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TRANSCRIPT: EPISODE 67
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Please note that these are unprecedented times and markets can react very quickly to news. The views expressed are at the time of recording and could change.

[INTRODUCTION]
Darius McDermott (DM): I'm Darius McDermott from FundCalibre and this is the Investing on the go podcast. I'm delighted to be joined by today by Eric Moffett who is the manager of the T. Rowe Price Asian Opportunities Equity strategy. Got that right on one go, that's a start.

[INTERVIEW]
[0:22]

DM: So, thanks Eric for taking the time to talk to us. Asia is a little further along in the crisis: first in, first out. One thing which has been really important is balance sheet strength, businesses' abilities to be able to survive through the lockdowns, etc, I know it's a key thing, a key factor, for you. Would you like to talk about balance sheets and what you look for, and you know, how you analyse that?

Eric Moffett (EM): Thanks Darius, it's good to be with you again.

You know, when it comes to balance sheets, I tend to avoid balance sheets, which is to say I like companies with net cash balance sheets and not a lot of debt.

DM: Yeah so strong.

EM: Strong, very strong. So, you don't, there's not much to analyse and that always serves you well in downturns. I'd say during this particular episode though in Q1, we did reach a point where anybody with any balance sheet was assumed that they're going bankrupt, basically in March. And so I actually found myself looking at a couple companies and investing in a couple of companies, that had balance sheets just cause I felt like the market was just throwning out all the babies with the bath water. But on the whole, I tend to prefer net cash, cash-generating companies and they do really well when folks start to worry about balance sheets.

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DM: And you know, I know that you're normally a low turnover manager and we've already just dipped into, sort of the volatility in markets in Q1, but you've been quite active actually much more so than your normal low turnover, buy and hold strategy. Would you like to talk us though some of that repositioning and some of those changes you've made?

EM: Yeah, you know, during past market downdrafts I usually don't do very much of anything cause the good quality things just hold up really well and it's quite easy. This time, however, we saw more dislocation than I've ever seen and so, in many ways, it felt like it was like a 'going out of business' sale or you know, Black Friday in the States where people are tripping over each other to buy, you know, the bargain televisions on sale. There were just so many good companies that' for a few weeks - a period of time anyway - got really, really attractive. So, I bought 14 new names in the first quarter.

DM: Wow, that's a big number.

EM: I mean, oftentimes quarters go by, I don't buy anything at all that's new. But we saw some real high-quality companies, many of which had been on my radar for years, just suddenly fall down to two a good prices and we jumped on them. And so we were really, really busy. It was a lot of fun being an investor in Q1. We were very active.

DM: Any sort of areas or was it just a breadth of the market that had those sort of opportunity-set or was there any sort of sector or that really jumped out and you went 'I've been waiting for this valuation'?

EM: Well, you know, it was more about geography and so you mentioned at the beginning how there's sort of a 'FIFO' thought in terms of the virus and then when countries open, I'd argue it was the same in terms of where investment opportunity was, early in the quarter clearly it was China as stuff was getting hit there. But then when they had their peak daily cases early in February, that market bottomed quickly and held up like a rock, I suspect China's been one of the best markets globally, year to date.

DM: Yeah it has.

EM: Later in the quarter is really Southeast Asia and India, they got hit as they started to get hit by the virus. And so, in many ways I've just been following my attention with the virus as it kind of moves around the region. And really Southeast Asia and India had been most recently hit.

DM: And does that mean you've been adding in those areas or…

EM: Yes, absolutely. I have, I have. So, in Indonesia there's a multinational company that is in the consumer staple space, been on my radar for six years, used to trade at 50 times earnings, briefly went down into the low twenties. We bought that. And there've been others but we were just jumping opportunity where we saw them and often times that opportunity it didn't last long, but fortunately we were able to build up good positions in some of these stocks.

[4:27]

DM: And you do have decent overweight in consumer discretionary, consumer staples, including a couple of Chinese companies in the sort of hotel, restaurant and leisure space.

EM: Yeah.

DM: You're clearly confident that the Asian consumer is going to come out of the crisis strong and stay strong?

EM: Well, I think the verdict's still out, frankly. I always focus on the working-class consumers you know, the folks buying Louis Vuitton bags and stuff, their incomes can go up and down pretty dramatically with the economy. And that's not where I focus. But when you look at working class incomes across most of emerging Asia, they've steadily risen over the last, you know, 10, 20 years. And then China in particular over the last 10 years. It doesn't comes in and grow an eight and 9% clip. Part of this is minimum wages going up and part of it's just that the workforce stopped growing for demographic reasons a few years ago, but the economy keeps growing. So labour has good pricing power.

