

## TRANSCRIPT: EPISODE 391

2 April 2026 (pre-recorded 24 March 2026)

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### [INTRODUCTION]

**Staci West (SW):** Welcome back to the Investing on the go podcast brought to you by FundCalibre. This week offers an insider perspective on Asian markets as we cover how to evaluate AI opportunities, navigate dividend growth and balance income with long-term capital growth in the region.

**Chris Salih (CS):** I'm Chris Salih and today I'm delighted to be joined by fund manager Richard Sennitt. Richard has the distinction of managing three Elite Rated products at FundCalibre, in the shape of the Schroder Asian Alpha Plus and the Schroder Asian Income fund. He also manages the Schroder Oriental Income Trust. Richard, thank you very much for joining us today.

**Richard Sennitt (RS):** Well, thank you very much for having me.

### [INTERVIEW]

**CS:** It's no problem at all. Let's start with tech, which obviously Asia is sort of home to some of the fastest growing tech companies in the world. Obviously AI has had an amazing run, particularly in the US. How do you assess AI as a theme in Asia? I mean, are there sectors or countries you particularly prefer? And is the opportunity a bit further behind? Is the upside still there? Maybe just talk to us through that please.

**RS:** Yeah, sure. As you say, obviously AI is a very strong, powerful, global thing, but I think from an Asian perspective, it sort of really manifests itself in the sort of really the enablers around AI. So it's much more in the companies that supply into the US hypescalers, for instance. So the people that manufacture the semiconductor chips and the associated products is where Asia's particularly strong. So here you're thinking of companies like TSMC, Samsung Electronics would be examples of that, and where we tend to find those companies, these largely in North Asia, so Korea and particularly in Taiwan, which have quite long supply chains and have got and have got a rich sort of deep venture companies, which have exposure to that particular theme.

## TRANSCRIPT: EPISODE 391

And I think, you know as long as there is this structural growth in in, in AI demand and the need to continually increase spend there, those companies will be beneficiaries of that. So Korea and Taiwan are benefiting from that. You are also seeing places like China increasingly look at getting into some of that manufacturing side of things. It is a bit harder for them around some of the restrictions that they have. But where I guess they've been a bit more sort of in the news you would've seen over the course of the last sort of 12, 18 months is more around their sort of large language models and so on.

So if you think things like Deep Seek, remember we had that sort of Deep Seek moment a year ago, which is their particular large language model, which was shown to be, you know, very very powerful. And their internet platform companies, there are, you know, bit similar to what we've seen in the US around the hyperscalers. There have been investing quite a lot in semiconductor CapEx related to AI. But for now at least, it's difficult to know exactly where the sort of returns from that are gonna come.

**CS:** When you say CapEx in related to AI, is that things like, I dunno you know, the warehouses, the electrification, that sort of thing around AI, you know, having the hubs that can sort of transfer, can take the energy on board, that sort of thing. What sort of things are you looking at in terms of those related CapEx opportunities?

**RS:** Yeah, within the internet platform companies, it's a bit more around sort of just investing in compute power, so semiconductors, those sorts of things. But there are there are other companies which sort of which you can get exposure to, which include things around, for instance, as you say, the sort of power supply into those data centres.

**CS:** Data centres is the word I was butchering. I couldn't think of, that's what I was thinking maybe China or someone like that might excel there.

**RS:** Yeah. So they are building those out and they are supplying into different parts of the supply chain. I mean, interestingly across, you know, Asia and globally, there are other areas which are benefiting from this sort of things along the reorientation of the grid spend on CapEx related to transmission and distribution for obviously supplying into those what is a power hungry industry. And all those industries do benefit from that.

I'd say that, you know, the other side of the coin within a sort of AI perspective is that, you know, more recently I guess we've seen in markets globally is a bit more sort of focused on some of those companies that potentially sort of could be losing out from sort of a AI disruption. And so they tend to be more on the sort of software side of things. So asset like companies for instance where they're investing, they tend to be more in either software as a service or they could be in sort of e-commerce platforms or, you know, travel online travel agents for instance would be other examples of that their companies, which which you know, potentially do get a bit disruptive from this, but it's a lot. We don't know where, how and how it's all gonna pan out. So it's still very early days there.

