

# View from

the trading floor – Asian Dividend Income



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## Asian equity markets appear attractive

We remain positive on the outlook for Asian markets in the medium to long term, although recent events in Europe make us mindful of the short-term risks. Economies are underpinned by strong fundamentals and valuations remain attractive on an historical basis, as shown in the chart below. Investors in Asian equities, in our view, are better served by having an exposure to domestic Asia rather than to businesses exposed to the export cycle. Overall, we believe a number of defensive sectors, such as consumer staples and utilities, now look overpriced and we see a lot more value in areas such as financials, property, consumer discretionary and telecommunications.

### MSCI Asia ex-Japan 12-month forward price to earnings ratio



Source Datastream. MSCI Asia Pacific ex-Japan Index 12-month forward price to earnings ratio, monthly data from May 2002 to May 2012.

## The threat to the region: Imported risks

The risks to Asian equity markets are that we revert back to a 'risk-on', 'risk-off' environment that dominated 2011. The first quarter of 2012 was far more rational from an investor's point of view, however, the debt problems in Europe that impacted financial markets worldwide late last summer have not gone away but have simply been delayed. If the global macroeconomic and financial environment remains relatively stable then Asia should do well. If, however, the problems in Europe spiral out of control the underlying fundamentals for the Asia Pacific region, and incidentally the rest of the world, will be severely undermined.

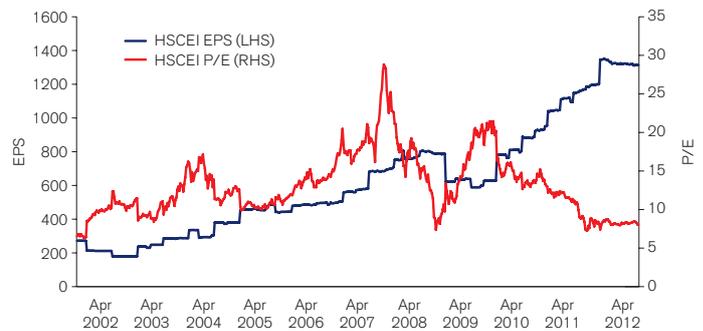
## Country allocations driven by bottom-up stock selection

### China

In our view the Chinese economy is the most able of the Asian markets to ride out any global economic volatility. A hard economic landing for the country, which we believe is highly unlikely, has already

been priced in by the market. As the chart below shows, valuations of Chinese companies over the last 10 years have never been consistently cheaper on a price to earnings (PE) basis or more attractive from an earnings per share (EPS) standpoint. It has taken the Chinese government roughly three years to cool the economy down following the effects of the four trillion yuan (\$586 billion) stimulus package implemented late in 2008. Now that consumer price inflation, currently at 3.4%, appears to be under control and gross domestic product growth sits at 8.1% (quarterly percentage change year-on-year), rather than the 11.9% expansion experienced at the turn of 2010, the onus is on the Chinese government to focus on growing the economy rather than slowing it down.

### 10-year China valuation: HSCEI EPS versus HSCEI P/E



Source Bloomberg. Hong Kong Stock Exchange Hang Seng China Enterprises Index earnings per share and price to earnings ratio, monthly data from October 2001 to April 2012.

### Thailand

Thailand remains our largest relative country position, where we have an exposure of approximately 11%. Even though Thailand has been one of the best-performing Asian markets over the last five years, we still feel it encompasses some extremely attractive valuations. Since the government coup in 2006, Thailand's economy has shown considerable resistance to anti-government campaigners. We feel that after this recent political jostling, there will be a lot of pent-up demand for consumption and infrastructure spending coming through in the next two years, which should keep earnings reasonably buoyant.

### Australia

Although Australian company valuations do not look expensive, the market as a whole remains unattractive to us. We are not keen on the current price environment for the resources sector so we do not own much in domestic-led Australian stocks or resource companies. What we do own, from allocating on a bottom-up stock-picking basis, are some very good companies, such as multinational packaging company Amcor, which operate globally but happen to be Australian.

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## Key investment themes

**Banks:** The region's banks remain well capitalised and liquid but undervalued, whilst showing the potential for increased profitability owing to the reduction in overseas competition.

**Property:** We believe the sector is set to be the beneficiary of lower interest rates, high savings ratios and affordable property prices.

**Infrastructure:** Government infrastructure spending should remain strong across the region to offset the slowdown in exports.

**Telecommunications:** This sector continues to offer investors exposure to companies with non-cyclical revenue streams, strong levels of cash flow generation and rising yields.

**Greater China:** The Chinese economy, in our view, is the most able of the Asian markets to ride out any global economic volatility and the excess liquidity generated is likely to be of particular benefit to Hong Kong and Taiwan.

## Examples of stocks we favour

(Data for the following companies sourced from Datastream unless otherwise stated and accurate at 30 April 2012)

**Charoen Pokphand (CP) Foods:** A Thai producer of chicken, pork and shrimp with significant and growing exposure to the rest of South East Asia and the Indian subcontinent. Trading on 13.0 times estimated 12-month forward earnings, the business is very well run and has significant potential to trade off a higher multiple and provide strong dividend growth as it moves down stream into branded ready made meals and other products.

**CTCI:** The largest integrated engineering and construction firm in Taiwan, which is benefiting from the strong increase in investment in power plants in Asia. Traditionally involved in the construction of petrochemical facilities, CTCI has successfully moved into the higher-margin business of power plant construction. The order book has grown rapidly in recent years, which provides reassuring visibility of earnings for the next few years. The stock trades on 13.5 times 12-month forward earnings, with an attractive dividend yield of 4.3%.

**Fraser and Neave:** A leading Pan Asian consumer group with core expertise and a strong standing in the food and beverage, brewing, property and publishing & printing industries, which is based in Singapore. The company trades on 13.1 times 12-month forward earnings, with a dividend yield of 2.6%.

**MGM China:** Following the company's initial public offering in June 2011, this Macau casino operator recently declared its first dividend with an implied yield of 5.9%.\* Trading at 12.3 times estimated 12-month forward earnings the stock is a growth play that should also become a very good dividend distributor on the back of the amount of cash the company is generating.

**Taiwan Cement:** Although recent cement prices have been relatively weak in China due to oversupply and the slowdown in infrastructure spending, we think, in the medium to long term, Taiwan Cement is set to benefit from economic growth in southern China. The stock trades on 11.8 times 12-month forward earnings and offers investors an attractive dividend yield of 5.7%.

## Outlook

Asian equity valuations and fundamentals remain attractive and we continue to be positive about the outlook for Asian equities over the medium to long term. Overall, we retain a domestic bias, particularly towards businesses within the financials, property, consumer discretionary and telecommunication sectors, rather than export-led firms. Despite expected volatility from European sovereign debt issues and global growth concerns in the near term, corporate balance sheets, earnings and dividend yields remain resilient. This should create opportunities for us to add to our preferred positions.

**Mike Kerley, fund manager of the Henderson Asian Dividend Income Unit Trust and the Henderson Horizon Asian Dividend Income Fund.**

\*Source: VC Research.

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