From PowerHouse to PowerCentre

The Megatrends Shaping Asia's Economic Leadership in a Post-Covid World

Part One: Changing Demographics

UOB Asset Management

Asia as a PowerCentre

A number of megatrends prevalent in Asia have increased in potency since the Covid pandemic. Three megatrends stand out as having the potential to put Asia at the helm of future global growth. In a three part series, we examine each of these megatrends in detail and the investment opportunities that are expected to emerge or strengthen as a result.

- Changing demographics
- Go Green
- The Digital Economy

Part One: Changing Demographics

As in the rest of the world, Covid heightened a number of pre-existing population trends. This further accentuated the change in Asian countries' age and income profiles, and will have a significant long term impact on Asian economies.

Content:

Investing In Asian Megatrends

Equity ownership is one of the most powerful forces of wealth creation. The process of securitising equity ownership into small shares opens that ownership opportunity to everyone. With equity ownership, one's wealth can grow by more than what one's labour can earn, and the opportunity is not limited to only those with the capital to start businesses. In the modern world, anyone with any amount of savings can participate in wealth creation and this simple process is one of the most egalitarian features of modern society.

But within these equity opportunities there are different potential approaches to investing. In this report, we highlight the opportunities in focusing on megatrends as an investment opportunity. This contrasts with the common practice of leveraging on short-term market events.

Most basically, a broad market diversified fund has usually been able to provide returns in relation to the economic growth of a country or region and the risk premium involved in the market. Megatrend investments, on the other hand, are trying to target the structural trends that go beyond the normal market trends. Over the years there have been strong structural trends that have provided outsized returns beyond normal risk premia associated with the investments. These megatrends have frequently been challenging to analyse but over years can yield returns far beyond what normal markets can provide.

For example, in the late 1990's, investments in internet stocks was a megatrend that captured the imagination of many investors. Henry Blodget, who was an equity analyst with CIBC Oppenheimer in 1998, famously predicted that Amazon stock would soar from the then price of $250 per share to over $400 per share by the end of the year. This seemed an outrageous call at the time, but within three weeks it had surpassed that value.

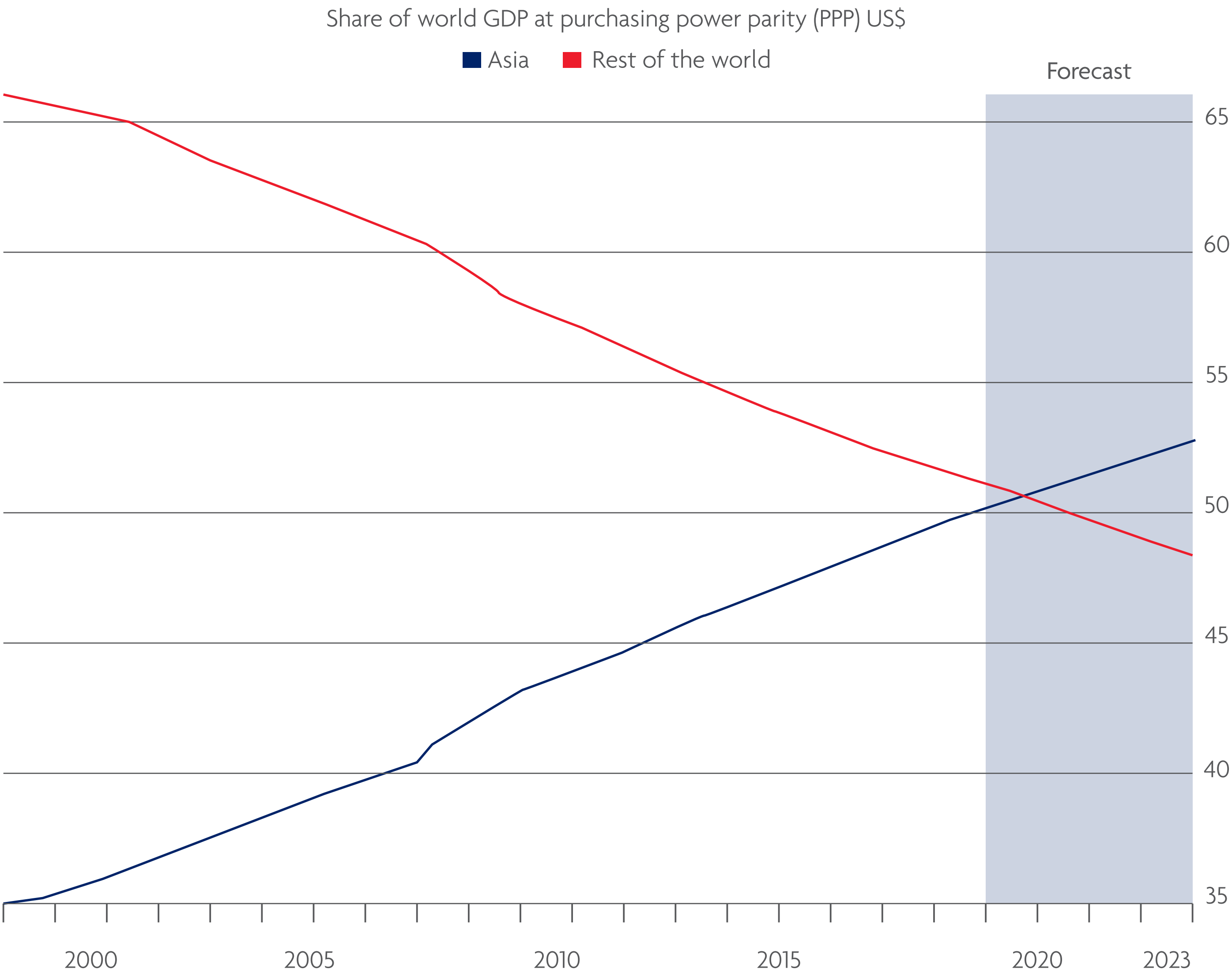
This highlights investors' desire to participate in new trends. By the end of 1998, Amazon had risen to 10 times its price at the start of the year. But then the dotcom bubble burst and by 2002, Amazon shares fell back to levels seen at the start of 1998. Many highlighted the fallacy of investment "fads". But over time and throughout the cyclical ups and downs of markets, strong structural trends can persevere.

