Asia in charts

Opportunities in a post-pandemic new normal

December 2020

HSBC Global Asset Management

Key takeaways

- Asia is undergoing an economic recovery, led by mainland China and North Asia. In 2021, the recovery is expected to broaden to the rest of the region
- Asian governments and central banks are expected to continue to support the economies, although with a potentially less expansionary stance
- The pace of recovery could be affected by a slow labor market recovery, hit to household incomes and private sector balance sheets, default and bank asset quality risks as well as debt sustainability concerns
- Fund flows into Asia credit have been strong in 2020, and this is a trend expected to continue in 2021 as global investors intensify their search for yield in a low to negative rate environment
- Asian equities are expected to see a strong bounce back in earnings in 2021's post-Covid environment and the stabilising GDP growth in the region should provide support for the earnings outlook
- Digitalisation in Asia is accelerating, and mainland China continues to lead the world in ecommerce, with forecasted ecommerce revenues in 2020 expected to be more than double that of the US. While the internet sector in mainland China is seeing regulatory uncertainties, digitalisation and overall supportive government policies for the sector should continue to act as catalysts in the medium to long-term
- In Asia, nearly half a billion people will be aged 65 and older by 2025 and Asian consumers are increasingly interested in health and lifestyle changes. Evolving socio-economic factors and ongoing institutional support place the healthcare sector in a favourable position for continued growth

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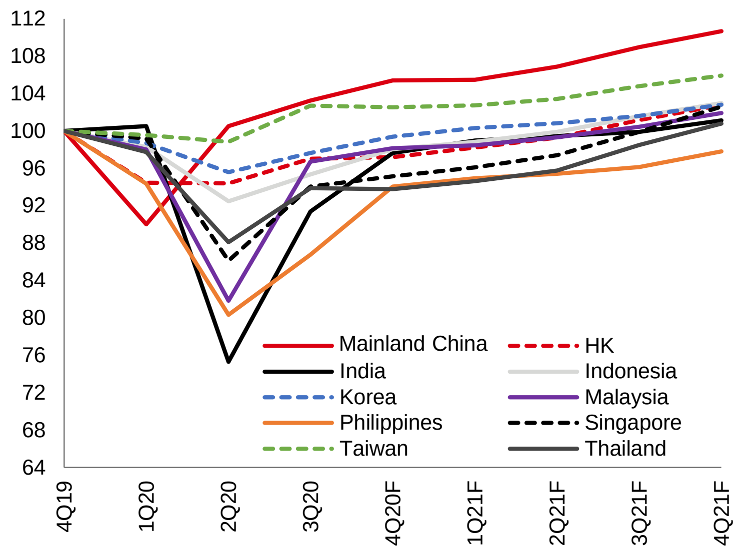
Widening road to recovery

Recovery led by mainland China and North Asia should broaden to the rest of the region

Asia is experiencing an economic recovery, from the Q2 2020 trough. Recovery has been driven by gradual relaxation of mobility restrictions, significant policy stimulus in 2020, and resilient external trade. Mainland China and North Asia have outperformed in terms of economic growth in 2020. In 2021, the recovery should broaden to the rest of the region, with a larger scope of catchup growth for India and ASEAN economies. The prospect of widely available effective vaccines has reduced the threat of COVID-19 and brightened the cyclical growth outlook.

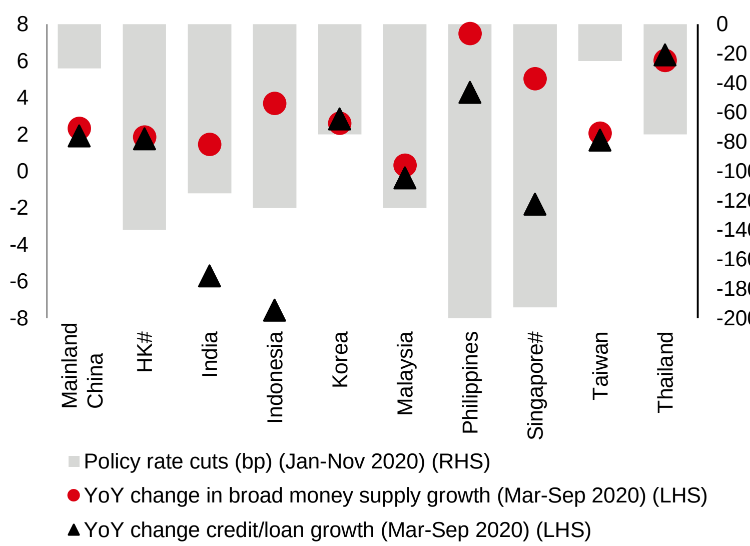
Real GDP index (seasonally-adjusted) [1]
4Q19=100



