



Monthly Manager Commentary Newton Asian Income Fund



Jason Pidcock

January 2008



For Professional Investors Only

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Economic and market developments

It was a turbulent start to the year as the credit crisis tightened its grip on world equity markets. The downgrades of monoline insurers, followed by the scandalous trading disaster that rocked Societe Generale, did nothing to help sentiment. Fears of a US recession became more entrenched as employment growth slowed, while the rescue package of fiscal aid and interest rate cuts from the Federal Reserve (a shock 75 basis points followed by another 50 basis points at the end of the month) provided little comfort for investors. Against this backdrop, emerging markets were sold down heavily with China/Hong Kong, Korea, Singapore and India taking the full brunt of the blow, whereas South East Asian economies were relatively unscathed as Malaysia, Indonesia and Thailand fell the least. We feel that valuations in Asia post the sell-off are looking very attractive, and further downside risk from here is limited. However inflation, driven by rising food and energy prices, is becoming more of an issue across Asia. The Chinese government has been implementing price controls across a range of goods and services. We believe these short-term measures will not have the effect the government intended, and that sooner or later, China will need to re-value its currency to remove the build-up of inflationary pressures within its economy. Overall, this should provide a positive boost for Asian markets.

Fund performance

The Fund outperformed in this environment of volatility. One of the strongest contributors was **The Link Reit** in Hong Kong, which owns roughly 10% of Hong Kong's retail space. Hong Kong is a direct beneficiary of the interest rate cuts in the US given the Hong Kong-dollar peg, and this is having a positive effect on the domestic economy and Hong Kong property stocks overall. **Taiwan Mobile**, which is one of the Fund's top ten holdings also did well, announcing solid earnings as well as a larger than expected dividend. **Gamuda**, the Malaysian construction company, saw earnings upgrades on higher projected construction and property earnings, helping to boost the share price. Outperformance was also found in other Malaysian holdings such as **Public Bank**, which once again delivered on earnings growth and dividend surprise. On the downside, **Dore Holdings** shares continued to languish, and **Babcock and Brown** companies in Australia were weighed down by concerns over financing. **FKP Property** was another casualty of the global liquidity crunch, as the shares dived in sympathy with peers in its sector.

Fund activity

Stellar performance from **Gamuda**, the largest holding in the Fund, led us to trim the position slightly to prevent it from breaching our self-imposed limit of not holding more than 5.5% in any given stock. We continued to reduce our positions in financials such as **DBS**, **ANZ** and **Maybank**, preferring to put more money in those names we felt had fallen too far, such as **Simplo Technology**, **Dore** and **Pico Far East Holdings**. We also bought back shares in **Petrochina**, which we felt were pricing in an overly pessimistic oil price scenario.



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Outlook

Looking ahead, we expect markets to continue to exhibit high levels of volatility. Risks to the global economy look to be skewed to the downside and we see many challenges ahead for 2008. More restrictive liquidity conditions, higher energy prices and a slowing US economy will play a key part in moderating global growth. Although the environment remains challenging for Asia, we feel that the slowdown emerging from the developed world shouldn't dampen the structural Asian growth story, which is supported by solid fundamentals. Asian company earnings growth continues to be well underpinned by a growing domestic economy, fuelled by urbanisation and industrialisation. At the consumer level, savings rates are high and incomes are rising, while at the country level, current account surpluses and foreign exchange reserves provide a substantial buffer. At corporate level, gearing ratios have been brought down significantly with many companies now sitting on net cash balances. However, against an uncertain global macroeconomic backdrop, we shall continue to focus our attention on Asian domestic demand companies with strong cash flows and cash balances. We feel these companies should be more insulated from the effects of a weaker global economy, but at the same time should benefit from structural long term growth trends, and appreciating currencies.

J Pidcock, January 2008



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