



3Q2024 quarterly update: There Will Be Blood



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Today's agenda



1. The case for Asia
2. The Japan carry trade
3. Chinese deflation
4. Electric vehicles
5. Malaysian FDI
6. Vietnamese communism



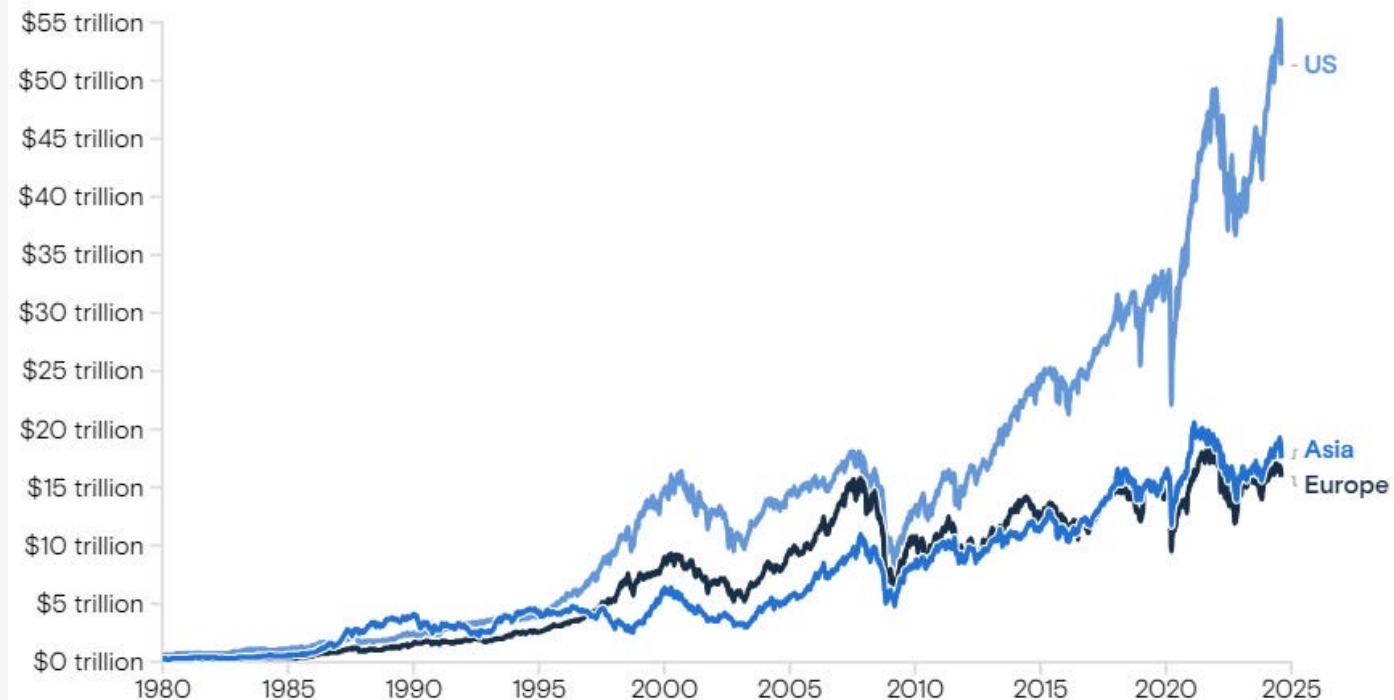
1. The case for Asia

The US market has become frothy – Europe / Asia, not so much



The US equity market's size reflects the dominance of the US economy

Market capitalization



Source: Goldman Sachs

Source: Datastream, Worldscope, Goldman Sachs Research
Asia including Japan

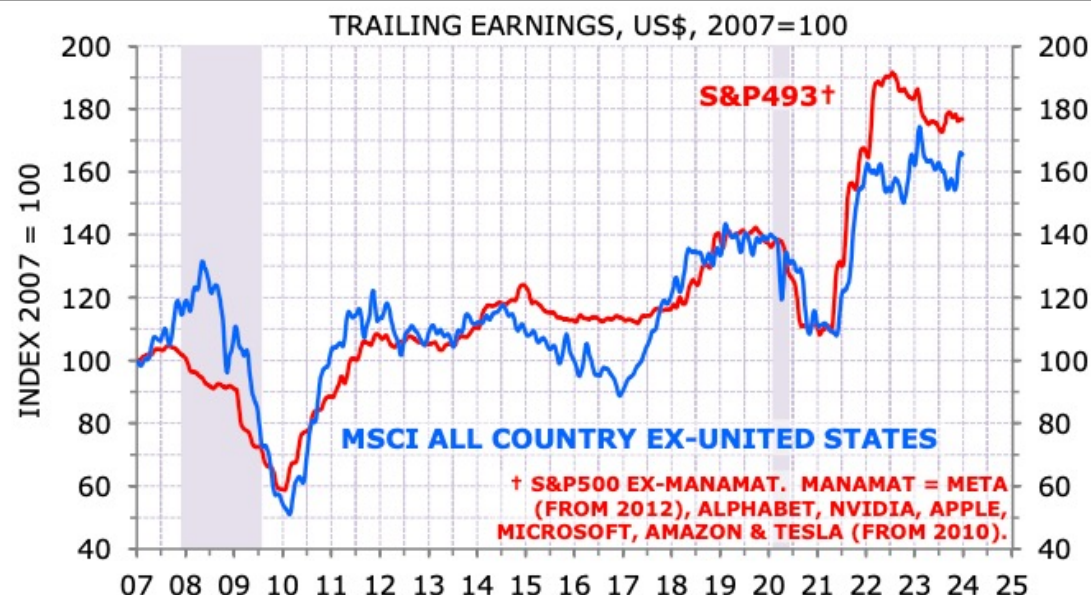
**Goldman
Sachs**

The only reason to own US stocks is the Mag 7,
otherwise US EPS growth has been largely identical to
that in the rest of the world



Exhibit 2

America not as exceptional ex the Big 7



Source: Minack Advisors

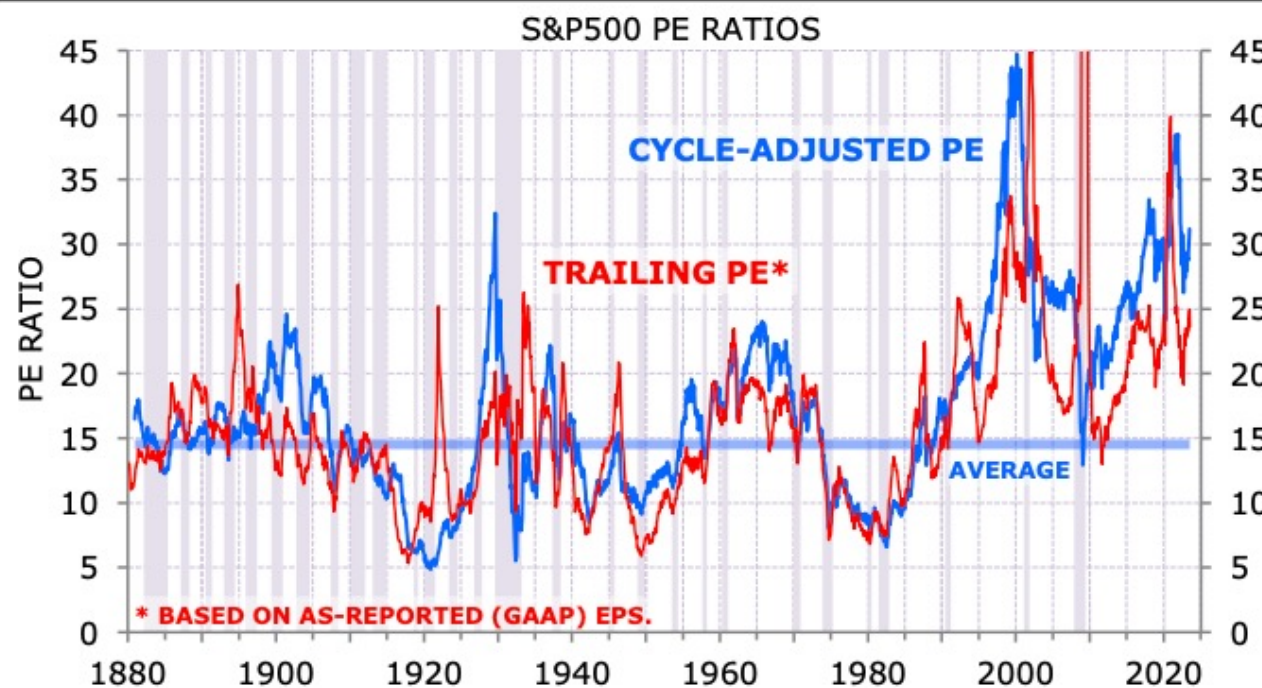
Source: MSCI, Standard & Poor's, Bloomberg, NBER; Minack Advisors

US valuations are now exceptionally high on both CAPE & PE



Exhibit 1

Valuations are high. And have been for a while



Source: Minack Advisors

Source: Shiller, Standard & Poor's, BLS, NBER; Minack Advisors

We've been in a growth bubble



Exhibit 4

Growth bounces versus value in 2023



Source: MSCI, IBES/DataStream, NBER; Minack Advisors

Source: Minack Advisors

The US Dollar index looks like it's breaking down



Source: TradingView

MSCI Asia Ex-Japan index has been flat with no excitement



iShares MSCI All Country Asia ex Japan ETF (AAXJ)

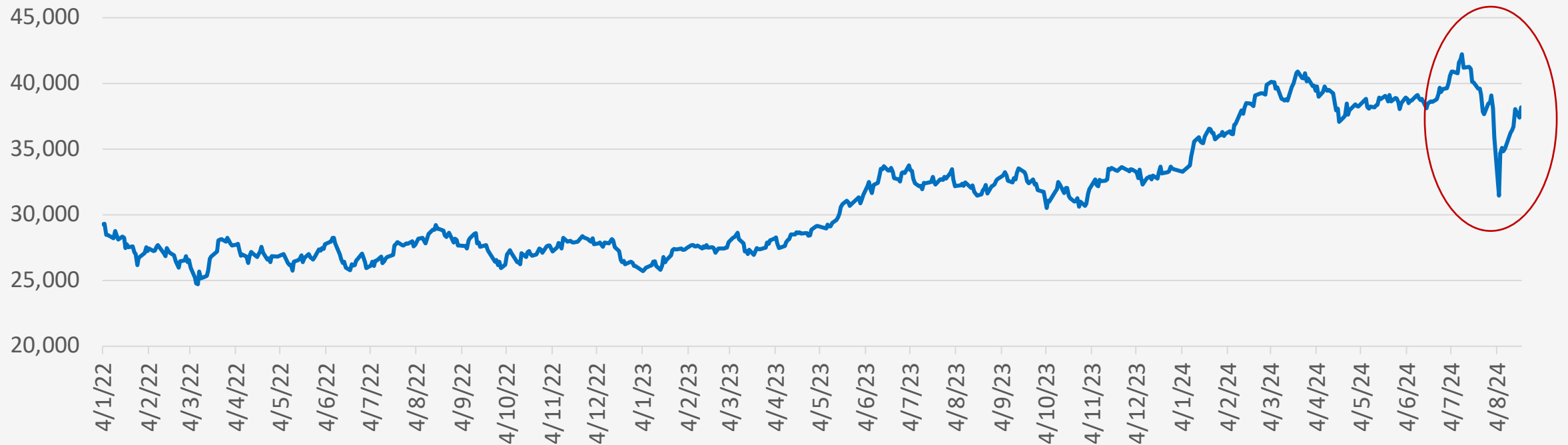


Source: Yahoo Finance

Some froth in Japan as earnings benefitted from the weak yen... but that trade is most likely over at this point



Nikkei 225



Source: Yahoo Finance

Chinese equities have been particularly weak...



iShares MSCI China ETF



Source: Yahoo Finance

Asia Pacific ex-Japan trades at 13x next year earnings, fair enough. China/HK looks cheap, as does the Philippines and Singapore



MSCI AC Asia Pacific universe market valuations

	PE (x)		Earnings growth (%)		PB (x)		Div yield (%)		ROE (%)		Div payout (%)	
	2024F	2025F	2024F	2025F	2024F	2025F	2024F	2025F	2024F	2025F	2024F	2025F
AsiaPac ex-JP	14.6	12.8	17.9	14.8	1.7	1.6	2.7	2.9	11.4	12.0	40	38
Japan	16.0	14.5	4.5	9.4	1.5	1.4	2.2	2.4	10.1	10.5	31	32
Australia	17.2	16.6	(1.7)	4.5	2.3	2.2	4.0	4.0	12.2	12.0	68	67
China	10.0	8.9	9.8	12.6	1.2	1.1	2.9	3.1	10.9	11.3	28	27
Hong Kong	11.6	10.4	10.8	9.9	0.8	0.8	4.7	5.1	6.6	7.0	56	55
India	24.7	21.2	11.2	16.5	3.8	3.4	1.2	1.4	16.8	17.3	32	30
Indonesia	12.5	11.6	1.8	8.5	2.2	2.1	4.7	4.9	17.0	16.9	58	55
Korea	11.7	9.1	101.2	27.5	1.1	1.0	2.0	2.1	9.4	11.0	23	20
Malaysia	14.6	13.4	11.9	8.4	1.3	1.3	4.0	4.3	10.0	10.4	60	59
Philippines	11.8	10.6	11.5	10.7	1.6	1.4	2.9	3.0	13.8	13.8	33	32
Singapore	12.4	11.9	5.3	4.0	1.4	1.4	4.7	4.9	10.7	10.6	59	60
Taiwan	21.1	17.7	23.0	20.4	3.0	2.7	2.3	2.6	14.8	16.0	50	47
Thailand	16.1	14.0	11.9	15.6	1.5	1.4	3.3	3.7	10.0	10.9	52	51

Source:
Jefferies

Note: Based on MSCI index universe. Japan, India: years beginning 1 April. Australia: years ending 30 June. Source: FactSet, I/B/E/S, Jefferies

Summary



- The US equity market has become frothy
- US companies ex-Mag 7 have not outperformed
- Meanwhile, growth stocks remain in a bubble
- Asian markets ex-India are not frothy at all
- The cheapest markets in Asia on P/E are Hong Kong, the Philippines and Singapore



2. Thoughts on Japan

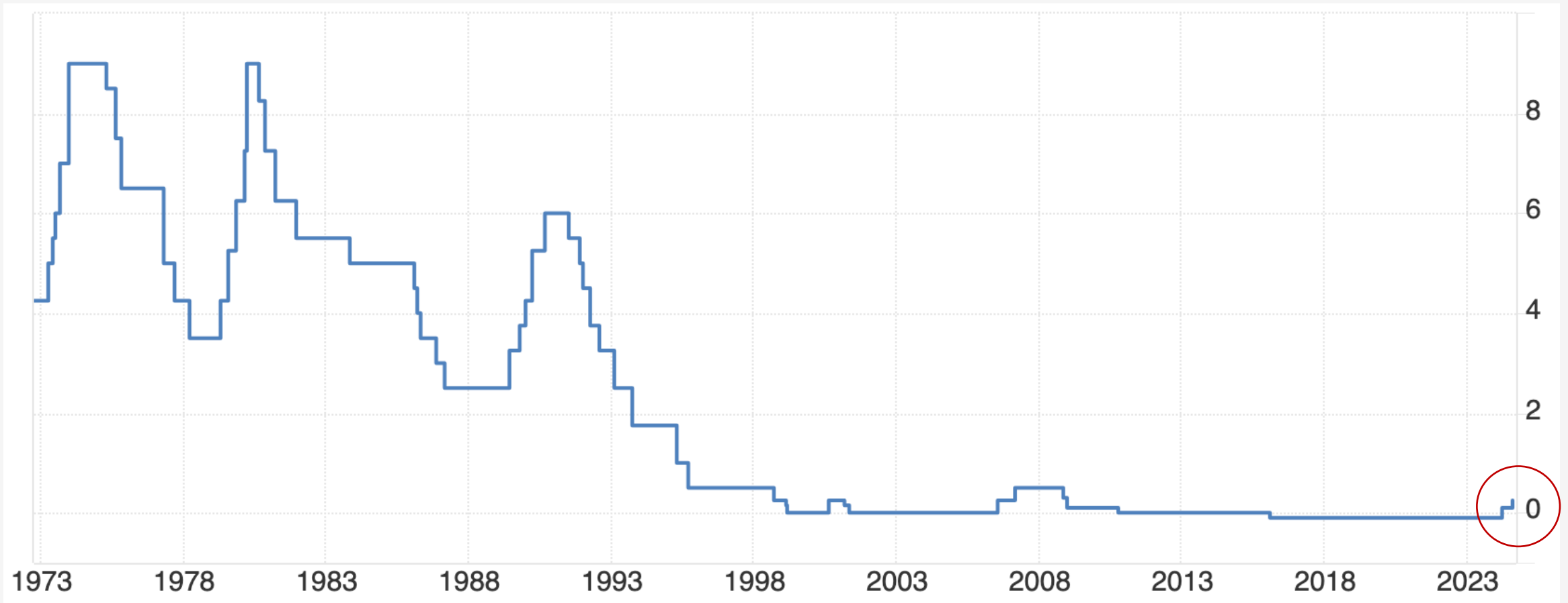
My July trip to Tokyo... the yen was CHEAP!



