

Why sustainable growth supports ASEAN equities

Despite global inflation fears, the Association of South-east Asian Nations is in a cycle of high-quality, balanced economic growth, suggesting equities are set fair

While volatility has returned to global equity markets in 2018, the positive outlook for equities in the fast-growing Association of South-east Asian Nations (ASEAN) appears intact.¹ Sustainable economic growth, firm corporate earnings momentum and resilient consumer confidence look set to drive the region's equity market forward. Indeed, a moderately more volatile market environment presents opportunities for exploiting stock mispricing.

There are many reasons for rising volatility. First among them is the monetary tightening in the US and elsewhere at a time when global equity and fixed income valuations are high. There is also the geopolitics of trade wars and real wars – although the declaration of peace on the Korean peninsula reduces the risks.

At Columbia Threadneedle Investments we believe that Asia ex-Japan, including many of the ASEAN countries, is in a cycle of high-quality economic growth. Its pace will be moderately rapid yet sustainable, supporting steady profits growth and providing a positive backdrop for stock markets.² Broadly speaking,

governments are pursuing careful fiscal, monetary and exchange rate policies. Even the elections due in several ASEAN countries over the next two years are, generally speaking, not expected to spark excessive tensions which would disrupt growth and equity markets.

ASEAN economies are tending to grow at the top of their historical range, with the IMF forecasting GDP growth of 5.3% in 2018 and 5.4% in 2019.³ There are signs of inflationary pressures building, and rates may be tweaked higher, yet there are no indications of major tightening cycles – just small upwards adjustments to policy. Further, countries such as Indonesia, Malaysia, the Philippines and Thailand have major infrastructure development programmes under way, which should boost demand in the short term and productivity in the medium term.

China's lead

China is leading the way for ASEAN in this new era of balanced growth. Recent rhetoric suggests that Xi Jinping, China's president, is poised to continue the quality growth agenda



Quality growth: China is leading the way on a new agenda for expansion

that he introduced on taking office in 2013. Prioritising 'high quality' rather than simply 'high' growth, his administration successfully introduced supply-side reforms to reduce excess capacity in parts of the economy and raise productivity. Online ecommerce also helped to stimulate consumption of goods and services, allowing China to reduce its dependence on investment demand and so balance the economy.

China's high debt-to-GDP ratio is a source of concern, which may have implications for the region's smaller countries. That said, financial practices have been tightened and banks are lending with greater prudence than they were 10 years ago. Additionally, China's debt is mainly domestic, with very little borrowing from overseas, giving the government scope to manage the situation. Even so, China is likely to slow somewhat as financial leverage is reduced. The IMF forecasts that GDP growth of 6.9% in 2017 will slow to 6.6% in 2018 and 6.4% in 2019.³

Normalising rates

It is 'advanced economies' that may cause further jitters in ASEAN's financial markets as the year unfolds. Since 2014, advanced economies have experienced a continued, if at times halting, recovery from the recessions that followed the 2008-2009 global financial crisis and euro area sovereign debt crisis. The IMF forecasts that these economies' GDP growth rates will increase to 2.5% in 2018, up from 2.3% in 2017.³ Yet stronger growth also means that inflation is picking up. As a result, interest rates in these countries will start to normalise from their very low levels – in other words go up.

This normalisation of rates is bound to spook equity markets. However, Columbia Threadneedle Investments believes that the Federal Reserve and key central banks across the world have enough leeway to trade-off inflation and interest rates without threatening the outlook for sustainable economic growth. Historically, when

such trade-offs have been taken to prolong the growth cycle, the performance of global equities has remained positive.⁴

Equities set fair

In ASEAN, the era of moderation looks set to remain in place. Fears that inflation in advanced economies will lead to a prolonged tightening of interest rates, with negative implications for ASEAN markets, appear premature. South-east Asia's combination of sustainable economic growth and rising corporate earnings suggests that equities are set fair for 2018.

Sources:

- 1 ASEAN has 10 members: Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam.
- 2 Asia's New Era of Sustainable Growth, 2018 Annual Perspectives, Columbia Threadneedle Investments, January 2018.
- 3 IMF World Economic Outlook 2018. *Cyclical Upswing, Structural Change*.
- 4 Asian Equities Poised for Growth in 2018, Columbia Threadneedle Investments, January 2018.

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