Q1 2021

Quarterly Commentary

Aberdeen Standard Investments

Aberdeen Standard Asian Opportunities Fund

Main Changes & Influences

- Asian stocks rise in first quarter but lag their global peers.
- We initiate five stocks in the period, with three in China, including Nari Technology.
- Asia remains attractively priced relative to its growth prospects.

Market Review

It was a quarter of two halves for Asian equities, which ended the period higher but lagged their global peers. Prior to Chinese New Year, markets strengthened on improving economic data, progress in vaccine rollouts and massive fresh stimulus in the US. Several Asian markets reached record highs as a result.

But the period after saw a correction of regional markets. A jump in bond yields hurt investor confidence, causing stocks to pull back. China-related concerns dominated as well. The first high-level talks between China and the Biden administration in the US started on a frosty note. Regulatory focus on some sectors and broader policy tightening in China also hurt sentiment.

As a result, China stocks, especially those in the onshore China A-share market, were weak. Southeast Asian countries such as the Philippines and Indonesia, which continued to struggle with elevated Covid-19 infections, declined. On the other hand, Taiwan was one of the best-performing markets, thanks to robust chip exports. Singapore did well too, benefitting from an investor rotation into cyclical and value stocks.

What we've been up to

While rising valuations limited our opportunities, we took advantage of market volatility to introduce companies that enjoy structural growth drivers and have good fundamentals.

We initiated five stocks, with three in China. First, **Nari Technology** supplies power-grid automation and industrial control products to State Grid and South Grid, which dominate electricity distribution in China. The company is therefore best placed to benefit from power grid reform.

Meanwhile, **Glodon** is a leading software provider for construction budgeting on the mainland. Beijing's push for infrastructure development will support its goal of expanding into the growing markets for cloud-based solutions and construction management.

Third, **Wanhua Chemical** supplies chemicals used in polyurethane products common across many industries, including rigid and flexible insulation foam for homes and refrigerators. With its cost advantage and technological knowhow, the company has garnered close to a quarter of global market share.

Elsewhere, Dutch-headquartered **ASM International** is the global leader in single-wafer atomic layer deposition technology, a high-precision process that deposits ultra-thin films onto a wafer. As semiconductor chips shrink, demand for such processes is increasing, thereby expanding the size of its market.

Lastly, US-listed **Sea** has key businesses in online video gaming, e-commerce and payment platforms across emerging Asia. The group owns the leading Asean e-commerce platform, Shopee, and earns most of its revenues from Southeast Asia. It is winning against its rivals in Indonesia, and continues to strengthen its ecosystem to deepen its penetration elsewhere in Asia.

Against these, we sold Asian Paints, Astra International, CNOOC, Li Ning and Swire Properties, for better opportunities elsewhere.

Outlook

While rising inflation is emerging as a cause for concern, we believe this will be temporary, driven by higher energy and food prices, as well as bottlenecks as economies re-open. The fiscal stimulus, both in the US and elsewhere, is also unlikely to lead to sustained inflation given the amount of slack in the global economy. Hence, we expect major central banks to keep policy loose for now. This underpins the recovery story, as well as Asian stock valuations, which remain reasonably attractive compared to developed markets, such as the US.

In an environment of rising costs, companies with stronger pricing power, such as those in the portfolio, should fare better. They will likely be able to pass on the cost increases to their customers, while protecting profit margins. We will stay watchful of macroeconomic developments and assess their potential impact on the portfolio, monitoring company earnings and forecasts for clues. While we track market developments closely, we invest based on a long-term horizon. We believe many of the changes sparked by the pandemic are here to stay, including faster adoption of cloud computing, e-commerce and 5G networks. In addition, Asia's burgeoning middle class will fuel rising demand for healthcare services and wealth management, while the region's urbanisation and infrastructure needs remain vast. We remain focused on quality Asian companies that are best-placed to capitalise on these structural growth opportunities.

Performance Review

During the quarter, the Fund rose by 2.9% and underperformed the benchmark's return of 4.1%[1].

Stock selection in South Korea was a key reason behind the underperformance, as our holding in **Samsung Electronics** underperformed. This was despite strengthening fundamentals in terms of better-than-expected memory pricing and end demand that led to chip shortages across many parts of the semiconductor supply chain. The weakness was, however, more than offset by the strength of our holdings in contract chipmaker **Taiwan Semiconductor Manufacturing Co** and our non-benchmark exposure to semiconductor equipment maker **ASML**. The Dutch company remains a beneficiary of rising capital investments, particularly in the regionalisation of the semiconductor manufacturing supply chain. Meanwhile, shares in **Hon Hai Precision Industry** rose after the iPhone assembler set a sales record, as orders for 5G iPhones soared.

By sector, banks weighed on returns the most. Our exposure to India's **Kotak Mahindra Bank** and Indonesia's **Bank Central Asia** proved disappointing. Nevertheless, we believe they remain well positioned to benefit from rising economic activity as recovery continues to take place in both countries. Their impact was also mitigated by our holding in **China Merchants Bank**, which did well.

