June 2019
FOR PROFESSIONAL INVESTORS ONLY

J O Hambro Capital Management Group

A View From Asia

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Convulsion: a sudden, violent, irregular movement of the body, caused by involuntary contraction of muscles and associated especially with brain disorders such as epilepsy; a violent social or political upheaval

Our long-planned 'company visit' trip to China could not have been better timed. A breakdown of negotiations between the US and China prompted President Trump to impose higher tariffs on a wider range of product imports from China. Combined with the imposition of sanctions on Chinese telecom and technology giant Huawei, this has convinced almost all seasoned observers of geopolitics that the 'genie is out of the bottle'. The posturing and counter-moves by the two global economic giants is just the start of what could be a long lasting 'economic war' for ideological dominance in the decades to come. It is beyond my remit to posit on this development, yet suffice to say all countries will need to rethink and adjust as we undergo a massive change to the current global political and economic order.

Most of the companies we met were cautious to downbeat. To generalise, as industrial profit growth in China slows sharply and export orders come under a cloud, almost every firm is understandably affected. There was a common thread running through most companies' future expectations – government policies will save the day. I met a few companies that rank very high on the quality and growth score (in the healthcare and consumer space) but valuations reflect a lot of positivity. Those are on my radar to buy in case markets face further challenges but overall the mood in China was combative and downbeat.

Our working assumptions are that growth rates (in China and globally) will moderate while volatility of growth will increase. Not just in China but governments and central banks across the world will increasingly try to cushion negative outcomes in almost every country. Hence, risk of policy mistakes –knowable only in hindsight – will exacerbate asset price moves. Corporate capital expenditure and consumer spending might have a high degree of caution as confidence and clarity is diminished.

In other news, election results in Indonesia and India have given an increased mandate to incumbents. Both leaders face similar challenges: revitalising growth, job creation, growing income levels and infrastructure investment are the priorities. These challenges have no immediate solutions. In a challenged external environment bordering on protectionism, government subsidies will play an increasing role to help the lower strata of society. The constraint will be the fiscal deficit of both countries, but, from what I have read, the initial thrust of both governments will be on devising strategies towards this end.

As an example of what Indonesia has done in the past few years, look at the table below.

Indonesia: purse wide open

Programme	Recipients (m)	Budget realization (Rp tn)				
		2015	2016	2017	2018	2019T
Smart Card	20.0	7.1	10.3	10.3	10.5	10.8
Direct Cash transfers	10.0	5.6	10.0	11.3	17.3	34.0
Health Security	216.2	20.3	25.5	25.5	25.5	26.7
Food subsidy	15.4	21.8	22.1	19.8	20.8	20.8
Subsidized micro loan	4.0	1.9	5.1	13.0	18.0	16.7
Village fund	-	20.8	46.7	59.8	59.8	73.0
Subsidized mortgage	-	5.1	12.6	14.1	9.6	11.4
Total (Rp tn)		82.6	132.3	153.8	161.5	193.4

Source: CLSA Securities.

Despite these efforts, growth has been difficult to come by. In Indonesia's case in particular, there is an urgent need to address relatively inflexible labour laws. This has been the most cited reason for the lack of significant relocation of manufacturing at a time when firms are looking for alternatives to China.

From a portfolio standpoint, there is a fair bit of defensiveness through most of our holdings. I have tried to focus on companies that have managed the disruptive forces of online commerce and stand a better chance of success. With uncertainty emanating from restrictive trade policies, vigilance of second order effects (like moderation of consumer demand) will be one of the main variables to monitor. There is genuine concern over the economy in China, yet even in these times there are pockets of growth. As I mentioned, I am keen to add to a couple of names in the 'A' share market if there is a further sell-off.

JOHCM Asia Ex Japan Fund

5 year discrete performance (%)

Discrete 12 month performance (%):

	31.05.19	31.05.18	31.05.17	31.05.16	31.05.15
A USD Class	-10.51	0.46	22.47	-11.61	11.34
Benchmark	-11.00	17.09	28.13	-17.34	10.26
Relative return	0.55	-14.21	-4.41	6.92	0.98

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 May 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.