

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. Economies are underpinned by strong fundamentals and robust domestic demand. Consumption is strong due to rising disposable income (higher wages), savings are high and banking systems are well capitalised and liquid. From a corporate standpoint companies have low levels of debt, are highly cash flow generative and are much more prudent with capital expenditure. The most compelling point is valuation. Asia ex-Japan trades at just over ten times forward earnings and is only 16% away from the lows recorded during 2008. These levels of valuation have only been seen twice in the past ten years and on both previous occasions represented attractive entry points.

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



Source: Datastream, MSCI Asia Pacific ex-Japan Index 12 month forward PE ratio, monthly data, from 21 October 2001 to 21 October 2011.

But we are mindful of the risks

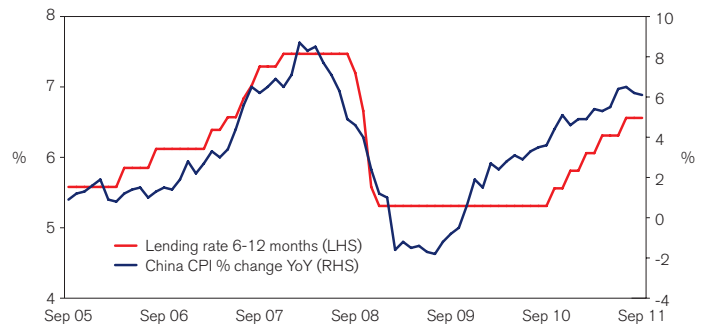
The weaknesses from an economic standpoint centre on exports and domestic policy. Export earnings will need to be revised down if global growth weakens and this will have an impact on overall valuations. It will particularly impact the more export orientated economies of Taiwan and Korea. Policy mistake is also a key issue. Most Asian governments and central banks have been trying to fight inflation and speculative investment (especially property) over the last few years. There is a risk that these measures go too far and drive down domestic growth at a time when trade related activity is also weakening. Although we do not expect there will be a hard landing in China, it is this economy which is at greatest risk of making a policy mistake, which would have a material impact on the region's growth profile. Although valuations are attractive, we expect Asian markets to remain volatile in the short term as the deliberations in Europe and the outlook for US growth take centre stage.

What areas do we like?

We currently think China offers the best combination of value and growth in the region and is the economy best placed to ride out economic volatility in the rest of the world. With China having already spent the last eighteen months tightening monetary and fiscal policy through raising interest rates and reserve requirement ratios for banks, the authorities have considerable firepower to respond to any global slowdown by easing monetary policy. As the chart below shows, inflation in recent months has shown signs of peaking and if the downtrend is maintained China could move off its tightening stance. Within China, banks and industrials look the most attractive.

Elsewhere, we like Thailand, for its strong domestically focused economy and attractive valuations, and Singapore, which is successfully positioning itself as the business hub for South East Asia and the Indian subcontinent. Financials in China, Singapore, Thailand and Taiwan are appealing, as are attractively-valued consumer plays in most markets. We also still like telecommunications, despite the recent outperformance, for their strong cash flow generation, attractive dividend yield and ability to monetise the huge growth in data usage in the years to come. Overall, we prefer domestic sectors and remain cautious on exporters and resources/materials.

Could China be nearing a stage where it stops monetary tightening?



Source: Datastream, China Consumer Price Index, China 6-12m lending rate, monthly data from 30 September 2005 to 30 September 2011.

Examples of stocks we favour

(Data for the following companies is accurate at 31 October 2011)

Shanghai Industrial – A Chinese conglomerate backed by the Shanghai government with businesses in toll roads, water treatment, tobacco and property. The company is attractively valued at a 40% discount to net asset value, trading on 7.3 times earnings and providing a dividend yield of 4.2%, with catalysts to realise that value coming through in the next few quarters. We expect the parent company to inject attractively-priced water and property assets into the listed vehicle in the months ahead and this,



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combined with positive performance from the other businesses, should be the catalyst for a re-rating.

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 at 13.8 times earnings the business is very well run and has significant potential to trade off a higher multiple as it moves down stream into branded instant meals and other products.

CTCI – A Taiwanese industrial construction company which is benefiting from the strong increase in investment in power plants in Asia. Traditionally involved mainly 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 11 times earnings, with a 6.3% dividend yield.

ICBC – China's largest and most conservative bank. We expect loan growth of 15% this year and next, and a marginal increase in non-performing loans, offset by rising net-interest margins. The bank derives a return on equity of greater than 20% yet trades on under two times price to book, with a 4.5% dividend yield. We believe ICBC should be a big beneficiary of a loosening of government policy in the months ahead.

Kangwon Land – Korea's largest casino group is set to benefit from a doubling of capacity in 2012 and improved transportation links as its assets are near the venue for the 2018 Winter Olympics. The stock trades at a significant discount to other Asian gaming stocks and has a compelling dividend yield.

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