So far that income growth story continues. However, I'm a little bit worried about what deglobalisation could mean if the US and Europe stay locked down for too long. That could hit a lot of employment in China. If the trade war tensions, you know, lead to cut orders or folks moving manufacturing elsewhere, that could move unemployment higher and move incomes in the other direction. So that's something I'm watching very closely right now, but I still hold a lot of the names like Yum China where you've got good value for money. You know, good convenience, good hygiene, because a lot of these companies can just take share from a lot of the companies that we're competing with that had bad balance sheets or just don't have their scale.

[6:05]

DM: And you touched briefly, and I think this is potentially the big fallout of COVID is the deterioration in the relationship between the US and China. There's also a presidential election in the United States and it does appear that some of the anti-China feeling isn't just held in the Trump camp, that it's held by the Democrats as well. Does this worry you? Or do you think this is just something that will blow away with the election as we go through 2020?

EM: Well, there's no doubt that this year we're going to see a pretty persistent, I think negative rhetoric as far as China goes. And a big part of that is that it's an election year. And this is one of the few bipartisan issues we have in America these days. So that's probably not going to change. I think if we do see a change in administration in the States though, the rhetoric can completely change, the links between the two countries could go through more normal diplomatic channels. There'll be no more Twitter, presumably, and so I think the relationship could improve on the margin, but make no mistake about it. There's no love lost right now. And I think the rhetoric will continue into the election.

The thing that concerns me much more though is what's going on between China and Europe. So last year I was often asked, well, wait a second, we've got the US/China trade war. Doesn't this mean that it's going to really hit Chinese growth? You're going to have unemployment everywhere. How can China survive this? And you know, the reality is the US only counts for about 18% of China's exports, and so while it certainly did hit certain sectors and companies we talked to noticed what was going on with the trade war, they were able to trade with all these other countries. And one of the key things they were all happy about was that the relationship with Europe was still good. Europe wasn't following the US in this trade war. They weren't following on the tariffs. And China's diplomats worked really, really hard to make sure that Europe didn't start to gang up on China and the trade war didn't move to the continent. But now it seems like the opinion in Europe is changing and you know, there's the G3 are still critical for China's trade. That's Europe, Japan and the United States. And if Europe and perhaps even Japan is going to start encouraging their companies to move out of China. Then China has got a really big problem. I'm sure they're working real hard on this, but I'm much more concerned about what's going on in the US, or rather the Europe/China relationship, than I was last year when it was just the US and China.

[8:44]

DM: Yeah, that's really interesting because it has been the US/China trade war that's dominated that headlines and it's a really interesting observation that you're saying that Europe is as important to China as the US, so that that's something which I hadn't considered particularly.

Another thing which has been going on throughout COVID is of course is the big fall in the oil price. It appeared that March we had a double whammy as sort of COVID hit developed markets, but also was, you know, we actually had negative oil on the futures, on the West Texas. Does the oil price fall have any particular impact across your region? Generally a net importer of oil?

EM: It's like a gift, it's a beautiful thing, the vast majority of the reason I invest in import said oil. Is when prices go high, they feel it on inflation. It creates a lot of problems. But the falling oil prices has been a huge boom. When you think of global emerging markets, there's the Asia bit and the non-Asia bit, the non-Asia bit broadly are commodity exporters', Asia is an importer, so these low oil prices are great. And if I look across Asia, India is probably one of the greatest beneficiaries and these low oil prices have given them the fiscal space just when they need it. Now looking forward, of course what goes down can also go up. And if you believe oil prices are going to be maybe higher a year from now, even if they're not high in absolute terms, that can make for some tough comparisons. But you know, as far as this year goes, these low oil prices are really, really good for Asia.

[10:27]

DM: And are you finding, cause we talked a little earlier and you said that sort of China had bottomed first and then you know, the markets in India had been weaker. Are you finding India particularly attractive given the low oil price? And the fact that it's down much more now and in relative terms and absolute terms than say China, the other big Asian market?