Monetary policy expected to continue to be accommodative but with less policy space

Benign inflation, lack of major external imbalances in Asia, and the US Fed's average inflation targeting framework should allow Asian central banks to keep policy rates low for longer. We expect largely stable monetary policy in most parts of Asia in 2021 but with less room for policy maneuvering, given the aggressive easing that took place in 2020. We expect targeted easing measures and liquidity support to continue. Overall, an abrupt exit of policy support in 2021 is unlikely.

YoY change in growth rate (%) [1] (bp)



3-month interbank rates used for HK and Singapore

Source:
1. CEIC, Bloomberg, HSBC Global Asset Management as of December 2020

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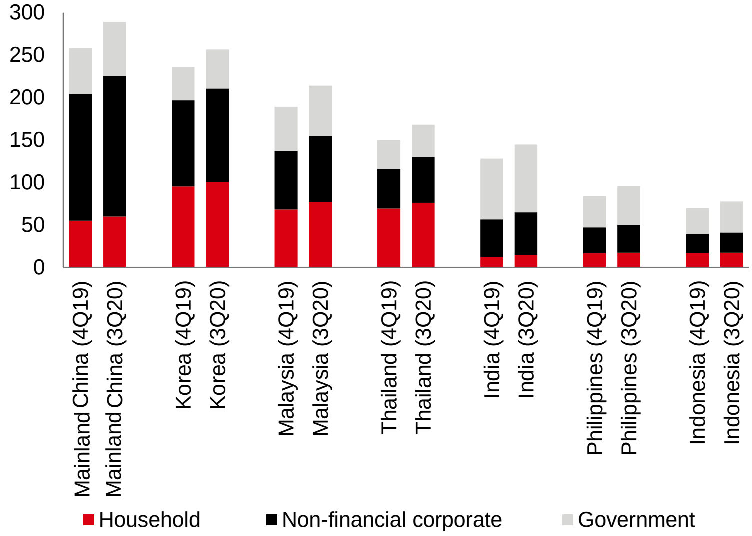
Restoration and reformation

Coming to terms with lasting economic scars from the pandemic

While Asia overall has controlled the virus better than other major regions, the pace of recovery in Asia could be affected by a number of factors, including a slow labor market recovery, hit to household incomes and private sector balance sheets, default and bank asset quality risks as well as debt sustainability concerns. A return to pre-Covid levels of output/GDP is likely for most Asian economies in the second half of 2021, but the region may take longer to return to the pre-pandemic medium term growth potential.

Debt to GDP ratio (2)
% of GDP



Placing a greater policy focus back on structural reforms

Attention is now turning to placing a greater policy focus on structural reforms to boost longer-term growth potential. In China, the 14th Five-Year Plan focuses on indigenous technology and innovation capacity, domestic (consumer) demand, and the pursuit of higher quality growth. Many Asian economies are also continuing to press ahead with structural reforms and deregulation to improve ease of doing business and to shore up economic resilience. India, for instance, where FDI policy in a number of sectors have been relaxed, saw an increase in gross FDI inflows (between April and September 2020) by 11% year-on-year, despite the emergence of the pandemic.[3]

Mainland China: Key areas of developments under the proposed 14th Five-Year Plan (2)

Innovation & technology self-sufficiency	Culture
Economic/ industry upgrading	Green development
Boosting domestic market	High-level, high-quality opening-up
Deepening reforms	People's quality of life
Agricultural & rural	Peaceful China
New urbanisation	Military & defense

Source:
2. CEIC, Bloomberg, HSBC Global Asset Management as of December 2020
3. Reserve Bank of India as of November 2020

