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Investment Insights from Silicon Valley

www.allianztechnologytrust.com

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*Source: Allianz Global Investors GmbH.

Big technology and corporate governance

They may have been good investments, but are they good corporate citizens? This is the question increasingly asked of 'Big Tech'. While these digital giants have delivered undoubted benefits to the consumer, have those benefits allowed them to grow too big, to the extent that they can neglect their responsibility to wider society?

It is a reasonable question. Current antitrust legislation is, to some extent, inadequate to deal with the influence of these companies. The US government has largely left these companies free to grow, but there are emerging signs of anti-competitive behaviour. It is clear that many big technology companies copy good ideas and then have the scale and resources to stymie the competition. They have sharp elbows, using the powerful user data they collect to their long-term competitive advantage.

There are growing calls for some sort of regulation and this is increasingly recognised by governments. This has been notably more prevalent in some countries. The General Data Protection Regulation (GDPR), the new European legal framework for personal data protection that comes into effect on 25 May 2018, for example, is an important step. China has also proved a tough environment in which to operate. 'Big Tech' have started to recognise that they will need to increase their lobbying efforts around the world as they come under greater scrutiny, but also to address some of the social responsibility issues, such as privacy and competition.

Checks and balances

Part of the problem is that these companies are so cash-rich; they don't need significant support from capital markets. This makes for an uneven relationship and little shareholder power. At the same time, many have grown quickly and lack the governance infrastructure of more established companies.

Nevertheless, there are checks and balances. In these companies, talent is the key resource. The largest Silicon Valley companies recruit the smartest and most talented graduates with high and attractive starting salaries. Usually half of the employee compensation comes from the share price. If it falls, many vote with their feet. To keep them, they need to have a share price that keeps rising. So far, they have been able to do that and to keep their good employees. However, it is notable that for other companies, where share prices have been weaker, people have been less happy and staff turnover has been higher.

However, it is an imperfect mechanism. We believe that executives might have been quicker to fix some of these companies' problems if they had felt more pressure from shareholders. Ultimately, these companies may need to be more responsible to attract shareholders. From our point of view, we have known these companies and the people that run them for a long time. We use that position to exert influence as best we can.

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BEST INVESTMENT
TRUST

INVESTMENT
WEEK
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Top 100 Funds 2014
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Top 100 Funds 2016
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investors
CHRONICLE
Top 100 Funds 2017
Allianz Technology Trust

At the heart of technology

To build and use this influence, we believe it matters where you are in the world. Although rivals have emerged, Silicon Valley remains the heart of global technology innovation. The major global technology companies – Apple, Facebook, Netflix, Cisco, eBay, Nvidia – all have their headquarters there, while the region attracts around one-third to one-half of all venture capital funding in the US. It remains the best place to launch a technology business, attract the right funding and fill it with the right people.

We have been based there since it started. This gives us two key advantages as we see it. First is the chance to get to know companies better. We don't just meet the chief financial officer, or investor relations representative, or whoever is willing to get on a plane to New York or London, we meet the whole management team. Second, is understanding the 'buzz'. This is a nebulous concept, but it means going to all the major conferences, talking to companies about what is going on, where they are seeing innovation. This means that we see the exciting technology as it emerges from private companies. It's much easier to figure out the hype from the reality than it would be from a distance.

Until recently, there were no meaningful rivals for Silicon Valley's crown. However, as technology investors we need to be aware of the growing influence from China. Today it runs almost as a parallel universe to Silicon Valley and valuable businesses have been created in TenCent and Alibaba. The business models from China are different, but often highly effective. The US technology companies know this: Facebook watches TenCent and vice versa; each is learning from each other.

There are areas where China is notably ahead of the US. In the payments area, for example, Alibaba and TenCent have pipped ahead with mobile wallets, while the US and Europe are still wedded to their credit cards and reward systems. As such, we make sure we visit China frequently to understand the trends there as well – particularly on the Consumer, where it is leading.

This has given us real insight in certain areas. For example, our work in China has helped us learn that social media doesn't have to be winner-takes-all. There, a number of different platforms are successful. Individual platforms appeal to individual user groups, rather than one platform dominating everything. Silicon Valley remains at the core of the global technology industry, but there is much to learn from China as well.

GrassrootsSM 1

In picking up new and interesting insight, we travel, we analyse, we talk to the wider technology community. However, every product needs to appeal to those outside Silicon Valley. To test that, we use our GrassrootsSM community. This global network is unique to Allianz Global Investors and comprises in-house employees, journalists, field force researchers and more than 50,000 industry contacts. This network will tell us, for example, how the latest iPhone is being received.

Most recently, we tested our long-held position on the security sector. There had been concerns that the move to the Cloud was reducing the reliance on third-party security provision. The research showed the opposite was the case, and that the move to the Cloud was creating more demand for security services. This is valuable insight that helped inform our positioning in the security sector. GrassrootsSM remains an important tool in our decision-making.

¹GrassrootsSM Research is a division of Allianz Global Investors that commissions investigative research for asset-management professionals. Research data used to generate GrassrootsSM Research reports are received from reporters and Field Force investigators who work as independent, third-party research providers, supplying research that is paid for by commissions generated by trades executed on behalf of clients.

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