US\$3 Gyudon →



A small rate hike...



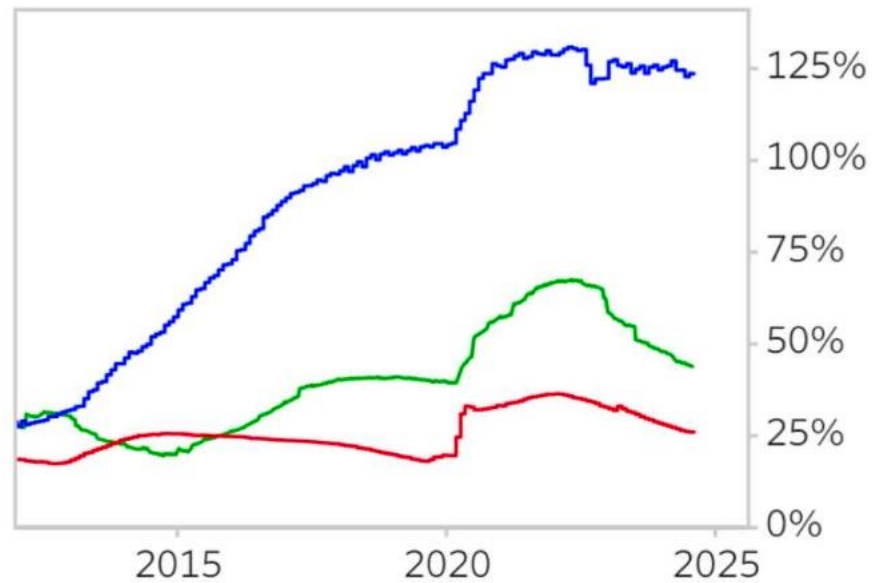
Source: Trading Economics

... along with a planned shrinking of the BoJ
balance sheet...

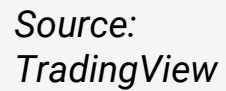


Central Bank Balance Sheet (%GDP)

— BoJ — Fed — ECB



Source: Bridgewater

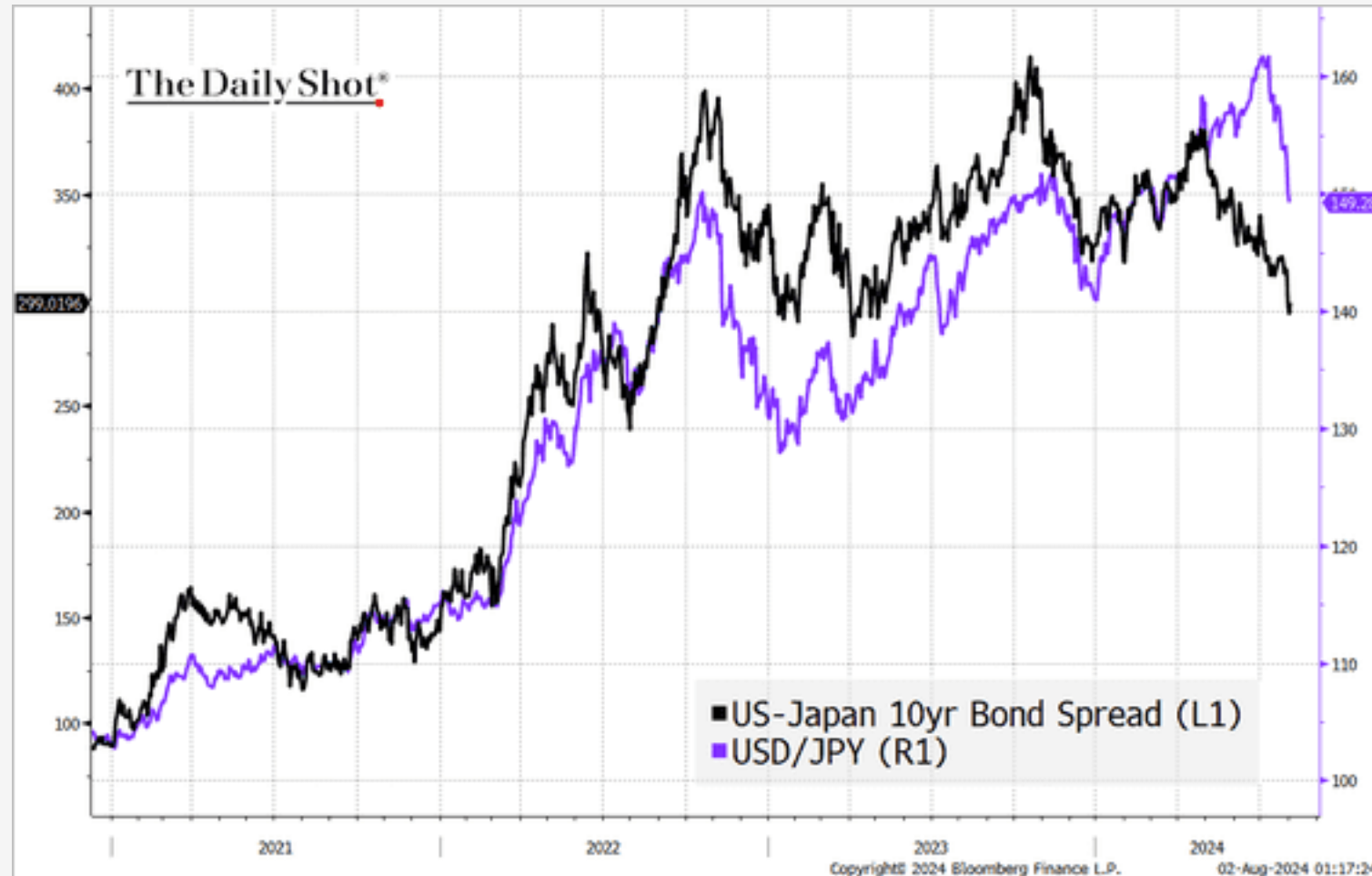


... which led to a risk-off episode with a partial retracement

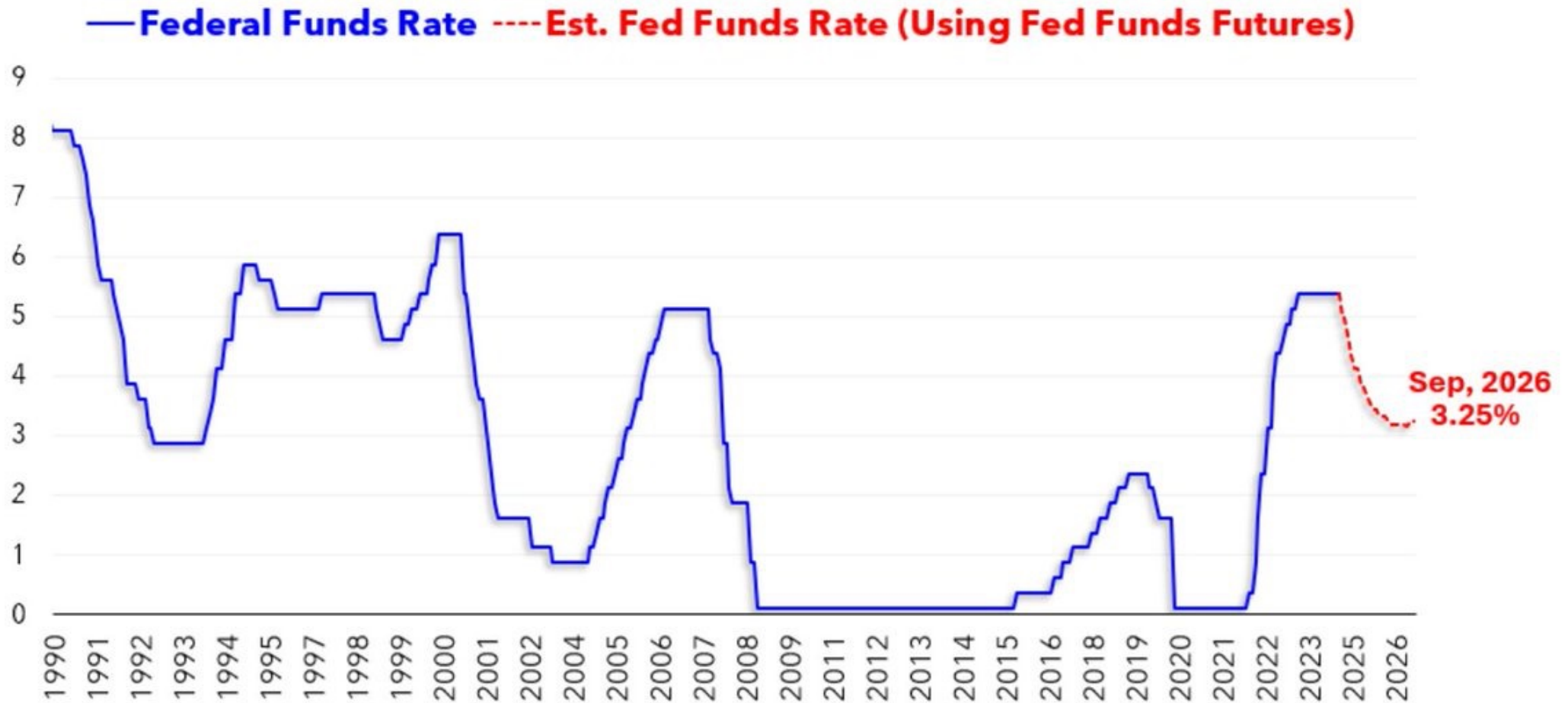


Source: TradingView

Long-term picture: US-Japan interest rate differential has peaked



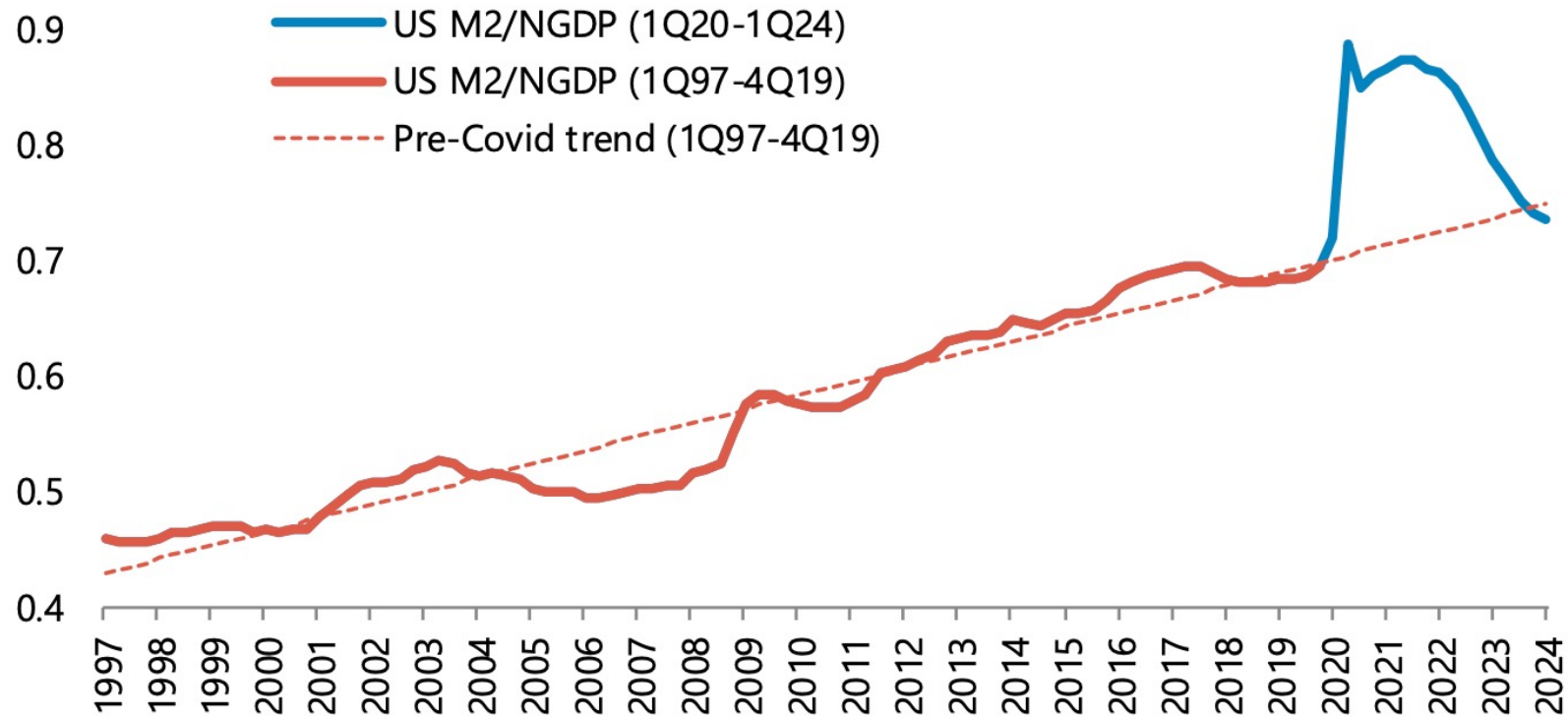
The primary driver will be lower US interest rates