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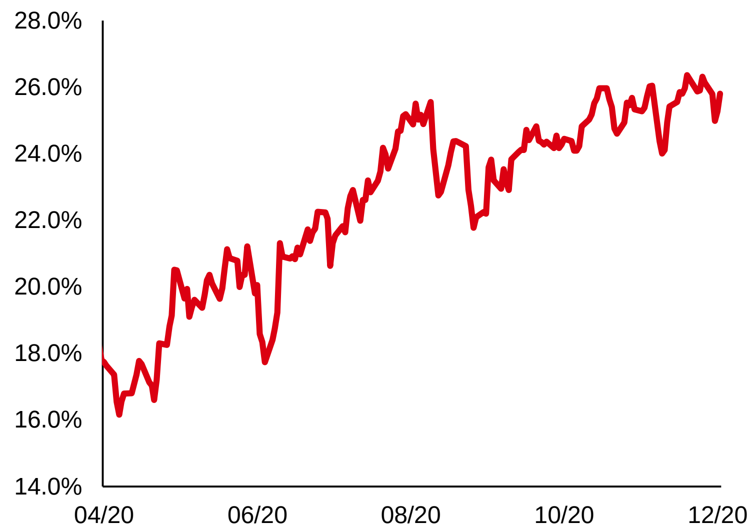
When the rates go low, flows go…

Continued search for yield as low to negative rates persist

The US Federal Reserve has moved to a flexible average inflation target regime, and a majority of the FOMC members are not anticipating rate hikes until at least the end of 2023, which only prolongs the lower for longer scenario. In such a market, the proportion of investment grade bonds yielding negative rates has increased from 18% earlier in the year in April to the current 26% (as of 3 December). The low to negative rate environment lifts the appeal of Asian assets that can offer a premium as investors search the world for yield.

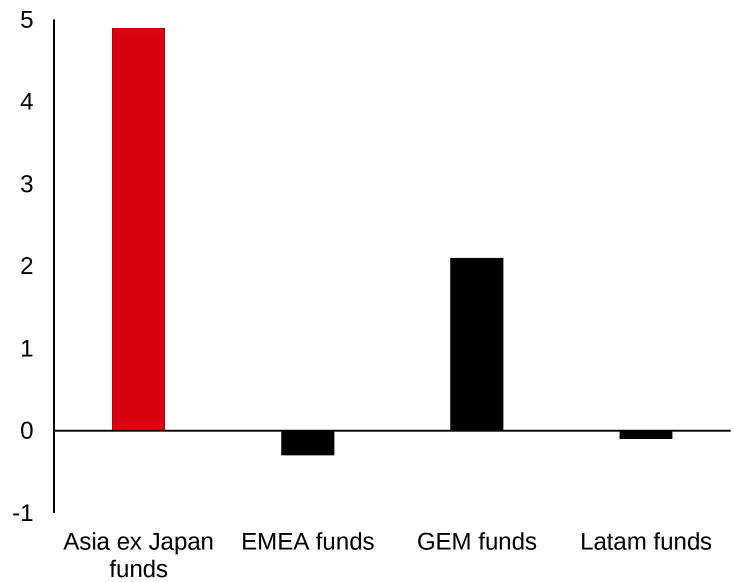
% of bonds in Bloomberg Barclays Global Agg Index with negative rates [4]



Fund flows to Asia bonds expected to be well supported

Fund flows to Asia credit have been strong in 2020, despite the sell off that occurred in March at the height of the market panic. Overall, emerging market bond funds have attracted capital, led by Asia ex Japan hard currency funds. This is a trend expected to continue in 2021 as global investors intensify their search for yield – Asia USD bonds offer a yield premium to bonds in the US, Europe and even emerging markets.

Emerging market hard currency funds by region, flows year-to-date (USD billion) [5]



Source:
4. Bloomberg as of 3 December 2020
5. HSBC Global Research, EPFR, as of 6 November 2020

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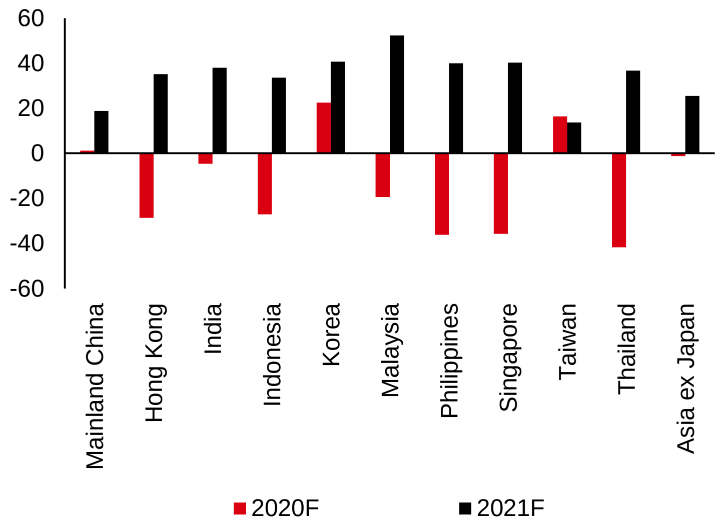
Spotlight on strong corporate fundamentals

