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Daryl Liew on Asia Pacific ex Japan

(IA) Asia Pacific excluding Japan: Over three years

	3yr % chg	Rank	Vol monthly	Fund size (£m)	Morningstar rating™
Top 5					
Veritas Asian	78.51	1	3.98	787.09	★★★★★
Smith & Williamson Oriental Growth	77.67	2	4.45	14.08	★★★★★
JPM Asia Growth	75.85	3	4.35	228.51	★★★★
Hermes Asia Ex Japan Equity	75.18	4	4.64	2,880.67	★★★★★
IP Asian	74.66	5	4.67	1,658.22	★★★★★
Bottom 5					
Emerise Pacific Rim Equity	29.23	84	3.90	141.49	★
CF Canlife Asia Pacific	29.15	85	4.20	127.72	★★★
Templeton Asian Growth	28.74	86	4.64	3,709.83	★★
Matthews Asia Funds Asia Small Co	28.14	87	3.99	67.40	★★★
Aberdeen Global Asian Smllr Coms	19.77	88	3.71	1,454.93	★★★★
SECTOR AVERAGE	49.61		4.26	610.76	

Performances calculated bid to bid, net income re-invested, GBP to 03/12/17. Source: © 2017 Morningstar.

Asia continues to benefit from the synchronised growth in the global economy, on the back of easy monetary policies and benign inflationary conditions. Geopolitical threats in the region have also dampened down in recent months.

Against this favourable backdrop, Asian companies are generating strong earnings growth, which has in turn driven regional equity markets 30% higher this year. The North Asian markets of China, Korea and Taiwan have enjoyed the bulk of the earnings upgrades due to their greater exposure to global supply chains, and this could be poised to continue into 2018.

What then could derail the surging Asian locomotive? One risk could be the price of oil. The recent rumblings in the Middle East could potentially cause a spike in oil prices which could then lead to tighter monetary conditions and adversely impact global trade.

A second threat is China's renewed commitment to deleveraging following the 19th Communist Party Congress. If this process is not managed carefully, it could trigger a regional or even global market correction like the ones experienced in the summer of 2015 and January 2016.

These risks are a concern as several Asian markets – India and most of South East Asia – are trading at the upper end of their respective five-year valuation ranges, putting them at risk of correcting should earnings growth fail to materialise.

Bull Points

Synchronised global growth

Strong corporate earnings

Bear Points

Spike in commodity prices

China deleveraging too quickly

While these risks are not in our base case scenarios, we have a preference for the North Asian markets where valuations are not as stretched. China H-Shares and Korea are still among the cheapest markets in Asia, trading at forward price-to-earnings ratios of 8.0 and 9.5 respectively.

We see opportunities for better equity market returns in North Asia in 2018 driven by a combination of both earnings growth and multiple expansion.

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