

# ASIA INSIGHT

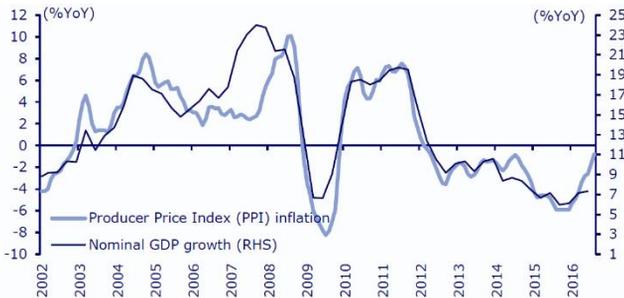
5<sup>th</sup> October 2016

## Market Review

The MSCI AC World Index inched higher in September, rising 0.6%, whilst the MSCI AC Asia ex Japan Index posted a 1.6% gain led by Hong Kong (+3.7%), Taiwan (+2.9%) and China (+2.5%). By sector, Technology (+3.9%) led the way while the Energy sector (+3.0%) continued to recover as the benchmark Brent regained USD50. The Philippines (-5.6%), Thailand (-3.5%) and Malaysia (-2.9%) headed the other way which was unhelpful for the two regional funds.

All returns above are stated in USD terms.

### China: Nominal GDP growth and PPI deflation



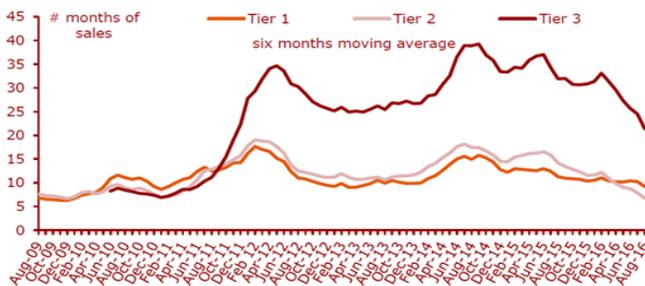
Source: CLSA, National Bureau of Statistics, CEIC Data

## Growth

There is further evidence to suggest that growth prospects in the region are improving. We noted the steady improvement in Chinese PMIs last month and Asianomics' Jim Walker is confidently predicting that August's year-on-year export growth across the region will turn positive for the first time in almost two years with only Malaysia and the Philippines yet to announce August data. Given the recent rally in commodity prices, it is quite possible that the September Chinese Producer Price Index, due to be released shortly, will produce the first positive-year-on-year reading since January 2012. Does this precede an acceleration in nominal GDP growth as CLSA's Chris Wood's chart above suggests? If so, this would provide a major boost to corporate China's revenues.

The question, however, is whether this improvement in economic growth is sustainable or not, and we would argue that this varies substantially from country to country. The strength of the Chinese residential property market over the past year has been quite remarkable, as the sharp decline in inventory in the chart illustrates.

### For-sale property inventory



Source: Local Housing Bureaus, Soufun, CRR

n.b. tier 3 inventory data here represents 20 relatively strong cities and is not representative of lower tier cities across the board

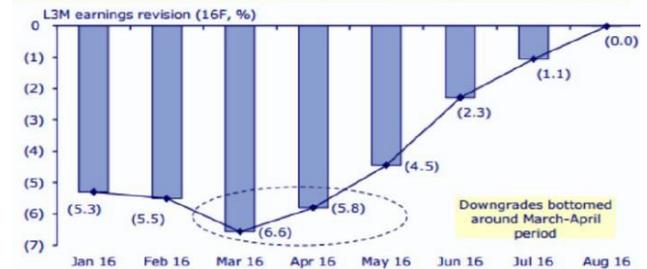
The property sector has been vital in sustaining, or underpinning, otherwise flagging growth. Interesting, therefore, that Wang Jianlin, Chairman and Founder of Dalian Wanda Group (China's largest property developer) recently described the Chinese residential property market as "the biggest bubble in history". Across the real economy, China Reality Research reports that income growth continues to decline sharply and also sees signs that the Chinese love affair with online shopping is on the wane.

In India, strong domestic demand remains the key growth driver and a good monsoon season, together with the recent increase in civil servants' compensation, should maintain or accelerate this momentum, as will the ongoing government infrastructure spending. Robust GDP growth is even more remarkable given the absence of any real upturn in private sector investment where deleveraging remains a key corporate focus, especially in the infrastructure and capital goods sectors.

It is noteworthy that the Reserve Bank of India continues to apply pressure on the banking sector, especially PSUs (public sector banks), to write off, or dispose of, NPLs – an easier task following the enactment of the new Bankruptcy Code earlier this year. This will not stop many, indeed most, PSUs' capital deficiencies being exposed, but this is surely preferable to just sweeping everything under the carpet. A new private sector investment cycle, when it arrives, will ensure solid growth for the next few years.

The "foot-in-mouth" diplomacy of Philippine President Duterte remains a frustration, and certainly the more squeamish foreign investors have been aggressive sellers over the past few months, but progress on the ground has actually been impressive. In a country crying out for better infrastructure, Duterte approved nine infrastructure projects worth USD3.6bn in his first 100 days of office. Although the Indonesian tax amnesty declarations fell a little short of official targets, we judge the first stage of the program a success and a vote of confidence in the Jokowi administration. In Thailand, the government is finally moving faster after the positive referendum result. A fourth double tracking project was recently approved. The first two have been awarded, the third is up for tender this month and a total of seven double tracking projects should be underway by the end of 2017. In Bangkok, bidding on three new mass transit lines in Bangkok is underway. All encouraging stuff.

### MSCI Asinx: Rolling 3M earnings revision



Source: CLSA

## Outlook

The Fed blinked again and – famous last words – the traditional seasonal weak period for equities is almost over. Downward earnings revision seem to have run their course (see chart above) and we remain encouraged by regional valuations that remain inexpensive in relative and historical terms.