Expected rebound in earnings growth for Asian equities

Asian equities are seeing attractive valuations, improved earnings growth, EPS upgrades, and increases in ROE. Other short and medium term drivers supporting the asset class include accommodative monetary policies and still low foreign investor positions. Asian equities are expected to see a strong bounce back in earnings in 2021's post-Covid environment and the stabilising GDP growth in the region should provide support for the earnings outlook; the current consensus for 2021 EPS growth is coming in at 25.5%, versus the -1.3% figure from 2020E. The earnings rebound is expected to be broad based.

EPS growth year-on-year (%) (6)



Asia high yield default rates to stay lower than other regions

With respect to default rates, Asia high yield has so far fared better than other markets in 2020, with a year-to-date default rate of 2.7%, which is markedly lower than the US high yield market at 6.7%. Defaults in Asia bonds in 2020 have been idiosyncratic. In 2021, the default rate in Asia high yield is still forecasted to be lower than in other global markets. The lower default rate in Asia credit can be attributed to a number of factors, including Asian issuers' solid fundamentals and Asia ex Japan's higher GDP growth versus other regions.

Default rate in high yield USD markets (7)

	2019 Actual	2020 YTD	2021 Forecast
Asia	**1.6%**	**2.7%**	**2.6%**
EM Europe	0.0%	3.3%	1.1%
Latin America	2.0%	4.4%	3.6%
EM (total)	1.2%	3.2%	2.8%
US	2.9%	6.7%	4.0%

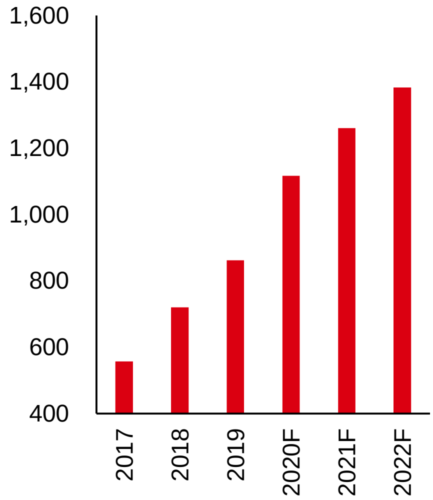
Source:
6. Credit Suisse, Refinitiv, data as of 23 November 2020
7. JP Morgan as of 7 November 2020

Investment themes – Internet and innovation

Digitalisation: China leads the world in ecommerce revenues

Internet penetration in mainland China has increased by 5.8% between June 2019 and June 2020, to reach 67%. [9] The pandemic has accelerated internet services penetration particularly in rural areas. Despite the increase, mainland China's internet penetration rates are still low compared to developed markets and indicate room for growth. Even so, mainland China's ecommerce market is already the largest in the world, with 2020 ecommerce revenues forecasted to be more than double that of the US. While the internet sector is seeing regulatory uncertainties, digitalisation and supportive government policies for the sector should continue to act as catalysts in the medium to long-term.

Mainland China ecommerce revenues (USD billion) [8]



