

Go east: Asian equity markets remain attractive

By Simon Flood

Contrary to the downbeat market expectations of late 2011, the global macro environment for the first quarter of 2012 turned out to be much more encouraging. Systemic risks in Europe declined following the European Central Bank's ("ECB") massive liquidity injections and markets remained resilient in the face of the largest sovereign default in history. US economic data has continued to reflect a cyclical upturn, with meaningful improvements across manufacturing, credit growth and employment.

Against this backdrop, global risk assets rallied strongly. Asian markets lifted themselves from the doldrums of 2011, with the MSCI Asia Pacific Index showing strong double-digit returns for the first quarter of 2012. The natural question for global investors, therefore, is whether they should remain in Asian equities or for those who are not yet invested, if they should consider doing so.

Asian market watch

From our vantage point in Singapore, Lion Global Investors ("LGI") sees a number of opportunities in Asia. For the long-term investor, in particular, the investment case for the region remains strong, supported by Asia's good fundamentals and (in stark contrast to Europe) the solid balance sheets of both the public and private sectors. At the same time, further Asian consumption growth is on a structural uptrend, supported by increasing urbanisation and strong income growth. In the near term, Asian economies and markets should also enjoy some uplift from a firmer recovery in consumption demand from the US.

Within Asian equity markets, China has one of the most attractive valuations and could do well in 2012 once the current uncertainty with respect to growth and the transition of power to a new leadership team is concluded. While China's economic momentum is moderating, LGI's central scenario remains that of a soft landing for China's economy. Inflation has eased significantly from the peaks of 2011 and we expect domestic demand to gradually improve as earlier selective easing measures start to work their way through the system. China's export and manufacturing sectors should also experience a tailwind from the improved economic conditions in the US.

We are also confident in the outlook for our home base, Singapore, which hosts some of this region's most attractive companies. Recent economic data has been better than expected; we could also see a potential upgrade to Singapore's GDP forecast and corporate earnings on the back of the improving global economy.

Global risks

While the situation has stabilised in Asia, we remain watchful of potential risks. Tensions over Iran are already causing oil prices to rise and this could short-circuit the cyclical recovery if sustained. Actual military hostilities also cannot be ruled out. In Europe, the ECB has bought time for the European financial system, but the medium-term debt sustainability of Greece and Portugal is uncertain, as is the political will for reform in countries experiencing painful recession. The leadership transition in China and the US presidential election may also result in an impasse over economic policy.

What this means is that some of the macro-driven volatility we had seen in 2011 may resurface in the later part of 2012. For the long-term investor, such volatility can present opportunities to pick-up equities and bonds of companies that have good growth potential. Our strategy is to remain invested in risk assets, until we see signs of the macroeconomic cycle turning due to inflationary pressures and/or policy tightening. In terms of sectors, we favour Asian consumption plays, global cyclicals and high dividend stocks, as well as corporate bonds of Asian companies with sound fundamentals.

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Asian Equity Portfolio Weightings

- China: Overweight
- Hong Kong: Neutral
- India: Neutral
- Indonesia: Neutral
- Japan: Neutral
- Malaysia: Underweight
- Philippines: Underweight
- Singapore: Neutral
- South Korea: Overweight
- Taiwan: Underweight
- Thailand: Overweight
- Vietnam: N/A
- Australia: Underweight
- New Zealand: N/A

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