UBAM – best selection asia

Quarterly Comment | Q2 2021

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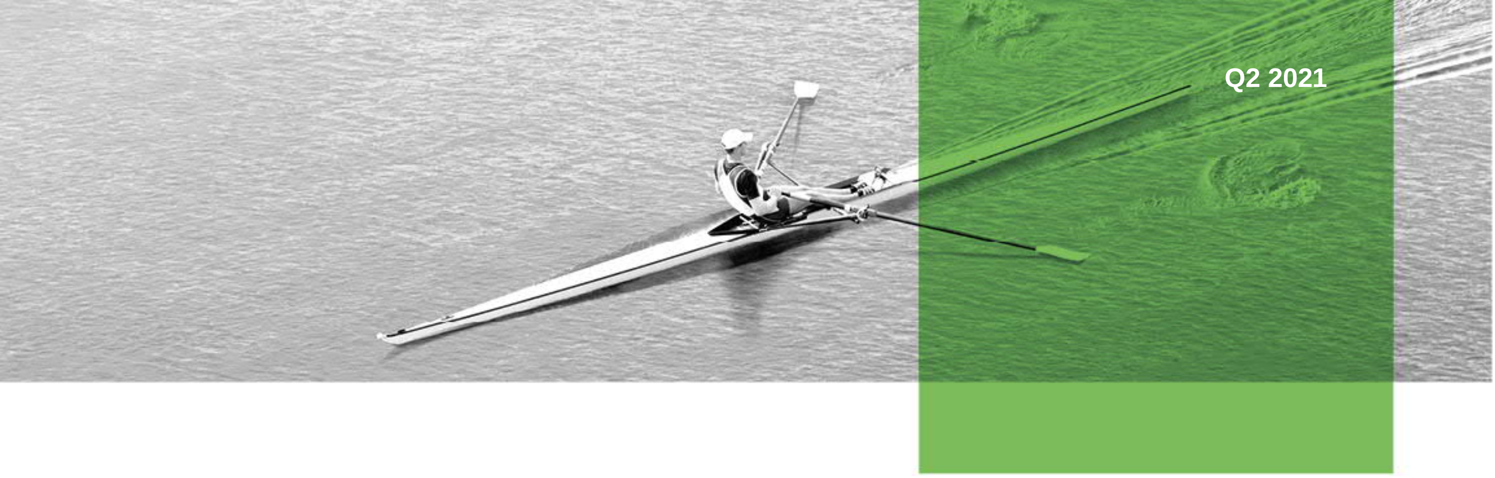
Market Comment

- During the June quarter, Asia equity market seems rather smooth or even quiet on the surface as it marked +3% gain. But it was macro heavy, news sensitive, sentiment driven, volatile market. As investors digest the US inflation will be transitory, 10-year treasury yield gradually came off, but the tapering concern didn't go away easily. Therefore, short-lived reflation trades including financials, cyclicals, and materials moved aggressively to both up and downsides. Reopening expectation and macro concerns squared each other; market was eventually flat.
- It was a consensus that Biden administration won't turn China relationship better soon and now we can comfortably confirm consensus is correct. Moreover, clamping down Chinese internet giants by government added more fuel to the fire. And PBoC's hawkish stance didn't help much on China's performance last quarter.
- ASEAN countries revealed two weaknesses; the first was poor handling of Covid-19, specifically delta variance and the second was vulnerable macro situation. Covid new cases spiked up in most of the ASEAN countries and India, and they are generally high tourism dependent economies. And tapering discussion in the US exposed the vulnerability of ASEAN currencies, money flow into the equity market was against their favor.
- We continue to like global recovery beneficiaries, Korea, Taiwan, Hong Kong and Singapore in 2H and we are cautious on China and ASEAN. During the second quarter, we have changed our stance on India to negative and back to neutral when the covid-19 cases went up. We were not worried about the muted activity since this could be a short term but we were worried about India's political environment as PM Narendra Modi's approval rate hit historical low. India managed to control the virus much sooner than expected and Modi's popularity followed as well, hence we have narrowed underweight position accordingly.

Sources: UBP, Bloomberg Finance LP.



