Thoughts on Asia. **Investment Strategist Peter Lucas reviews his outlook for Asian markets.**

Many moons ago, when I was Ashburton's global strategist, I used to talk a lot about Asia. I was drawn by its low valuations, favourable demographics, comparatively low debt levels and the prospect of the Asian consumer emerging as the main driver of growth in the global economy. After a decade and a half, how has it fared? In short, not too shabby. According to Bloomberg, the MSCI Emerging Asia Index has beaten its World Index equivalent by 1% per annum. Strip out Wall Street and its big tech glamour stocks and the margin of outperformance rises to 4% per annum. The question is, having outperformed to that extent, is there still a good case for investing in Asia? The short answer is yes, particularly given the events of 2020.

The great thing about demographics is their predictability. If you know how many 20-year olds there are today, you will be able to forecast with some degree of accuracy how many 25-year olds there will be in five years' time. And that information can be helpful in forecasting economic and financial trends. Much of the West was in a demographic sweet spot in the 70's, 80's and 90's as the big post-war Baby Boom generation drove a boom in consumption and in time, massive savings flows into financial assets. All that has now changed, with the Baby Boomers now in retirement and drawing down on their savings. Asia, with its much younger demographic profile (China excepted) is in a much better place, which bodes well for economic growth and for inflows into the financial assets. So that's one big tick.

Valuation-wise, Asian markets are not as cheap as they were, but they still offer reasonable value relative to their Western equivalents, and most notably Wall Street. So that's at least a half tick.

Asia's trump card is its potential for catch-up growth. In the past 30-40 years China has demonstrated what can be achieved with the right leadership and the right policies. And that story still has legs. Asia accounts for only a third of the world's stock market capitalisation, but almost two-thirds of its population. Surely that gap must close in the long run.

Debt levels have risen in Asia and most notably in China, to the point that some have been motivated to predict market crashes and worse. It's not obvious, to me at least, why we should be more concerned about debt in China than debt in any number of ageing, ex-growth Western economies. Indeed, the research companies that I consider to be sensible China watchers are saying – as they have for several years – that the country's debt levels are not yet at levels that should concern us. Indeed, some have argued that the build-up in debt is merely a natural consequence of the country's very high savings ratio.

Which brings us neatly on to COVID-19. Whatever the rights and wrongs of the lockdown policy – and I am sure we will be debating that one for years to come – it has come at considerable cost. Debt levels in the developed world were already high by historical standards and have now been pushed into nosebleed territory. In most cases this has been directly or indirectly funded through Central Bank purchases of bonds and money supply growth is through the roof. US M1 is up 41% and M2 is up 24%. These are higher numbers than were seen in the 1970's.

Meanwhile, Asia has had a relatively good pandemic. Perhaps because of lessons learnt through earlier viruses, Asia has contained COVID-19 better than most Western countries, with smaller economic costs. Consequently, thus far at least, Asia has not had to resort to the extreme monetary policies being employed elsewhere. This should be good news for inflation and markets in Asia, at least on a relative basis. Remember, in the inflationary 1970's the currencies and markets of the countries that chose not to monetise the increase in oil prices with easier monetary policy (e.g. Germany and Switzerland) generally fared the best.

In conclusion, although the story has evolved a little, the case for investing in Asia remains as compelling as ever, particularly when you consider some of the alternatives. Wall Street, or at least parts of it, are now very overvalued and Europe has all risks stemming from the construct of the euro. And that's before you consider the challenges of extreme income inequality, political instability, unhelpful demographics and inflation risks.

In the late 1980's I remember reading a book on long-term cycles which predicted that the centre of gravity would shift from West to East in the years ahead. At the time, most would have assumed that Japan would be next in line to be the world's economic and political powerhouse; now China looks the more likely candidate. Either way, it is looking increasingly like this will end up being Asia's century.

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