

# ASIA INSIGHT

13<sup>th</sup> March 2018

## Review

The MSCI AC Asia ex Japan Index retreated 5.0% during February largely tracking the 4.2% decline in the MSCI AC World Index. India declined 6.7% over the month with China (-6.4%) and Korea (-6.4%) close behind. ASEAN markets performed well with Thailand (+2.3%) and Malaysia (-1.4%) outperforming. By sector, Consumer Staples (-2.9%) and Utilities (-2.5%) outperformed while the Telcos (-6.8%) and Real Estate (-7.2%) underperformed.

Note: All figures above are total return and in US dollar terms.

Source: Bloomberg.

## China – “Power tends to corrupt, and absolute power corrupts absolutely” Sir John Dalberg-Acton, 1834-1902.

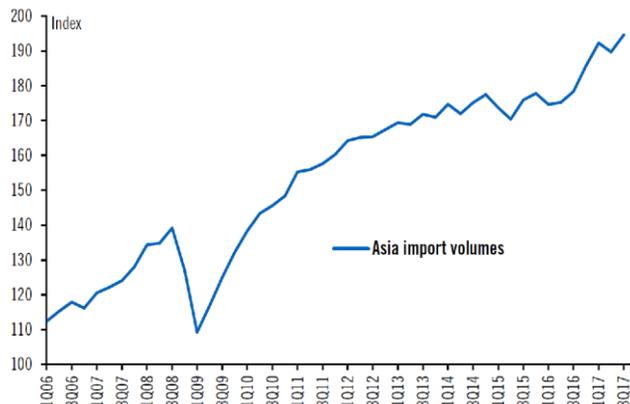
The Chinese constitution, adopted during the 5th National People’s Congress in December 1982 limited an individual to a maximum of two five year terms as President. This limit was removed during the 13th National People’s Congress in March which paved the way for President Xi Jinping to remain in office indefinitely. To many observers this will be seen as a long term negative. Imagine, for example, what a mess China would be in if the infamous Hu Jintao and Wen Jiabao were still at the helm!

In a shorter term context however, the improved 'visibility' of policy is likely to be perceived as a positive. President Xi is broadly popular, has restored the Chinese people’s faith in the Communist Party, has worked wonders to reverse the disastrous policies of his immediate predecessors and has done much to eliminate corruption.

We can look forward to the continued roll out of the Belt and Road Initiative with positive implications for regional growth. We can also expect further supply side reform with the consequent implied increased predictability of profitability. We can expect further deleveraging, a continued focus on suppressing the shadow banking system and increased centralisation of power.

A good example of how rapidly the current administration is 'de-risking' the financial system is given in the chart below. When President Xi came to power only 20% of bank loans were to consumers, that number is now nearly 50%. The days of cheap loans to unprofitable and overleveraged state-owned enterprises are well and truly over. Yes, there are still legacy problems within the financial system but the proactive stance of the administration, which last week took over the management of the ailing Anbang Insurance Group, remains impressive.

## Asia Import Volumes



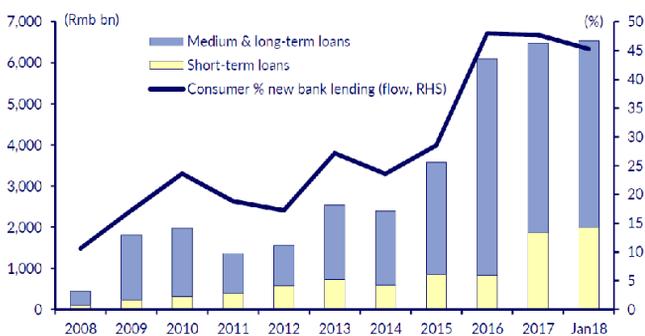
Source: Haver Analytics, Asianomics Group

## India and ASEAN - Growth Picking Up

There have been a number of encouraging data points in India of late. Electricity consumption rose by 8.3% y-o-y in January, up from 5.6% in December. Likewise oil consumption grew 10.3% y-o-y versus 7.5% in December. Auto sales remain strong; two wheeler sales rose 33% y-o-y in January while commercial vehicle sales rose 40% y-o-y. Port traffic growth accelerated to 13.6% y-o-y. Finally, corporate sales growth (ex financials and oil companies) accelerated from 6.6% in 2Q17 to 11% in 3Q17. As yet there are few signs of corporate margins improving but we expect this will occur over time.

It is not just India; the chart above from Asianomics illustrates very neatly just how strong domestic demand is across Asia. Import volumes are already some 40% higher than pre-global financial crisis levels. Clearly China is the biggest factor but we remain very encouraged by the trends in infrastructure spending across ASEAN. In Malaysia infrastructure projects include the second Mass Rapid Transit in Kuala Lumpur, the Pan Borneo Highway, the East Coast Rail Link and the Kuala Lumpur - Singapore high speed rail project. In Thailand the Eastern Economic Corridor (EEC) project is ramping up fast; last month the EEC board approved a high speed rail project connecting the three airports (Suvarnabhumi, Don Muang and U-Tapao) worth US\$6.5bn. In the Philippines meanwhile, the Government recently received a US\$6.7bn unsolicited proposal to upgrade the Ninoy Aquino International Airport from a consortium comprising seven of the country’s largest conglomerates (including portfolio holding Ayala Corporation).

## China incremental consumer lending (annualised flow)



Note: Data up to the 12 months ended January 2018

Source: CLSA, PBOC, CEIC Data

## Outlook

The somewhat hawkish opening remarks from the new Federal Reserve Chairman Jerome Powell have rattled the already shaken bond and equity markets. As always, Asia tracks the daily movements in developed markets so the short term outlook remains decidedly mixed.

The difference is that Asian equities are not overvalued and that the region retains excellent economic and earnings momentum. We remain optimistic.