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Asian Equities Are Attractively Valued, End Of Fed Certainty Could Help In 2016 - REYL

Tom Burroughes, Group Editor , 18 December 2015

Asian equities, which have been through a torrid year, could be set up for gains in 2016, argues the Swiss private banking house.

Next year could see Asian companies' returns on equity start to rise again, paving the way for a re-rating for Asian stocks and if history repeats itself, this week's rate rise by the US central bank could actually lead to a market rally, REYL, the Swiss bank, says.

In previous episodes when markets have awaited a rate rise by the Federal Reserve, stocks have tended to drop ahead of such a move but then bounced once the first rate hike of a cycle was out of a way.

"If history repeats itself, a Fed rate hike in December will help set up Asian equities for a good 2016," Daryl Liew, head of portfolio management, REYL Singapore, said in a note. His comment came a day after the Fed raised rates by 25 basis points – a widely expected move by the central bank to move from a zero-rate policy that was in place for nearly seven years. Yesterday, US stock indices such as the S&P 500 slipped from the open, while European and Asian bourses mostly rallied.

"Asian equity markets have had a rollercoaster year. A strong start saw the MSCI ex-Japan index peak in April before suffering a steep correction till September, before staging a bounce in October. Still, as at end-November the index is still down -12 per cent and likely to post another year of negative returns. Valuations however remain quite compelling. The graph below shows that the trailing price-to-book ratio for the MSCI Asia ex-Japan index is close to the levels last seen after the bursting of the tech bubble in 2001 and not far from the trough levels during the Asian and the Great Financial Crisis," Liew said.

"Interestingly, the close correlation between earnings and the price-to-book ratio has broken down since the GFC. This is due to steadily falling ROEs [returns on equity] for Asian companies since 2010, a likely result of widespread de-leveraging of corporate balance sheets and pressure on net margins as earnings expectations have been consistently lowered," he said.