

# Principal Asset Class Series – Asia Pacific Equity



## Asia Pacific Market Introduction

- As International Monetary Fund (IMF) predicts, this round of the economic recovery will be driven by the emerging Asian markets. The overall economic growth rate may accelerate to 8.6% in 2021, better than that of 5.1% for developed economies and 6.0% for the global economy.
- China serves as the engine of global economic growth. Taking the MSCI AC Asia ex Japan Index as an example, China has the highest weighting of 37% in the benchmark, followed by Australia, Taiwan and South Korea, accounting for 12-14%. India, with a double-digit projected growth, also has a weighting of about 9% (Figure 1).
- According to the report of Asian Development Bank, the Asia-Pacific region has become the biggest contributor to global gross product (GDP), reaching a 34.9% share in 2019 from 26.3% in 2000. However, the overall market cap of Asian Pacific region only accounts for 14% of the world index. Many investors are yet to invest in Asia. The region is likely to continue to attract capital inflows.
- With the Asian countries changing their economic structures and a continuous expansion of the middle class, the range of industries available for investment is broadened. Among them, digital transformation has become a hot investment topic. The Information Technology sector accounts for more than 20% of the index, with quite a number of new economy and chip manufacturing names in top 10 investments. The Financial sector, with the opportunity to take advantage of a steepening yield curve, has the second-highest weighting. As one of the major growth drivers in the region, consumer discretionary also represents for around 17% of the benchmark (Figure 2).

Figure 1: MSCI AC Asia Pacific Ex Japan Country Weights<sup>1</sup>

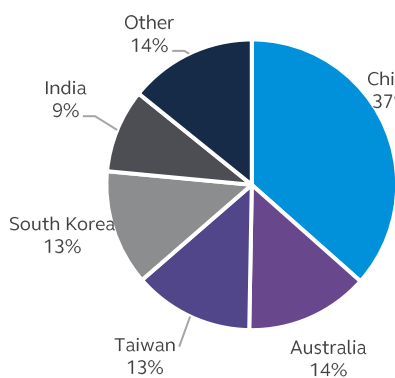
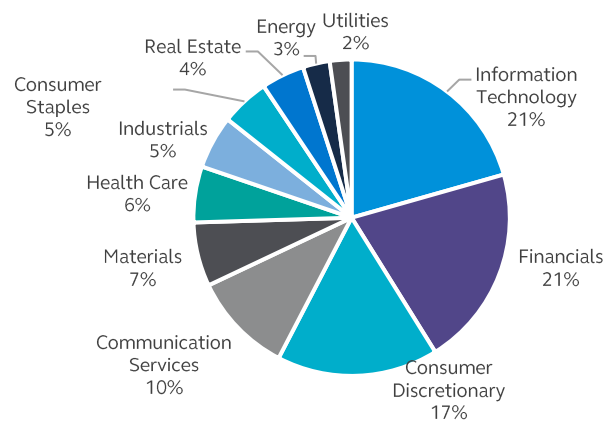


Figure 2: MSCI AC Asia Pacific Ex Japan Sector Weights<sup>1</sup>



## Why should Asia Pacific equity be considered now?

- Historical performance: In the past 20 years, MSCI AC Asia ex Japan Index has outperformed the world index by about 1.4 times cumulatively (Figure 3). Since 2021, Asia-Pacific stock markets rose over 2%<sup>Δ</sup>. The stock markets in the region may continue to benefit from the cyclical recovery.
- Positive capital inflow: Even though the US dollar has rebounded, Asian equities continue to record capital flows, with more than US\$94 billion in the first three months of 2021. Against Asian currencies, the US dollar is expected to remain weak. Capital is likely to continue to flow to high-growth markets.

- Valuation advantage: Along with market corrections, the forward P/E ratio of the MSCI AC Asia ex Japan Index was around 17x at the end of March. That is lower than the nearly 20x P/E of the World Index in the same period.
- Higher dividend yields: The operating environment and balance sheets of Asia-Pacific companies are improving. With more emphasis on shareholder returns, stocks' dividend yields in the region are generally higher than that in the world (Figure 4).