Why? Because COVID-era excess money supply is now gone



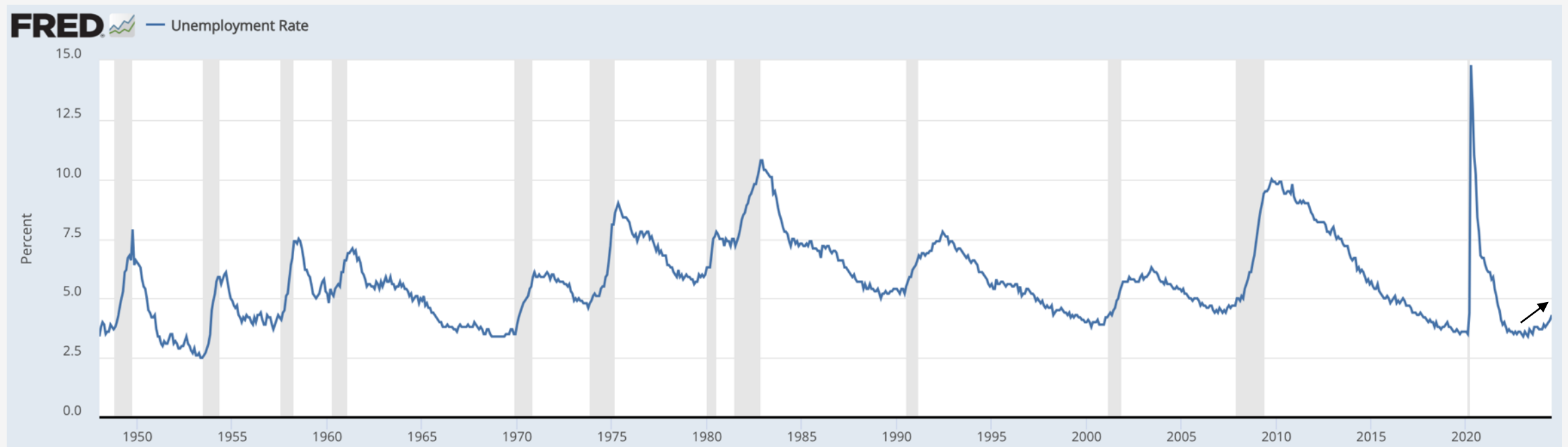
US M2 to nominal GDP ratio



Source: Bureau of Economic Analysis, Federal Reserve, Jefferies

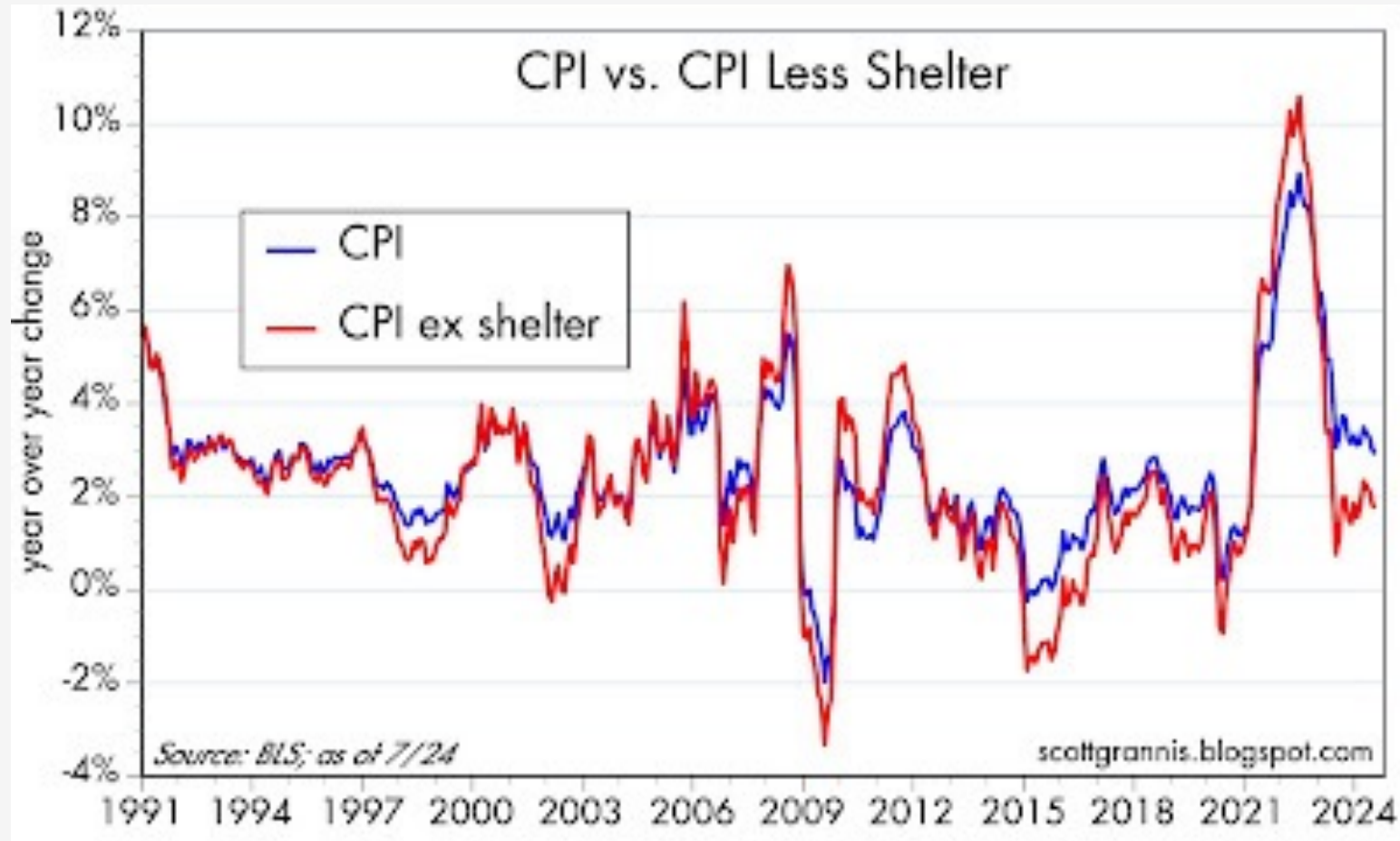
Source: Jefferies

And US job market is weakening, though at a slow pace



Source: FRED

CPI ex-shelter now ~2%... 18 month lag from October 2023 means headline CPI will hit 2% by April 2025



Source: Scott Grannis

Summary

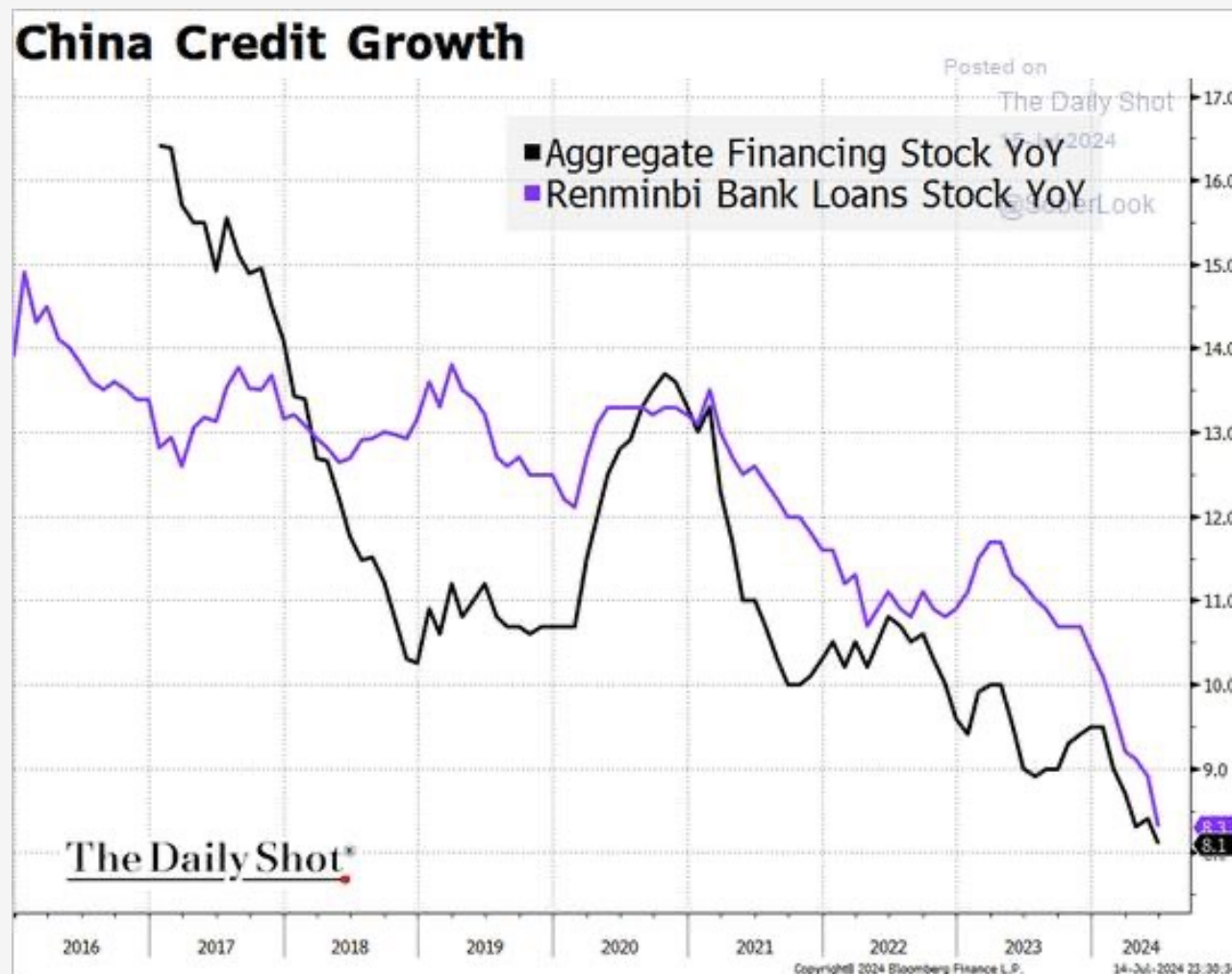


- During my July trip to Tokyo, it was obvious that the yen was exceptionally cheap
- But a 31 July rate hike to 0.25% along with QE tapering caused the yen to strengthen
- Nikkei 225 fell precipitously due to its high proportion of export earnings
- 162 was probably the bottom given that the US-Japan interest rate differential has peaked
- A weak US job market and subdued inflation means



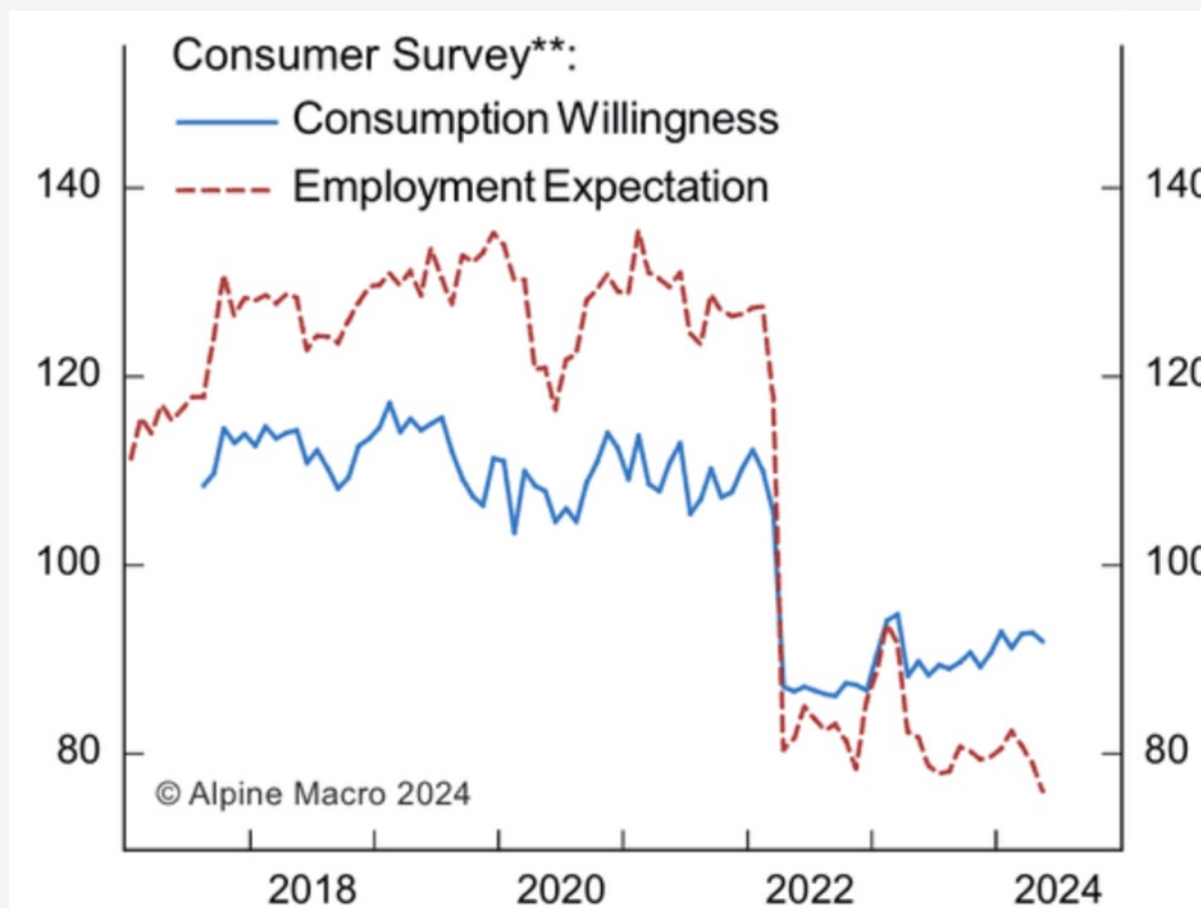
3. Deflation in China

What are PRC policymakers up to?



