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FOR PROFESSIONAL INVESTORS ONLY

A View From Asia

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Taking stock

A sense of calm prevails over markets. There is a general view that trade tensions between the US and China are unlikely to result in the apocalyptic rupture that seemed possible just a few months ago. Perhaps the reality is that risk perceptions changed and stocks rallied after the Federal Reserve did an about turn on raising rates. Who is afraid of a dovish Fed?

Amongst businesses in China, there is a unanimous agreement that despite a deal, risk profiles and rules of businesses have altered. Almost every management team we speak with has confirmed they either have started to, or are in the process of, planning a move away from China for their manufacturing plants. In industries that are sensitive to national interests (increasingly revolving around hi-tech and data), rules will be made up as we go along. In the interim, the Chinese government has tried to soften the slowdown in the Chinese economy by adopting looser monetary policy, reducing VAT and cutting individual income taxes. Despite an uncertain outlook, there are pockets of growth, as attested to by very good results by two of our holdings: Li Ning (18.4% sales growth with 38.8% profit growth) and Foshan Haitian (16.8% sales growth and 23.6% profit growth). Both stocks have seen decent appreciation year to date but long-term trends are positive and give confidence to remain invested.

Elsewhere in the region, Indonesia and India go to the polls this month. Mr Widodo in Indonesia (elections in April) and Mr Modi in India (elections in April/May) are both hoping for a strong result to retain their respective grips on power. Opinion polls and chatter in both countries reflect some jitters for the incumbents. If they do lose, or do not attain a majority, markets will not take the results well. In my view, even in that case, the situation is unlikely to be like Malaysia where we have witnessed a reversal of several policies of the previous government. In Malaysia's case after the alleged corruption and mismanagement, the new government had little choice but to scupper several policies and projects.

In both Indonesia and India, there seems to be unanimity on spending more on infrastructure and creating employment opportunities. The pace of execution of these policies will be in focus after the elections. The good news is that both countries raised their interest rates last year to defend their currencies in face of a strong US dollar. That has driven real interest rates to 3.5 - 4%, leaving ample room for cuts (in India, we have already seen the first of a series of cuts) if the Federal Reserve remains dovish. High real interest rates in both countries are proving a challenge to those businesses and consumers that rely on credit to stimulate demand. These potential cuts in rates might help soften the uncertainty that could arise in case of election results that markets do not anticipate. Indonesia and India do represent a large part of the portfolio. I am cognisant of the risk around elections, but also recognise that event risks are difficult to predict. The companies I own suggest resilience through tough economic conditions and that is what I remain focused on.

Populist policies prevail

Speaking of elections and outcomes, one large common trend is unfolding in several Asian countries. Implementation of populist measures, especially transfers to the lower strata of society and the farming community. Big issues such as universal basic income, cheap or free healthcare and education have been in the limelight across the world post the 2008 financial crisis. Yet Asia will most probably implement some of these measures faster than the developed world. Apart from the far-reaching impact on the social, economic and political fabric in those countries, this extreme populism will become a template as leaders notice how easy it is not just to promise but also to deliver in a digitally connected era.

Take the example of election results in Thailand, which indicate a fractured mandate and some kind of coalition government. I'm not sure if it's entirely relevant who forms the government (after all, we had a military-led government after the coup and the economy did chug along!). It may be more relevant to look at the ideas floated by some of the parties. The top three parties are pledging subsidies to farmers, one suggests a national minimum income, four out of five propose a wage hike for unskilled workers by 20-48%, two favour minimum salary for college graduates, others a cut to personal income tax by 10%, another a cut in VAT by 2%. In addition, there are debt moratoriums and a variety of income transfers.

In India, we have seen debt waivers for farmers, extremely subsidised healthcare coverage, interest rate subvention for housing loans, an unconditional transfer of Rs.6,000 (US\$85) per year to marginal farmers, and a promise by the opposition of a universal basic income for the poorest in society. Indonesia is no different while Singapore too has quietly been increasing the social transfers to those who represent the lowest 20-30% of society. It seems to me that government debt and rising deficits are not a concern (after all, don't richer countries get away with ever-rising national debt?).

Nevertheless, Asia remains hostage to the liquidity constraints of a US-centric monetary system. If you think the Fed is done raising rates, the populist measures implemented will not have dire consequences in the medium term. However, this trend towards populism will be a double-edged sword. Rising wages increase costs for businesses; perhaps higher taxes for the rich; higher disposable income relative to status quo. If the global economy is likely to be tepid, domestic demand stimulated through higher government spends and deficits could be a cushion for Asia.



JOHCM Asia Ex Japan Fund

5 year discrete performance (%)

Discrete 12-month performance to:

	31.03.2019	31.03.2018	31.03.2017	31.03.2016	31.03.2015
A USD Class	-10.77	11.86	16.94	-11.20	11.48
Benchmark	-5.17	25.41	17.40	-11.78	10.79
Relative return	-5.91	-10.80	-0.39	0.65	0.62

Past performance is no guarantee of future performance.

Source: JOHCM/MSCI Barra/Bloomberg, NAV of Share Class A in USD, net income reinvested, net of fees as at 31 March 2019. The A USD Class was launched on 30 September 2011. Benchmark: MSCI AC Asia ex Japan NR (12pm adjusted). Performance of other share classes may vary and is available on request.

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