Performance Review

- The portfolio outperformed the MSCI Asia ex Japan (NR). Both stock selection and asset allocation contributed positively to performance.
- We have been increasing underweight position in China last quarter due to government regulatory risk and hawkish policy stance. China underperformed the market and US listed companies were punished more severely. Sector or theme performance showed divergence, any company with the possibility of regulatory intervention suffered from the volatility. Wuxi Bio is considered as the safest health care company in the sector, EV supply chain CATL and BYD are one of the few policy beneficiaries. East Money is an internet based local broker and US ADR delisting became good news for them. Despite Xinjiang cotton issue, Shenzhou International was strong thanks to strong sportswear demand. Luxshare corrected before due to potential US sanction but it came back as it didn’t happen. China Gas was down due to the placement and gas incident. We’re waiting for the optimal point of the exit. Real estate (Longfor) and insurance (Ping An) sector sentiment wasn’t good due to unfavorable policies.
- Korea and Taiwan performed very nicely last quarter; all outperformed the market hand in hand. GDP growth and earnings consensus are steadily revising up for both countries. We added two new names here, Hugel and Feng Tay. Hyundai Motor performed well thanks to global exposure but IT sector was a disappointment for both countries. Samsung Electronics, SK Hynix in Korea and TSMC, Mediatek in Taiwan refused to move up although all of them reported fantastic earnings under serious chip shortage. And the reason behind negative selection effect in Taiwan is due to container bottleneck. We had one company since last year, but we sold it right before Suez canal incident.

Portfolio Activity

- We have increased US exposure by adding Techtronic, Man Wah, increased Singapore and Financials at the same time by adding DBS. CKH was for adding GARP exposure. These were funded from China especially internet giants, Alibaba and Tencent and from ASEAN in general, Siam Cement and Bank Rakyat.
- Raised cash for redemption but actively reduced overall India exposure as we turned negative on India due to significant Covid-19 surge. But UPL was increased for excessive correction.
- Added two alpha names in May. Feng Tay is a Taiwanese OEM shoemaker for Nike and other brands. Sportswear demand is strengthening as the world comes out of Covid-19 cycle. Hugel is a Korean Botox maker and at the point of purchase, it was about to launch the product in China and now it did successfully. Top notch quality but cheaper pricing for China and upcoming US, Europe launching. Increased Nari, power grid solution is a structural beneficiary of power generation mix change. For India, we started to narrow the underweight just after one month which is a quite rare case but the situation around Covid-19 changes faster than expected, therefore we have added back some of the position, HCLT and ICICIBC.

Outlook

- Strong economic data and the momentum of the recovery have been a key driver of equity markets this quarter and with no doubt shall provide continued support. This was evident in the exceptionally strong March quarter reporting period, which saw the average earnings result beat expectations by over 20%. The stellar performance of the market since the drawdown in March 2020 has seen the MSCI World Index rally 93% in USD.
- The global economy is expected to rebound sharply this year thanks notably to the large support packages that many countries have pledged. The rebound in some EM countries may, however, be slower than initially planned due to the delayed deployment of vaccines and the appearance of new Covid-19 variants.
- A strong recovery is expected in Q3, but mainly driven by the rebound in domestic demand in developed countries. With the reopening of the economy, demand surged for goods and services after a long lockdown. US consumers spent the direct support delivered by the US Administration in Q1, but they still have large excess savings. In Europe, a similar rebound is underway from Q2 onwards, as governments prevented a large rise in unemployment and protected household incomes. Confidence is increasing further. GDP is expected to accelerate from the reopening phase thanks to a surge in domestic demand. US, UK and European growth should be close to double-digits in H2-21. Consumption and investment should benefit from deployment of the recovery plans adopted in the EU and discussed in the US, but emergency help to sectors and labour will end with reopening economies.
- Central banks will show more divergent strategies; some will shift their communication in favor of a more neutral stance, preparing markets to a tapering next year. Some central banks have mentioned their willingness to taper or adjust rates in the future: Canada, New-Zealand, Korea, Sweden and the UK's BoE have moderated their bond purchases. The Fed should explicitly talk about tapering in Q3 and prepare markets to reduce its purchases in 2022. To the contrary, the ECB should continue to purchase bonds in 2022 as inflation should be back below 2%.

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