Figure 3: Performance Over Past 20 Years<sup>2</sup>

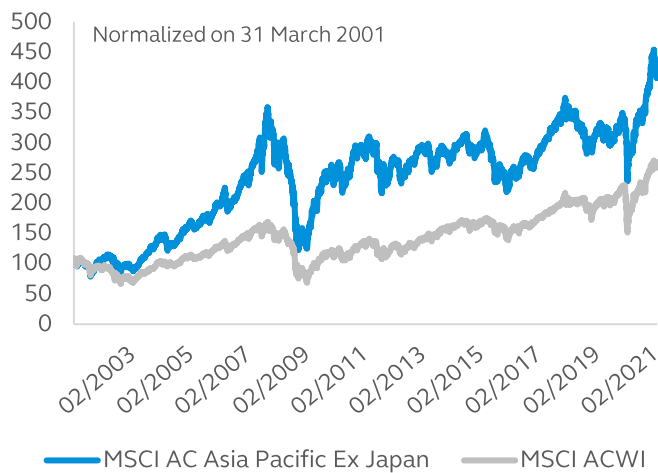
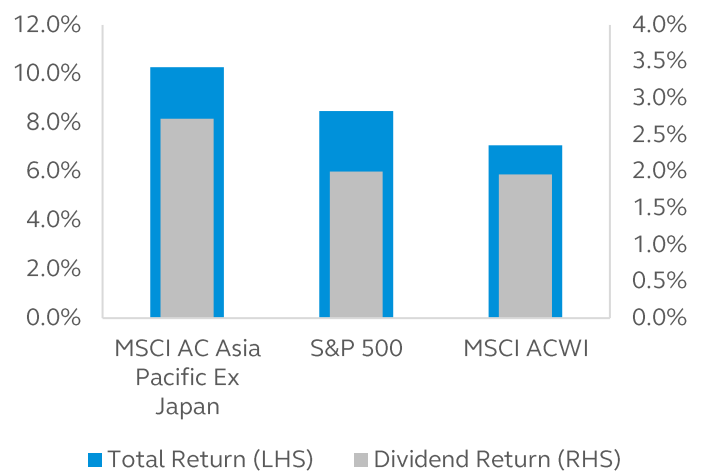


Figure 4: Annualized Return Over Past 20 Years<sup>2</sup>



<sup>2</sup>Source of data: Bloomberg, Principal Asset Management Company (Asia) Limited. As of 31 March 2021

## Top Picks of the Region/ Sector

Country/ Region	Sector
<b>South Korea</b> <ul style="list-style-type: none"> <li>Stock valuations are relatively attractive when compared to other regional markets</li> <li>Driven by the recovery of external demand in the semiconductor and automotive sectors, the country's export gradually made up lost ground in the second half of 2020. The situation is expected to further improve this year</li> </ul>	<b>Information Technology</b> <ul style="list-style-type: none"> <li>A global chip supply shortage, amid stronger demand for smartphones, computers and consumer electronics products, as well as the accelerated development of electric vehicles and infrastructure will provide momentum for a continuous increase in demand for chips</li> <li>Earnings growth potential is better than that of the technology stocks in developed markets. The global market share of leading companies is expected to continue to rise, which is beneficial to the profit prospects of the sector</li> </ul>
<b>Taiwan</b> <ul style="list-style-type: none"> <li>Technology industry makes up more than half of the index</li> <li>The average dividend of Taiwanese stocks is relatively higher than its regional counterparts. Even if bond yields increase, the market still enjoys a certain degree of competitiveness from the perspective of dividends, which may attract foreign investment</li> </ul>	<b>Consumer Discretionary</b> <ul style="list-style-type: none"> <li>The economy of some parts of Asia reopened earlier. With the control and fade-out of the pandemic, the pent-up demand for consumption may take hold and fuel sectoral recovery. The annual earning growth* of the sector may reach 50%, significantly outperforming the market</li> <li>Accelerated development of e-commerce in the region may benefit industrial leaders</li> </ul>
<b>Hong Kong</b> <ul style="list-style-type: none"> <li>Secondary listings are making Hong Kong a more important fund-raising venue and may attract further inflow of international capital</li> <li>Low valuations of Hong Kong stock market might benefit as rising bond yields accelerate a rotation out of high-growth stocks into value stocks</li> </ul>	<b>Industrial</b> <ul style="list-style-type: none"> <li>With the support of cyclical recovery, value sectors, like industrials, that are more correlated with the economy are expected to benefit from stock rotation</li> <li>Earnings prospects of the sector (2021 EPS forecast: ↑49%*) are higher than ↑27%* of the overall market</li> </ul>

\*Source of data: Bloomberg, Factset, Principal Global Asset Allocation. As of 31 March 2021

## References:

<sup>1</sup> Source: MSCI, Principal Asset Management Company (Asia) Limited, as of 31 March 2021

<sup>2</sup> Source: Bloomberg, Principal Asset Management Company (Asia) Limited, as of 31 March 2021

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