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MARKET INSIGHT

MAY 2016

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Market analysis

View from Asia

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Asia Heating Up

An intense heat wave is currently sweeping through South East Asia with the highest ever temperatures being observed in several countries. Mercury levels have crossed the 40°C (104oF) mark in parts of Thailand and Vietnam, while authorities in Malaysia closed schools to protect students from the sweltering heat. The record high temperatures and accompanying dry weather is an effect of the strong « El Niño » this year and the advance of climate change.

As temperatures rise in South East Asia, the region's stock markets have also similarly been on fire, and have been the stellar outperformers so far this year. The Indonesian, Thai and Malaysian bourses have delivered double-digits gains year-to-date in USD terms, an impressive feat considering the steep plunge in global markets in the first few weeks of the year. Indeed, Asian and Emerging Markets have enjoyed a strong rebound since the bottom in January as they have been unshackled by the easing of two major macro concerns.

Repricing of Fed Rate Hikes

The first major development has been the repricing of expectations of US Fed rate hikes. From pricing in four rate hikes in December last year, the market is now expecting just 1 rate hike for 2016. This moderation in Fed rate expectations has had a significant impact on the USD, with the USD weakening against almost all other currencies. Asian currencies, which corrected against the greenback last year, have enjoyed a nice rally so far in 2016, with South East Asian currencies like the Malaysian Ringgit and the Indonesian Rupiah enjoying the biggest gains. The more positive outlook for local Asian currencies has caused a reversal of capital flows, as money has come back to South East Asian assets, helping to drive South East Asian markets higher.

China Economy & Currency Stabilising

The second development has been the stabilization of the Chinese economy. The Chinese government has learnt from the policy mistakes made in the beginning of the year. Market communication has improved significantly while errant policies have been rectified. China growth concerns were truly put to bed after Premier Li Keqiang publicly committed that the country will hit a minimum 6.5 % GDP growth target this year, coupled with the announcement of various pro-growth policies.

China's recently released Q1 GDP data backs up Premier Li as GDP growth came in at 6.7 %, driven by an acceleration in fixed asset investment growth (up 10.7% yoy in Q1) and real estate investment, suggesting that the stimulus policies are starting to have a positive effect. After contracting for several months, China's official manufacturing PMI has also now moved back into expansion territory, coming in at 50.2 for March, while the services PMI has stayed strong, expanding to 53.8.

In addition, concerns that the RMB will have to undergo a steep devaluation have mostly dissipated with the weakness of the USD this year. This has been supported by a significant fall in cross-border capital outflows from China and stabilization in China's foreign currency reserves.

North vs South Asia

The combination of both these improvements in the macro environment has helped spark a strong recovery in commodities and risk assets. Asia and Emerging Market assets have been the major beneficiaries, reversing the steep slide in January to chalk up gains so far this year. Within Asia, North Asian markets have generally underperformed South Asian markets. Japan, China, Hong Kong and India are still in negative territory on a year-to-date basis, while most South East Asian markets have done well.

The table and chart below shows the year-to-date performance and current valuations of various Asian markets. After the strong run this year, it is not surprising that a couple of South East Asian markets are now trading at the upper end of its historical valuation range, with Malaysia close to its 5-year high. Vietnam, by comparison, has been somewhat of a laggard amongst South East Asian countries this year and as such, continues to be attractively valued – it is currently trading at close to the lowest current price-to-earnings (PE) multiple among

the major South East Asian countries at 13.8x, but has the highest expected earnings growth at 17.5 %.
Part of the reason for Vietnam's underperformance this year can probably be put down to geopolitics. Vietnam held its 12th National Congress in January where there was a change in three of the four top leadership positions. Despite the leadership change however, no drastic changes are expected on the policy front, with the new leaders likely to maintain the status quo. In addition, Vietnam has a lot riding on the Trans Pacific Partnership Agreement (TPP) being ratified, and there are question marks over whether the US will be able to ratify the agreement with both leading US Presidential candidates Hillary Clinton and Donald Trump reportedly opposing the TPP in its current format. The uncertainty over the adoption of TPP does not appear to have stopped foreign companies from expanding their operations in the country. Registered foreign direct investment into Vietnam in 1Q16 more than doubled from the same period the previous year, driven by the construction of processing and manufacturing facilities. As such, we continue to be positive on Vietnam.

Japan Looking Interesting

As one of the worst performers in 2016, Japan is now starting to look interesting. The Japanese stock market has been dragged down by scepticism over the effectiveness of central bank policies and disappointment over the impact of Abenomics on the real economy. After the selloff, the Topix is now trading at close to 5-year lows, at just 13.3x current PE. Meanwhile, there are noticeable improvements being made in corporate Japan, with companies now increasingly focused on boosting shareholder returns and improving corporate governance. Certain industries and sectors in Japan also continue to see strong growth – like tourism and real estate. We think there are some interesting buying opportunities in the land of the rising sun.

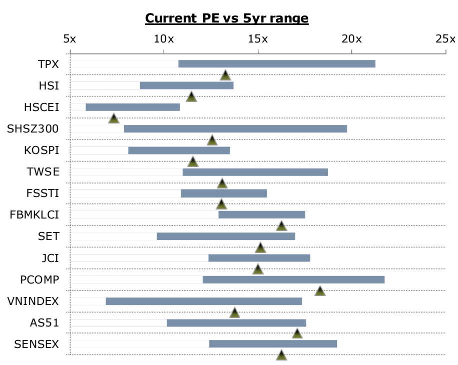
Asia & EM Still Under-Owned

Even though Asian and EM equities have rallied 18 % and 23 % respectively from the bottom in January, there still could be room for further upside. International investors still appear to be heavily underweight Asia and EM in their portfolios, even though US$37bn in foreign funds flowed into EM debt and equities in March alone. As such, the positive momentum for these assets still could drive prices higher. In addition, the favourable macro environment with the weak USD and benign inflation has given Asian countries the leeway to pursue easy monetary and fiscal policies if the need arises.
The onset of the mid-year monsoon season will bring some much needed relief to South East Asia in the coming months, cooling temperatures and rejuvenating the parched land. Let's hope that the fires fuelling the region's stock markets are not doused by the rains and will continue smouldering.

Asian Markets Performance & Valuation

27-Apr-16

Indices	YTD Return % CCY	YTD Return % USD	Current PE (x)	Forward PE (x)	Est YoY EPS Gr. %	PE history 5yr Low	PE history 5yr High
TPX	-10.3	-2.7	13.3	12.4	7.7	10.8	21.3
HSI	-2.3	-2.4	11.5	10.4	10.4	8.7	13.7
HSCEI	-6.7	-6.7	7.3	6.7	9.0	5.9	10.9
SHSZ300	-14.8	-14.8	12.6	11.2	12.5	7.9	19.8
KOSPI	2.8	5.9	11.5	10.5	9.7	8.1	13.5
TWSE	2.9	4.9	13.1	12.2	7.3	11.0	18.7
FSSTI	0.4	5.1	13.1	12.4	5.5	10.9	15.5
FBMKLCI	0.0	9.9	16.3	15.1	8.0	12.9	17.5
SET	10.2	13.0	15.2	13.4	13.5	9.6	17.0
JCI	4.8	10.3	15.0	13.0	15.5	12.4	17.8
PCOMP	3.7	4.0	18.3	16.5	10.5	12.1	21.7
VNINDEX	3.4	4.2	13.8	11.7	17.5	6.9	17.3
AS51	-1.0	5.3	17.1	15.6	9.5	10.1	17.6
SENSEX	-0.4	-0.8	16.3	13.6	19.8	12.4	19.2



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