Fidelity Connects

Eileen Dibb, Portfolio Manager
Pamela Ritchie, Host

[00:03]

Voiceover: Hello, and welcome to Fidelity Connects, by Fidelity Investments Canada – connecting you to the world of investing and helping you stay ahead. On this episode of Fidelity Connects, Portfolio Manager Eileen Dibb discusses with host Pamela Ritchie the outlook for the Asia-Pacific equity markets and where she is finding opportunities overseas.

She dives deeper into the impact of the recent U.S. elections, specific sectors and trends, effects of COVID-19 on Asian investments and her investment philosophy, which has resulted in one of her mandates receiving a 2020 Lipper Award.

Eileen says the vaccine announcement in early November changed the game of what she is looking at in terms of opportunities. Now her horizon is two to three years out.

Generally, Eileen tends to go where she believes there is the most potential for a company. For example, technology in Asia and China. Tech exports in Northern Asia tend to be 20-40% of exports. She says she is very opportunistic in what she is looking at and where she will go with the fund.

Commentary surrounding COVID-19 and financial markets is frequently changing.

Today's podcast was recorded on December 11th, 2020

[02:00]

Pamela Ritchie: Eileen, I don't know if you know but often we speak to Jurrien Timmer, one of your colleagues. He joins us on Mondays to frame out the week, and for some time he's been talking about having a proper allocation to EM. Within that discussion, we really would like to get your thoughts broadly on how the Asia-Pacific region needs to feed into that story and the exposure to it. The U.S. dollar is obviously part of it, what's the other big piece?

Eileen Dibb: Jurrien's case for EM does hinge partially on the currency but it's also about growth in the region. Cyclicality in Asia tends to be quite high. When we go into early cycle on markets like ASEAN, [*indecipherable*] countries, slightly less so North Asia, it tends to be good. The cyclicality of the region really drives Asian EM exposure.

[02:59]

Pamela Ritchie: You mentioned some of the there. This whole debate about whether we are in an early cycle of a bull market. This is a global question, it seems to get put to, sometimes, U.S. markets and other markets. Talk to us a bit about cycles, about flows, where you see things going.

Eileen Dibb: Flows into ASEAN over the past decade have been generally flat. North Asia has actually seen a lot of good flows, things have come up, obviously China being a huge market in Asia and North Asia in particular; but ASEAN, not so much. So you're seeing a real differentiation there even across the region.

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Pamela Ritchie: We recently have been reading about this Regional Comprehensive Economic Partnership. It's essentially a trade agreement. It seems to be a little bit early days of it, but certainly China is playing a very central role with, essentially, all of its neighbours. Can you fill us in on what we need to know about that, or if it's got significance right now?

Eileen Dibb: The RCEP has been drafted and approved by 15 countries I believe, 10 countries in ASEAN. It actually originated in Indonesia, not with China. Ten countries in ASEAN and five other developed countries in Asia, including China. Two of the countries that did not come to this partnership are India and Taiwan. They have not joined the Regional Partnership. It represents about 30% of global GDP. So that's quite significant for any sort of trade agreement, and it's going to be very important in the region probably over the next 10 years.

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Pamela Ritchie: Since we've spoken to you, there's been the U.S. election, President-elect Biden is on tap to take over in January… What does this change in terms of geopolitical positioning, in terms of opportunities for investment? It's going to be a different voice on the world stage.

Eileen Dibb: I think President-elect Biden is going to maintain some of the status quo. His platform is potentially going to be more bipartisan, and a lot of the things that we've seen coming out of the current administration have been driven bipartisanly. For example, the trade tariffs were not necessarily something brought in by this administration, but something that had been in the works. It had been in the works in the previous administration and didn't get completed. So it seems like there's not a lot that's going to change right off the bat, but global partnership is something that I think President-elect Biden will appreciate, and we could see a re-emergence of a trade partnership. Where the U.S. has backed away over the past four years from that international stage, we might actually be coming back to that. So you might see some attempt to reignite something similar to the TPP, it could be in the pipeline.

[06:36]

Pamela Ritchie: It's very interesting when we look at the rise of some of the valuations of Asian stocks. Some of them seem to have been rising for some time, but when you look at them relative to the U.S. they're not overly expensive yet, are they? Or is that correct? You fill us in.