Today, Amazon stock is worth 650 times what it was worth in early 1998. With the benefit of hindsight, it is clear that megatrends can and do prevail. However, not all megatrends do as well as the Amazon example. Normal broad market investments already give investors a strong way to participate in the wealth creation that come with growing economies. Megatrend investing, although potentially powerful, must prove to be a strong structural trend outside the normal directional benefit of economic growth. Plus, the benefits can take years to bear out.

At UOB Asset Management, we seek to give investors access to both. We aim to offer our clients the traditional participation of broad market wealth creation and potentially steady average market returns. In addition, we look to uncover exciting megatrends and investment themes that have the potential for stronger long-term returns.

While identifying impactful megatrends can be challenging, our analysts and portfolio managers see several of these and are starting to employ them into the funds that they manage. We acknowledge that there are a number of important trends and sub-trends – and therefore investible opportunities – in the world today, including those that have been boosted by the Covid pandemic. However, we believe that many of these are subsumed within the broad megatrends that we are examining in this report.

Figure 1: The Asian century has begun



Source: IMF, FT, UNCTAD definition of Asia

Our extensive Asian network places us at the heart of many of these megatrend opportunities. In 2020, Asia's economy officially overtook the rest of the world combined and kicked off a new era of Asian economic leadership that some experts are calling the "Asian Century". Today nearly half of the world's 500 biggest companies by revenue, and over a third of the world's 330 unicorns, are Asian.

But Asia is not just an engine of growth. It is also becoming a centre of activity. The new Regional Comprehensive Economic Partnership (RCEP) which came into force at the start of this year is the world's largest trading bloc by economic size. Members include 15 East Asian, Southeast Asian, and Pacific nations and the bloc accounts for 30.5 percent of the world's GDP, against the European Union's 17.9 percent and the USMCA's (United States-Mexico-Canada) 28 percent. Intra-regional trade prior to RCEP already amounted to US$2.3 trillion in 2019, and this number is now expected to rise by a further US$42 billion.

The Covid pandemic has also opened the world's eyes to Asia's operational capabilities. Despite the fact that most Asian countries have lower average incomes and a less mature public sector than in the US and Europe, they were able to demonstrate remarkable efficiency in dealing with the pandemic.

To date, many global investors still appear to think that US and European companies are at the forefront of key investment themes. But not only does Asia offer some of the world's most exciting megatrend opportunities, Asian companies are often best placed to tap them. UOB Asset Management's network of investment managers across the region allows for intensive research into the sectors and companies that have the potential to benefit from key trends.

