

Allianz Global Artificial Intelligence

September 2017



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Fund manager

Summary

- Technology stocks within the MSCI World underperformed the broader equity market in September.
- The fund posted a gain and outperformed the broad equity market.
- There were several transactions during the month.
- The current economic and financial backdrop is likely to remain favorable for investments in artificial intelligence and advanced robotics.

Market environment

Global equities gained in value as positive economic news helped markets overcome continued heightened geopolitical tensions and the second major hurricane in a month to hit the Caribbean and southern US states. In economic news, data indicated that the US economy was continuing to show moderate growth with little evidence of a pick-up in inflation. Euro-zone equities rallied as positive economic news helped markets to overcome heightened geopolitical tensions. Technology stocks within the MSCI World Index underperformed the broader equity market. Sector performance was decidedly risk-on with value and small market capitalization factors outperforming growth and large-cap biases. This seemed to be in reaction to the general improvement in macroeconomic conditions globally. At the subsector level, the cyclical semi-conductors and communications equipment segments were among the strongest performers while higher-growth, defensive areas such as software and Internet lagged. Hardware and storage segments did well with the notable exception of Apple.

Performance analysis

During the period, the fund posted a gain and outperformed the broad equity market as measured by the MSCI World Index. Our overweight position in memory chip manufacturer **Micron Technology** was among the top contributors during the period. Shares surged after the company reported strong fiscal fourth quarter results and provided a better-than-expected near-term outlook for revenues and earnings. Underlying the constructive outlook is tightness in the supply of memory chips and lean channel inventories. We see multiple ways for the company to generate compelling earnings growth.

The **Trade Desk** was also among the top contributors during the period. The company provides a self-service platform for ad buyers to purchase and manage data-driven digital advertising campaigns using their own teams across advertising formats. The company's management was on the road during the month meeting with investors and recaps suggest that consensus estimates could be too low and longer-term expectations could underappreciate the growth trajectory.

Our position in online programmatic marketer, **Criteo**, was one of the top detractors during the period. Criteo's products allow marketers to track consumers that have visited a client's website and re-target ads to that consumer. Shares came under pressure as the company confirmed that Apple's newest online browsers for both desktop and mobile would include intelligent tracking prevention (ITP) features. Fears of ad blocking technology in browsers are not new for Criteo. The company's algorithmic advantages optimize the targeting of ads across devices which enables Criteo to amass the highest quality inventory available by ad platforms. Producers of high quality content have better leverage to require consumers to pay for their viewership through ads or subscriptions. We believe Criteo has relatively higher exposure to high quality content and ad experiences and is thus less exposed and perhaps helped by the proliferation of ad blocking tools which should more negatively impact lower quality content websites.

Our position in **athenahealth** was also a top relative detractor in September. The company provides cloud software solutions to health care providers that automates various aspects of practice management, like bill payment and scheduling. The company derives economic benefit when its customers use its software. The company recently acquired AI-powered platform Praxify. Praxify has created machine learning, mobile-centric workflow solutions for clinicians and their patients, including a virtual assistant mobile app. athenahealth is integrating the underlying technology into its cloud platform, including using natural language processing to update patient records based on physicians' spoken notes. Overall, we believe technology providers in the healthcare market have the opportunity to leverage their vast data and AI technologies to capture greater value for their shareholders. athenahealth, with its millions of patient records, has begun the journey to leverage this opportunity.

Portfolio strategy and activity

During the period, we sold storage systems maker, **Western Digital**, as the uncertainties regarding the company's dispute with its partner Toshiba has persisted. The stock has strongly appreciated since we first initiated the position and we had been trimming the position into strength. At this time we saw better risk reward opportunities in other names benefitting from the developments in artificial intelligence.

We sold consumer credit data aggregator, **Equifax**, following news of its data breach earlier this month. We believe the company will have to take considerable efforts to restore trust with consumers and the institutions that they partner with. As such, we believe earnings could be materially impacted for the foreseeable future.

We also exited online travel site, **Expedia**, following the departure of the CEO who left to run Uber. We saw this persona as key in the management of the company's various entities and believe execution risks may be elevated in his absence.

Finally, we sold **Facebook** in order to lock-in profits. We redeployed the proceeds from these sales into a new position in semiconductor capital equipment maker, **Applied Materials**. The company's customers are leading chipmakers in the memory and foundry/logic space that produce the underlying hardware that enable AI applications.

Outlook

The resilience of global equity markets has been surprising given the heightened geopolitical uncertainties surrounding U.S. politics, European elections, and military tensions in Asia. Heightened debt levels and demographic shifts continue to present structural challenges for most developed economies and are likely to remain headwinds to growth for the foreseeable future. Countries seeking to improve their prospects for growth are increasingly looking to foster investments in automation technologies that improve factor productivity. Several large organizations, such as Softbank, have even set up substantial investment funds to participate in the potential wealth creation opportunities from these developments. As such, the current economic and financial backdrop is likely to remain favorable for investments in artificial intelligence and advanced robotics.

A recent report from CB Insights reveals that venture capital arms of large corporations are investing in artificial intelligence at an accelerating pace. Funding in the first half of 2017 has already exceeded total funding from 2016. Since 2012, some of the major recipients of funding have been companies in the Cyber Security, Healthcare, and Internet of Things (IoT) sub-sectors.

Our strategy has done well versus the broader markets as companies are leveraging advances in artificial intelligence to develop new products, solve more customer problems, and deliver greater economic value. As the adoption of artificial intelligence broadens, more companies are seeing the benefits of the technology. Although year-to-date advances in the broader market indices have been disproportionately driven by moves in mega cap technology stocks, such as Apple, Google, Amazon, Facebook, and Microsoft (each of whom are aggressively investing AI technologies), overall market breadth has been healthy. We continue to see much more significant long-term potential in the smaller and midcap oriented companies that are transforming their businesses by leveraging AI technologies. We continue to believe the AI space is in its infancy and we expect many of the AI components enablers and early adopters represented in our holdings to be among those facilitating and consulting on these projects. Starting with experiments today, we see massive potential for AI to be infused in many human experiences and our holdings to benefit as a result.

Opportunities

- + High return potential of stocks in the long run
- + Investments specifically in the artificial intelligence area
- + Currency gains possible
- + Broad diversification across numerous securities
- + Possible extra returns through single security analysis and active management

Risks

- High volatility of stocks, losses possible. The volatility of fund unit prices may be strongly increased.
- Underperformance of the investment theme possible
- Currency losses possible
- Limited participation in the yield potential of single securities
- Success of single security analysis and active management not guaranteed

Important notes: A performance of the strategy is not guaranteed and losses remain possible. A security mentioned as example above will not necessarily be comprised in the portfolio by the time this document is disclosed or at any other subsequent date. This is no recommendation or solicitation to buy or sell any particular security. Data gross of fees; calculation at the net asset value (BVI method) based on the assumption that distributions are reinvested and excludes initial charges. Individual costs such as fees, commissions and other charges have not been taken into consideration and would have a negative impact on the performance if they were included. Past performance is not a reliable indicator of future results. **Calculation based on the most expensive share class.** The statements contained herein may include statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. We assume no obligation to update any forward-looking statement.

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