Asia Insight

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Market Review

The MSCI AC World Index slipped 0.6% in June whilst the MSCI AC Asia ex Japan Index managed a 2.7% advance. For the first half of 2016 the MSCI AC World Index gained 1.2% whilst the MSCI AC Asia ex Japan Index rose 2.2%.

Both regional funds had a decent month, outperforming the indices thanks to good stock selection. For the first half the Asian Focus Fund slipped 1% in line with the index, while the Oriental Focus fund gained 4.8%, comfortably ahead of the index. Please refer to the fund factsheets for further information.

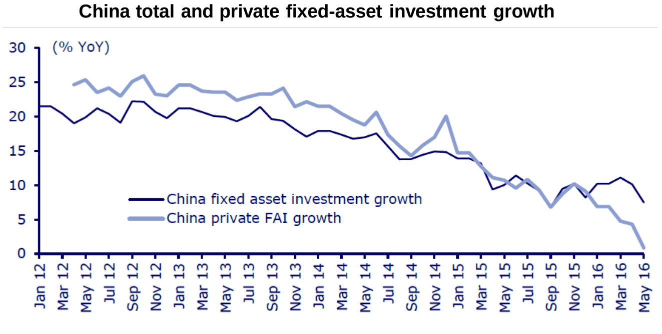
All returns above are stated in USD terms.

China

For all the talk earlier this year of a stimulus package in China, we find the chart below enlightening. Last month we noted the small decline of Indian CAPEX in 1Q16, the first decline for two years, commenting that this decline was driven by the private sector. While state-owned enterprises will no doubt follow instructions from on high and build more roads to nowhere (or equivalent), the investment intentions of the private sector have cooled dramatically.

This will be of particular concern to Beijing since it is the private sector which generates the vast majority of new jobs. The weaker trend in CAPEX is consistent with the reversal of the 1Q16 spurt in credit growth. Credit extended in April-May this year is 37% lower y-o-y. Capital expenditure is by far and away the main driver of economic growth and slowing CAPEX suggests the growth outlook remains muted.

China total and private fixed-asset investment growth



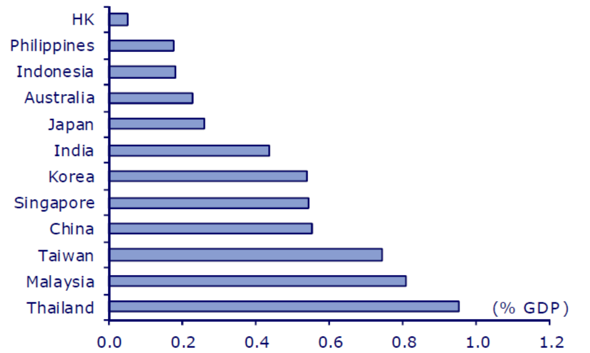
Source: CLSA, National Bureau of Statistics, CEIC Data

Brexit and Asia

The immediate impact of the Brexit vote was felt in equity markets (with Japan particularly hard hit as the yen appreciated). Non Japanese markets, however, rallied strongly the following week and ended the month ahead, as noted in the market review.

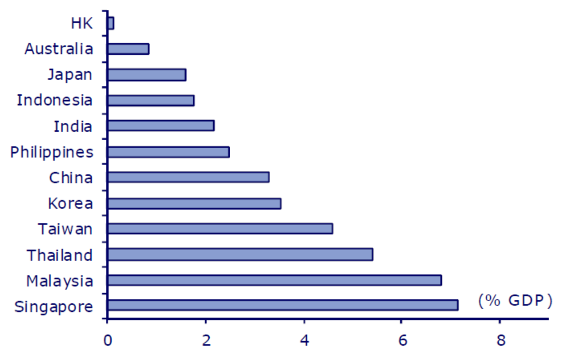
From a trade perspective, the impact on Asia of potentially weaker exports to the UK is minimal (as shown on the next chart). Exports to the UK account for less than 1% of GDP. Should Brexit undermine economic activity more broadly across the EU, the impact would be more noticeable with exports to the EU accounting for up to 7% of GDP in the cases of Singapore and Malaysia (as the second chart illustrates).

Exports to the UK, % GDP



Note: Domestic exports Hong Kong and Singapore
Source: CLSA, CEIC

Exports to the EU, % GDP



Note: Domestic exports Hong Kong and Singapore
Source: CLSA, DataStream, CEIC

Whether it is slowing growth in China or political and economic uncertainty in the EU, the fact is that global deflationary pressures continue unabated. According to CLSA's Chris Wood some US$12tr of G7 bonds now have a negative yield. The regional portfolios both hold some exporters, notably Samsung Electronics, TSMC and Minth, but the bulk of the portfolio remains focussed on domestically-orientated concerns. Without doubt, the more domestically-driven Asian economies with excellent demographic profiles (the Philippines, India and Indonesia) continue to look more and more attractive.

The Asian Focus Fund additionally holds a number of Japanese exporters. The persistent strength of the yen simply compounds the underlying problem of weak global growth and sagging demand. We would expect to see analyst and company forecasts continue to edge lower and we will act accordingly.

Outlook

While technical analysis is not a driving force of our investment process, we were interested to note that Asianomics technical guru Chris Roberts' "new 52-week highs indicator" has just given its 10th buy signal since 2003 for the MSCI Asia ex Japan Index. The historic success rate of this buy signal is 80%!

HT&SD