Elsewhere, the Fund's underweight to China contributed to performance as investors fretted about policy tightening and increased regulatory scrutiny. This triggered profit-taking in high-growth names that had rallied over the past year, including Pinduoduo, Xiaomi and Nio, which the Fund does not hold. Our holding in property developer **China Resources Land** was also a key stock contributor. It rose in tandem with the sector, supported by demand recovery and a new land supply policy that is expected to reduce land costs. These outweighed the impact of holding **Shanghai International Airport**, **Yunnan Energy New Material** and the **Aberdeen Standard SICAV I – China A Share Equity Fund**, all of which surrendered some of their gains from last year. Other laggards on the mainland included private-education provider **New Oriental Education & Technology Group,** amid speculation of regulatory tightening of the after-school tutoring sector, and data-centre developer **GDS Holdings**, although its quarterly results were in line with our expectations.

Overweight Sectors

- Information Technology – our overweight is due to our conviction that Asia is home to some of the world's leading technology companies with good long-term prospects, such as South Korea's Samsung Electronics and Taiwan Semiconductor Manufacturing Co.
- Financials – we see companies in the sector as proxies for economic growth in Asia, particularly in their respective domestic markets. Demand is driven by an expanding middle class and the low penetration rate of financial products.
- Materials – our overweight is partly due to our exposure to cement companies, which are well positioned to benefit from infrastructure development across the region.

Underweight Sectors

- Consumer Discretionary – our underweight is primarily due to our current underweight position in Alibaba.
- Energy – we are wary of the cyclical nature of earnings that typifies the sector, coupled with significant state interference in many of the national oil companies.
- Industrials – our underweight is due to the cyclicality that typifies the sector. Our exposure is mainly in conglomerates with more diversified revenue streams, or high-end machinery names where we see compelling long-term growth opportunities.

Overweight Countries

- Singapore – it is an open economy, backed by sound economic policies amid a stable political environment. It is home to many well-run businesses, with high standards of corporate governance and scope to expand across the region. Locally listed companies also offer good exposure to neighbouring emerging economies.
- Netherlands – our overweight is due to our non-benchmark positions in semiconductor equipment and technology suppliers ASML Holdings and ASM International, which generate the bulk of their sales in Asia.
- Indonesia – the archipelago is home to several good quality companies. As Southeast Asia's most populous country and well-endowed with natural resources, its long-term potential is undeniable.

Underweight Countries

- Korea – a relatively mature economy with well-known brands such as Samsung and Hyundai, but the domination of huge conglomerates makes the business landscape less competitive, while moves to prevent hostile domestic takeovers have also raised concerns.
- Taiwan – the market is home to several interesting businesses, but most are in lower-quality cyclical industries. Corporate transparency is also generally poor vis-a-vis markets such as Singapore and Hong Kong.
- Malaysia – we are underweight to this market largely because we have difficulty finding stocks in the large cap space that meet our quality and valuation criteria.

[1] **Past performance is not an indication of future results.**

Overweight Stocks

- Samsung Electronics – one of the global leaders in the memory chips segment, and a major player in smartphones and display panels as well. It has a vertically-integrated business model and robust balance sheet, alongside good free cash flow generation.
- Tencent – the Chinese internet giant continues to strengthen the depth and breadth of its ecosystem. We see tremendous potential in its advertising business, as it starts monetising across its dominant social-networking platforms and payment system.
- TSMC –the world's largest dedicated semiconductor foundry, TSMC provides wafer manufacturing, wafer probing, assembly and testing and design services. We think it is well positioned, given its scale and technological leadership

Underweight Stocks

- Alibaba – we initiated a position in the Chinese e-commerce giant. The company has diversified successfully into areas like cloud computing, while its core retail business remains highly profitable with solid earnings visibility.
- China Construction Bank (non–holding) – we remain wary of the heavily regulated banking environment in China.
- Reliance Industries (non–holding) – we do not hold the energy and telco conglomerate due to corporate governance concerns.

Top Contributors

- Hon Hai Precision Industry – the iPhone assembler set a sales record, as orders for 5G iPhones soared.
- ASML Holdings – the Dutch company remains a beneficiary of rising capital investments, particularly in the regionalisation of the semiconductor manufacturing supply chain.
- Pinduoduo (non-holding) – policy tightening and increased regulatory scrutiny in China triggered profit-taking in high-growth names such as Pinduoduo.

Bottom Contributors

- Aberdeen Standard SICAV I – China A Share Equity Fund – the fund surrendered some of its gains from last year.
- Bank Central Asia – the Indonesian lender disappointed over the quarter, but we believe it remains well positioned to benefit from rising economic activity as recovery continues to take place in the country.
- Yunnan Energy New Material – the world's largest maker of lithium-ion battery separators succumbed to profit-taking.

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