EM: Yes, yes I am. However, it's unclear to me how long their lockdown is going to last. You know when you think about the world's response to this virus, you basically have the developed world response, which is to spend a lot of money to help tide people over, help to keep company’s going and this is a great thing. And the developed world has the money to spend. When you talk about some of these poor emerging markets, so they simply don't have the balance sheet to keep things locked down for too long. You know, you've got hundreds of millions of people who need to work today in order to eat today. And these governments don't have the ability to pay everybody's salary. And so I'm a bit worried about India, which went into this virus crisis already in tough economic shape, now to be spending money left and right and extending the lockdown, indefinitely. I hope they get out of it and I do find really attractive stock prices in some sectors, but I think it's too early for them to declare victory. So, I'm constructive, but I'm not really going overweight yet.

[11:55]

DM: And with all the obvious doom and gloom that COVID has brought to the world, you're actually based in Hong Kong and hence you're further out of lockdown, has life returned to normal? Is there some light at the end of the tunnel for those of us stuck in a lockdown Europe?

EM: Indeed. You know, I was talking to a friend in the States the other day and he's like: “talking to you is like talking to the man from the future, you know, and I hope my future is like that.” So in Hong Kong, you know, we were hit kind of in late January and we've been through a good three months of lockdown and, I've got three year old twin boys, and three months of homeschooling them, man, that's taken years off my life for sure. The good news is school starts next week. Actually, school starts this week for those boys. So that's good. Restaurants today absolutely packed, traffic on the roads, you know, but that's because we've had a few weeks now with no virus cases and so we're one of the few parts of the world that has that, plus closed borders, and so things really are returning to normal.

I think for those of you sitting in Europe, there are a few things about our life here that I think are going to be part of your life there. And so, you know, one of them is a temperature checking. I probably had my temperature checked like nine times today. You know, get on a bus temperature check, go into a shop, temperature check. Every building has those thermal scanners testing everybody who goes in, and man oh man, if you're the person who coughs in an elevator, you're going to be shamed like you've never been shamed in your life. So temperature checks is one. Masks is another. Everyone wears masks pretty much all the time. You know, there's some debate about to what extent this helps, when healthy people wear the masks, but it's just become the social norm that does stop the spread as well.

Testing, testing, testing. Clearly, we got to get some of these testing bottlenecks unclogged around the world. But once they're unclogged you know, we're able to test more broadly, we'll both be able to contain the disease, but also be able to, you know, have certificates, like in China, you literally have an app on your phone, that if it's green, it shows that you're, you know, you're good to go. And you can go in the movie theatre If it's a yellow or red, either because you've been through someone by someone infected or you yourself are perhaps sick. You can't go anywhere.

So, I think life will return to normal. I promise you, even there where you're sitting, but it won't be exactly the same kind of life you remember pre-virus. But I'm here to tell you it's possible.

[14:25]

DM: And maybe then just finally, Eric, if you would just talk us through, I looked through your portfolio and I see Treasury Wine Estates, an Australian holding, wine consumption I'm sure has generally gone up, certainly in the home, if not cause we can't go to bars or restaurants. Tell us a little bit about the stock please.

EM: Very good. So, this is of course an Australian wine company, but more than half the business is in Asia. And the real driver is the Penfolds wine brand in China. I don't know what the brand equity that is in Europe, but in China it's one of the very, very top wine brands. So, at the time we engaged the stock was down more than 50% year to date, covered and rated by our analyst down in Sydney. He's our head of research down there. And so, a lot of damage had been done for the stock already. As it pertains to China, a lot of the expensive wine is consumed in restaurants and of course they were all closed in the first quarter. Now they're opening again. And their business selling in the developed world, had a lot of the pantry loading effect, which is to say in Australia that people just cleaned out wine inventory as they saw lockdown coming, which is a great thing.

But it's a high-quality branded consumer company, that has a global reach, has very good brand equity in China. And we basically bought it on the premise that China clearly was starting to open up and that part of the business would improve and that eventually lockdowns would ease in the US and in Australia and elsewhere, and we were able to get it at a very, very, very cheap price. And so, it's a really great example I think of the quality company that never before would have traded at reasonable valuations, but because of all the dislocation in Q1 we got a great price, at least for a short time, and took on the opportunity. How can you go wrong investing in wine? Right.

DM: Well, exactly. Listen, Eric, thank you so much for taking the time to speak to us. Give us, not just a tour of Asian stock markets, but also the good news that there may be some light at the end of a sort of COVID lockdown that we're enduring in Europe at the moment. So, thank you very much for your time today.

EM: Thanks for having me.

DM: For more information on the T. Rowe Price Asian Opportunities Equity fund please visit fundcalibre.com, or to subscribe to the Investing on the go podcast, please subscribe at fundcalibre.com