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Structural Themes Shaping the Opportunity in ASEAN Equities

INSIGHTS

Favorable demographics, combined with a number of unique investment themes, are creating a positive backdrop for ASEAN's equity markets.



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The Association of Southeast Asian Nations (ASEAN) is a unique investment region that primarily offers investors exposure to southeast Asian markets including Singapore, Indonesia, Malaysia, Thailand, Philippines and Vietnam. There are a number of supportive demographic trends that are driving ASEAN's positive longer-term picture, which we believe have the potential to stimulate economic growth. For one, ASEAN today has the third-largest aggregated population in the world, behind China and India. The region's GDP was also among the fastest growing in the world in 2022, estimated at 5.5%.¹ This large and relatively young population, and an increasingly wealthy middle class, are further contributors, and indeed already driving exciting changes in consumption patterns.

These demographics, combined with a number of investment themes unfolding in the region—from the evolution of consumption behaviors, to supply chain enhancements, to technological upgrades, to the green transition—are presenting compelling opportunities in ASEAN companies. While these themes remain nascent compared to both developed and emerging economies, their development will likely accelerate given the deeply integrated logistical networks across ASEAN—with the region perhaps set to closely follow the developmental roadmap of predecessors such as China, Korea and Japan.



ASEAN is an economic union of member states in Southeast Asia designed to target cooperation and accelerate economic growth. It includes some of the fastest-growing economies in the world, and features an estimated population of more than 650 million.

1. Source: Asian Development Bank. As of January 2023.

Manufacturing and Supply Chain Upgrades

ASEAN offers investors access to a host of internationally competitive industries, which amid the heightened tensions in global geopolitics and the inherent fragility of concentrated sourcing, have benefited as global supply chains have shifted from a “just-in-time” to a “just-in-case” approach. Many industries today have complex supply chains and face significant pressure to achieve a cost advantage by sourcing materials and conducting their activities across multiple geographies, making interconnectivity the primary key to success. Within this context, ASEAN’s geographic position allows for access to Europe, the U.S. and China via traditional shipping routes.

To capitalize on this shift, many ASEAN countries have introduced structural reforms, such as corporate tax cuts to enhance economic competitiveness, while also boasting a large and cheap labor base

relative to global peers (Figure 1). Ultimately, this combination has made ASEAN nations a low-cost manufacturing hub—which has provided companies with an opportunity to diversify and develop a resilient supply chain, while reducing overheads in the long run.

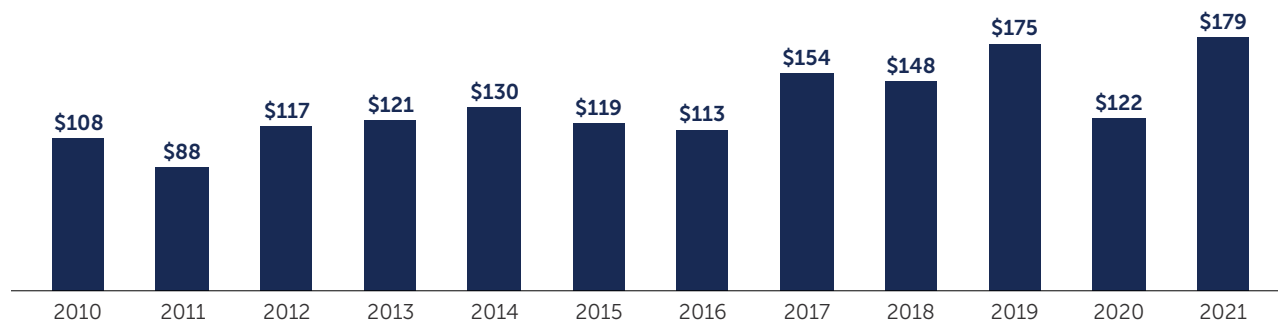
This favorable dynamic has driven global foreign direct investments (FDI) toward ASEAN nations over the years. More specifically, the region’s share of global FDI rose from a pre-pandemic annual average of 7% in 2011–2017, to 12% in 2020–2021, with a broad-based rise in manufacturing investments specifically in semiconductors, electronics and electrical vehicles (EVs) (Figure 2). Further, the ASEAN manufacturing supply chain has been a beneficiary of the escalating geopolitical tension between China and the U.S., with both nations steadily increasing their investment flows into ASEAN countries.

