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Asia Pacific Equities 2012 Outlook

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OVERVIEW

Simon Flood, Lion Global Investors' CIO, talks to Rita Raagas De Ramos of Ignites Asia (a Financial Times service) about his views on where the Asia Pacific equities market is headed for 2012.

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Simon Flood, CIO of Lion Global Investors

Simon Flood is the Singapore-based chief investment officer (CIO) at Lion Global Investors (LGI). As CIO, he is responsible for the overall direction and supervision of the company's investment division. He also serves as chairman of the company's investment committee.

Prior to LGI, Flood held a number of senior investment roles in the asset management industry and focused predominantly on the active management of portfolios for both retail and institutional clients. In addition to his fund management and investment team leadership roles, he has also held a number of senior regional business leadership positions.

LGI, which is a member of the Oversea-Chinese Banking Corporation Limited (OCBC) Group, had S$28 billion (US$21.6 billion) in assets under management as of Sep. 30, 2011. All of the assets entrusted to LGI are managed by the investment division, which Flood heads.

LGI offers investment solutions across asset classes to government and government-linked corporations, educational institutions, public and private companies, charities, non-profit organisations and retail investors. The company is 70%-owned by Great Eastern Holdings and 30%-owned by Orient Holdings Private, a wholly owned subsidiary of OCBC Bank.

***Ignites Asia*: What developments are you most closely monitoring due to their potential to affect the performance of your portfolio this year?**

Simon Flood: Europe remains the single most important issue we are monitoring, not just because of the effect on sentiment from the debt crisis developments but also because of the impact European banks could have on global liquidity as they deleverage to consolidate their capital positions.

We are also watching the situation in the U.S., particularly with regard to the intransigence of the two main political parties and the paralysis this is creating in the legislative mechanism. The delays seen during the negotiations surrounding the debt ceiling in July 2011 had intensified feelings of uncertainty, undermined confidence both at home and abroad, and exacerbated the volatility in the markets.

Finally, and with respect to Asia specifically, we remain focused on economic developments in China, whose economic prosperity will have a major influence on investor confidence in the region.

What are the biggest challenges that you expect to face in managing your portfolio this year?

With equity trading volumes subdued, the markets remain vulnerable to the possible repatriation of capital by foreign investors. The situation would be particularly acute should liquidity continue to tighten in the developed markets. Stock picking under these conditions will be challenging, as fundamentals may be overshadowed by technical factors.

How are you bracing to face those challenges?

Ultimately, prices will revert to their correct level, so we will continue to take advantage of buying opportunities presented by indiscriminate markets in Asia’s leading companies. We will continue to focus on identifying and accumulating high-quality businesses with strong balance sheets and dependable cash flows.

What are the biggest opportunities that could lead to a better performance for your portfolio this year?

Asia’s performance has been very much driven by external factors this year, and fundamentals have been undermined by money flows. A definitive solution to the European crisis and a return to focusing on Asian-centric issues would underwrite a return to fundamental analysis and fundamentally driven markets, which would be in our favour.

What were the biggest surprises and disappointments of 2011 in terms of how your regional portfolio performed? Do you expect any of that to affect your portfolio this year?

Contrary to market expectations, U.S. consumption held up relatively well in the second half of 2011, despite the U.S. debt ceiling crisis and the European situation. We expected this to benefit Asian companies in the last quarter of 2011, though it remains to be seen if the improvement in the U.S. can be sustained into 2012. On the negative side, the escalation of the sovereign debt crisis in Europe and the contagion to Italy and Spain caused risk aversion to spike more than had been expected. The Europe situation appeared to be reaching a crunch point in December, but the magnitude and complexity of issues involved mean that further volatility is to be expected.

Have you made any significant adjustments to your portfolio allocation over the past few months?

No. As active fundamental stock pickers within a macro thematic overlay, we will nuance the portfolio to take into account any significant changes in the macro picture. Though we expect a slowdown in Asia, both fiscal and monetary policy remains flexible enough for the region to avoid a major downturn. Much of this is in the price already, and our portfolio represents a balance between defensive characteristics and high-quality domestic cyclicals that we believe will perform well, given more stability in the markets.

What are the markets in Asia that will likely contribute the most to your portfolio's performance this year?

As we are fundamental stock pickers, we do not depend on any one particular market for our performance. The top-down strategy is to focus on domestic-related plays and to underweight the global growth and cyclical stocks. However, when viewed on a geographic basis, China has the most attractive valuations and could do well in 2012. We are also confident on the outlook for Singapore, which had a challenging year in 2011 but is home to some of the regions' most attractive companies, and which now trades at very reasonable valuations.

Which markets are you most bearish over?

We are concerned about the outlook for Australia given the tight domestic economy and the impact that the global slowdown is likely to have on the demand and pricing of commodities, which has been the key sector holding up corporate earnings for this market. We are also underweight in India in light of the continued economic slowdown, lack of progress on the policy front, and rapidly weakening fiscal and current account balances.

Which sectors do you favour?

We favour domestic cyclicals that will benefit from the region's good fundamentals and Asia's potential for long-term consumption growth. From an asset class perspective, we would like to play this theme through high-dividend equities, which provide relatively more stable returns in a volatile environment.

Which sectors are you avoiding?

We will avoid cyclical stocks of companies that are exposed to the global economies. The strength of global growth is likely to be capped, as low levels of demand and confidence in the U.S. are still too weak to bring unemployment down meaningfully. Given that the Eurozone accounts for about 20% of the global economy, the combined sovereign and bank deleveraging that will ensue there will inevitably have a knock-on impact on the rest of the world, including Asia.

What are your weightings within an Asia-Pacific equities portfolio?

- China: Overweight
- Hong Kong: Underweight
- India: Underweight
- Indonesia: Overweight
- Japan: Neutral
- Malaysia: Underweight
- Philippines: Neutral
- Singapore: Overweight
- South Korea: Overweight
- Taiwan: Underweight
- Thailand: Overweight
- Vietnam: N/A
- Australia: Underweight
- New Zealand: N/A