Asia Is Getting Younger ... And Older

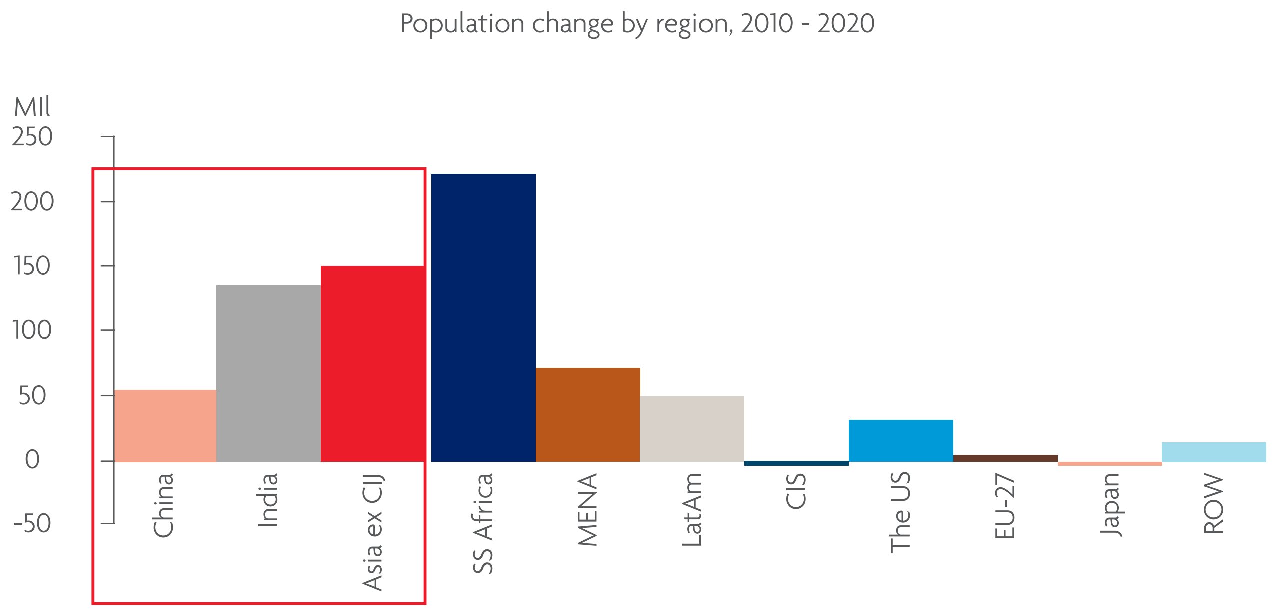
There have been many demographic transformations in play in Asia over the past few decades. However, several have reached a critical point in Asia's development and its relationship with the rest of the world. These are expected to have a significant impact on the region's investment landscape over the medium and long term.

Changing Demographics			
1. Population growth	2. Rise of millennials	3. Increasing affluence	4. Aging societies

1. Population growth

The world's population is still growing exponentially. It took more than 50,000 years for the world population to reach 1 billion people. Since 1960, we have added successive billions every one to two decades. According to the International Monetary Fund, the world population was 3 billion in 1960. It took just 40 years for the population to double to 6 billion. The United Nations projects that in the next 40 years, the population across the globe will surpass 9 billion, led by emerging markets in South Asia and Africa.

Figure 2: More and more Asians



Source: UN, OECD, UOB Economics, December 2019

Today, less developed countries represent the vast majority - 84 percent - of the world's population. This share was just 68 percent in 1950 and will continue to rise sharply because virtually all of the nearly 2 billion net additions to world population projected over the next three decades will occur in less developed regions countries. This is a major concern, because less developed regions, as classified by the United Nations, tend to be more fragile - politically, socially, economically, and ecologically - than their more developed counterparts.

However, strong population growth also means a younger population profile for these countries. A large population of younger individuals represent a more attractive balance between working age populations and retired workers. Growing populations also mean a large market for products and services, and a larger work force at a time of increasing labour shortage and supply chain kinks in the developed regions. And finally, the population skew toward younger profiles brings with it attractive sectors such as millennials.