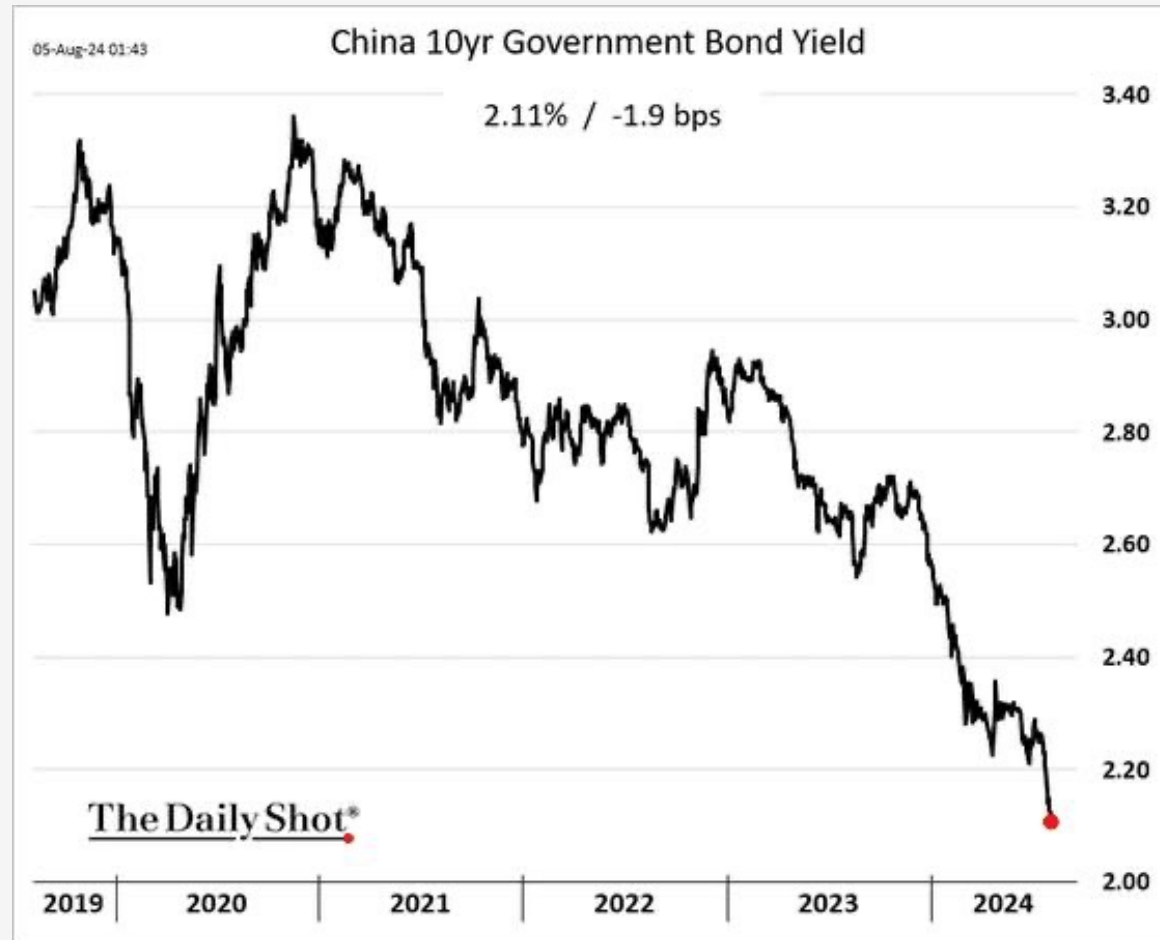
Source: The Daily Shot

Consumer confidence remains weak, even post-COVID



Source: Alpine Macro

Government bond yields tell the story: nominal growth is weak

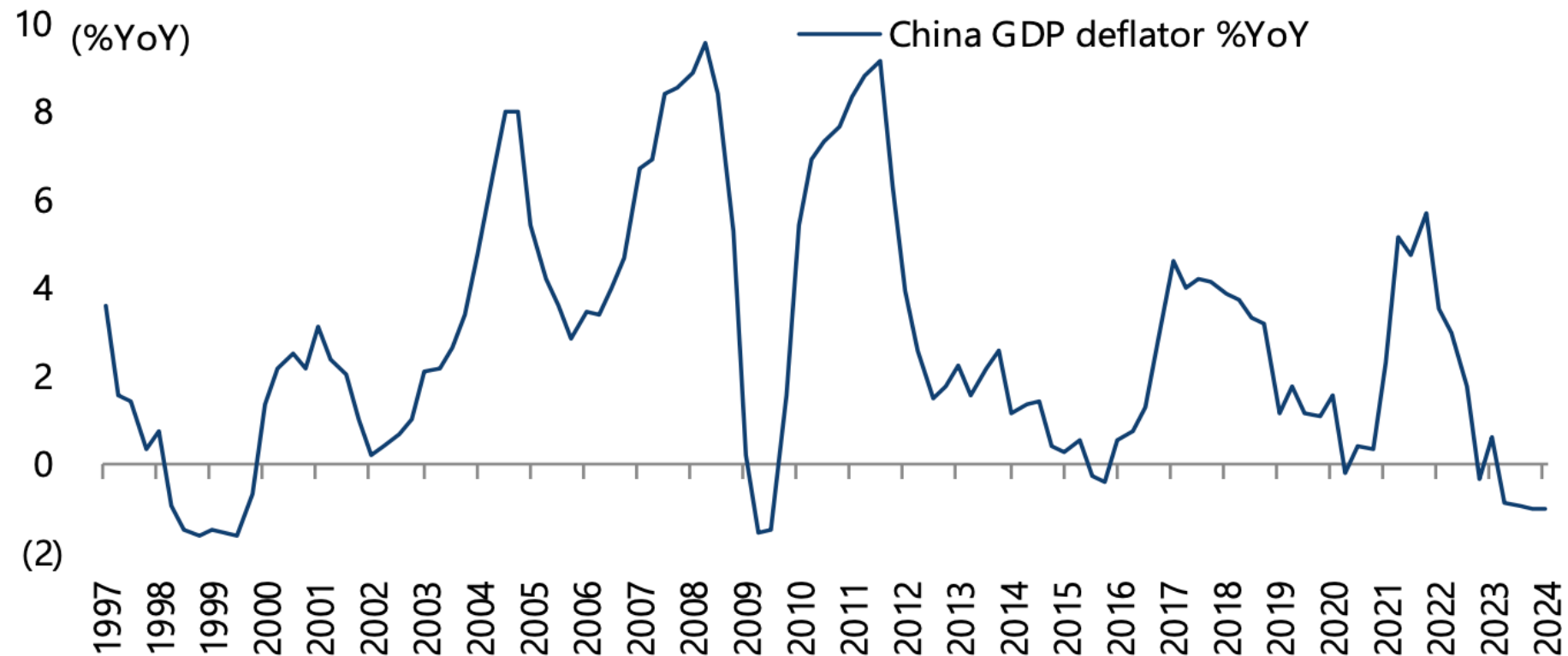


Source: The Daily Shot

We've now seen four straight quarters of deflation in China



China GDP deflator %YoY



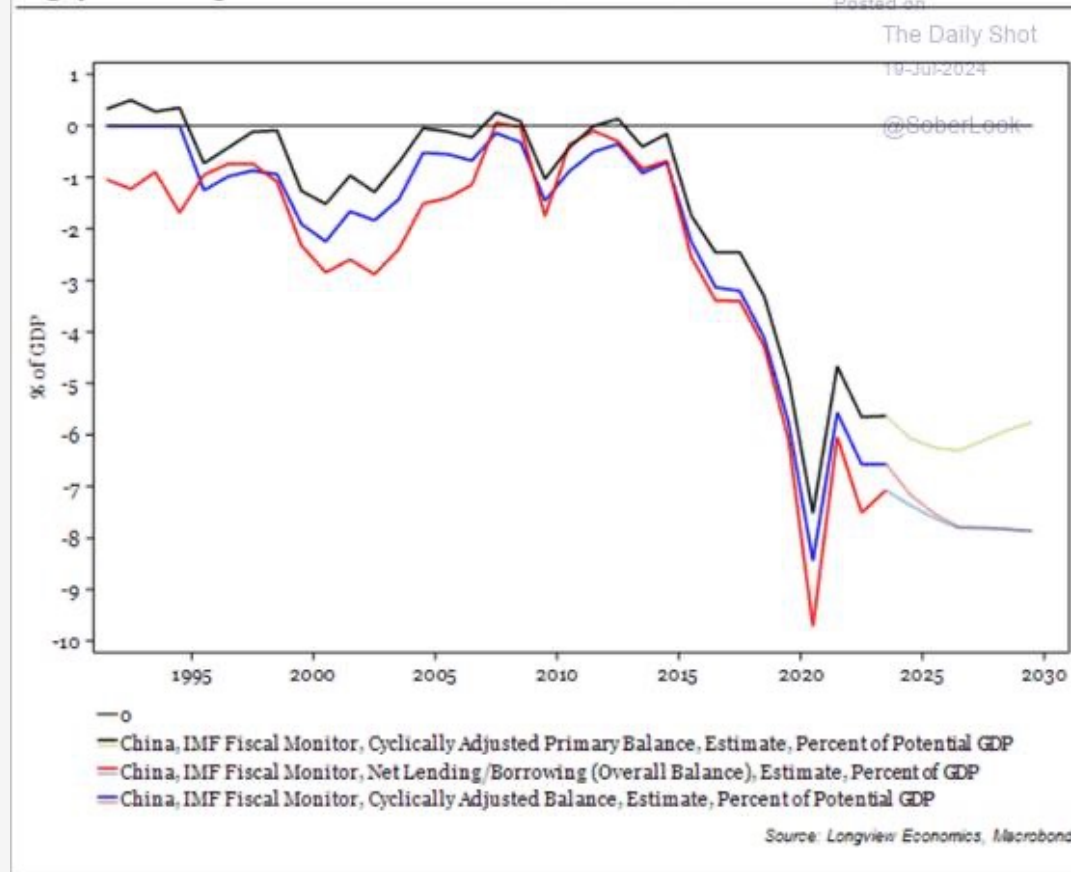
Source: CEIC Data, National Bureau of Statistics, Jefferies

Source: Jefferies

The government is spending but it doesn't seem to be enough



Fig 4: Chinese government fiscal balance (% of GDP)

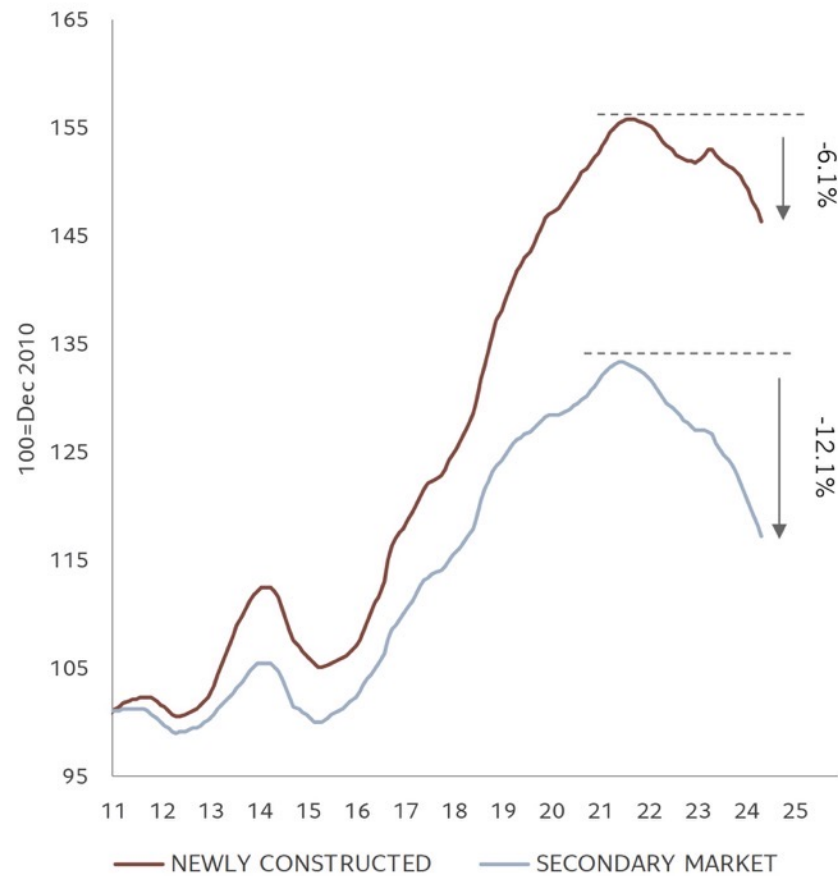


Source: The Daily Shot

The problem is partly a negative wealth effect from property

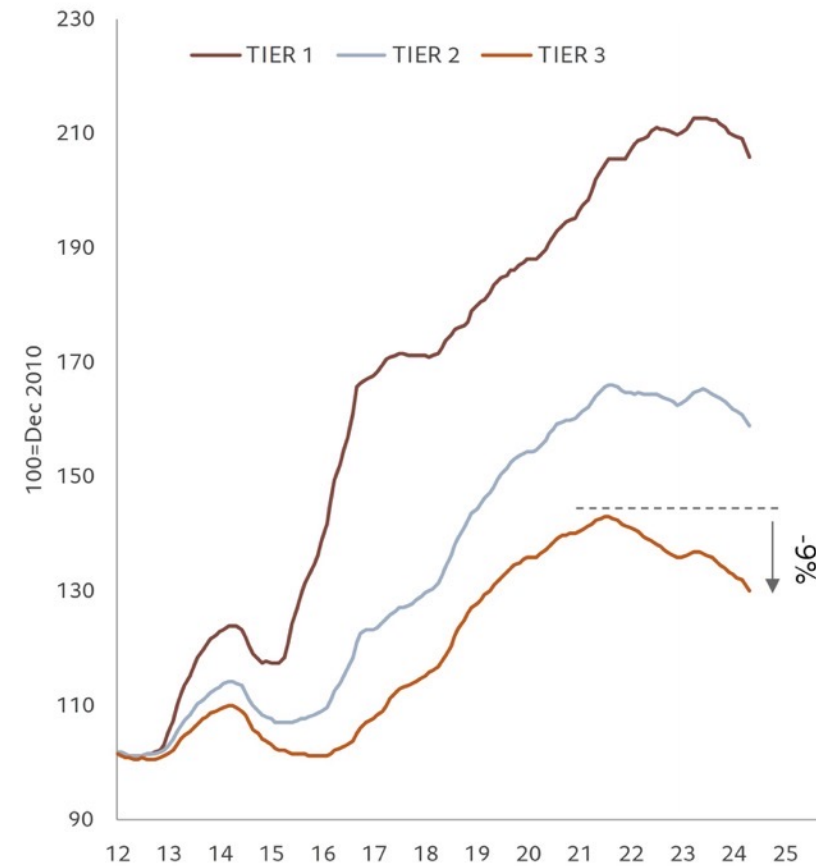


China home prices by market type (100 = Dec 2010)



Source: Pictet Asset Management, CEIC, Refinitiv

China home prices by tier cities (100 = dec 2010)



Source: Pictet Asset Management, CEIC, Refinitiv

Source:
Pictet

Global luxury goods sales is terrible, driven by Chinese weakness

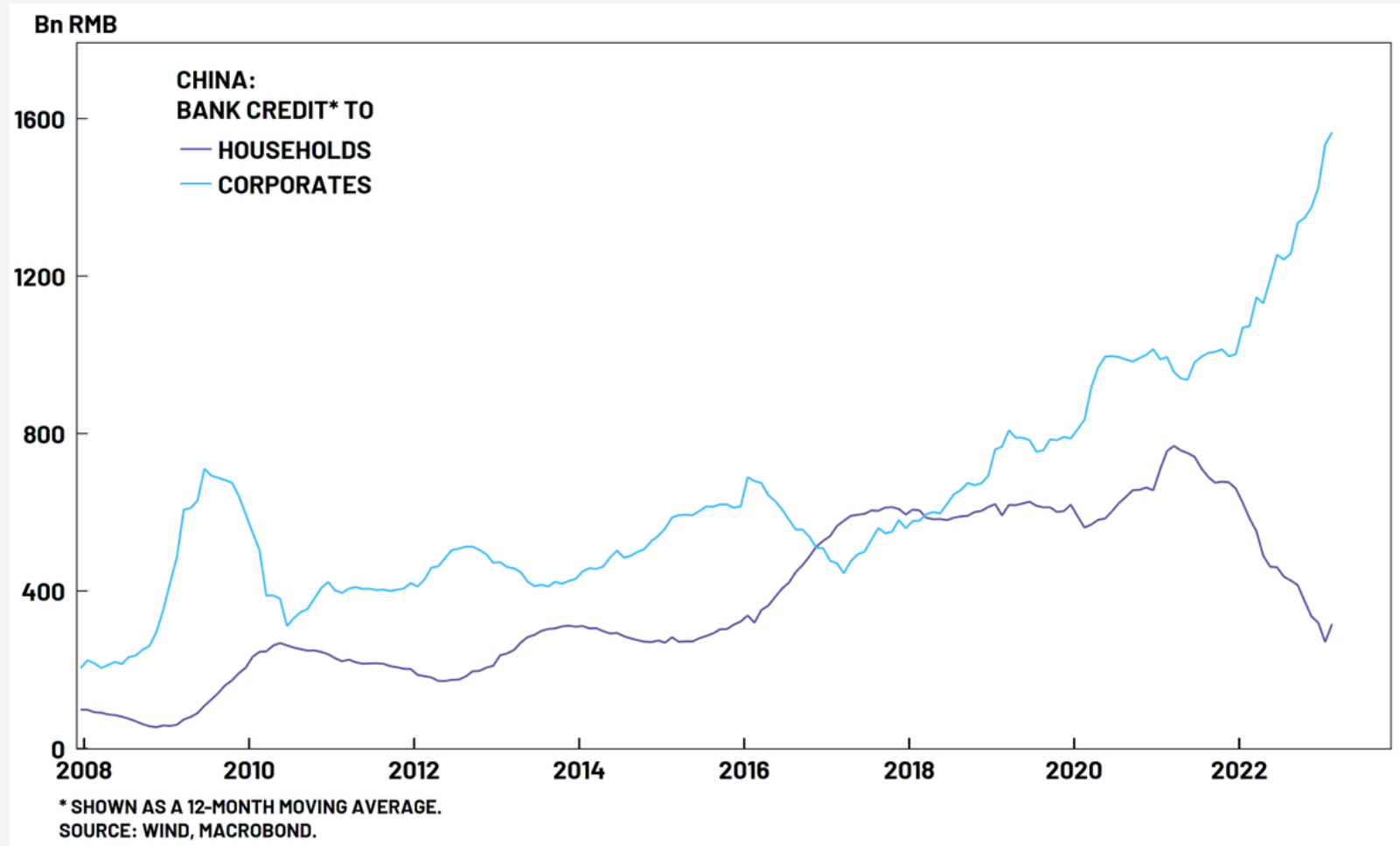


- Capri CEO: "Overall, we were disappointed with our first quarter results as performance continued to be impacted by softening demand globally for fashion luxury goods"
- Swatch Group: "The Group expects the Chinese market (including Hong Kong SAR and Macau SAR) to remain challenging for the entire luxury goods industry until the end of the year."
- L'Oreal: "Overall, we estimate that the market was down between 2% and 3% in the 1st half. Within that, there was a huge divergence in trends. Mass was up slightly, while luxury was down in high single digits"
- Marriott: "The primary change in our four-year outlook is Greater China's updated expectation of negative RevPAR growth for the rest of the year."
- Hermes: "It's very much pegged to the real estate market. And we can see that there is less appetite for buying luxury goods, and people are saving money more than spending money in China. So there's a drop in the footfall of especially aspirational clients, which are particularly hard hit."