Figure 1: ASEAN Offers Relatively Lower Minimum Wages (US\$/Month)



Source: International Labour Organization. As of 2021.

Figure 2: ASEAN Sees Rising Global FDI (US\$ Billions)

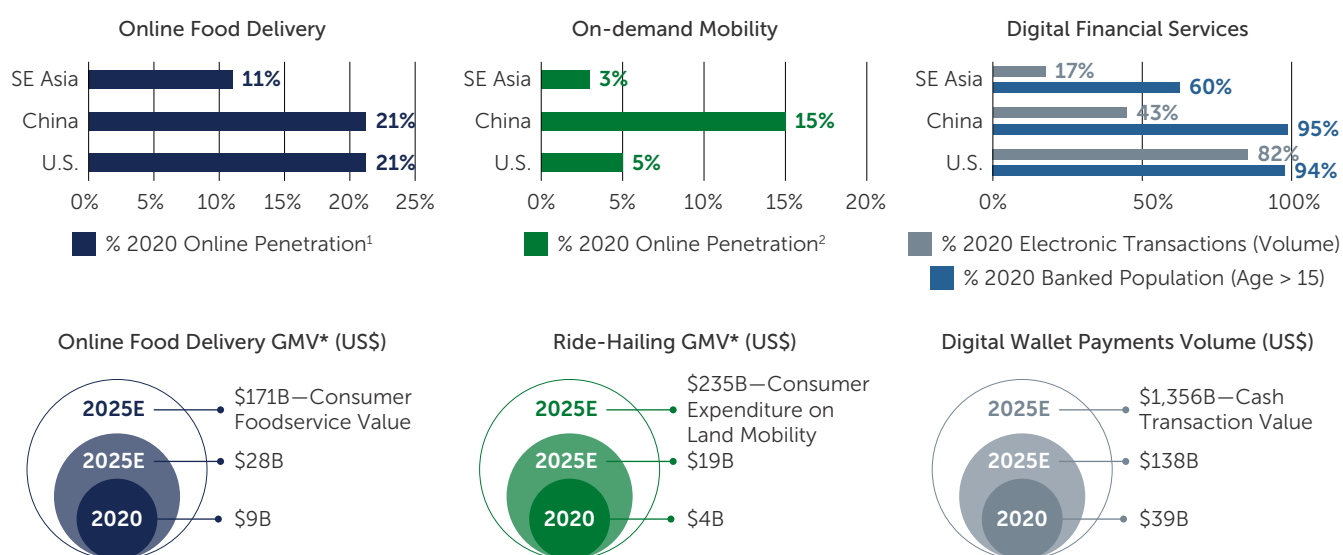


Source: ASEAN FDI Database. As of 2022.

Evolving Consumer Behavior and Technological Empowerment

With rising income comes more wealth, which tends to be followed by an evolution in consumption behaviors. In the 20 years from 1999 to 2019, household consumption in the six largest ASEAN countries—Singapore, Indonesia, Malaysia, Thailand, Philippines and Vietnam—grew by over 420%.² Today, we are witnessing the premiumization of products and services along with new options across the region, from beer to pet foods to medical tourism. At the same time, the development of ASEAN economies is coinciding with the wireless digital age and the growing penetration rate of smart phones—a trend that was further accelerated by the pandemic. When combined with ASEAN’s massive population, this represents a unique opportunity to expand into a variety of digital services such as online food delivery, ride-hailing and digital payments (Figure 3).