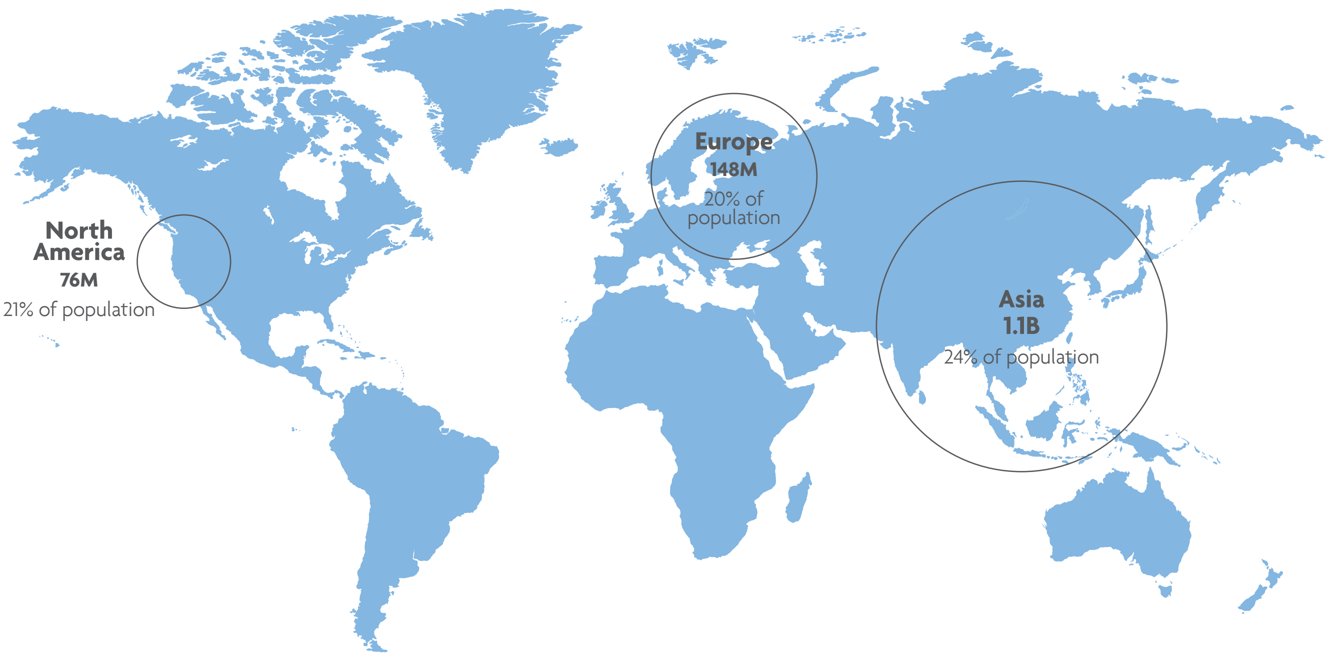
2. Rise of millennials

Consumers who are both youthful and affluent are a welcome prospect for businesses. Formally defined as the cohort of individuals born between 1980 – 1994, millennials globally are widely recognised to be better educated, more digitally savvy, and often more affluent than their parents. Millennials offer businesses the opportunity to cultivate customers who they can grow with and learn to support. This in turn helps secure a revenue stream that remains intact for many years, if not decades. Marketing departments around the world are targeting millennials as a key customer segment, and not surprisingly, many have their eye on Asia.

The number of millennials in Asia are a quarter of the world's millennial population. This is far in excess of those in the US and Europe. The same is true for those coming of age, i.e. Gen Zers – born between 1995 and 2012. Besides their total size, these Asia millennials and Gen Zers have consumer traits not shared by their US and European counterparts. According to a report by the Singapore Economic Development Board and Economist Intelligence Unit, they are not just digital natives but also mobile natives. Their heavy use of mobile e-payment and chat services to make and influence purchasing decisions means that they have broader and more complex tastes than Western millennials.

Figure 4: Asian millennials rule

Millennials (born 1980 – 1994) by region



Source: United Nations World Population Prospects, 2019

Chinese millennials are a particular force to be reckoned with. They were the first in the country to be born into the country's modern economic era and as such are also the first to enjoy true spending power and financial freedom. It is estimated that 70 percent of Chinese millennials own their own home, compared to 40 percent worldwide, based on an average annual income of about US$20,000 and an equivalent in annual debt.

Overall, Chinese millennials have more disposable income than their parents or their US counterparts, and are highly digitally aware. Therefore in contrast to the US, where the boomer generation remains the country's market movers, millennials are redefining all aspects of China's economic growth, social structures, and public sphere.

