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Asia Insight

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Market Review

The MSCI AC World Index rose a robust 7.4% in March while the MSCI AC Asia ex Japan Index jumped 11.2%. The stronger yen derailed the party in Japan although the MSCI still rose a respectable 4.7%.

Stronger local currencies were helpful in generating strong returns; the Korean Won, for example, gained 7.7% during the month. Early year high fliers such as Thailand and Indonesia underperformed while Korea (+14.1%) lead the pack. By sector, energy (+14.0%) and materials (+13.4%) had their day in the sun.

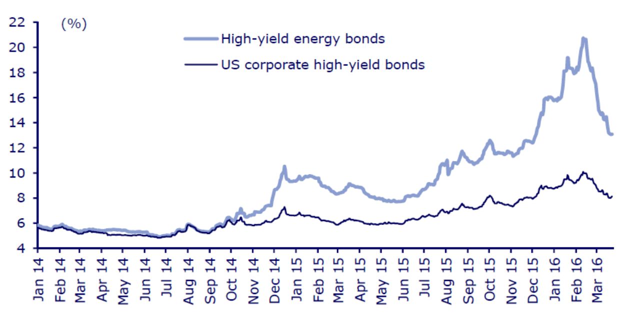
Our regional funds had a good month with both posting a double digit return.

All returns above are stated in USD terms.

New Leaders Absent

Developed and developing market equities made a strong recovery from the January selloff and are now back to all square, year to date. What interests us is that the market lows, both in January and February, coincided almost to the day with recent lows in the price of crude oil. CLSA's Chris Wood notes that the (modest) recovery in crude prices has resulted in a sharp decline in high-yield energy bond yields and, indeed, US corporate high-yield bond yields (see chart below). Wood argues that this improvement in credit market conditions has effectively rubbed off on traded equities.

Yields on Barclays US High-Yield Corporate Bonds Index



Source: DataStream, Barclays Capital

It is noteworthy that the energy and materials sectors have led the broader equity recovery. This makes us suspicious of the rally: rarely is a new bull run led by the previous bear market losers. In this respect it is also noteworthy that oil has already declined some 15% from its mid-March highs.

The portfolios have zero exposure to energy or commodity companies for reasons explained in earlier Asia Insights; the sharp slow down in the Chinese heavy industrial sector means that the major supply/demand imbalance is here to stay.

Chinese Banks

For some time the robust reported financial position of the Chinese banking sector has appeared strikingly at odds with the increasingly desperate financial condition of many of China's larger SOEs - their traditional client base - but cracks are finally appearing.

The "Big 4" reported lacklustre full year earnings and all cut their dividend pay-out out ratio from 33% to a suspiciously (centrally?) planned 30%. Headwinds for 2016 include falling net interest margins, rising non-performing loans, sharp increases in special mention loans and the PBOC's "encouragement" of debt to equity swops. We continue to avoid exposure to all Chinese financials.

Results

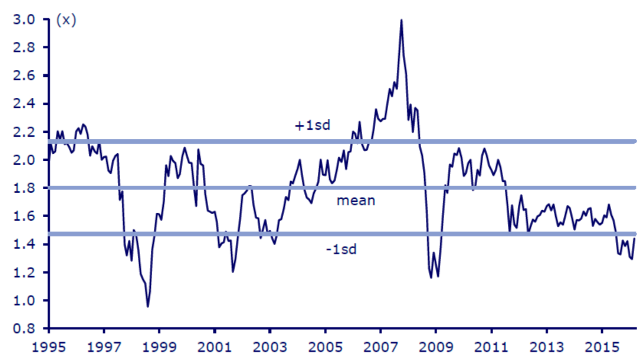
A cracking set of results from Minth Group saw the share price gain 28.5% during March while a very solid set of results from Samsonite left the share price 14.8% higher over the month.

Sun Art Retail, which reported in late February, rose 16.8%. Equally unloved Want Want gained 11.7% despite reporting lacklustre results mid-month. We find this most encouraging. The de-rating of Chinese consumer stocks has been nothing short of savage over the past year. Rising share prices despite indifferent results suggests a new leadership group may be at hand.

Stabilisation?

There are some recent data points suggesting that the headlong collapse of global trade is abating. Korea's March exports only fell by 8.2% y-o-y while China's March Caixin Composite PMI rebounded to 51.3. The Reserve Bank of India, clearly satisfied by the budget, cut rates by 25bps. The Thai Government finally appears to getting serious with regard to boosting infrastructure spending while the Philippines economy sails on serenely ahead of Presidential elections.

MSCI AC Asia Pacific ex-Japan Trailing PB



Source: Bloomberg

Outlook

We append our favourite chart above. For the same reasons many investors forget to sell during euphoric moments, many forget to place a bid when the outlook is grim. Forget commodities, forget energy and forget Chinese financials - just buy the rest.

For Asian investors it's been a tough five years in relative and absolute terms. Predicting short term moves is a mug's game but recall Buffett's great quote: "Price is what you pay, Value is what you get".

HT&SD