Eileen Dibb: Asia in general have held their valuations relatively well. ASEAN has gotten very inexpensive. As I said, flows have generally been out of the region and growth has generally been there, so valuations at this point are looking relatively good. North Asia, obviously, we have seen valuations expand. You've got some Chinese internet stocks that have come up. You certainly have valuations in secular growth stocks that have come up. So it depends on, which part but there's also a dichotomy. There's a dichotomy in Asia where you've got part of the market, particularly deep cyclicals and financials, that look relatively inexpensive, and then you've got growth stocks that are relatively fully value. So there's a lot going on there.

[07:58]

Pamela Ritchie: Let's talk about a few of the different types of rotations. There's obviously been a big discussion about out of growth towards more cyclical, so that's a piece of it. There's also just been a catalyst of the vaccine worldwide. The fact that people know it's coming and there is a light at the end of the tunnel has caused a huge rotation. What have you been doing? Has China taken part in that? Have some countries taken part in that more? How is it faring for Asian stocks?

Eileen Dibb: The vaccine has driven sort of a wave. Beginning in January when China started to have the virus, we were investing in Chinese internet and e-commerce and things that would be most effective as investments under a COVID scenario. Then we started to look towards growth names and growth that had been sold off with expectations for COVID to hurt the businesses, but yet they're really solid, fundamental businesses. That was sort of where we were over the summer. November 9th – I think that was the date – was the announcement of the Pfizer vaccine and 90+% effective possibly, relatively safe from what we've seen. This comes from one of our pharmaceutical analysts internally — talking to Alex, he has said that the safety profile of these vaccines that are coming out right now are something that look pretty good. That announcement by Pfizer, if you think about what happened, it changed that game, right? It changed where we were in January looking at COVID-related stocks, through the summer looking at secular growth and now having a vaccine. You think two years from now, three years from now because that tends to be my investment timeframe and investment time horizon, where do we go from now? It's another set of stocks, and so that's what I've been focused on over the past month. It's just about a month since the Pfizer vaccine was announced. We can talk more about that, what sectors we like now, where we think it's going.

[10:21]

Pamela Ritchie: Absolutely. It seems like the right moment also to ask you about AsiaStar. Let's get into the mandate of it — and we'll talk about the Japan Fund in a minute — but just sort of go over the broad strokes of the mandate for AsiaStar.

Eileen Dibb: AsiaStar is almost every country that qualifies in Asia as either an emerging or a developed market. Everything else that's out there that we don't invest in in Asia tends to be a frontier market. So it's about 13 countries everywhere. We can invest from Pakistan to China, Japan, Australia… you get a little bit of everything in this fund. The biggest component is Japan, but China is also rather large in the benchmark, Australia is large, and then you've got all of ASEAN. It's a nice diversified way to invest in Asia, to invest in all of the secular growth that's there and to, in times like this, possibly get the upside from the cyclical. I do allocate across countries – sometimes we're in a country, sometimes we're not – and across sectors, so there's nice risk diversification in something like AsiaStar where it's a lot of different things and it's timely. We tend to be very timely in where we're going, in what we're looking at. It's all backed by all of the resources that we have at Fidelity. All the stock work, all the sector work, all the macro work from Jurrien, from our GAA, global asset allocation team, macroeconomic team and that's what AsiaStar is. It's pretty concentrated, so it's about 50 to 60 stocks at any given time, but it does give great exposure to Asia as a region.

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Pamela Ritchie: You actually have just answered a couple of questions that have just rolled in right now. One of them is exactly on what you're looking at in terms of finding great companies to invest in besides the large-cap companies that everyone knows about. Can you just expand on that? It obviously goes back to the resources that Fidelity has, but just within the large-cap and others, how do you answer that?

Eileen Dibb: I tend to go where I think that there's the most potential for a company. Sometimes we do do a lot of the larger companies in Asia, particularly within tech. In tech, there does tend to be a lot of growth in China, a lot of growth, for example, from Taiwan. Tech exports in Northern Asia, China, Taiwan, tend to be between 20 and 40% of exports. When you have positive tech sector movement, these companies tend to do very well. And then you have smaller countries – not necessarily smaller population-wise, but smaller economically – and they tend to be a little bit more nichey. For example, a country like Thailand or a country like the Philippines, there are times when we will want to be there. Often when it is a smaller economy the companies also tend to be smaller. We can go into any of those areas just depending on what we're looking for at the moment. Is it a travel company in Australia or a medical company in Thailand? What are we looking for? What is that exposure? That really drives the market-cap as well. I don't love hugely illiquid companies, particularly in countries that have a little bit of risk, because depending on what country it is there can be more political risk or less, or governance issues possibly, and all of that goes into what we're investing at any one given moment, and always trying to really be in the best place. If it's small-cap, then it's small-cap. If it's larger-cap, then it's larger-cap. We're very opportunistic in what we're looking at and where we're going in this fund.

