

# ASIA INSIGHT

6th June 2018

## Review

The MSCI AC Asia ex Japan Index slipped 1.3% in May while the MSCI AC World Index gained 0.1%. China (+1.8%) and Taiwan (-0.2%) outperformed while Malaysia (-8.1%) and Thailand (-4.9%) underperformed. By sector, Energy (+0.6%) continued its good run and Consumer Staples (+0.4%) also held up well while Telecoms (-5.6%) and Industrials (-3.6%) lagged.

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

## The Come-Back King

While there was little doubt that Prime Minister Najib was unpopular following the 1MDB debacle, the victory by 92 year old Tun Dr. Mahathir Bin Mohamad's Pakatan Harapan (PH or the "Alliance of Hope") coalition in the recent Malaysian election was unexpected to say the least. PH and its allies captured 122 (50.9%) seats in the general election last month compared to the 79 won by Barisan Nasional who had held power continuously since independence (August 1957). Mahathir, a controversial figure, needs no introduction having been Prime Minister from 1981 to 2003 winning five consecutive general elections. He turns 93 next month!

Mahathir campaigned on a populist platform - abolish the recently introduced Goods and Services Tax, reintroduce selective fuel subsidies, increase and standardise the minimum wage and provide healthcare access for low income groups. A Royal Commission is to be established to investigate 1MDB (Mr Najib's passport has been revoked) and all large infrastructure projects are to be reviewed. Two substantial rail projects have already been cancelled.

Markets don't like uncertainty and, as noted earlier, the Malaysian market fell sharply after the election result. Construction stocks were particularly hard hit including portfolio holding IJM Corp which subsequently reported rather light results for the 4Q of their financial year (to March) in late May. IJM is a diversified concern with interests in property, plantations and infrastructure but the market chose to focus on the construction and related industrial businesses (combined they account for roughly half revenues and pre-tax profits). Rising commodity prices impacted margins in the industrial division but the huge construction order book (which amounts to circa four years revenues and is reassuringly diversified) and stronger property presales suggest better times lie ahead. The Company certainly thinks so - it has been purchasing its own shares repeatedly of late.

The bigger question for the country is when and if Mahathir, who has quickly followed through with his campaign promise to pardon Anwar Ibrahim (his former deputy in the 1990s), will step aside. Anwar is highly respected by the international community and his elevation to high public office would be very positively received. Anwar's wife, Wan Azizah Wan Ismail, has been appointed Deputy Prime Minister and is the first female to hold this position.

## China – Oozing Confidence

While the chat in markets continues to revolve around the threat of trade wars, rate rises and the like, a rather different perspective was observed while attending an investor conference in the beautiful city of Hangzhou last month.

Held by CITIC securities and their subsidiary CLSA the opening address was attended by circa 2,000 investors, the vast majority locals. The word is confidence. Not over-confidence in equity markets (although there was a bit of that) but confidence in the destiny of China and the wealth of opportunities out there for China's burgeoning ranks of entrepreneurs. Everyone is looking inward not outward as China's growth path is increasingly dominated by the rapid growth in domestic consumption. The speed with which workers previously employed in 'old' industries such as steel and coal have found employment in the service sector is breath-taking. Meituan - an online food review and delivery company backed by Tencent - employs 1.7mn scooter drivers and estimates that almost one third were previously employed in industries impacted by supply side reform. 80% work in tier 1 cities, over 70% are migrants.

### China's labour demand to supply ratio in 100+ cities

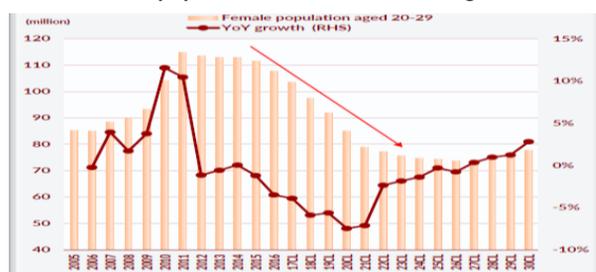


Source: Ministry of Human Resources and Social Security

China's deteriorating demographic profile and the rapid growth in the service sector is leading to an ever tighter labour market (see chart above) especially for skilled workers. Perhaps reacting to this fact, the reform of the Hukou system appears to be accelerating rapidly with 28 of the 32 tier 2 cities loosening Hukou policies over the past year. Unsurprisingly the authorities in each city are targeting younger, educated and skilled migrants. The outlook for factory automation remains excellent.

Talking of demographics, China is expected to repeal all restrictions on child birth shortly. The chart below depicts the size of the female population between 20-29. It has fallen 10% over the last five years and will fall a further 30% over the next five years. Scary.

### Female population at ideal childbirth age



Source: NBS, CRR

## Outlook

Bank Indonesia raised rates twice last month, Bankgo Sentral (Philippines) raised rates once. Both are likely to raise rates further. Additional rate raises by the Federal Reserve may keep investors nervous of the perceived weaker ASEAN economies.