



## Asia Today, and the Long Term

Perhaps this quote within the dialogue tells all: *“In contrast to the backlash against capitalism in the U.S. and Europe, there is a move in Asia and the emerging markets, towards much better corporate governance and a healthy and positive attitude to capitalism and entrepreneurship among the millennial generation, which dominates these countries.”*

Enjoy the read. Comments or questions always welcome.

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## Investment Outlook

### Asia Today, and the Long Term

As we get into the summer months, there are some headwinds, in the short-term, to our positive view of Asian markets. Most notably, the oil price has risen to US\$75 a barrel which will weigh on the current account and trade balances of China, India, Japan, and the major Asian economies. Also, we do not yet have a definitive trade agreement between the US and China, and the uncertainty has been exacerbated by the US pressure to remove waivers from the Iran oil sanctions (both China and India import a lot of oil from Iran). World trade growth has slowed over the last 12 months from 4.5% to 3%, and this is particularly affecting exporters in Europe.

Nevertheless, the first quarter has seen stronger-than-expected earnings, and economic growth in the Asia Pacific region has held up well. China is still the key driver of the global cycle. Although the Chinese economy accounts for around 19% of world output, the contribution of Chinese economic growth is now approximately 30%, according to the IMF. Last year, moves by the Chinese government to deleverage slowed down growth, but since January, we have seen a move to introduce new stimulus through tax cuts as well as infrastructure spending. This makes us a good deal more confident about the outlook for China and the region, and the 32% jump in the Chinese index in the first 4 months indicates a return of domestic investor confidence. In our view, this is the beginning of a longer-term recovery and opening up of the Chinese A Share market, which will see a rise of China's market capitalization from 50% of GDP to something more like the 150% we see in the USA and Europe.

As we have observed before, there are parallels with Japan in the late 1980s after the Plaza Accord with the US, which led to strong capital inflows with a strong yen and high savings rate. In this regard, we have analyzed carefully the debt position in China, and we remain



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confident that, although corporate debt has risen and recently US dollar denominated borrowing has grown, the high savings rate (over 50% of GDP) and foreign exchange reserves of US\$3 trillion are more than sufficient to offset these concerns. Having recently started reading The Hundred Year Marathon, about China's strategy to replace the US as the global super power, I remain convinced that it will be very difficult to keep China down, particularly with regard to technology, where they are still moving ahead rapidly with artificial intelligence, robotics, 5G, telecom and, perhaps most interestingly, biotechnology and other innovations in the medical sphere. We expect that, with the concerted commitment of the Xi Jinping national team, growth will be maintained at 6%, and we would not be concerned if it fell to 5%.

Meanwhile, India is holding the world's largest democratic election, with 900 million voters over a 6-week period. There is some nervousness about whether Mr. Modi and his BJP party can maintain an absolute majority. Our expectation is that his economic reform program will be maintained even if he returns to power with the support of a coalition. Democratic systems are much harder to handicap for investors because of unexpected outcomes like Brexit, Mr. Trump's 2016 surprise election, or even recently, the Ukraine electing a comedian as their president.

India moves slowly, but steadily, towards greater prosperity and the inclusion of hundreds of millions of their citizens in the new digital economy. The expectation is that middle class consumption will rise from US\$1.3 trillion today to about US\$3 trillion within the next decade. This is the investment opportunity in India - in the field of consumer brands, travel and tourism, housing and savings products. India now has a US\$2 trillion market cap, and the domestic fund management industry, focused on Bombay, is growing at a rapid pace. India's economy is growing at nearly 8%, and it would not surprise us if wealth creation in India surpasses that of China over the next 50 years, given that it is a much freer system.