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Pamela Ritchie: Completely fascinating. It sounds like just a fascinating process. I'll ask you now about the Japan Fund because there's questions coming in about that. Tell us the broad strokes. Quite a different market, obviously, a developed market.

Eileen Dibb: Just a little bit of background. I have been managing Japanese equities for over 20 years now. It's a long time. That's really my background. I started out studying about Japan, learning the language. I lived in Japan for several years and the Japan Fund is a great way to look at one market. The interesting thing about Japan is that it has a lot of exposure to the region, but it's large, it's developed, it has great governance — not everybody loves the governance, there's some things that you could tweak and Prime Minster Abe certainly did that, but overall it's safe, it's developed, it's going to probably not have any issues with its debt, it won't be part of a debt crisis, I wouldn't think. So when you invest in Japan, and what we do is a lot of the growth in Japan, it's not everything in Japan all the time. Obviously we'll get some cyclical exposure when it comes, but really this fund is the best of Japan. That actually gets a lot of feed from the rest of the region.

You get exposure to China and you get exposure to other parts of Asia through that fund as well, but it's through Japanese companies. You get exposure to the U.S. There are [*audio cuts out*] companies that we really like in Japan, for example. That has great support from markets globally. Japan is an interesting one because it is an actual low risk way of investing in growth.

[16:59]

Pamela Ritchie: That's fascinating. It has always, in our lifetimes, been known as one of the most innovative countries and had some of the most innovative companies. That obviously continues.

Eileen Dibb: Yes. I have long looked at Japan. One of the things that I remember is back in the early 2000s, the first cell phones that had games on them were Japanese cell phones. They brought that to us. 3G, 4G, 5G… a lot of technology in Japan, going all the way back to the Walkman – my first Walkman back in 19whatever. They have this technological prowess and it's everything from electronics to electric vehicles to air conditioners. There's a lot there to choose from and it's constantly evolving. They constantly have new technology, some of which you might not even know about. The Swiffer – we all have Swiffers – that was originally a Japanese technology. There's a lot there to choose from on the innovation front, and it keeps coming. It keeps coming year in and year out. Good places to invest there.

[18:26]

Pamela Ritchie: How do you play EVs – and this is probably across Asia. Obviously electric vehicles are what everyone is talking about and thinking about, and we know that the Paris climate accords are all being discussed, their five year anniversary. It's very much in vogue and making a lot of people money. How do you play that?

Eileen Dibb: I tend to look at EV in terms of part suppliers. Obviously you've got the big OEMs as well who have EV exposure, but I do like to do parts. All the way back, again, 10 years ago we were looking at separators for EV batteries, and were they wet or dry, what were they and how did that play into the EV cars that we see on the road today. There's still those opportunities. Everything from brushless motors to batteries. Panasonic has the gig factory that produces batteries for Tesla. There's all these opportunities out there. For me, I like the parts aspect of it. When you think about EVs, and you think about the parts that go into them, it's a different set of parts. It's more electronics, it's more battery, you don't have the big engine, and so it's a different thing. Then it's counting, right? It's counting the volume of the parts that are in each car. How many motors do you need? How many connectors do you need and [*audio cuts out*] behind EV and parts tends to be just that. How many more of the part made by this company are they going to need compared to the past where we didn't need as many cars, we're not quite as electronic. They're more electronic, but they're nowhere near as electronic as EVs.

[20:30]

Pamela Ritchie: It's fascinating. I think you mentioned banks just a little bit earlier on. There's obviously a lot of Asian banks that are very interesting to look at. It's been one of the top cyclical discussions about when that comes back. How do you look at the Asian banking world at this stage?