From an income perspective, we don't tend to have much exposure to those sorts of companies because they don't tend to pay much in the way of dividends. And the other, from a geographic perspective, I suppose the only other point worth mentioning on that side of things is on for India, which has obviously been a historically a centre of IT services provision. And there, you know, that that is an industry where potentially you see AI disruption as AI becomes more proficient at coding and those sorts of things. And so less manpower is sort of required and so on. So that is sort of a bit of a headwind for that industry.

## TRANSCRIPT: EPISODE 391

**CS:** Okay, obviously AI is a big thing that takes up a lot of column is maybe just talk me through some of the other themes that have been that sort of where you see the opportunities in Asia in the next sort of three to five years. I mean, you've got regime changes, you've got the likes of the new programming career. What are the sort of one or two that sort of jump out to you as the opportunities?

**RS:** Yeah and you're right because I think everyone gets quite fixated with it with AI at the moment, I suppose unsurprisingly, and the market has reflected in that in the sense it has been quite narrow. I guess from my perspective, what I'm sort of been encouraged to see more recently is that there has been a bit more of a broadening out of the market, certainly from an earnings perspective. And I think, you know, if that continues, that's obviously encouraging.

I mean, some of the areas that I like outside of outside of AI have been some of the things where I've been overweight for a while include things like financials. You know, that is a sector where it's quite broad in the sense it's quite heterogeneous. So it's not just banks, it's also insurers, it's also exchange companies. And the long-term growth which we're seeing coming through in Asia more broadly should benefit those companies as penetration of sort of financial products improve.

So if you think sort of insurance products, for instance, so life, all sorts of different forms of protection, health and so on very lowly penetrated in Asia compared to Western markets. And as things have things, as the market grows and the economies continue to develop, we should see increased penetration of those products, which will drive those industries. And on a sort of similar to what you can see that happening in banks in a sense as banks, we sort of think of as being lenders, and of course that's very important part of their job, but also an area of growth from an Asian perspective has been sort of how that sort of wealth management side of those businesses has been growing over time. And that should continue to grow and be of increasing importance for some of the banks across the region as well.

**CS:** You mentioned those banks and the financials in general insurers, et cetera. Is it widespread or is it centred on countries like Singapore and Korea in particular?

**RS:** Yeah, so from a Singapore perspective, we have been overweight in the banks there. And I guess it's Singapore's sort of been benefiting certainly the financial sector's been benefiting from, its sort of increased importance as a financial hub within the region. And that has been a real driver of those well the wealth management side of those businesses, but the businesses more broadly. The other thing I'd say that's been a bit of a help for some of those Southeast Asian banks has been the sort of diversification of supply chains out of China into Southeast Asia. And obviously, you know, Singapore banks and other banks in Southeast Asia are obviously there and can help finance the associated expansion which goes along with that. So there have been beneficiaries of that trend.

The other thing I think from a sort of, and I think you alluded to thereby sort of pointing to sort of Singapore and Korea is that some of these countries have got certainly more have made strides or have continued to make strides or improving their focus on shareholder return and capital return.

So Singapore's already always been a pretty good dividend pay and return of excess cash, but over the last couple of years, the banking sector there has started to optimise that given the high levels of sort of capital ratios that they have. But in career it's been more around a program of sort of value up. Historically a bit like that we've seen in Japan over the last couple of years. And there I guess the story has been a bit more of a focus on in improvements in corporate governance, shareholder focus. And this has seen some companies

## TRANSCRIPT: EPISODE 391

start to increase their dividend payout ratios, for instance. And some of the banks have been examples of that.

**CS:** Okay. Just quickly on Singapore before we move on do you see it as a bit of a portfolio, a bit of a diversifier, or are there certain attractions to, compared to other countries from sort of a portfolio construction perspective?

**RS:** Singapore has traditionally been a bit more defensive than other markets in the region. It's been good at returning cash to shareholders. It's corporate governance has generally been pretty good and therefore it tends to be slightly lower beta than the rest of the region. But even there, over recent year or so, we've started to see improvements in shareholder focus as well as I mentioned in the banks, that's come through in increased dividend payouts and even share buybacks. But also in other industries, you know, there has been a sort of if you like a consolidation in some of the poorer returning areas. And that has made for what is quite a good market structure and you know, in these sort of uncertain times you could prove to be a bit more resilient than some other markets.

