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Fund Perspective

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Fidelity Asia Fund

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Summary

- **The portfolio is focused on finding the very best ideas across the region and most of these of late have tended to be in Greater China.**
- **Hong Kong in particular remains unloved, largely due to the hangover from the virus and politics, and depressed sentiments has created buying opportunities here.**
- **At the sector level, there is a large overweight to tech, with exposure focused on memory and foundry companies like SK Hynix and TSMC where valuations look more attractive.**

Could you briefly recap your investment approach?

The Fund is a concentrated portfolio of 20-35 high conviction names. When analysing a company, I focus on three key variables - fundamentals, sentiment and valuation - and there tends to be a contrarian element to new ideas. Negative sentiment attracts my attention and we clearly had lots of that through February and March earlier this year.

From this, I look at the valuation, cross-check against fundamentals and focus on areas where I think we have an edge versus the market. Ideally what I'm looking for are long-term structural winners that have been mispriced and fallen out of love with the market due to a short-term issue.

High growth and momentum names in sectors like tech have led markets globally over recent months. How has this impacted the portfolio?

The portfolio has a large overweight to tech although this is focused on hardware and semiconductor names, with zero exposure to the likes of Alibaba and Tencent. This all comes back to my assessment of fundamentals, sentiment and valuation and the potential risk-reward. The well-known internet stocks have a lot of momentum behind them, have performed very strongly of late and I think you could argue that valuations are looking excessive.

Against this backdrop, I see more attractive opportunities in memory and foundry names such as SK Hynix, and more recently TSMC. These companies are second derivative plays on the more popular areas of tech and I think the risk-reward profile looks better in this part of the market. They benefit from structural tailwinds of increasing technology use, and especially in the case of SK Hynix (memory), have cyclical elements to their business that can also be attractive.

A note should also be made on ASML, another key holding that is listed in the Netherlands, but the majority of its economic exposure sits in Asia. The company produces essential products for chipmakers (TSMC and Samsung are major clients) and it is starting to move into services which should be margin accretive. I don’t see anyone else getting close to challenging their tech leadership in lithography, a crucial and complex part of the semiconductor value chain, so it is essentially operating in a monopoly with a highly favourable long-term outlook.

Where are you finding opportunities outside of tech?

I think the market continues to overlook travel-related areas. Vaccine developments have put a floor under stock prices of late, but sentiment remains negative and valuations very attractive among quality companies that have the strength and resilience to get through the coming months. Travel-related names I own include Galaxy Entertainment, and BOC Aviation.

Elsewhere, Hong Kong as a market remains unloved, largely due to the hangover from the virus and politics. Depressed sentiment has created buying opportunities and the portfolio maintains a large notional overweight to Hong Kong. The majority of this exposure is to companies with large overseas operations so exposure to the Hong Kong economy is a lot lower than the listing weight in the portfolio suggests.

For example, and looping back to the travel theme, Macau casino operator Galaxy Entertainment is a significant position that I added to the portfolio in March amid market volatility. The company has a very strong balance sheet, some of the best assets in Macau and a successful track record. It also stands to benefit from the reopening of Macau’s borders and a recovery in tourism. This is a Hong Kong listed company, but its success is driven by Chinese tourists. This is a name I have further added to as investors took a negative view on Hong Kong politics, which has no bearing on the company.

Do you see a second wave of the virus as the main threat to markets?

The virus is front and centre for everyone, so it is largely factored into investors' assessments. Therefore, I don't see it as a major risk. I think a surprise rebound in inflation would be more damaging. This isn't on people's radars - and isn't my base case - but if we saw a pick-up in inflation it would be damaging to a number of areas and could put the brakes on the broader market.

What is your view on the ongoing US-China trade tensions and how do you factor this into your stock picking?

The market has been focused on companies that are on the US Entity List, but I think there could be collateral damage to a broader range of stocks. It is questionable whether this risk is currently reflected in valuations when we look at some parts of the equity market. For example, what would happen to the smart algorithms behind Alibaba and Tencent's platforms if Nvidia could no longer work with Chinese firms? To me, it comes down to fundamental analysis and an assessment of the potential risks facing each individual company.

That being said, surveillance company Hikvision is the portfolio's largest holding and it has been in the crosshairs of US-China tensions. The stock price fell after it was added to the US Entity List in 2019 which obviously restricts its ability to do business in the US. Sentiment remains relatively negative but the fundamental and valuation picture is more positive. There are a lot of growth opportunities for Hikvision as pretty much anything you can see with your eyes is something that they could apply their equipment and technology to - robotics, facial recognition for payments, body temperature checks, airport check-in and immigration are all areas that can use their technology. There is a long runway for domestic and international ex US growth and the management has a great track record in delivering.

What is your view on the ASEAN markets?

It's an area that I continue to look at, but I find liquidity is an issue. Compared to other markets I would also argue that there are fewer long-term structural winners in the ASEAN markets. There are some examples, but they don't currently tick the box for me from a valuation perspective. As a portfolio manager, I look for the best ideas across the region and most of these of late have tended to be in Greater China.

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