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News

The View from Asia

Higher US interest rates could present significant upside for Asian equities

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18 Sep 2022

Among the concerns occupying markets in August were the hawkish Jackson Hole central bank conference, energy prices in Europe and tension around the Taiwan Straits. In Asia, the Indian economy remains an outlier where robust tax collections suggest a strong economic rebound from their COVID slump. The rest of the region remains in varying levels of slowdown. China's persistence with its zero-COVID policy is baffling to us from a socio-economic lens. Yet looked at from the lens power politics and the mid-October National Congress meeting it seems logical.

Until mid-2021, stocks that fit the ESG theme were propelled higher irrespective of their valuations or whether they genuinely possessed ESG characteristics. Conversely, energy and other 'anti-ESG' stocks fell as investors shunned them. Valuations for anti-ESG stocks became cheap; disdain and pessimism prevailed. Triggers for upside were unknown and timing uncertain.

Does this in any way chime with the situation for China? In our view, China is the new anti-ESG portfolio. We have some hunches for where things could go: the leadership may pivot to the economy after the National Congress is out of the way, adding to stimulus and further easing; bad news no longer impacting Chinese stocks that badly. But outcomes are uncertain. The current risk-reward scenario seems fair and hence my optimism. The macro risks are evident; if we believe the Fed officials, rates might stay higher for longer. That drives the US dollar higher, leading to capital outflows. Yet our view is that asset allocators should start layering into Asian equities. This extended period of pessimism could change and if that happens, marginal capital flows could mean significant upside for Asian equities.

Samir Mehta manages the JOHCM Asia ex-Japan Fund. Find out more here.

Sources for all data: JOHCM/MSCI Barra/Bloomberg (unless otherwise stated)

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