Millennials in developing Asian markets will also come to prominence over the next decade. However, unlike their Chinese counterparts, this is not the result of individual earning power, but of inter-generational wealth transfers. It is estimated that US$ 930 billion will change hands over this period as Asian Boomers enter their 70s and 80s. This transfer exercise will see millennials in control of 35 percent of Asia's wealth in the next five to seven years.

3. Increasing affluence

If demographics is destiny, then a growing middle class is a decisive factor in investment outcomes. While access to growing populations is a plus for corporates, profitability is based on those growing populations developing a middle class that will consume discretionary goods, build homes, furnish homes, buy cars, and raise children.

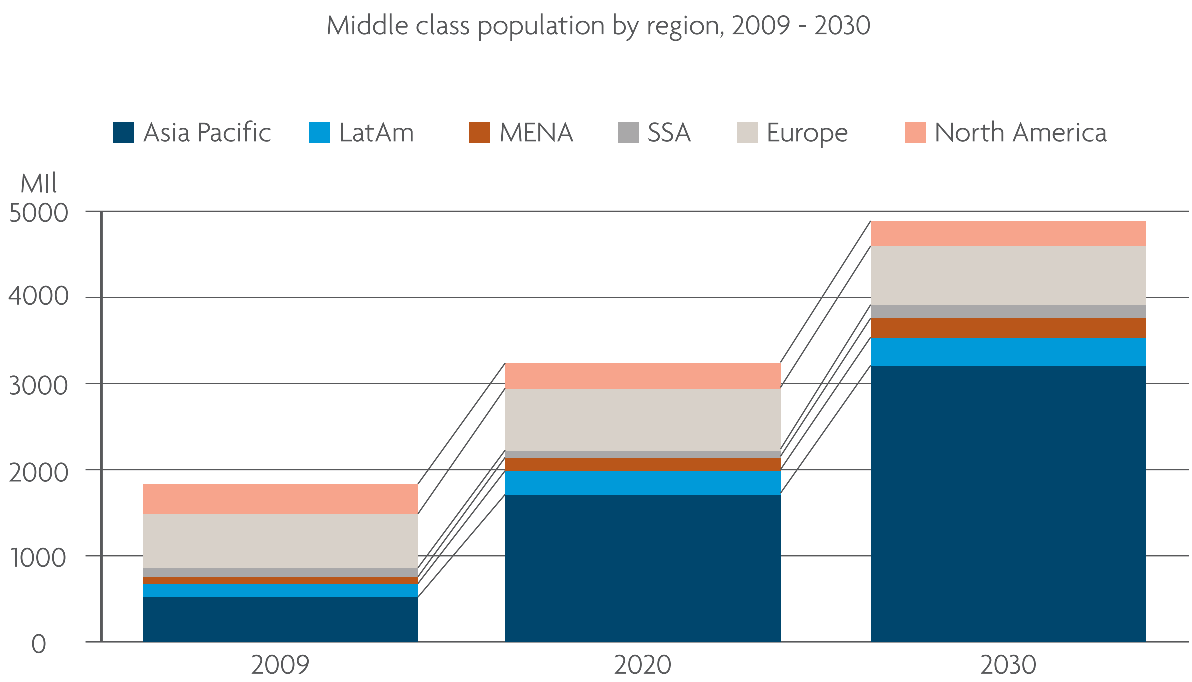
This aligns to widely applied definitions of "middle class". Over the years, analysts have used either an absolute global definition or a relative one for each country. In both cases, the definition is anchored on purchasing power. A range of US$11 - US$100 in purchasing power parity (PPP) per capita per day is commonly used to characterise "middle income" households. Meanwhile, those only capable of daily spending that is less than US$11 is characterised as "poor and vulnerable".

In 2019, a tipping point was reached. We know of course that the middle class segment has continued to expand in developing countries. But two years ago, it was estimated that globally, the number of individuals with a purchasing power exceeding US$11 equalled those with a purchasing power below US$11. This suggests that in many developing countries, there is now a critical mass of middle-class households.

Asia is both the biggest contributor and beneficiary of this demographic dividend. This region is where the highest middle class growth has and will come from in the coming decade. Going forward, developed markets are not expected to see any meaningful growth of their middle class population. In contrast, the middle class in Asia has more than doubled in the past decade and is expected to double again in the next decade.

Asia's middle class already accounts for more than half of the world's middle class population and over 40 percent of global middle class consumption. In the next decade, the growth of this segment in Asia is expected to be larger than the current total size of the equivalent segment in developed markets. This will not only help sustain global growth, but elevate Asia into a position of global consumer-led economic leadership.

