Matthews Asia

Matthews Asia Perspective

Why Asia's Markets Might Weather U.S. Market Storm

Robert Horrocks, PhD
Chief Investment Officer
Matthews Asia

Investments involve risk. Past performance is no guarantee of future results. Investing in international and emerging markets may involve additional risks, such as social and political instability, market illiquidity, exchange-rate fluctuations, a high level of volatility and limited regulation.

Volatility is back. And with volatility, maybe the first signs of a change in market leadership? What was noticeable about the falls in the market in January and early February was that the large-cap growth names that had performed best during the rally also performed better in both the fall in the markets and the recovery. The market had seen a narrow group of stocks leading the rally go even narrower.

Until the recent falls in the market, that is.

There had been indications that earnings growth in China in particular had been broadening out beyond just a few industries. This would normally presage performance broadening out, too, as the premium previously paid for the few growth areas of the market starts to dissipate and investors look to companies for better value. We would also anticipate small- and mid-cap companies to benefit from such a trend. Indeed, this is broadly the pattern we have seen in Japan over the past few years: reflation causes a market led by financials, ETF flows push up large caps. Later on, however, it is the small- and mid-cap companies that take up the running.

The first real cracks seem to be appearing in the S&P 500, too. The recovery from the acute falls in late January and early February had been greeted with some relief. But it soon petered out under the weight of weak earnings and rising U.S. Federal Reserve policy rates (the Fed hiked rates again on March 21). All this is exacerbated by valuations that are far from cheap. Has the U.S. rally finally come to an end? It is too early to say but I would not be surprised if U.S. equity returns are much weaker going forward than they have been over the past few years. This seems an obvious statement, but the emotion of momentum in markets can often prevent people from seeing clearly what is right in front of them.

What does this mean for Asia's markets? In the short term, if the U.S. market is falling, Asia will fall, too. But there are reasons to expect Asia might stabilize before the U.S. Why? Three reasons: valuations are cheaper in Asia; profits are weakening in the U.S. and growing in Asia; monetary policy is tightening in the U.S., loosening in Asia. This is what happened after the global financial crisis: Asia bottomed first, rebounded fastest. If the center of the problem is the U.S., why can't that happen again? The old saying that the U.S. sneezes and the rest of the world catches a cold may be too pessimistic. Asia's economies and markets look to be in healthier shape right now.

Important Information

Matthews Asia is the brand for Matthews International Capital Management, LLC and its direct and indirect subsidiaries.

The information contained herein has been derived from sources believed to be reliable and accurate at the time of compilation, but no representation or warranty (express or implied) is made as to the accuracy or completeness of any of this information. Matthews Asia and its affiliates do not accept any liability for losses either direct or consequential caused by the use of this information. The views and information discussed herein are as of the date of publication, are subject to change and may not reflect current views. The views expressed represent an assessment of market conditions at a specific point in time, are opinions only and should not be relied upon as investment advice regarding a particular investment or markets in general. Such information does not constitute a recommendation to buy or sell specific securities or investment vehicles. This document does not constitute investment advice or an offer to provide investment advisory or investment management services, or the solicitation of an offer to provide investment advisory or investment management services, in any jurisdiction in which an offer or solicitation would be unlawful under the securities law of that jurisdiction. This document may not be reproduced in any form or transmitted to any person without authorization from the issuer.

In the United States, this document is issued by Matthews International Capital Management, LLC. **In Singapore**, this document is available to, and intended for Institutional Investors under Section 304 of the Securities and Futures Act ("SFA"), and to Relevant Persons pursuant to section 305 of the SFA, as those terms are used under the relevant law. It should not be circulated or distributed to the retail public in Singapore. **In Hong Kong**, this document is issued by Matthews Global Investors (Hong Kong) Limited, licensed and regulated by the Securities and Futures Commission (SFC). **In the UK**, this document is issued by Matthews Global Investors (UK) Limited, which is authorised and regulated by the Financial Conduct Authority ("FCA"), FRN 667893. In the UK, this document is only made available to professional clients and eligible counterparties as defined by the FCA. Under no circumstances should this document be forwarded to anyone in the UK who is not a professional client or eligible counterparty as defined by the FCA. This document has not been reviewed by any regulatory authorities.

©2018 Matthews International Capital Management, LLC