**CS:** Okay. You mentioned a bit earlier, obviously the uncertainty at the moment, I'm gonna timestamp it for listeners in case they think we're out of date or anything, but it's sort of the morning of the 24th of March. So obviously the war in Iran caused a lot of uncertainty in terms of oils prices surging, issues with supplier, its supply routes with the straight formula who's been disrupted and closed, which is sort of 20% of the oil goes through there. We are getting lots of concerns and analyst implications on global inflation energy costs and markets. How do you evaluate the impact of that in Asian economies and markets broadly? Or do you just try and ignore it in terms of how you manage the funds and the trust for the longer term?

**RS:** Obviously what's going on has I implications for Asia and the region not least of all that that Asia is a net importer of oil and gas. So from the perspective of a rising oil or gas price, that that clearly is a headwind and the knock on to sort of, you know, potentially onto interest rates, et cetera can be an issue or could be an issue if rates were to go up globally as it sort of tightens tightens liquidity.

I mean, we very much sort of manage the portfolio from a bottom up perspective, so we're very much focused on the companies the sort of durability of the returns of those businesses through time. And we try to take a longer term view on companies and you know, the analysts who are based out of the region, they'll go out and, you know, part of their role is to sort of, you know, factor in, you know not only a base case for valuation, but also a bear case and a bull case. And that provides a good framework to understand what's being priced into stocks at any moment in time. And that can be useful if you're taking a longer term view about what about when you want to be buying oor selling companies.

**CS:** So, sorry, for somewhere like India for example, that has that bit of association with the higher oil price not necessarily being the best thing, is it just a case of that's there in the background to be aware of rather than directly impacting those companies straight away?

**RS:** It depends on a sector by sector basis. I mean, clearly some companies are gonna be impacted more directly by rising fuel prices or the macro environment. But, it is very much a case of gain looking at the business, looking at the long term potential of that business, where are it its returns versus its cost of capital, where do we think they're gonna lie? You know, over not just the sort of next year, but potentially over the next five years and how much of that is priced in, if you like, into the individual stock name. So it's hard to disassociate yourself completely from the macro events that are going on. But the principle driver of the way that we manage money is on a stock basis.

## TRANSCRIPT: EPISODE 391

**CS:** Okay. I wanted to finish by asking a sort of few questions on the Schroder Oriental Income Trust. It's AIC dividend hero, or it's a Next Gen dividend hero, it's got 19 years of dividend increases and I believe it hopefully touch wood celebrates its 20th anniversary later this year. Maybe just talk to the listeners about how you sort of balance the search for income and capital growth and how you communicate the trade off between sort of yield and growth potential.

**RS:** Yep. Yeah, I think it's a important point because it does mean that the vehicle perhaps can perform differently in different sorts of markets. And I should say from an income perspective, we're very much focused on, you know generating a natural income if you like. We're not looking to pay out of capital, you know, we obviously it's a trust, so we do have reserves that we can use, but that been obviously generated by previous dividends paid by underlying companies over the years. So it's very much that focus on natural. Therefore, the types of businesses that we are gonna own are naturally gonna have to have a natural income because we're gonna need to have we're gonna have to have dividends paid by those companies that can then be paid out to shareholders within the trust.

That income rationale does mean that you're likely to have a bit of a value tilt to the trust rather than it be more focused on a growth area. And that's because there's certain areas of the market where perhaps you're likely to get less exposure to that don't really pay much in the way of dividends. So, you know, within an Asian context, one of those areas would be say Chinese internet platform companies who don't pay much in the way of dividend. And so we don't have much in the way of exposure to that area. But what we don't do is just screen the universe for the highest yielding stocks and sort of backfill the portfolio with that. What we are looking to do is to buy into companies that have got an income rationale to own them, but they've also got potential upside to their fair value as well.

**CS:** That must be interesting for you because you've got places like you, we talked about Singapore and Korea, but you've also got places like China where it's becoming more of a dividend culture slowly there. Is the pool growing as fast as it's ever grown for you at the moment?

