



March 2014

Investment Insights

from **Silicon Valley**

www.rcmtechnologytrust.co.uk

Walter Price Lead Manager, RCM Technology Trust

With over 40 years of experience of investing in technology companies, Walter Price has witnessed the technology sector improve user productivity through the revolution in semiconductor design, the birth of the personal computer and the arrival of the internet. Based in San Francisco, giving him close proximity to many of the world's most innovative companies, he heads up the Global Technology Team which manages US\$4 billion* in assets.

Technology in the news

In last month's newsletter, we mentioned the burgeoning trend of internet security. Major retailers have been stung by the coordination and sophistication of recent cyber-attacks and have been forced to address the holes in their security systems as a matter of priority. The Christmas 2013 season saw groups such as Target and Neiman Marcus hit by fraudsters.

Groups specialising in firewall management have been among the key beneficiaries of an increased focus on security. In the most recent attacks, hackers have operated behind the corporate firewall, using a company's own security credentials to penetrate its network and look for information to steal. During these raids, product information is repurposed to send out stolen information from ecommerce companies. This is a much more pragmatic and utilitarian way to hack, rather than a lone guy trying to infiltrate the Pentagon. Companies are finding that while the Internet provides tremendous opportunities, it also has its hazards.

Groups such as FireEye and Palo Alto Networks, both of which are held in the portfolio, have been among the early beneficiaries of corporate scrutiny of their security systems. Fire-Eye, for example, works with companies, putting its system in behind the firewall to look at the systems in place. In 90% of cases, it finds that security has been compromised in some way and is then in a position to offer the appropriate solution. Palo Alto Networks offers all network security functions, including firewall monitoring. It strives to offer better security than legacy firewalls,

*Source: Allianz Global Investors Europe GmbH as at December 2013. This is no recommendation or solicitation to buy or sell any particular security.

by building its firewall into a company's platform.

The extent to which these groups have the incumbents rattled was seen in February, when Michael DeCesare, president of McAfee, Intel's security software division, was forced to defend the group's future prospects. He claimed that large existing players like Intel Security and Symantec would still dominate this fast-growing sector. Investors do not appear to be convinced. Palo Alto Network's share price is up over 25% over the past 12 months, while Symantec's is down over 20%.

Google has also recognised the potency of this trend, investing in another two cyber security start-ups in March - Ionic Security and Jafco Ventures. Venture capitalists are increasingly backing companies in a position to deal with the growing threat of cyber crime.

eHealth - blue sky thinking

Changes in the US healthcare system are generating a swathe of new investment opportunities. In the summer of 2013, the trust made an investment in online healthcare portal eHealth, with the aim of capitalising on this new trend.

The Patient Protection and Affordable Care Act of 2010 requires US states to establish online marketplaces for health insurance by the year 2014 or default into the federal government's exchange, healthcare.gov. eHealth operates websites that allow consumers to obtain rate quotes and do side-by-side comparisons of health insurance plans. These services bring more transparency and choice to what is often a complicated system to navigate. The company has partnered with the federal government to allow

individuals in the 34 states that have not established their own exchanges to buy insurance through their platform. It's also possible that, over time, state exchanges may partner with the group. With the prospect of higher volumes driven by ACA customers and additional opportunities in the Medicare and employer markets, we think eHealth can grow its top-line considerably over the next several years.

Time to revisit Tesla?

Electronic car maker Tesla Motors has been a significant holding. Its share price more than tripled during the trust's financial year to the end of November 2013. Tesla has been dubbed the 'Apple of autos' for its ability to design and build high quality, luxury cars popular with drivers and environmentalists alike. It is expanding into new markets which could support solid growth for some time to come.

Fitting in with the trust's ongoing theme of big problems creating big markets, China has a chronic pollution problem. 71 out of 74 cities monitored in China over 2013 did not meet state environmental standards according to the country's Environmental Protection Ministry. As a result, China is potentially a huge market for Tesla: the Chinese government is very supportive of electric cars and is likely to encourage their widespread adoption.

In the meantime, the group is investing around \$2bn in a factory to help it produce cheaper batteries for a mass market electric car within three years, having focused exclusively on the luxury market to date. Again, this could be transformative for the group. Not only should it allow it to penetrate new markets, but also to

improve production times for its existing range.

Controversy has centred on its valuation and the shares have undoubtedly had an astonishing run. This led us to take some profits, but Tesla's recent success in China and longer-term prospects with their mass market electronic vehicles has led us to maintain it as one of the top 25 positions in the trust.

Technology valuations

Technology has been one of the clear winners of the past 12 months, partly because of its perceived cyclicality and partly because of a few high profile IPOs. Ao.com, for example, saw its share price rise over 30% on its first day's trading on the London Stock Market. Nevertheless, we would argue that there are still plenty of inexpensive technology companies in which investors could make a substantial return. The US technology sector in aggregate is trading on around 14.8x next twelve months' earnings versus 15.3x for the wider US market.

Beyond the 'glory' stocks, the key is to distinguish those companies that still have the potential for a re-rating. Among these are companies with potential to significantly improve their free cash flow. One of the areas in which we believe this situation could unfold is the communications infrastructure space. We hold groups such as Alcatel and Juniper. Juniper has recently committed to reducing \$160 million in operating expenses and to return around \$3bn to investors after activist investor Elliot Associates targeted the company, leading to a significant uplift in the share price. We think it's important not to dismiss swathes of the technology market as ex-growth without examining what is going on beneath.

All sources Allianz Global Investors Europe GmbH unless otherwise noted. This is no recommendation or solicitation to buy or sell any particular security.

Investing involves risk. The value of an investment and the income from it may fall as well as rise and investors may not get back the full amount invested. Competition among technology companies may result in aggressive pricing of their products and services, which may affect the profitability of the companies in which the Trust invests. In addition, because of the rapid pace of technological development, products or services developed by these companies may become rapidly obsolete or have relatively short product cycles. This may have the effect of making the Trust's returns more volatile than the returns of a fund that does not invest in similarly related companies. Past performance is not a reliable indicator of future results. The value of an investment and the income from it may fall as well as rise and investors may not get back the full amount invested. The views and opinions expressed herein, which are subject to change without notice, are those of the issuer and/or its affiliated companies at the time of publication. The data used is derived from various sources, and assumed to be correct and reliable, but it has not been independently verified; its accuracy or completeness is not guaranteed and no liability is assumed for any direct or consequential losses arising from its use, unless caused by gross negligence or wilful misconduct. The conditions of any underlying offer or contract that may have been, or will be, made or concluded, shall prevail. 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 a marketing communication issued by Allianz Global Investors Europe GmbH, an investment company with limited liability incorporated in Germany, with its registered office at Bockenheimer Landstrasse 42/44, D-60323 Frankfurt/M. Allianz Global Investors Europe GmbH is registered with the local court of Frankfurt/M under HRB 9340 and is authorised and regulated by the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin). Allianz Global Investors Europe GmbH has established a branch in the United Kingdom, Allianz Global Investors Europe GmbH, UK Branch, which is subject to limited regulation by the Financial Conduct Authority (www.fca.org.uk). Details about the extent of our regulation by the Financial Conduct Authority are available from us on request. RCM Technology Trust PLC is incorporated in England and Wales. (Company registration no. 3117355). Registered Office: 199 Bishopsgate, London, EC2M 3TY.