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# Investment Insights

from Silicon Valley

[www.allianztechnologytrust.com](http://www.allianztechnologytrust.com)

## Walter Price Lead Manager, Allianz Technology Trust

With over 40 years of experience of investing in technology companies, Walter Price has witnessed the evolution of the technology sector from the birth of the personal computer to the arrival of the internet and now the shift to cloud computing. 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.

## The connected car

**There is almost nothing that illustrates the pervasiveness of modern technology better than the development of the connected car. A few short years' ago, cars were a technology-free zone, and yet now technology is promising to transform the driver's experience and improve road safety.**

The connected car has real practical appeal for drivers, including internet radio, which means more personalised radio and fewer ads. This can make for a profoundly different in-car entertainment experience. At the same time, connected cars have real time traffic and navigation, which could lead to a reduction in stress for drivers. In theory at least, they can avoid accidents, traffic hotspots and find the smoothest route home. Connected cars can record and disseminate headlight, windshield wiper or traction control data to work out driving conditions, enabling drivers know when to stay at home.

There are also safety considerations. For example, connected cars could communicate both with each other and with centralised traffic management systems to reduce accidents. It raises the prospects of cars being 'aware' of each other (key for the development, ultimately, of a driverless car). Drivers can see how economically they have been driving, whether they are taking corners too fast, and get a realistic appraisal of their driving from an impartial source (a computer).

There are obstacles, of course. The development of connected cars is a slower process than, say, the development of a smartphone. Cars have a far longer product cycle, up to five years in some cases and flexibility is hindered to some extent, by safety

laws and regulatory requirements. But as with most technology, it will likely become cheaper to have a connected car. Tesla, for example, charges an additional \$4,000 on an \$80,000 car. If history is any guide, the cost should dramatically decrease over time.

The connected car as it stands has plenty of appeal: It simply makes driving a more enjoyable experience. We believe it represents a great opportunity for those companies that are involved.

## China's 'other' Internet retailer

Amid the excitement over the Alibaba IPO, a second Chinese online retailer - Vipshop Holdings - has been quietly attracting investors. The company listed in New York in November 2012 and the stock went nowhere for over a year. Since then, possibly as Alibaba has won headlines and investors have become more comfortable with the concept of a Chinese internet retailer, the share price has taken off, rising 184% over the past year alone (<http://markets.ft.com/research/Markets/Tearsheets/Summary?s=VIPS:NYQ>).

Vipshop specialises in 'flash sales', either of time-limited, in-season discounted goods, or off-season stock clearance. Similar sites in the UK and US - the Outnet, BrandAlley - have built considerable traction with consumers. Luxury is mixed with everyday items and the site has proved particularly popular in non-tier one Chinese cities where outlets are scarce. The group has some first-mover advantage in that brands prefer to partner with a limited number of sites to sell as much of their inventory as possible. It is an industry where scale and brand are important.

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

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Its latest set of results showed third quarter net revenues up by 130% year on year to US\$883m. It increased its active customers to 9.5m, up 137% over the same period. Alibaba continues to be an important position for us, but the success of Vipshop shows the importance of looking from side to side every now and then.

### Managing risk in technology

Technology has historically been seen as a volatile sector, but is currently experiencing some of the lowest levels of volatility on record. To give an idea of scale, the CBOE Nasdaq 100 Volatility index is now trading at a level of around 15, having spiked up to a level of 24 on 24 October. Putting this in context, the index hit over 60 at the peak of the financial crisis in 2008, but also spiked above 40 in late 2011.

Volatility may be low at the moment, but it is extremely uncomfortable for investors when it does emerge and this is not always easy to predict. We make no claims to always be able to defend against volatility, but we do have a number of advantages in managing it: Longevity, for example. We are one of the longest tenured teams in the industry and having seen a number of market cycles, we know when to hold our nerve.

However, we are looking at ways to manage risk better. Historically, the trust has shown periods of significant outperformance in buoyant markets, but has given some of that back during weaker markets, so we are working to ensure shallower troughs by altering characteristics of portfolio at times of greater stress. This has already proved effective and we believe it will shore up investor returns, if – or more likely when – volatility re-emerges.

### Grassroots – finding the next technology winner

Silicon Valley remains a hotbed of technology innovation, but separating products that have widespread appeal versus those that may have elegant technology, but no resonance with end buyers is a significant challenge. Wall Street analysts don't tend to be very helpful in assessing new models, and new companies. Often they do not extend coverage to smaller, more innovative companies and, if they do, don't always understand them well.

A good example of this is the iPhone. At its launch, seven years ago, relatively few Wall Street analysts recognised its significance. Certainly, few predicted that Apple would sell 6.1m iPhones over the next five quarters.

To build an understanding of whether a product will find traction with consumers, we use Allianz 'Grassroots' research surveys. This helps us build a picture of expected demand for a product or service. The Grassroots research team has a global network of over 300 independent journalists and field force researchers, experts in their field, who use their knowledge to conduct customized surveys that answer key questions about a company's products/services. Depending on the feedback, this information can enhance conviction in an investment thesis or lead us to revisit the thesis. We believe Grassroots research ultimately provides an information advantage that other investors may not have.

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

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