**RS:** Yeah, I mean there definitely if you look at programs across the region that are focused on improving shareholder returns, as you say, we're seeing that clearly in Korea, in Singapore, we're seeing it in as you say, mentioned in China amongst certain companies. So from that perspective, there is a push to in a lot of these markets to improve shareholder returns through dividends, but also sometimes through buybacks as well. And part of that is driven by domestic investors in those countries that are asking for more, more dividends.

The other thing which I think is important is that, you know, when you look at Asia as a whole, it is a big region, there is a lot of choice from a dividend picker's perspective if you like. So for an active manager of money in Asia to find names which are in different economies, different industries of interest from an income perspective, and therefore it's quite a good diversifier from that perspective. And people sometimes question, you know, the resilience of dividends coming out of Asia, and yes, Asia is a bit of a cyclical market, but payout ratios are generally quite low. And what that does mean is that if things do slow down, there's not necessarily a direct need for companies to cut their dividends in line with the fallen profits.

**CS:** And if memory serves the trust - Oriental Income - still has tech as perhaps its largest sector exposure, but you have been trimming it down a bit recently. We talked about AI earlier. Is that just a concern about how expensive things are becoming in AI or are you just finding better opportunities elsewhere? Maybe just, just run us through how that approaches to tech within the Oriental Income Trust.

## TRANSCRIPT: EPISODE 391

**RS:** Yeah. You're absolutely right. If you looked at the trust sort of 12, 18 months ago, we would've been overweight in IT. We've been set selectively reducing that over over the course of the last year or so. And that you know, that is a reflection of in part how well the sector as a whole has done from a valuation, from a price perspective and what that means for valuations of the sector. But it's also a reflection of the, you know AI is clearly a great structural industry from a growth perspective, but it will most likely be cyclical as well in the sense that at the moment supply of a lot of the semiconductors is relatively limited and there's little supply coming on over the next one, two years. But as we get closer to that coming through, people will start to be a bit bit more concerned about potential supply coming on, particularly if some of the returns on the investment that these big US companies are making doesn't pan out as they expected. So all I'm doing is really recognising the fact that some of these stocks have have done quite well on that basis rather than sort of a big shift in view of the underlying fundamentals.

**CS:** Okay. And you mentioned the fundamentals there, but obviously there's a few areas that you have sort of been adding to when the defensive sort of space, the likes of utilities, consumer staples and healthcare that perhaps not the things that people immediately think of when they think of Asia, perhaps a bit more when it comes to Asian income. Maybe just explain the reasoning behind it. Is it the uncertainty or is it the ripples of China's changing views? What's pushed you into those three areas?

**RS:** Yeah, I mean, it's more around, I've sort of got suddenly got a bearish outlook for the region or that I wanna, because of what's been going on or anything like that. I mean, I've been slowly doing this over time. It's more a reflection of where the stock opportunities are coming up from a valuation perspective. Those sectors that you mentioned have been have lagged the overall market over the last 12, 18 months or so. And therefore, unsurprisingly from a valuation perspective, they're starting to throw out more opportunities from a from a stock perspective than they had done previously. So again, it's that sort of, I guess a natural sort of rotation that you see as valuations in some areas start to become a bit more full in other areas, they naturally become a bit more attractive. So it is a reflection of that.

**CS:** And just quickly, in terms of the overall balance of the portfolio, so obviously in tech, you'd expect the sort of the growth element to be stronger in the sort of the income and dividends to be slightly lower when you move away from that. Do you try and maintain that balance by looking for other areas where it's more leaning towards growth over income? Or is it if the shape of the portfolio changes you're just happy to accept that?

**RS:** The shape of the portfolio changes because of the sort of, if you like the pull on capital from, you know, relative from individual stock names. What I'm not doing, if you like, is saying, oh, I wanna buy a growth stock here and a defensive stock there. As such, I'm looking at the individual stock and what I think its potential return could potentially be over time, the income rationale and so on and so forth. And because of that income rationale, I think what you do see relatively consistently through time is that the sort of overall blend of the portfolio will end up on that sort of value to with a value tilt rather than a growth one. And you know, the size of that may depend a bit on, you know, what's in vogue or not in vogue at the time.

**CS:** Okay. On that note, Richard, thank you very much for spending some time with this today.

**RS:** Not at all, thank you very much for having me.

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