in an immediate decrease in the NAV per share and the capital of the Fund available for investment in the future and capital growth may be reduced, in particular for hedged share classes for which the distribution amount and NAV of any hedged share classes (HSC) may be adversely affected by differences in the interests rates of the reference currency of the HSC and the base currency of the Fund.

What Happened in May

The Fund lagged the benchmark FTSE MPF Hong Kong Index in May as initial market gains following indications of a tariff truce between the US and China gave way to profit taking in the second half of the month. Stock selection in the consumer discretionary sector was the main detractor, partially offset by a positive contribution from financials.

At a stock level, a detractor last month was a company which positions itself as the "Oriental Starbucks", specializing in premium whole-leaf teas. The company listed in March, initially making strong gains before seeing some profit taking over the last month. Through its differentiated franchise model and longer term potential for overseas expansion, we believe the company should be able to deliver sustained longer term growth and therefore deserves a valuation premium over its peers in the sector.

Conversely a key contributor was a biotech company focused on autoimmune and oncology related drug development. Share price momentum continued from April when the company announced positive results from their phase 3 clinical trial for a new product. The biotech sector overall has performed well year to date, buoyed by news of global pharmaceutical companies replenishing their product pipelines by licensing new drugs under development in China for sales around the world.

Outlook and Strategy

Since recovering from the tariff-induced volatility post "Liberation Day" in early April, China's equity markets have gone into something of a lull. To an extent this has been caused by uncertainty over the direction of ongoing China-US negotiations, and the prospects of a more substantive trade deal or otherwise.

The other key unknown is to what extent China's government policy will be ramped up to offset the weakness in exports, a key driver for the economy in recent years and an important contributor to China achieving its closely watched gross domestic product (GDP) growth target. There are a number of factors at play in our view, not least that the extent of the downturn in exports – and therefore the degree of further government stimulus required to offset this with stronger domestic demand – is challenging to gauge.

Nonetheless, given that policymakers have reiterated this year's GDP target of "around 5%" several times since "Liberation Day", it is in our view a question of when, not if, we see further policy measures. This is especially the case given that the latest housing market data was modestly weaker, and showed an ongoing, albeit mild, decline in property prices.

A key issue is rebuilding consumer confidence, which took a major hit in 2022 as a result of Covid policies, the subsequent weaker employment outlook and the downturn in the property market. China's consumer confidence index is based on a scale of 0 to 200, where 200 indicates extreme optimism, 0 extreme pessimism, and 100 neutrality. In the years before Covid, China's consumer confidence index typically tracked a level close to 120. The latest reading is 88.4, which at least marks a pick-up from the low point last year.

This weaker confidence is reflected in how spending patterns have changed in recent years, resulting in a surge of household bank deposits to more than USD 20 trillion. Mobilising these resources will be an important part of China's domestic demand recovery. As such, the focus on the private sector, which accounts for around 90% of employment in China and within this, technology and AI, is likely to be an ongoing feature of policy.

While the timing of a recovery in the feelgood factor within China is hard to predict, our view is the direction of government policy will continue to be supportive for equities. Combined with the strong state support for domestic equities in the form of direct buying of exchange traded funds (ETFs), we believe the downside in China A-shares in particular remains quite limited.

Portfolio activity in May focused on adding selectively to stocks that should benefit from a recovery in domestic demand, especially related to consumer spending. We also added to healthcare exposure. As well as holding positions in biotech companies with promising late stage drug pipelines, we are becoming more confident in the outlook for private hospitals.

The portfolio is positioned with relatively close to benchmark sector allocations so that stock selection is the key relative performance driver. At month end the largest sector overweight is basic materials , while the largest underweight is consumer staples.

Source: Bloomberg, Allianz Global Investors, as at 31 May 2025 unless otherwise stated.

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