Xi Jinping is so far resisting measures to stimulate consumption... considering them wasteful as opposed to building manufacturing

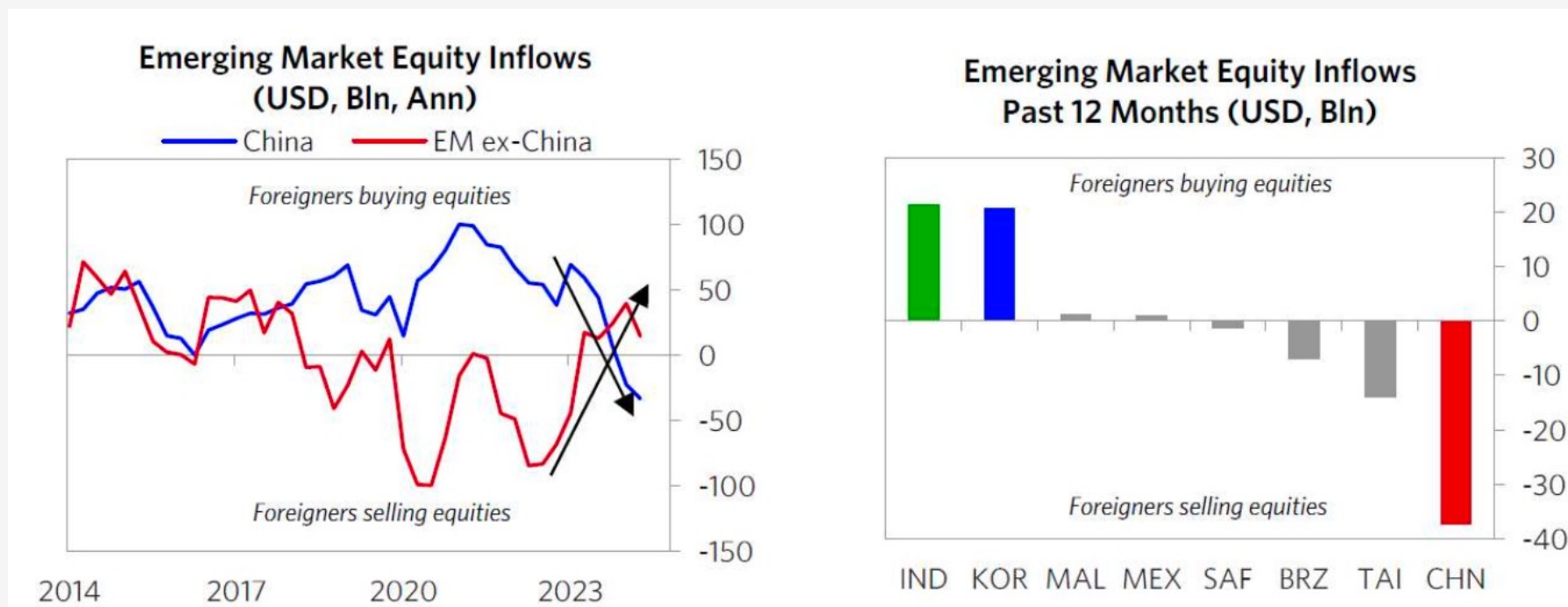


Households are delevering while new loans are going to SOEs



Source: Macrobond

Capital is now flowing out of China into Korea and Indonesia



Source: Bridgewater

I don't blame investors... dilution have detracted from returns



Exhibit 5

The earnings/EPS gap in China



Source: Minack Advisors

Source: MSCI, NBS, NBER; Minack Advisors

Summary



- PRC money supply growth continues to weaken
- Xi Jinping is voting against consumer stimulus, instead directing credit to manufacturing
- Bond yields are suggesting weakening nominal growth
- GDP deflator suggests 4 straight quarter of deflation
- Part of the problem is falling property prices, leading to a negative wealth effect
- This has led to falling collateral values and household deleveraging
- The luxury goods market is now exceptionally weak
- Investors are voting with their wallets towards other emerging markets



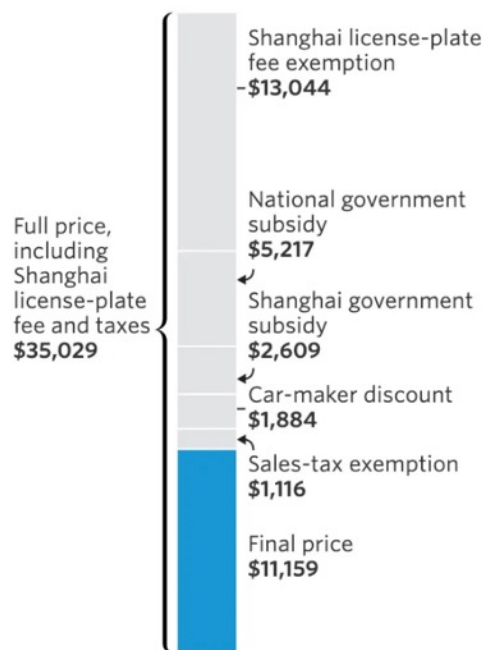
4. Electric vehicles

In China EVs enjoyed consumer subsidies from 2014 onwards



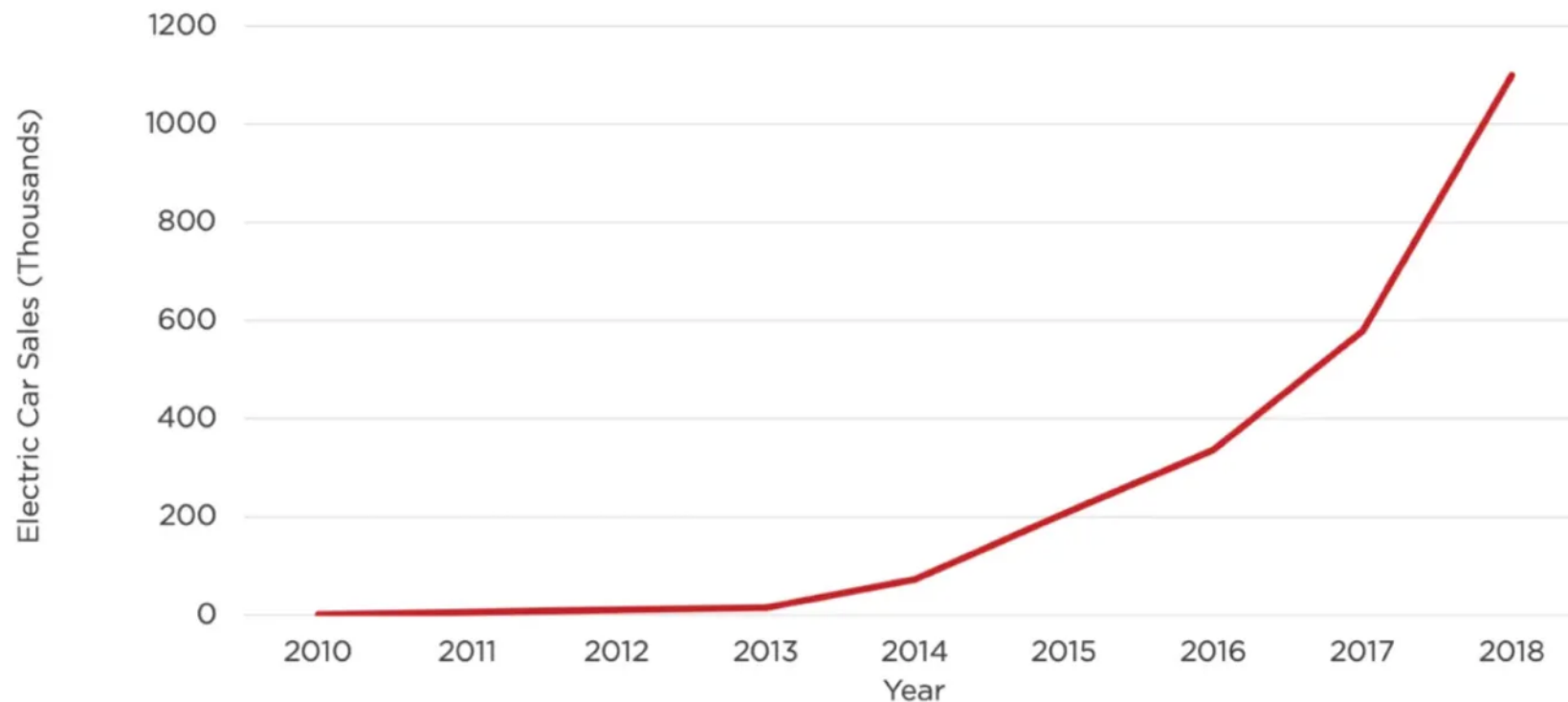
Beijing Bargain

Buyers in Shanghai can get a 68% discount on a Beijing Auto EV160 electric car thanks to various perks and incentives.



Source: Beijing Automotive Industry Corp.

Figure 13-2: Electric Car Sales in China 2010-2018

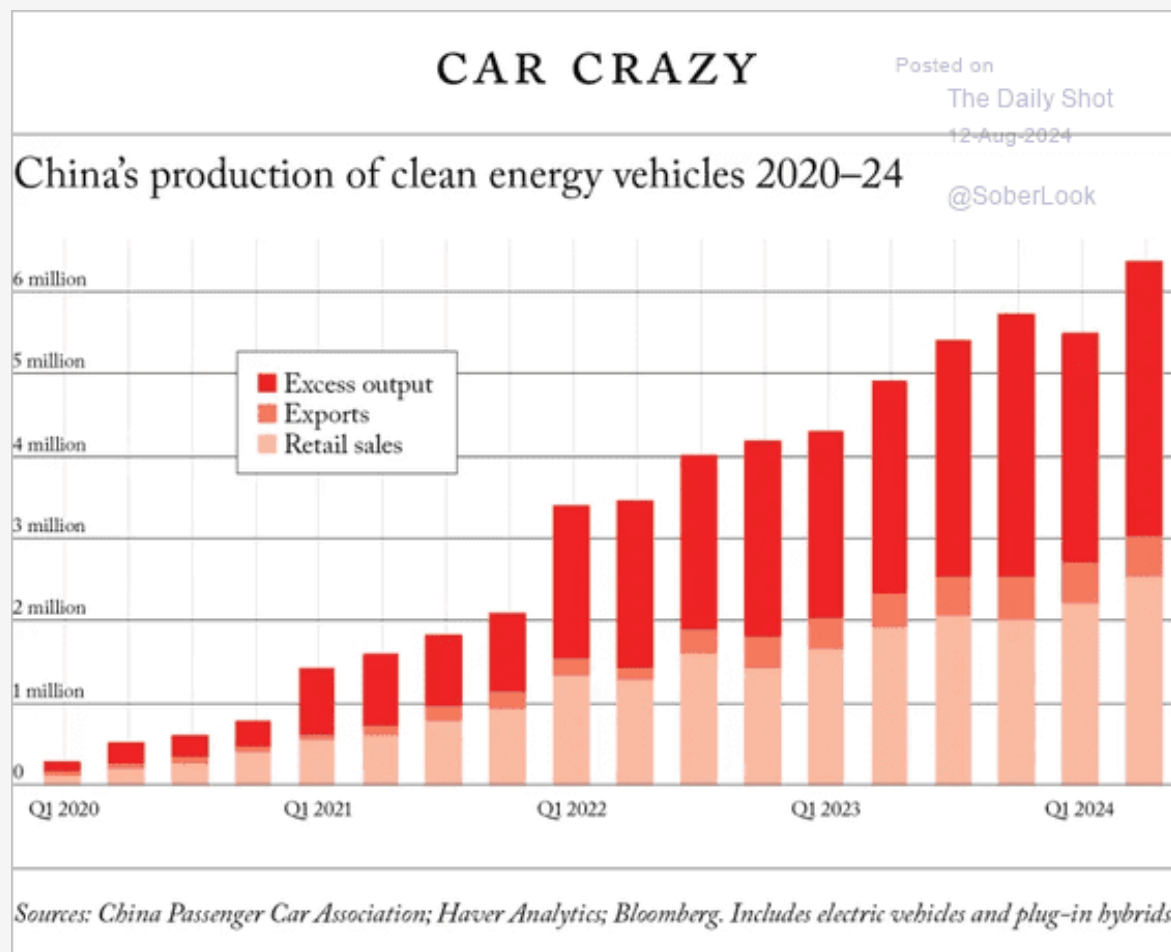


Source: BAIC

From 2019, government pushed ride hailing companies to become electric, then NDRC ordered local gov to remove EV license plate restrictions

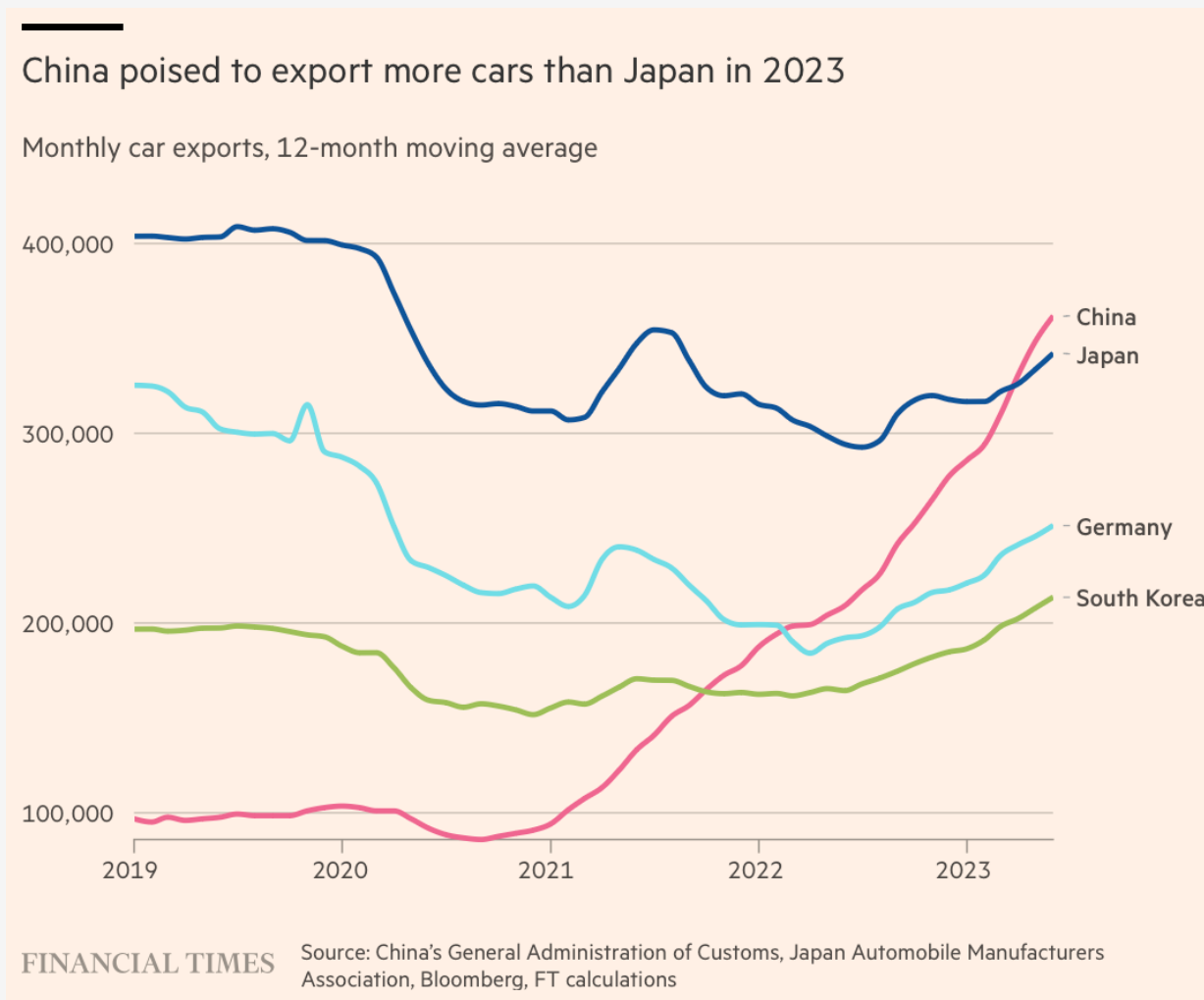


NEV / CAFC credits along with subsidies is now incentivizing supply, causing tremendous production of EVs in China



