



Matthews Asia Perspective

Uncovering Opportunities in Asia's Tech Sector



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So far this year, technology has been the best-performing sector in the MSCI All Country Asia ex Japan Index. Tech has taken up a large part of the broad index weighting and comprises about one-third of the overall index. Shares of some large-capitalization tech companies in Asia have delivered strong performance. As a result, they have driven up the tech sector weighting relative to the broader market. The question that is currently top of mind for many investors: Do these types of stocks represent the best opportunities in Asia's tech sector right now?

In terms of valuations, a lot of attention has been focused on internet-related businesses that are trading at high multiples with forward-looking one-year P/E (price-to-earnings) ratios of 40 or more. I believe investors generally should be careful about valuations for these e-commerce/internet-related names. I see more attractive valuations in other technology names that have reasonable forward-looking, one-year P/E's in the high single digits, especially relating to quality global franchises. On top of strong business fundamentals and reasonable valuation multiples, we see another layer that can support good share price performance because we believe that such companies can return more excess cash to shareholders.

As technology is such an integral part of daily life, we are interested in companies that have underlying businesses that are driven by a secular increase in data consumption. The smartphone is a prevailing device today that incrementally consumes a significant amount of data, creating demand in terms of data network capacity. This requires telecommunications companies to constantly increase overall network quality and bandwidth, creating interesting business opportunities for key suppliers.

The migration of 4G wireless technology to 5G, for example, is driving up wireless telecom capital expenditures. Certain businesses provide the telecom hardware equipment to enable the transition into 5G and these suppliers could see accelerating earnings growth in the years ahead. Valuations for these kinds of businesses, which are trading at much lower multiples, would be much different from those of well-known Chinese internet/e-commerce names. What is interesting about these names, however, is that many analysts still appear to be playing catch-up, meaning they will wait to see actual earnings before revising their forecasts. That is why we think there are investing opportunities in some of Asia's telecom equipment companies and data infrastructure businesses.

Another area of interest is semiconductors and the ways in which the so-called Internet of Things is changing how we as a society use smart technologies. The use of semiconductor chips in various devices has been growing steadily. It creates a market not only for the larger semiconductor companies, but opportunities for big and small businesses alike. Today, the overall semiconductor manufacturing process is changing rapidly to maintain and improve production efficiencies as the quality threshold for smart technology devices has been raised.

Lastly is the overall automation trend as manual manufacturing is being rapidly replaced by robots. Companies that are key component vendors are at a very interesting stage in that cycle. Many companies have already shown strong share price performance this year, but bottom-up stock research can uncover some of these stocks at reasonable valuations.

Index definitions

The MSCI All Country Asia ex Japan Index is a free float-adjusted market capitalization-weighted index of the stock markets of China, Hong Kong, India, Indonesia, Malaysia, Philippines, Singapore, South Korea, Taiwan and Thailand.

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