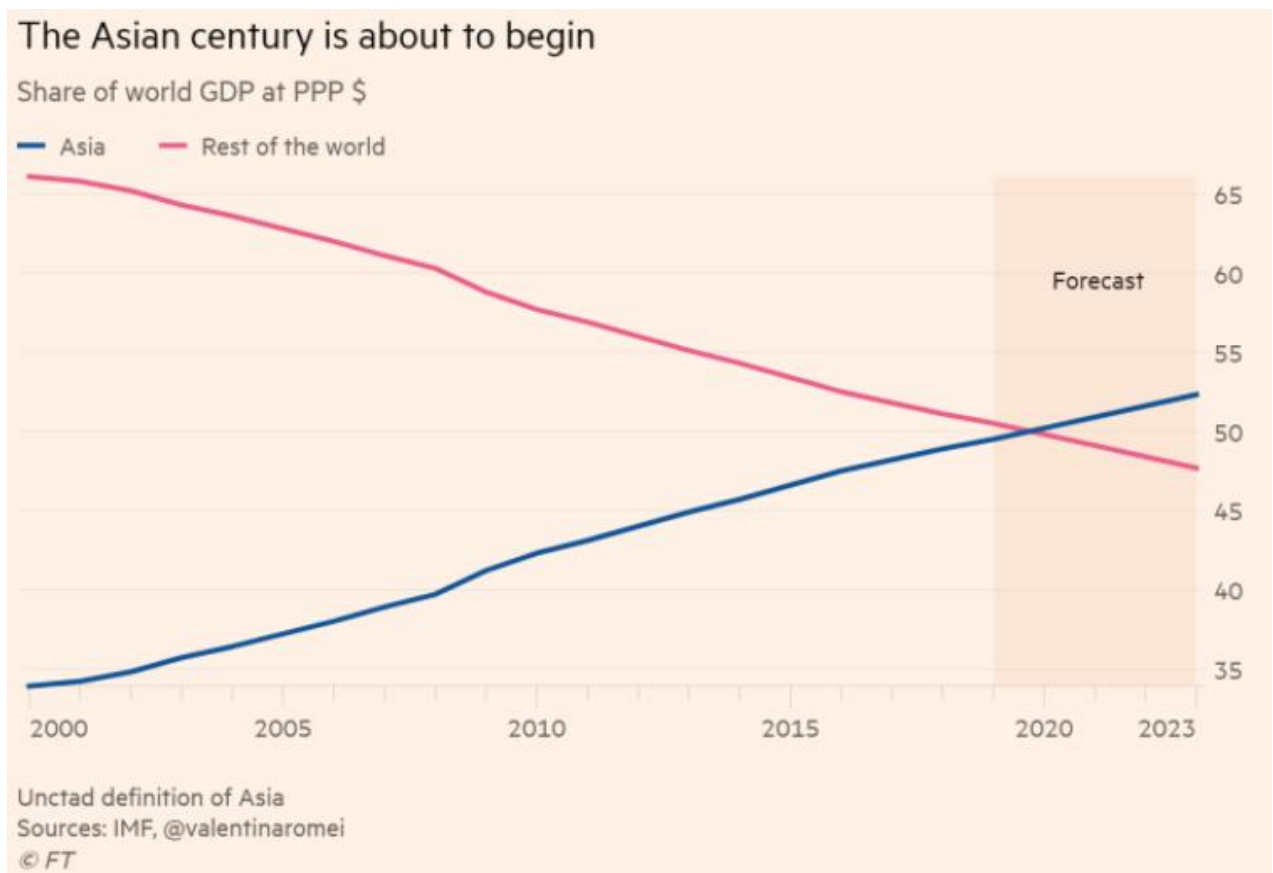
Meanwhile in Indonesia, we have had a decisive win by President Joko Widodo with over 65% of the votes, in another large democracy of 260 million. This will also remove uncertainty and bring more foreign direct investment to Java and the Indonesian islands. We see both the banking industry and the consumer sector as being the key drivers of growth in Indonesia,



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although infrastructure will be a very important area as well. Singapore, at the center of this dynamic region, has very good prospects to attract more capital, with almost \$1 trillion of high net worth individual wealth domiciled in Singapore, over 80% from international investors, notably Indonesia, Malaysia and Brunei. We favour the banking, real estate and oil service sectors in Singapore, and we continue to screen the high-yield and REIT sectors for interesting long-term investment opportunities in Singapore dollars.

Overall, there is a great deal more stability and predictability about the long-term picture in Asia than in Europe or the USA today. We do not expect any sudden or dramatic political changes, and the region is, in our view, in a very long-term cycle of catching up to its previous position, before 1800, in the world economy.





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As I outlined in the East-West Pendulum, from AD1 to 1820, the 2 largest economies in the world were always China and India. Although, historically, this growth has been centered on China and India, there have also been very wealthy and successful kingdoms in Indochina and the East Indies, which we see as being precursors of today’s dynamic Asian economies.

Long Term Economic Growth

<b>Country</b>	<b>Population (million)</b>	<b>GDP Growth (%)</b>
China (billion)	1.4	6
India (billion)	1.3	7
Indonesia	265	5
Germany	80	1.5
France	67	1.5
United Kingdom	66	1.5
USA	327	2
Canada	37	2
Brazil	208	1

*Source: Bloomberg and World Bank*

In addition to the quantitative factors, we should highlight the fundamental and qualitative changes that are taking place in the emerging markets, especially in Asia. In contrast to the backlash against capitalism in the US and Europe, there is a move in Asia and the emerging markets, towards much better corporate governance and a healthy and positive attitude to capitalism and entrepreneurship among the millennial generation, which dominates these countries.

Chinese ‘millennials’ alone (350 million) outnumber the entire US population. The other millennial countries, with young populations, are India, Indonesia, Pakistan, Bangladesh, Philippines, and Vietnam. In these nations, there is also a rapid improvement in financial technology – for instance, China’s mobile payments market is now 50 times bigger than America’s. Alibaba and Tencent handle 20 times more payments in 1 month than PayPal or other US companies. This transformation has been led by the millennial generation.



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With 60% of the world’s population in Asia, there is no doubt that the growth of middle class spending (defined as having daily income and spending up to US\$100 per capita), in that region, is a key indicator for all multinational companies. With growth at 5% or more, China, India, and Indonesia double their per capita income every 14 years; and, within the next 30 years, this large human population in the east will quadruple its annual spending. The “late mover advantage” will mean that solar power, mobile phones, and digital on-line business will rapidly transform the economies of Asia (and, indeed, Africa). It is surprising, therefore, that the emerging markets are selling at a 25% discount to the S&P 500 with this compelling growth story, and improvement of corporate governance, and treatment of shareholders being a major positive change.

**GDP at MER rankings (at constant 2016 US\$bn)**

GDP at MER rankings	2016 rankings		2030 rankings	
	Country	GDP at MER	Country	Projected GDP at MER
1	United States	18562	China	26499
2	China	11392	United States	23475
3	Japan	4730	India	7841
4	Germany	3495	Japan	5468
5	United Kingdom	2650	Germany	4347
6	France	2488	United Kingdom	3530
7	India	2251	France	3186
8	Italy	1852	Brazil	2969
9	Brazil	1770	Indonesia	2449
10	Canada	1532	Italy	2278

Source: CLSA

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Hong Kong



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