BLACKFRIARS ASSET MANAGEMENT

www.blackfriarsam.com

+44 (0) 20 7332 2270

Asia Insight

MARKET REVIEW

The MSCI AC World Index slipped 1.7% in January. By contrast, the MSCI AC Asia ex Japan Index and the MSCI Japan Index managed returns of 2.5% and 2.3% respectively. India (+7.9%) and the Philippines (+7.0%) led the way, Malaysia (-2.6%) trailed. By sector, telecoms (+5.9%) and real estate (+5.2%) pushed ahead while energy and materials lagged.

Please note our regional funds traded xd (a dividend equating to a yield of 1.6-1.8%) on 2nd January. Please also note that, with effect from 2nd February 2015, RBC has now taken over as the administrator.

All returns above are stated in US Dollar terms.

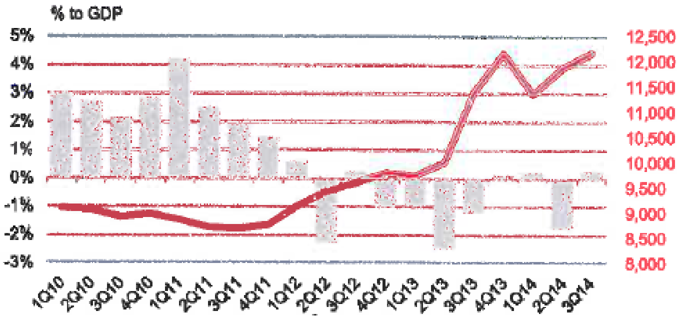
INVESTMENT TOURISTS

We travelled across South East Asia in January. The first point which struck home, as a friend drew up at a Bangkok petrol station, was how quickly and how significantly lower oil prices are impacting upon disposable incomes. The corollary of this is, of course, plunging headline inflation rates. Thailand's January CPI print was -0.4% y-o-y, Korea's 0.8%. Singapore's December print was 0.2% y-o-y, China's 1.5% y-o-y. Yesterday, Australia cut interest rates and India reduced the Statutory Liquidity Ratio following the surprise mid January interest rate cut. Today, China cut the Reserve Ratio Requirement 0.5% to 19.5%. From Bangkok to Beijing to Seoul, central bankers will remain under pressure to ease monetary policy further in 2015. For most economies in the region, lower oil prices are resulting in substantial improvements in the external accounts.

The bad news is that the domestic economies across South East Asia appear to have either lost (Thailand & Malaysia) or are losing (Indonesia) their mojo. Only the Philippines (driven by a private sector CAPEX upswing) and most of Indochina are bucking this trend. Further North the slowdown is even more evident as evidenced by GDP and PMI releases. At an individual company level, same store sales are flat at best. Only the most robust growth story is achieving either volume or value growth at the top line. Collapsing input costs will protect both margins and the bottom line to a large degree but growth per se, in what is traditionally considered a growth area, is in short supply.

Whilst the likes of portfolio holding BTS (the operator of Bangkok's Skytrain) can still point to high single digit ridership growth and Bangkok Dusit Medical Services is opening new hospitals as fast as it can, reflecting strong demand, other meetings proved a little more sombre. Steady as she goes but not much growth or visibility evident in the short term but, by and large, this is reflected in valuations.

Yields of 3-5% are commonplace and nowhere was this more evident than during meetings in Singapore. Solid, well managed companies where more than lip service is paid to the interests of minority investors. The Monetary Authority of Singapore has reacted to slower global growth by allowing the Singapore Dollar to depreciate gently since last summer. No doubt this weakness will continue in the short term but it simply increases the likely longer term returns.



And then there is Indonesia. The chart above (courtesy of CIMB) shows Indonesia's FDI minus the current account in grey bars and the currency (inverted) against the Dollar over the past five years. A deteriorating current account coupled with indifferent foreign direct investment flows seems to have had some bearing on the weak performance of the Rupiah over the past three years. The new Jokowi administration has scored big plus points with the recent effective removal of fuel subsidies. There are (as ever) high hopes of a sustained (and much overdue) infrastructure investment boom. There is, however, little talk about reforming the country's draconian labour laws which deter much needed FDI whilst the recent direct downward pressure on cement prices smacked of a populist agenda.

At a company level, nine meetings left us distinctly underwhelmed. It is quite possible that we met the wrong nine and highly likely we are being too cycnical but in our humble opinion the equity market is still considered as little more than an ATM by some. Sensible dividend policies, for example, are few and far between. The market overall is not desperately cheap and the more interesting sectors such as consumption and, more recently, construction are just plain expensive. The Rupiah has proven a poor store of value over the years and we will continue to observe from a safe distance for now.

MSCI

By deciding to include China focused, but US listed, internet companies with questionable VIE structures and rich valuations in their universe, our good friends at MSCI have decreed that passive investors in the region shall increase their exposure to China by 3 or 4 percentage points by the end of 2015. How appropriate to introduce this change in the Year of the Sheep! Our stock selection process is fortunately immune to this socialised capital behaviour but if you own an ETF be sure to open the bonnet every now and then and have a good look inside.

OUTLOOK

A decent start to 2015 for the regional markets. Growth remains illusive and we would not bet on much improvement across Northern Asia. The collapse in oil prices has significantly increased the probability of a decent cyclical recovery in India. Likewise a prolonged period of easy money and cheap petrol should allow ASEAN to rediscover its mojo later this year. Kung Hei Fat Choy!

HT&SD