Research Note

Can sustainable Asian investing pay off?

We know that Asia is highly susceptible to climate change and environmental degradation. But at a time of uncertain Asian equity markets, we ask Victor Wong, Head of UOBAM's Sustainability Office about the United Sustainable Asia Top-50 Fund, and whether there are real financial benefits to sustainable investing in Asia.

Hi Victor, to kick off, can you give us UOBAM's view of where Asian equity markets are heading?

Victor: Over the past few weeks, and especially since the US announced a lower inflation number for July 2022 compared to June 2022, we have seen global equity markets cheering up. The US's S&P 500 Index, for example, rose by over 10 percent in the past one month alone.

Over in Asia, the picture is mixed. ASEAN markets have risen in tandem with the US and Indonesia, as a net exporter of commodities, is one of the few markets in the world posting a positive year to date (YTD) return of 2 percent. Going forward, ASEAN markets look more resilient and likely to benefit from re-opening activities.

The Korea and Taiwan markets have also risen recently, but both are down by over 15 percent year-to-date, making them the worst performing markets in Asia. These export-dependent markets may take longer to recover fully.

China's SSE Composite Index was flat for the month and its top leadership seems to have fallen silent on growth targets. This, plus the lack of economic stimulus announcements and first half growth of just 2.5 percent, leads us to suspect that the country will fall short of its 5.5 percent target for 2022. While we are neutral on the Chinese market, we think it will stay volatile for a while longer.

Given this backdrop, why should investors consider Asian equities?

Victor: Given attractive Asian equity valuations, there is potential for these markets to trend back up quickly. However, global economic conditions, while not expected to give way to a deep recession, could stay tough in the short term. So, investors should brace for continued volatility as Asian businesses announce more negative earnings revisions over the next few months.

That said, it is helpful to put on a longer-term lens when thinking about Asian investing. Asia is one of the fastest-growing regions in the world. Already, nearly half of the world's 5000 biggest companies by revenue are Asian based[1], and the region received half of all new investment over the past decade[1].

In the wake of the Covid pandemic, this shift could become even more pronounced as global companies seek to co-locate their centres of production and consumption within Asia. We expect the region to dominate more of the global economy while becoming less reliant on global supply chains. There are therefore new and significant opportunities opening up in Asia that goes beyond the current investment landscape.

How does Asian investing differ from sustainable Asian investing?

Victor: Asia's large population is a driver of the region's growth. But it is also a big drain on natural resources and makes the region more vulnerable to adverse environmental conditions. For example, a McKinsey report estimates that by 2050, a climate change-induced heatwave could result in a loss of outdoor working hours that could put between US$2.8 and US$4.7 trillion of Asia's GDP at risk annually. In any given year, the potential for flood damage puts a further US$1.2 trillion of capital stock at risk.

Not surprisingly, Asian countries have seen an uptrend of government commitments and policy launches to address such threats. These include net zero and social development targets. In the face of such major developments, it makes sense for anyone interested in securing long term Asian equity returns to take into account the region's environmental, social and governance factors.

Asian sustainable investing is based on two basic concepts. Firstly, we seek to achieve positive returns by selecting Asian sectors and companies that can boost their profits by taking advantage of policy changes and the growing demand for greener solutions. Secondly, we aim to minimise risk by avoiding companies that could be negatively impacted by their slow transition to greener solutions and response to policy changes.

[1] McKinsey, Corporate Asia: A capital paradox, Jan 2020.

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