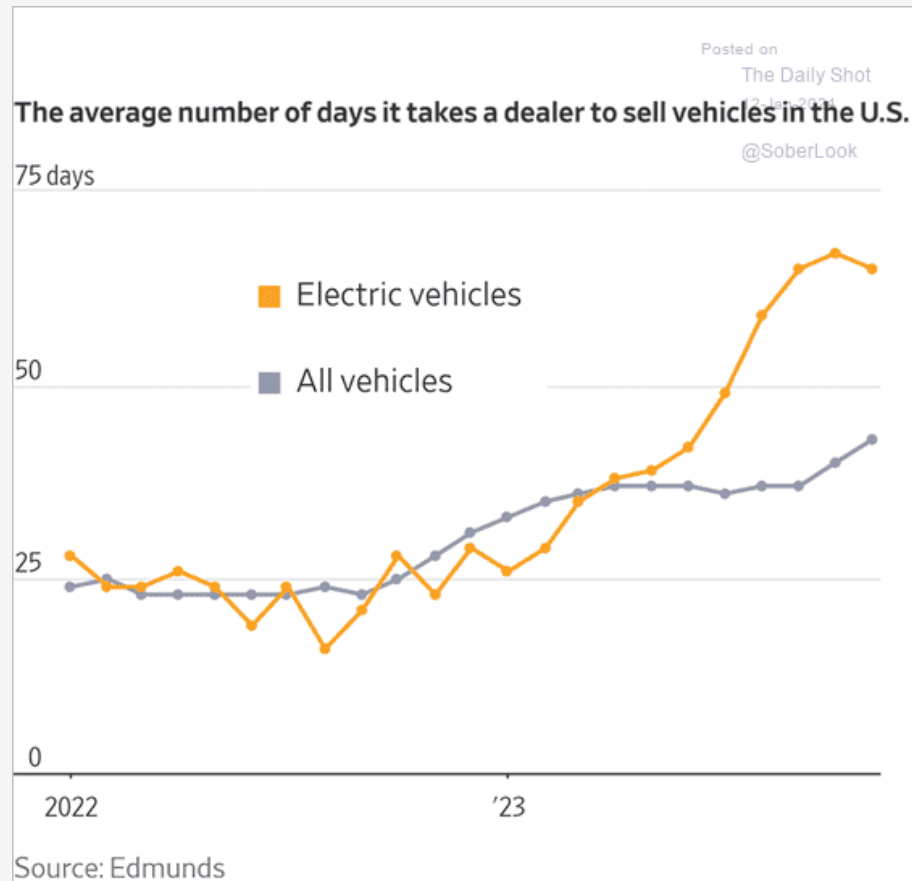
Source: The Daily Shot

There's a narrative that Chinese vehicles are taking over the world... but 1) mostly foreign brand vehicles 2) inventory pile-up



Source: Financial Times

When it comes to EVs, they're not selling well



Source: The Daily Shot, Twitter

Michael Dunne ✓
@dunne_insights

“Thailand now has 490,000 unsold EVs, according to the Electric Vehicle Association of Thailand (EVAT), equivalent to 63% of all vehicles the country turned out in the past 12 months.”

Thai subsidies for Chinese EV makers wreak havoc

Thai subsidies for Chinese EV makers wreak havoc on auto sector

From asia.nikkei.com

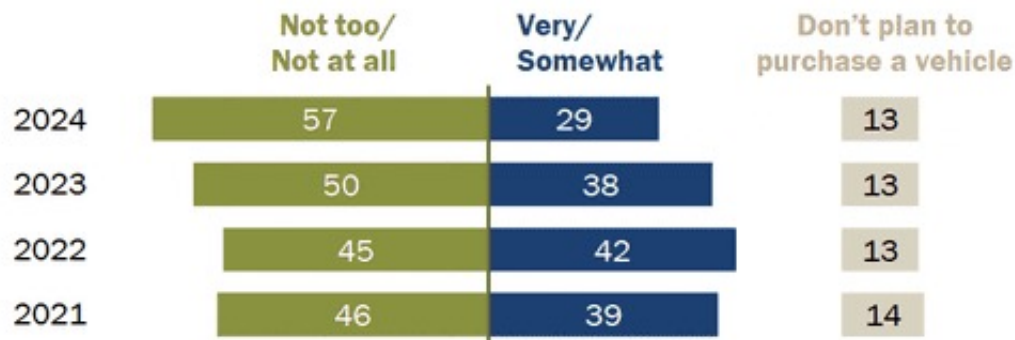
11:45 AM · Jul 26, 2024 · 42.3K Views

Elsewhere, consumers are becoming more negative about EVs, too



Declining share of Americans say they are likely to consider buying an electric vehicle

% of U.S. adults who say that the next time they purchase a vehicle, they are ___ likely to seriously consider purchasing an electric vehicle

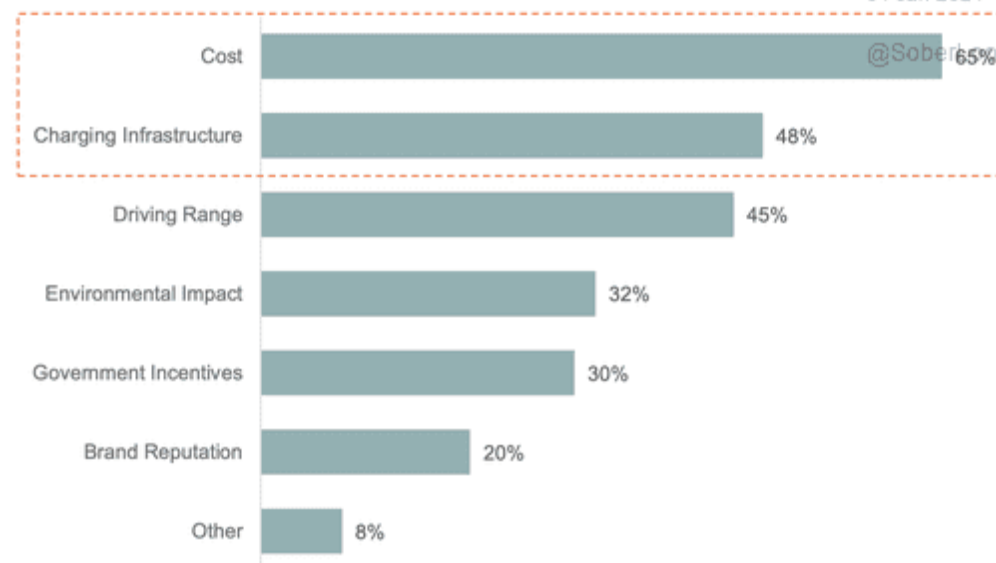


Note: Respondents who did not give an answer are not shown.
Source: Survey of U.S. adults conducted May 13-19, 2024.
"How Americans View National, Local and Personal Energy Choices"

PEW RESEARCH CENTER

WHAT FACTORS WOULD INFLUENCE YOUR DECISION TO PURCHASE AN ELECTRIC VEHICLE? (SELECT ALL THAT APPLY) (% OF RESPONDENTS)

The Daily Shot
04-Jan-2024



Note: N = 1,002
Source: Global X, December 2023

GLOBAL X
by Mirae Asset

© Global X Management Company LLC

Reasons to be skeptical about fully electric vehicles



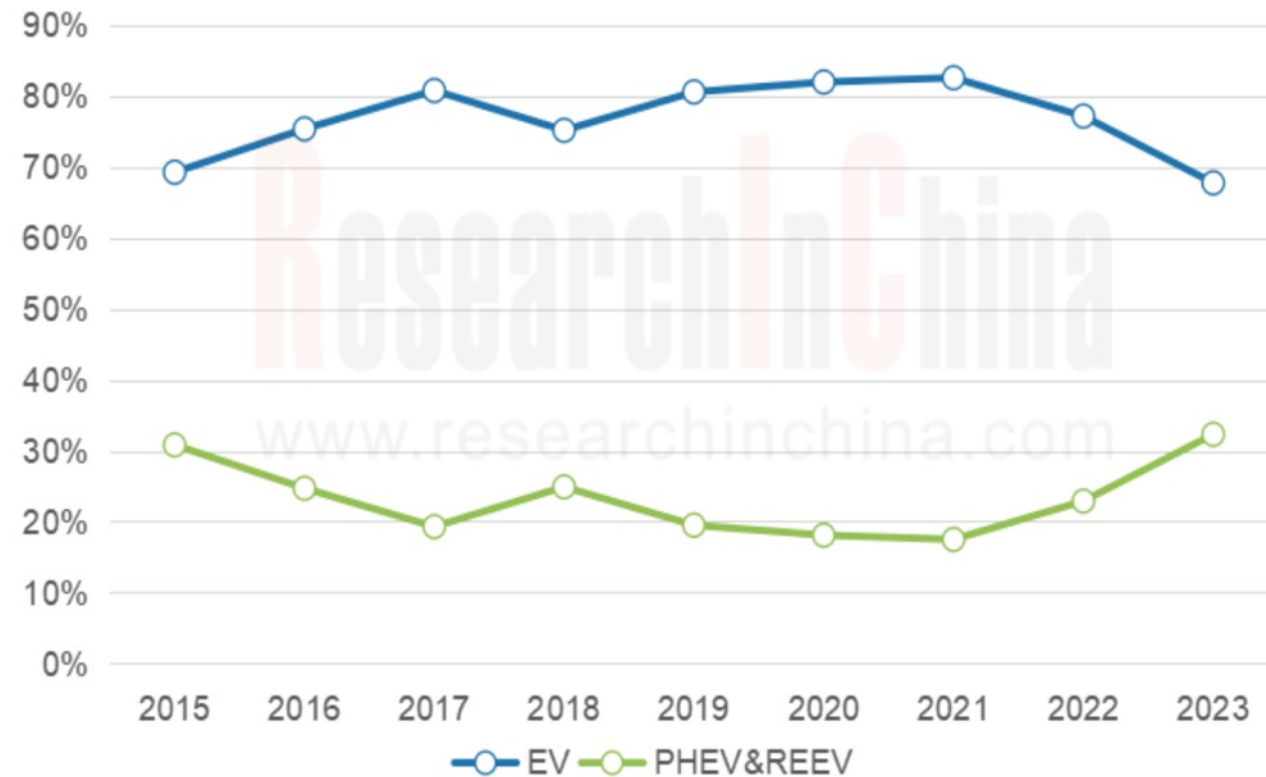
- Cost way higher than ICEs so require constant subsidies
- Batteries depreciate twice as fast as engines
- Long charging times reduce the attractiveness of charging stations
- Normal-priced EVs still have low range
- CO2 emissions profile just marginally better than hybrids and worse than public transport
- Fire hazards as it's more difficult to put out battery cell fires
- Geopolitical concerns among EU nations and the United States



Even in China, sales of NEVs is shifting towards hybrids



**Sales Structure of New Energy Passenger Cars (EV, PHEV & REEV)
in China, 2015-2023**



Source: Research in China

If hybrids become popular, platinum group metals & Astra will win



Source:
TradingView

Summary

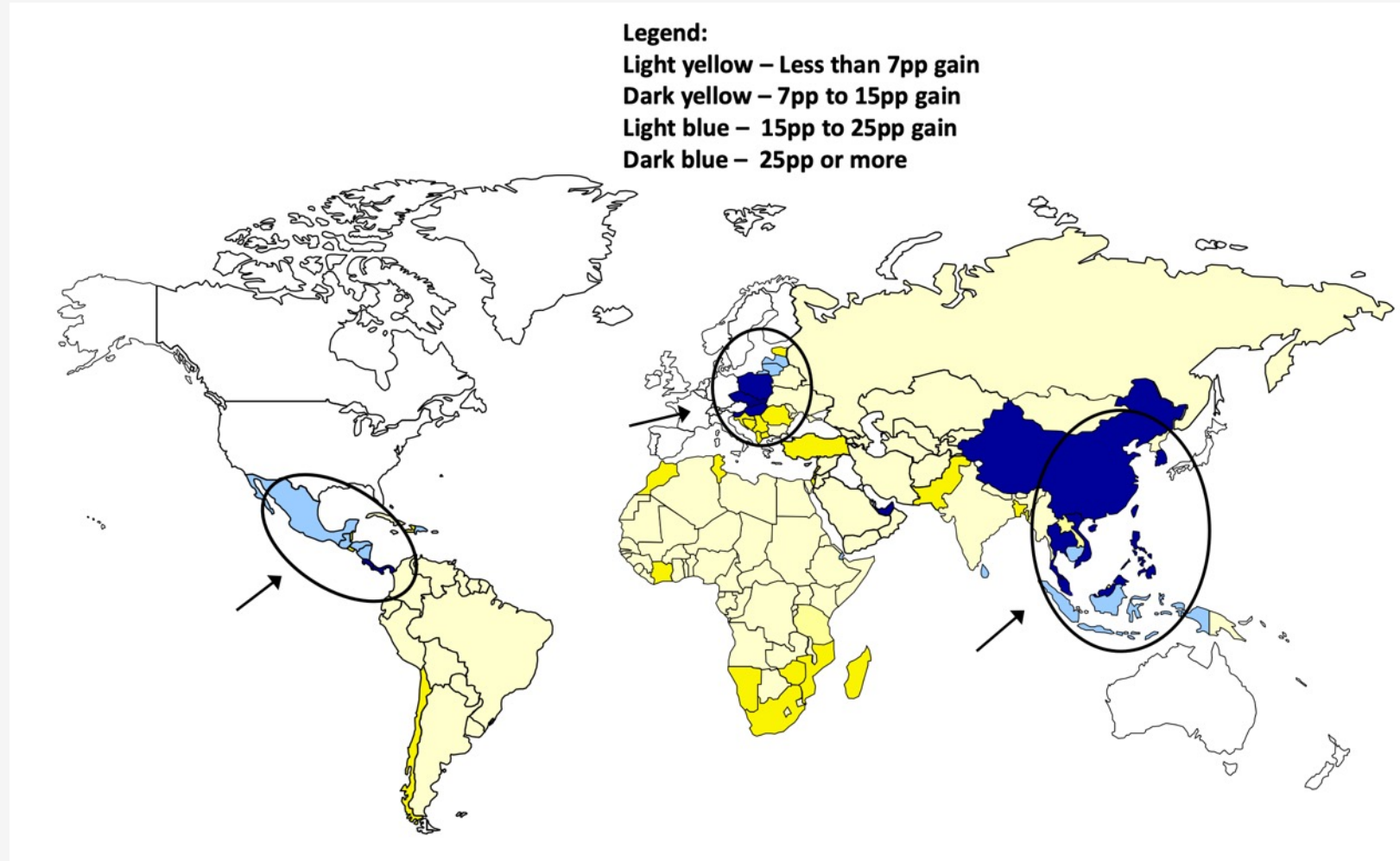


- The popularity of EVs has not been organic but driven by Soviet-style 5-year plans
- China's vehicle exports are booming, but mostly foreign brands like Tesla / Japanese
- EVs are proving difficult to sell, piling up as dealer inventory
- They're simply not that convenient compared to hybrids or ICEs, at least not given the price
- If hybrids continue to take market share, then platinum group metals and Astra Int'l will win



