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FOR PROFESSIONAL INVESTORS ONLY

# A View From Asia

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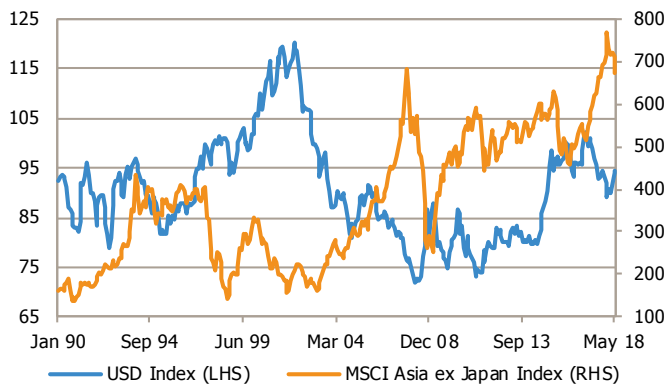
## Repair and recover

Emerging markets, including within Asia, have recently seen a torrent of selling. Several factors may have contributed to this negative turn of events: trade tensions; creeping protectionism; and political change in several countries, to name just a few. Yet a change in liquidity is, in my view, probably the main variable behind the weakness of emerging and developed Asian stock markets, and broader EM, in the first half of the year.

### A lurch in liquidity

The trade-weighted US dollar index, as the simplest proxy for liquidity in all risk assets, provides a snapshot of changing conditions in financial markets. Whether in times of risk aversion or in periods of rising US interest rates, a strengthening dollar funnels liquidity away from non-US countries and assets. Apart from expectations of interest rate increases, a planned reduction in the size of central bank balance sheets (quantitative tightening) has also played a big role in contracting liquidity.

### The dollar remains the reserve currency

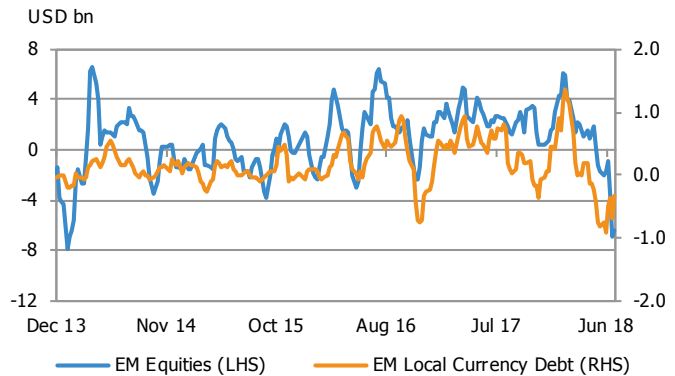


Source: Deutsche Bank.

Unlike in previous occasions of dollar strength, this time around the oil price has climbed quite sharply. Besides tighter liquidity and rising rates, higher oil prices are acting as another drag on economic conditions across Asia. Most countries are dealing with a hike in petrol and diesel prices, leading to lower disposable incomes. Current account positions have come under stress in some countries, as the region is a net importer of oil and refined products. These conditions are applicable to emerging markets in general, hence the reaction in terms of fund flows has been vicious. There is no better way to see this than to look at ETF flows in both emerging equities and debt markets.

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## EM investors abandon ship – major outflows in ETFs



Source: Bloomberg.

The good thing about economic and liquidity cycles is that they repeat themselves. The painful part, though, is the downturn, which can hit very hard and very fast when it happens.

### Remedial action

This year has been an annus horribilis for me. A few stocks have severely disappointed and hurt the Fund's performance. I have reflected and, I hope, now rectified my mistakes by repositioning the portfolio. In the face of what appear to be challenging conditions for Asian economies, the stocks that I have bought lately broadly share the same characteristics: a strong balance sheet; high cash flow-generating abilities; a domestic business orientation; and, finally yet importantly, signs of a turnaround from the effects of idiosyncratic slowdowns that each of them has had to deal with.