Eileen Dibb: Asian banks have been a tough place to be invested. I have shied away from banks. When you think about interest rates, you've got interest rates that have come down and they're negative, which means that spreads are also quite small. For banks to perform, you need to have spreads, you need to have credit growth. Right now credit has been relatively good in China, although the Chinese government has been watching personal credit. 2018 in China, for example, was a tightening cycle. Eventually we're going to get another tightening cycle out of China, possibly in housing. That's the direction they're going at the moment. You need rates to go up, you need rates to expand in order for banks to make money, and you need credit to expand in order for banks to make money. I have been overall wary of banks in Asia, but a little more interested recently as we're coming out of this COVID-based recession, and really just trying to think about what is going to make these banks work; maybe it's an Australian bank with commodities going better, things like that.

[22:21]

Pamela Ritchie: It's very interesting. I want to just kind of bring back the COVID world that people were investing in, the work from home. It certainly feels like, in North America, we're going back into a further work from home period, but Asia was out first and continues to keep it under control. How does that change the way you're looking at investments there versus here? People are looking at travel to come out the other side of this year, but is that something that you've been looking at for longer, for instance, in Asia? How does the time lag play into your investing?

Eileen Dibb: I apologize, there's a leaf blower out the window. I don't know if you can hear that or not, but I can hear it. There's always something, working from home. I think the timeline for COVID in Asia, first of all, has been earlier. They went in earlier in China. There's been some work done. Did they have a different strain of the virus in China than we're seeing here in the U.S. and in Europe, which was actually slightly less infectious. I don't know if you've seen a chart of this, but if you looked at it in the U.S. in March when everything started, that strain of the virus was 17%, it was relatively low. Now it's like 90%, and from what they've said it seems like that is much more infectious. It doesn't cause you to get sicker necessarily, but more infectious. So Asia has come out of this relatively well. It's going to be out of it relatively early, and part of that is also cultural. In a lot of countries in Asia they don't shake hands, they don't kiss on the cheek, they don't do a lot of the things that we would normally do when we greet people. Obviously we've talked about this before, the mask culture. We are getting used to wearing our masks. I have 24 now. I didn't have 24 masks before this. I may have had a box of masks because I use it when my kids get sick and I don't want to get sick, but I don't wear them everywhere, right? I think that you have seen mobility in China increase a lot. You have seen other countries where it hasn't taken off, a couple countries where it really has. Next year is really going to tell. Right now economic comps are difficult and people are still wondering what happens with fiscal stimulus? What happens with monetary stimulus? How much of that do we need? And how much of that is going to come into the economies? Do we need it? Do we not need it if we come out of COVID with a vaccine? The vaccine is going to take a while. I don't know if you've looked at this, but I've looked at some of these things, and in the U.S. there's about 350 million people, I'm going to be 349 millionth. A lot of people are not going to have this vaccine for many, many, many months. It all depends. But Asia has had less of it and that will help, that helps the economies come out sooner. I think next year we're going to lap some of these comps. Negative comps are going to become more positive. Asia as a cyclical market, we don't know where it's going, but that could help Asia to do well in the next 12 months.

[26:06]

Pamela Ritchie: I just want to talk a little bit, and it's not as much of a focus as we have in other times, but there's sort of a question about trade tensions. We won't go into all of them, but all it really means is that with Fidelity you have a certain type of access to certain opportunities across many Asian countries that we've been talking about that investors just don't have the opportunity to go into on an individual basis. Can you just broadly paint that picture for us?

Eileen Dibb: Obviously there's the ADR situation in the U.S. The U.S. wants Chinese companies to open up their books, and if they don't they might face delisting. We can invest in Hong Kong on the local market, obviously. And trade is interesting. Thinking back to one of the trade things we had talked about in the past was could there be a trade agreement between Japan and China? Just kind of circling back to the RCEP, that gives Japan and China a de facto trade agreement, and India is not a part of it. So when we think of all these things and all the political factors out there, this is all a part of that big mosaic. We put all the pieces together and trade is going to be big because the RCEP does some things in Asia that haven't been there before. And the U.S., we have to figure out where we fit in that and we have to rework that. As investors we decide what that means for us, where do we go from here? Do we buy eight shares and not ADRs if they're available? Capital markets in Asia are pretty liquid, so that's a good opportunity. As investors managing things like AsiaStar and Japan as well, we have a lot of access in a lot of different ways to different types of stocks within Asia.

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Pamela Ritchie: It's just an area that someone with a steady hand is able to go into with much more fortitude than those who just have less options. Eileen Dibb, it's always a pleasure to speak with you. Thank you very much for introducing us, reintroducing us and taking us further into your investment strategies.

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