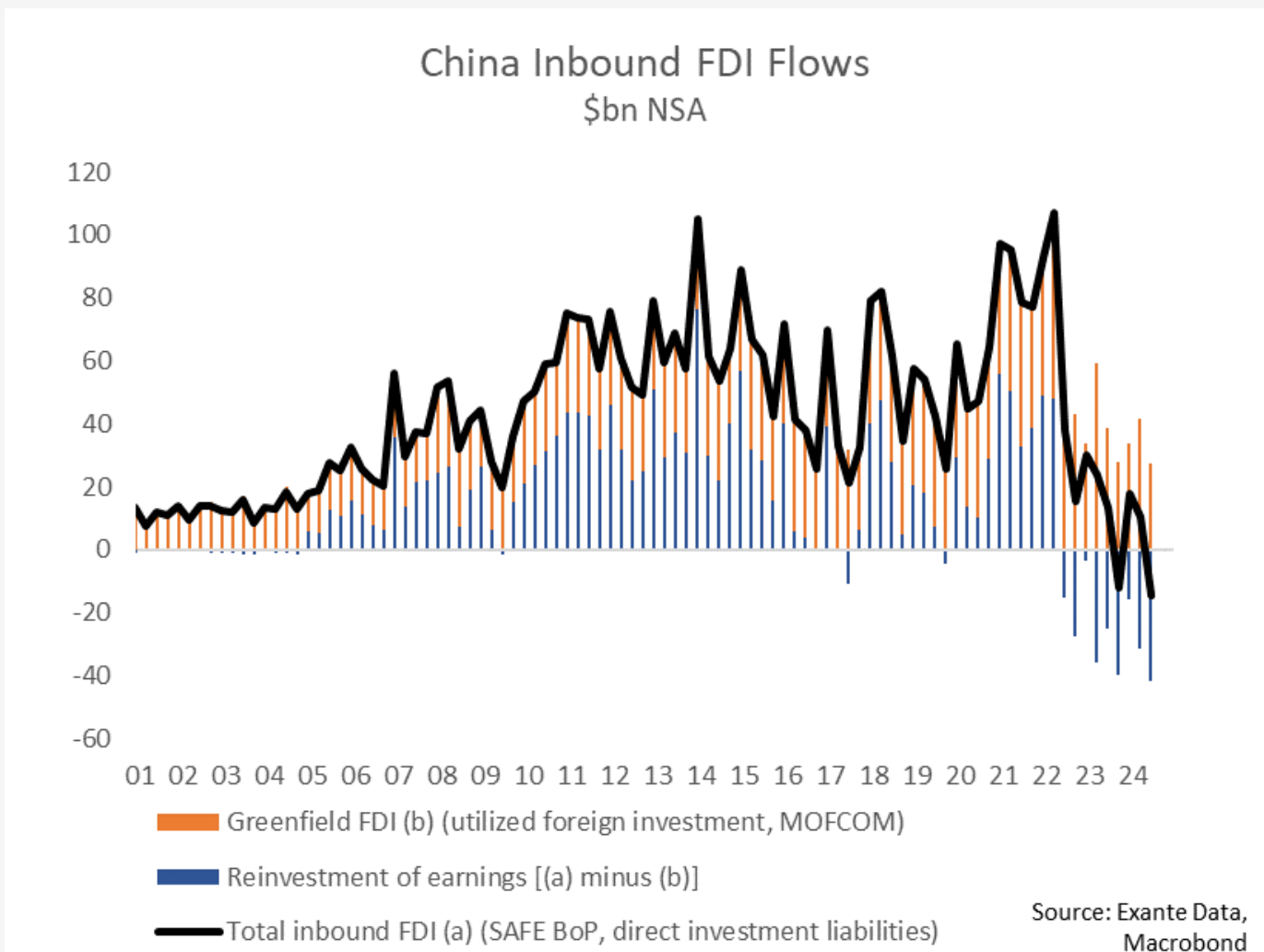
5. Malaysian FDI

Asia has become the manufacturing hub of the world since 1990



Source:
Emerging
Advisors

China's FDI has turned negative

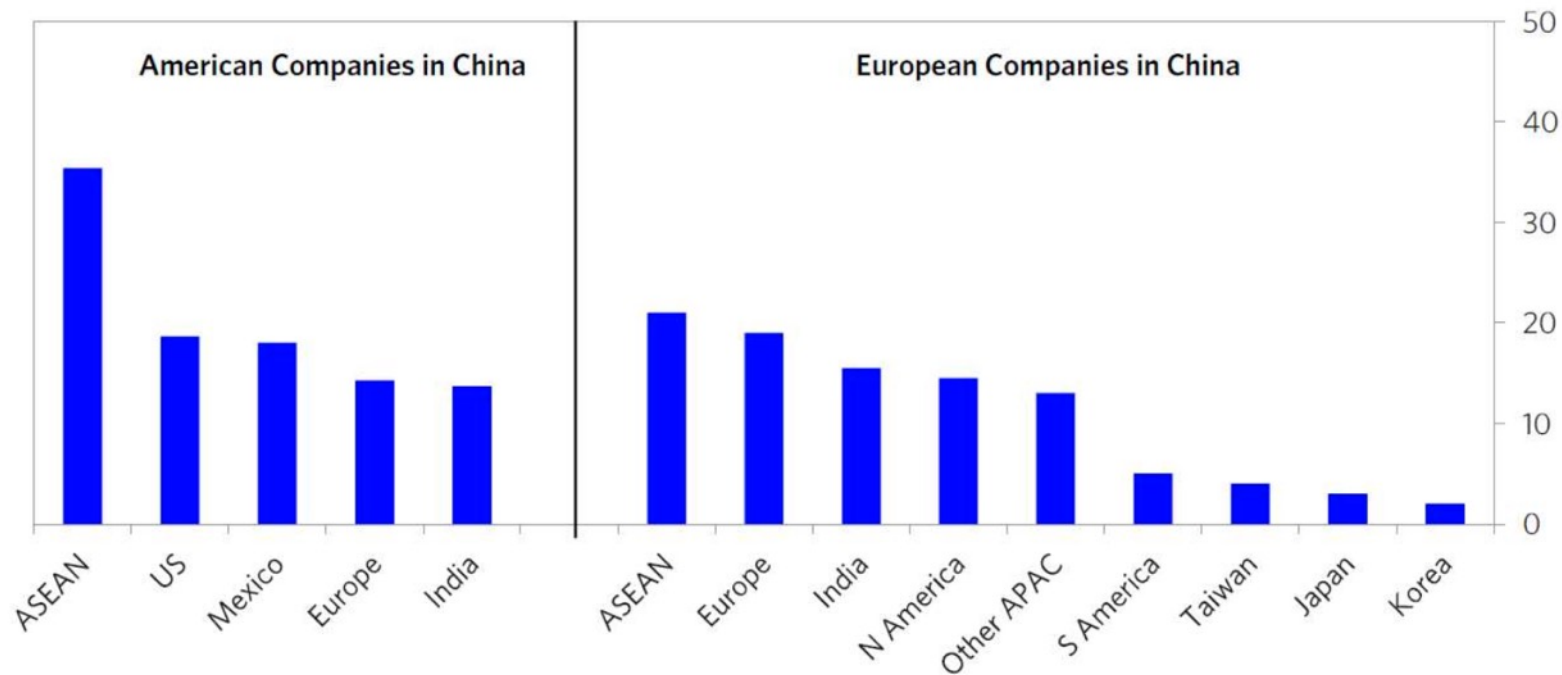


Source: Exante Data

ASEAN is the prime destination for new FDI

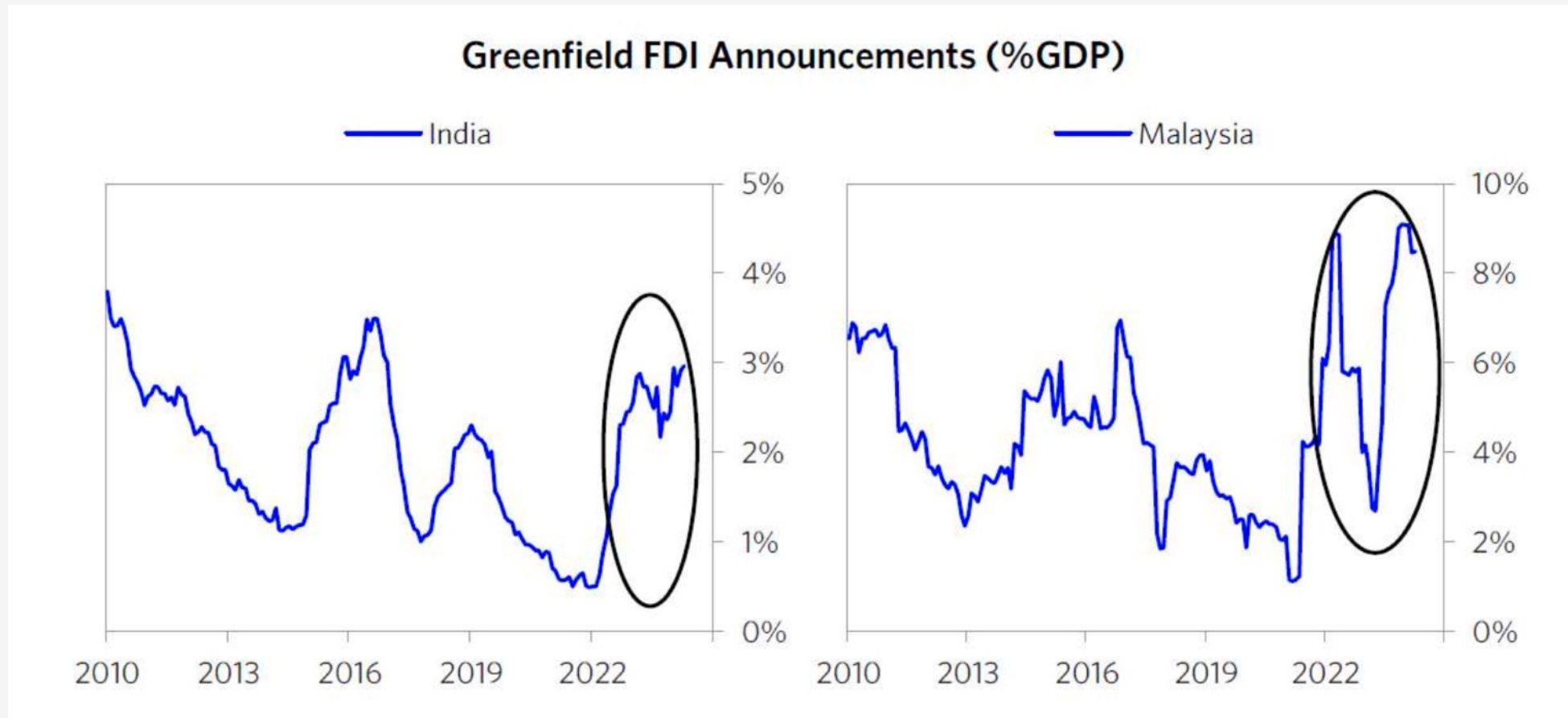


Destinations for Companies Shifting Investments Away from China (%Responded)



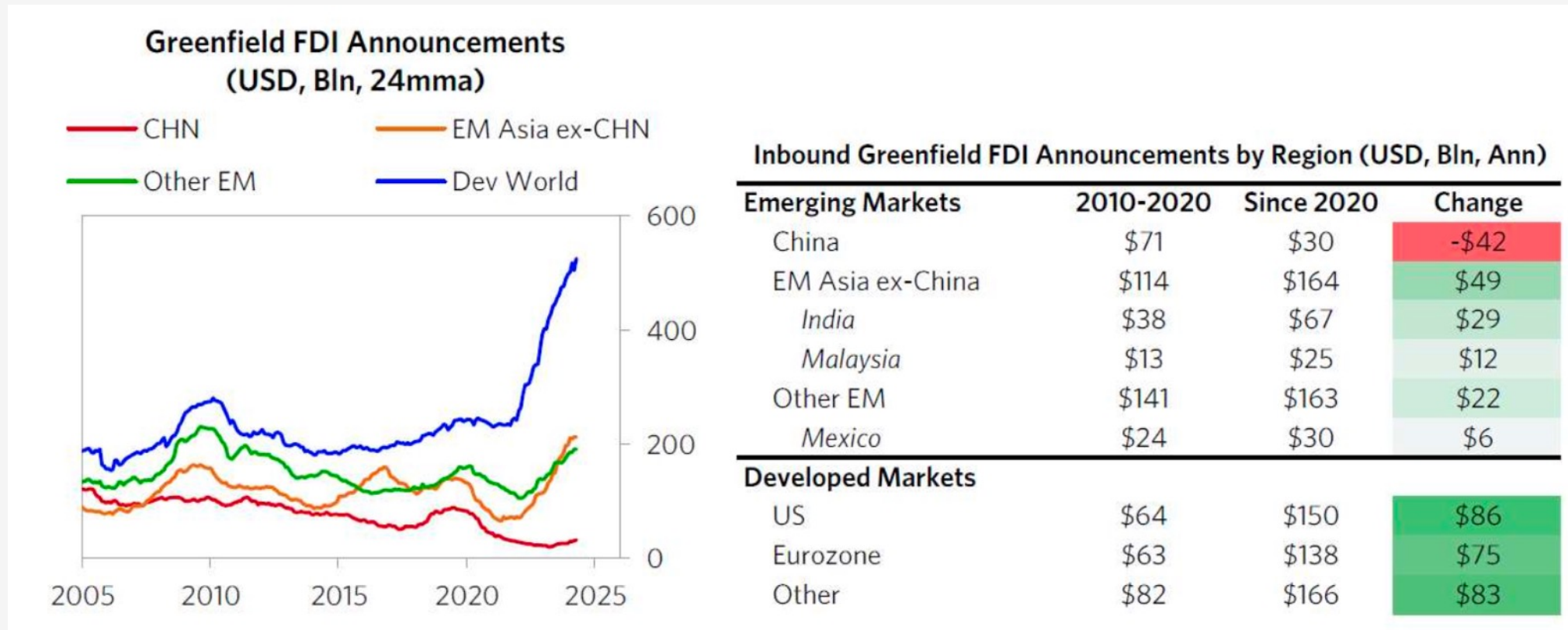
Source: American Chamber of Commerce in Shanghai, European Chamber of Commerce in China, as quoted by Nomura

India and Malaysia are the two favored nations for new FDI



Source: Bridgewater

Greenfield FDI into Malaysia are large vs the population



Source: Bridgewater

New investments are announced every other day



Texas Instruments announces \$3bn manufacturing investment in Malaysia

US-based semiconductor manufacturer Texas Instruments has announced a double deal in Malaysia, worth just over \$3bn.

Richard Gardham | 21 June, 2023

Share



Malaysia has received yet another boost with the news of a mega-investment from Texas Instruments. Credit: thetahoguy via Shutterstock.

Senai Airport City Attracts RM7.5 Bln Investments

09/07/2024 02:52 PM



Credit: Onn Hafiz Ghazi's Facebook

JOHOR BAHRU, July 9 (Bernama) -- Senai Airport City Sdn Bhd, a wholly owned subsidiary of MMC Corporation Bhd (MMC), attracted RM7.5 billion in investments via 150 investors.

Johor Menteri Besar Datuk Onn Hafiz Ghazi said the investors include Wiwynn Technology Service Malaysia Sdn Bhd, Hershey, Mercedes-Benz, DHL, Dyson, FedEx, Haitian, Fiffy and Supermicro. They are offering 28,000 job opportunities.