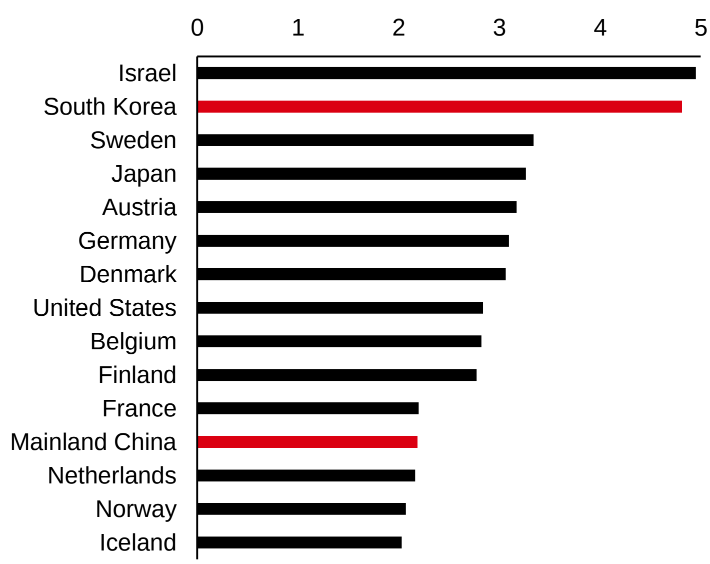
Top 5 markets, by ecommerce revenues 2020F (USD billion) [8]

Mainland China	1,117
USA	432
Japan	105
UK	97
Germany	88

Asian markets are increasingly leaders in global innovation

Innovation ecosystems across the Asian region have been thriving over the past few years. A number of cities in mainland China have risen as innovation hubs. In 2019, China spent a record amount on R&D, amounting to 2.23% of GDP, or RMB 2.2 trillion (USD 321 billion). Innovation in Asia ex Japan is not limited to just China – India has the world's third largest tech start up ecosystem; Vietnam and the Philippines continue to make significant progress, while South Korea already stands as a global innovation leader.

Top R&D countries & territories, ranked by by R&D expenditure as share of GDP (%) [10]



Source:
8. Statista as of November 2020
9. China Internet Network Information Centre (CNNIC) as of November 2020
10. World Bank, based on 2018 figures, latest available data as of November 2020

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Investment themes – Heathier today, wealthier tomorrow

Healthcare continues to be in a favourable position for growth

Even before the pandemic hit, Asia's evolving socio-economic factors and ongoing institutional support have placed the healthcare sector in a favourable position for continued growth. A combination of demographic trends, including an aging population, rapid urbanization and rising prevalence of chronic diseases, make an inarguably strong case for Asia's immense and growing healthcare demand. Bottom up equity investors can potentially capitalize on the structural changes occurring within Asia's healthcare sector as healthcare companies are increasingly placing more focus on innovation and moving up the value chain through research and development.

Healthcare in Asia [11]

Growth

Asia is expected to contribute to more than 40% of global healthcare spending in the next decade

Demographics

By 2025, nearly half a billion people in Asia will be aged 65 and older

Health awareness

Asian consumers are increasingly interested in health maintenance and lifestyle changes

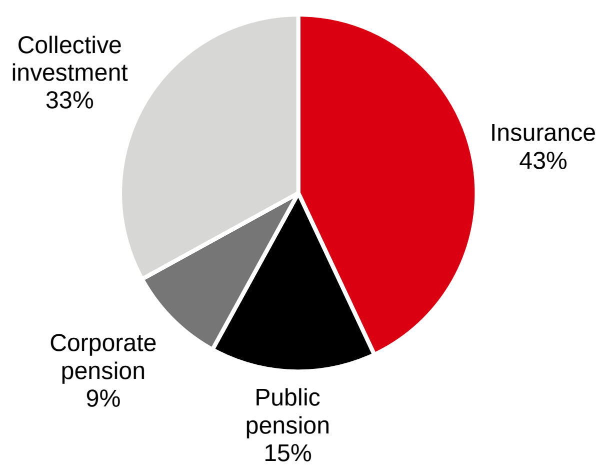
Low healthcare spending

All major Asia ex Japan economies significantly lag behind other major markets in healthcare expenditure per capita

Insurance products make up the largest share of AUM in Asia

In Asia, insurance products continue to be a preferred savings channel, with 43% of domestic AUM (excluding bank deposits) falling into insurance products. Taiwan and Hong Kong have the more developed insurance markets in Asia, with high life insurance penetration rates. Stages of development of the insurance industry differ across the Asian markets, with mainland China and India seeing low penetration rates but with room for expansion given growing consumer awareness, increasing middle class, urban migration, fast development of digital channels, and government support.

Breakdown of domestic AUM, excluding bank deposits [12]



Source:
11. Bain & Company, Asia-Pacific Front Line of Healthcare Report 2020, World Health Organization latest available data as of November 2020
12. HSBC Global Research as of August 2020

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