Figure 3: ASEAN Offers Huge Potential for Rising Penetration



Sources: Euromonitor; Grab; Credit Suisse Research. As of April 2021.

1. Based on % of total consumer food service that is ordered online (including online ordering for dine-in and takeaway).
2. Based on % of total consumer expenditure on ride-hailing out of consumer expenditure on buses, coaches and taxis and operation of personal transport equipment.

Note: Southeast Asia statistics on this page refer to Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam. E= Estimates. *GMV = Gross Merchandise Volume.

Resourcing the Climate Transition

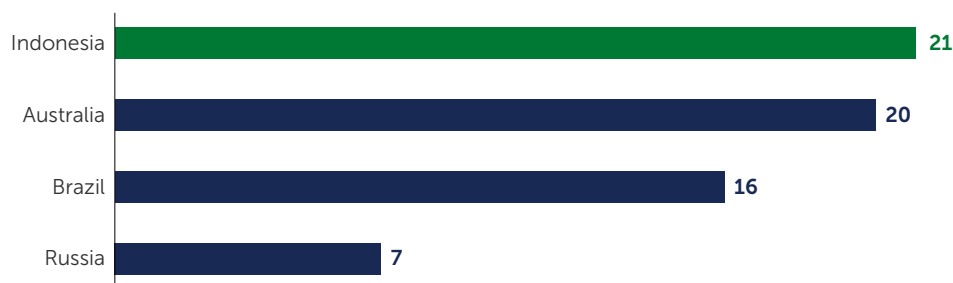
Within ASEAN, Indonesia stands out with its rich supply of commodities. This helped to support its economy in 2022 as exports grew on the back of soaring commodity prices, with shipments reaching a record-high of US\$292 billion.³ While the country is recognized for its supply of coal and palm oil, one of its most unique and rapidly growing exports is nickel—a key contributor to the global climate transition, specifically in terms of its input in EV manufacturing. While lithium is largely recognized as the key ingredient needed in EV batteries, often missed is the crucial role that nickel has to play. The use of nickel in lithium-ion batteries lends a higher energy density and more storage capacity to batteries, at a lower cost. This improved energy density and storage capacity means that EVs can get more mileage out of a single charge, a concept that has been a key challenge for widespread EV adoption.

2. Source: International Monetary Fund. As of December 2021.

3. Source: Indonesia Central Bureau of Statistics. As of February 2023.

Given that Indonesia has the largest nickel reserves globally, it has seen significant investments in production plants from leading global companies within the auto manufacturing and battery supply chains as they look to shore up supply. This surge in FDI will likely support Indonesia’s long-term economic growth and development through greater international trade and job creation.

Figure 4: Indonesia Has the Largest Nickel Reserves (Million Tons)

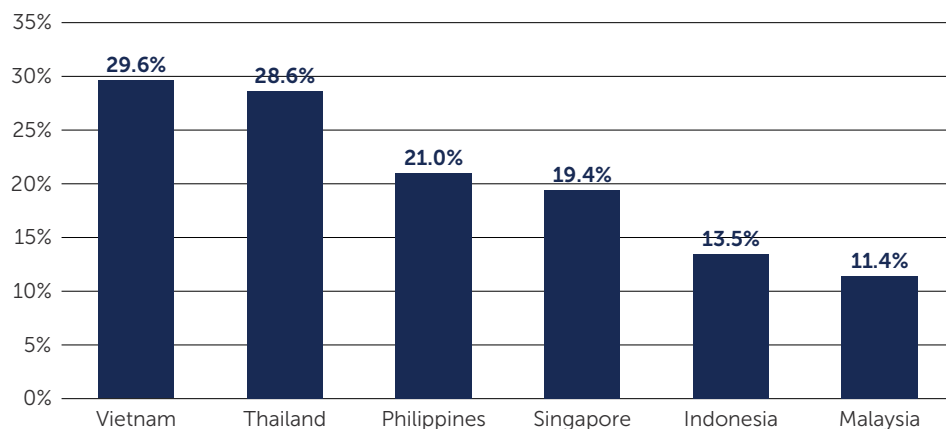


Source: Coordinating Ministry for Maritime & Investment Affairs of Indonesia. As of March 2021.