Malaysia boasts chip clout as Infineon opens \$10 billion factory

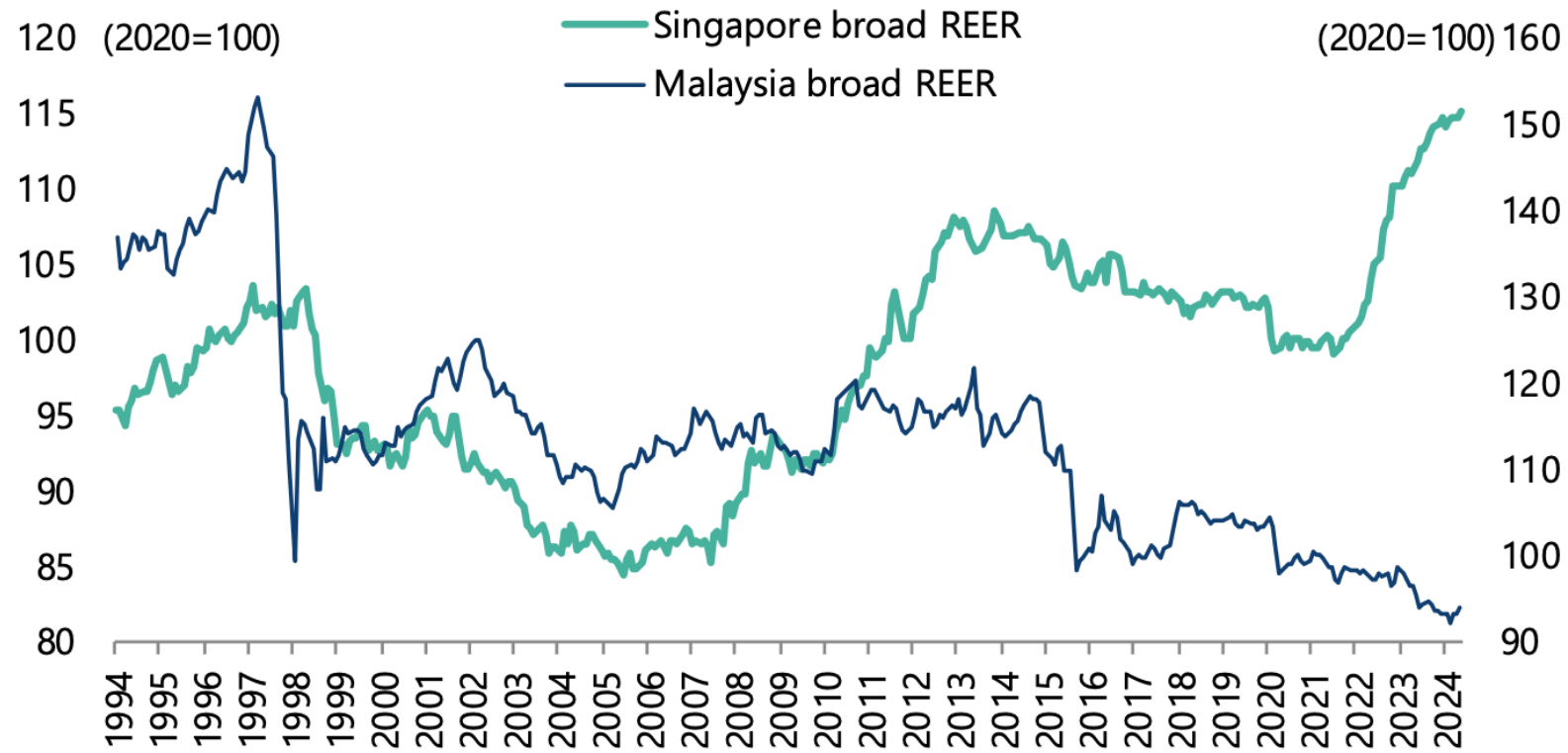


The new plant will focus on making power semiconductors that can help with decarbonisation in automotive, industrial and data centre fields. PHOTO: BLOOMBERG

The attractiveness of Malaysia is heightened by the weak Ringgit

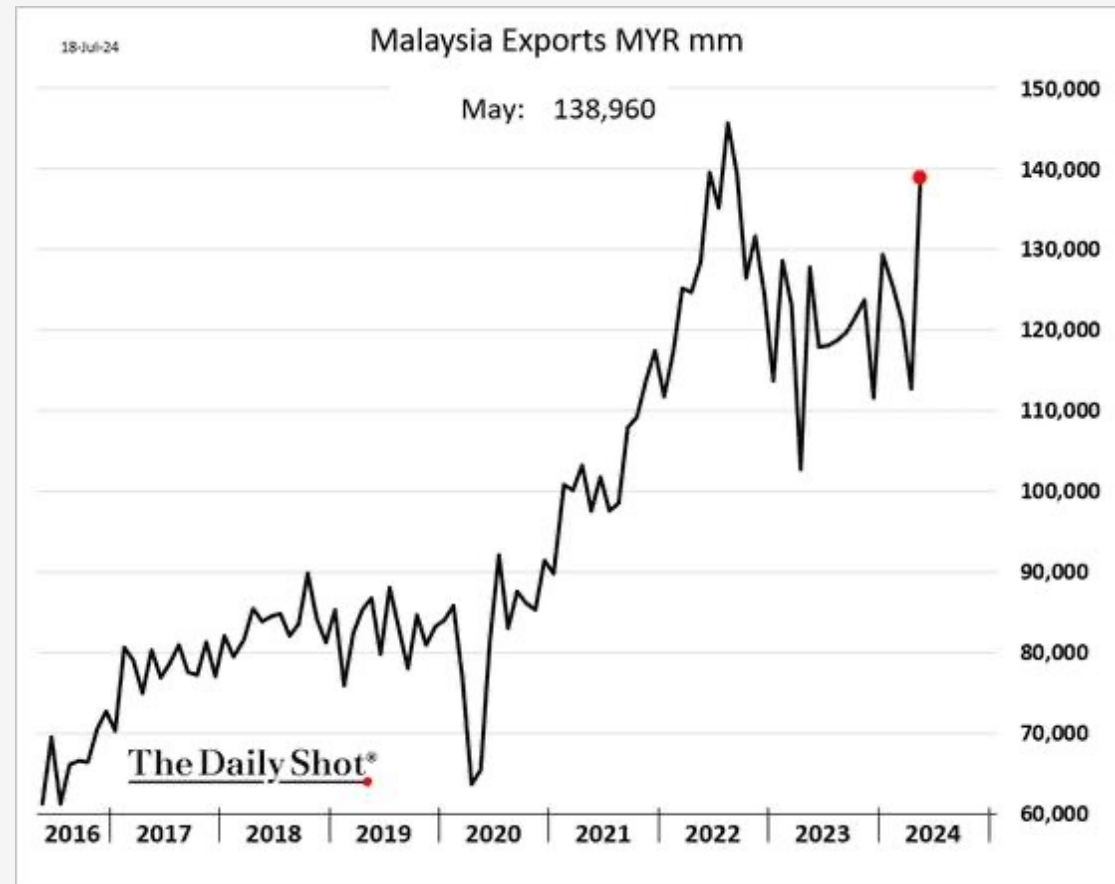


Singapore vs Malaysia broad real effective exchange rates (REER)



Source: BIS, Jefferies

Malaysian export numbers are now booming



Source: The Daily Shot

And finally the currency is catching a bid



Source:
Bloomberg

Summary



- Asia is the manufacturing hub of the world
- With complex supply chains, short distances matter
- China is turning inwards and FDI is moving elsewhere
- Malaysia and India seem to be favored by multinationals
- The weak Ringgit and strong infrastructure help Malaysia compete
- The capex boom is likely to benefit the local economy



6. Vietnamese communism

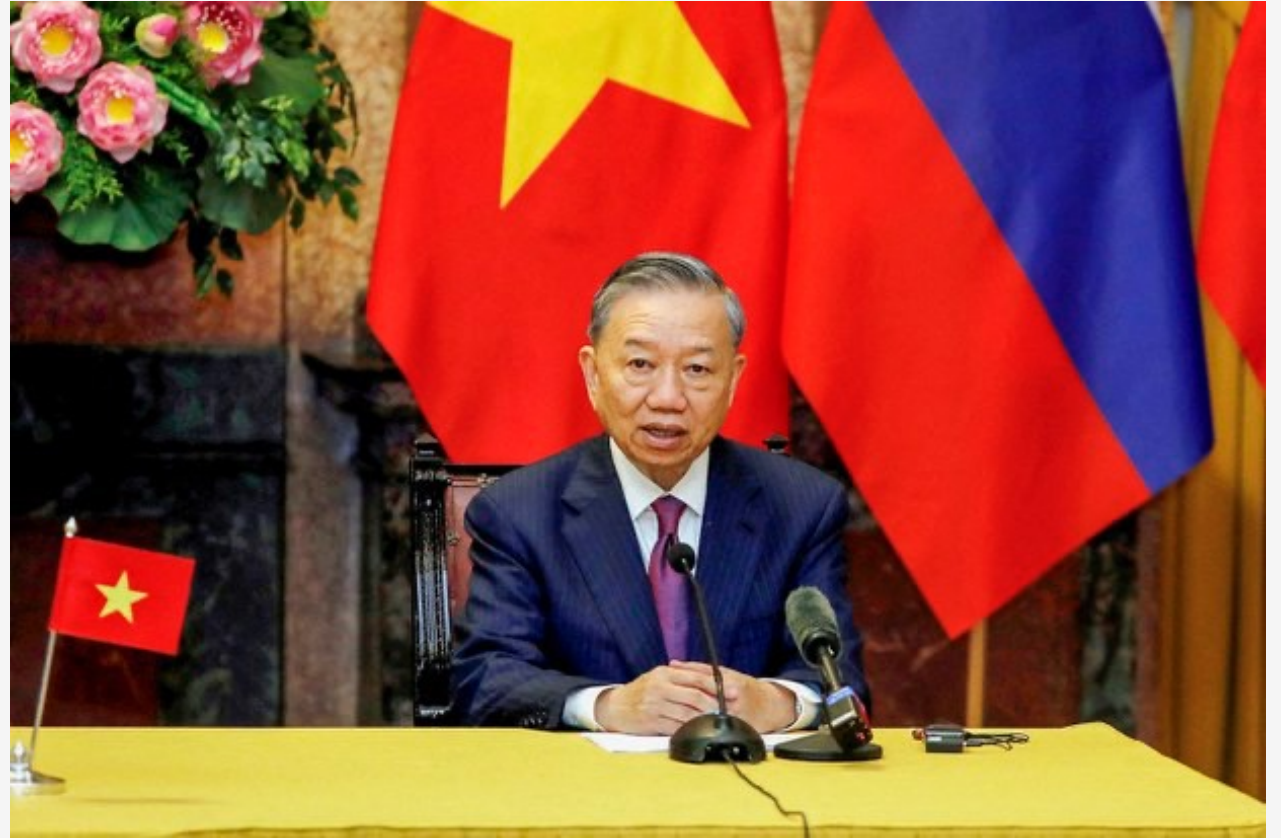
Nguyễn Phú Trọng out. Tô Lâm in.



Nguyễn Phú Trọng



Tô Lâm



The implications of To Lam's ascent to power



- Nguyen Phu Trong died recently due to “old age and serious illness”
- To Lam has taken over as General Secretary and President
- He has a background in public security and will consolidate power
- Vietnam used to have checks and balances (“four pillars”), now no longer the case
- To Lam will likely stay in power even after 2026, just like Xi Jinping
- He’s likely comfortable working with Vladimir Putin and Xi Jinping
- The Politburo is stacked with Lam’s allies
- Analysts are predicting a more authoritarian climate and tighter restrictions



Vietnam likely to become a PRC ally, just like Cambodia, Myanmar, Pakistan and Russia



"I am willing to establish good working relations and a personal friendship with you and jointly lead the creation of a China-Vietnam community of a shared future"

A new iron curtain is being formed... best to stay
on one side



Summary



- New Communist Party of Vietnam General Secretary To Lam took over on 3 August 2024
- He comes from a public security background
- Vietnam is likely to turn more authoritarian, in line with the precedent set by Xi Jinping
- He's said to be on good terms with Putin and Xi
- There's a high probability that Vietnam will end up with the Russia-Iran-China axis if and when a new Iron Curtain is being formed



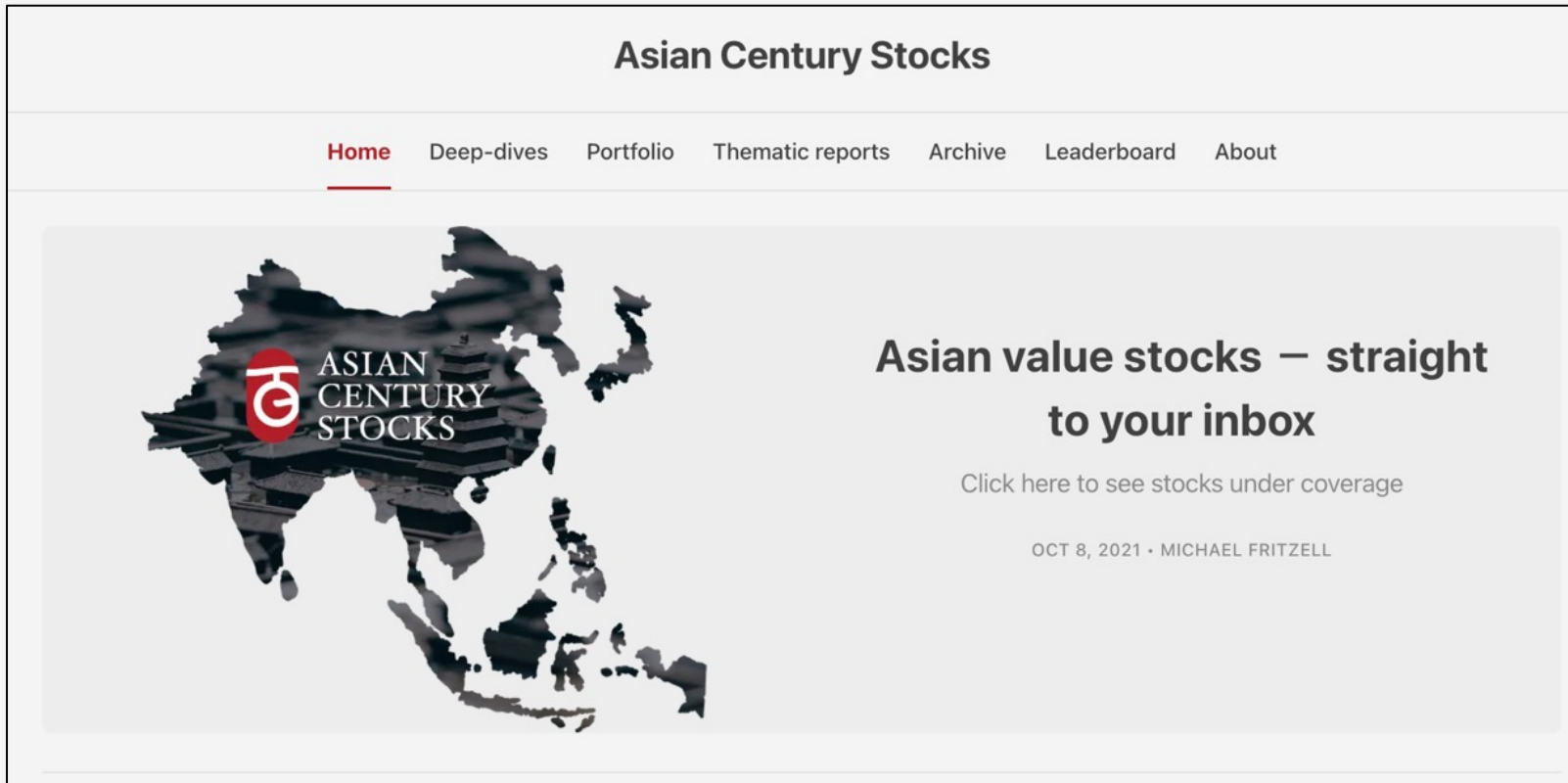
Final conclusions

Conclusions



- Lower interest rates post the presidential election will cause weaker USD
- A weaker USD tends to be a precondition for flows into Asia
- It helps that Hong Kong, Philippines, Singapore equities are cheap
- The yen probably bottomed at 162 and will slowly strengthen over time
- China remains mired in deflation and policymakers avoiding stimulus
- That's fundamentally negative for luxury goods sales
- Hybrids seem to be favored by consumers at the expense of BEVs
- Greenfield FDI is turning away from the PRC to India and Malaysia
- Vietnam is likely turning back into a more authoritarian regime under To Lam

Thank you!



Stocks discussed recently:

- Astra
- Lion Rock
- Yakult
- Samsonite
- Pacific Textiles
- Fu Shou Yuan
- MTR Corporation
- Kansai Paint

www.asiancenturystocks.com