China’s Reopening is a Near-term Tailwind

ASEAN is a popular destination for tourists globally, and tourism is a major driver of revenue for the region. Although ASEAN reopened its borders for quarantine-free travels in early 2022, Chinese tourists were largely absent until recently. China and the health of the Chinese economy—partially by virtue of its geographic proximity to ASEAN and the associated trade networks—are considerable factors influencing economic growth in the ASEAN region. However, following a challenging period, Chinese tourists are finally returning to the region. With China representing between 11–30% of tourists before the pandemic, this is likely to have a strong impact on local economies and potentially boost ASEAN countries’ current account balances (Figure 5).

Figure 5: ASEAN’S Exposure to Chinese Tourists (% of Total Arrivals in 2019)

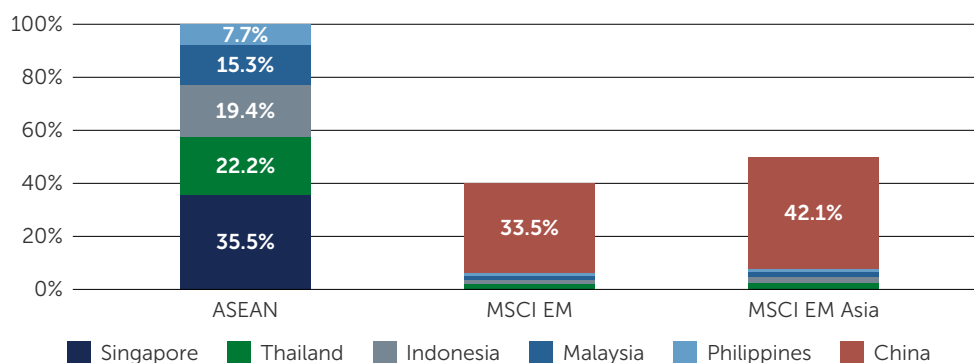


Sources: J.P. Morgan; CEIC Data. As of January 2023.

ASEAN’s Limited Representation in Global Indexes

While many investors are attracted to ASEAN equities as it provides access to fast-growing South Asian countries, we believe the asset class also provides a complementary exposure to existing global or regional emerging markets (EM) strategies. A crucial tenet of this argument is that ASEAN sits within the small “tail” of emerging markets, composing less than 10% of global EM and EM Asia indexes (**Figure 6**). This leads to lower levels of crossover, and correlation, which can help deliver the potential for enhanced risk-adjusted returns over the medium to long term.

Figure 6: Country Concentrations Across EM Asset Classes



Sources: Barings; MSCI. As of January 2023.

Figure 7: Correlation of ASEAN to Developed and Emerging Markets

	MSCI World (Developed Markets)	MSCI EM (Emerging Markets)	MSCI China
MSCI AC ASEAN (10Y)	0.5	0.8	0.5
MSCI AC ASEAN (5Y)	0.5	0.7	0.5
MSCI AC ASEAN (3Y)	0.5	0.7	0.5

Sources: Barings; MSCI. As of January 2023.

Key Takeaway

There are a number of supportive structural trends shaping the opportunity in ASEAN equities, many of which have been amplified by the pandemic and U.S.-China trade tensions. Against this backdrop, ASEAN companies stand to benefit—especially those with direct or indirect exposure to supply chain diversification, digitalization and technological upgrades, and the climate transition. We believe these are longer-term shifts that will continue to provide a positive backdrop to the region’s equity markets.

While near-term risks to global markets remain, many of the headwinds which have faced ASEAN, and EMs in general, are beginning to fade. This suggests that the region’s equity markets may be at a turning point, which presents an attractive entry point for long-term investors to gain exposure to a wide range of under-valued companies with strong growth potential.

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