Figure 3: Asian consumers dominate



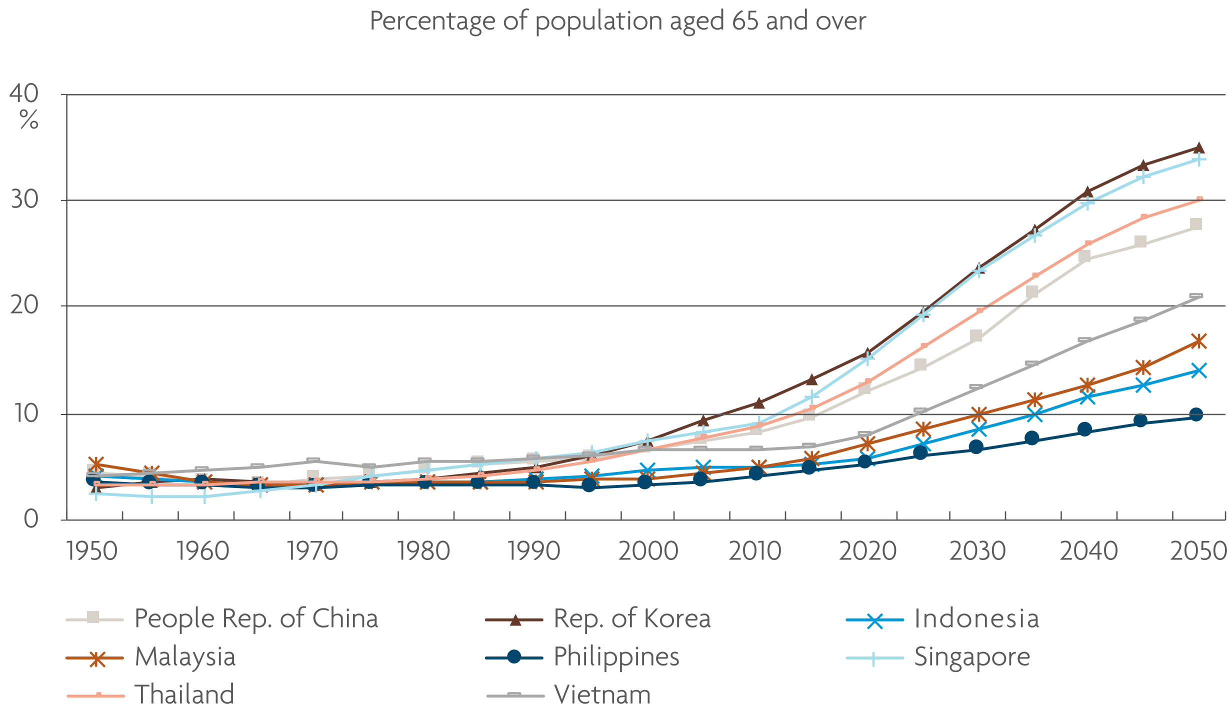
Source: UN, OECD, UOB Economics, December 2019

4. Aging societies

Population aging is the dominant demographic trend of the twenty-first century. This is not just a reflection of increasing longevity, but also steeply declining fertility rates and the progression of large numbers into the older cohorts. Never before in the history of mankind have such large numbers of people reached or surpassed the conventional old-age threshold of 65. One billion individuals are expected to be added to this cohort in the next three to four decades, on top of the more than 700 million people there today. Of this group, those aged 85 and over are growing especially fast and could exceed half a billion in the next 80 years. This trend is significant because the needs and capacities of the over-85s tend to differ significantly from those of aged 65 to 84.

A vast proportion of the over-65s will come from the Asian region. The Asian Development Bank (ADB) estimates that by 2050, 923 million of the world's elderly will be Asian. This puts Asia on track to become one of the oldest regions in the world. But alongside the absolute numbers, the pace of aging in Asia is also breathtaking. In almost all countries, the percentage of over-65s remained well under 10 percent until two decades ago. Since then, this share has risen steadily, especially in countries like South Korea, Singapore, and Thailand, squeezing into 20 years what took 60 years to evolve in developed countries.

Figure 6: Asia is aging fast



Source: Asian Development Bank

The progression of the population aging phenomenon differs considerably across countries. In Thailand's case, improvements in healthcare, a steep decline in birth rates, and increased life expectancy all helped to double the percentage of over 65s - from 6.6 percent in 2000 to 13 percent in 2020.

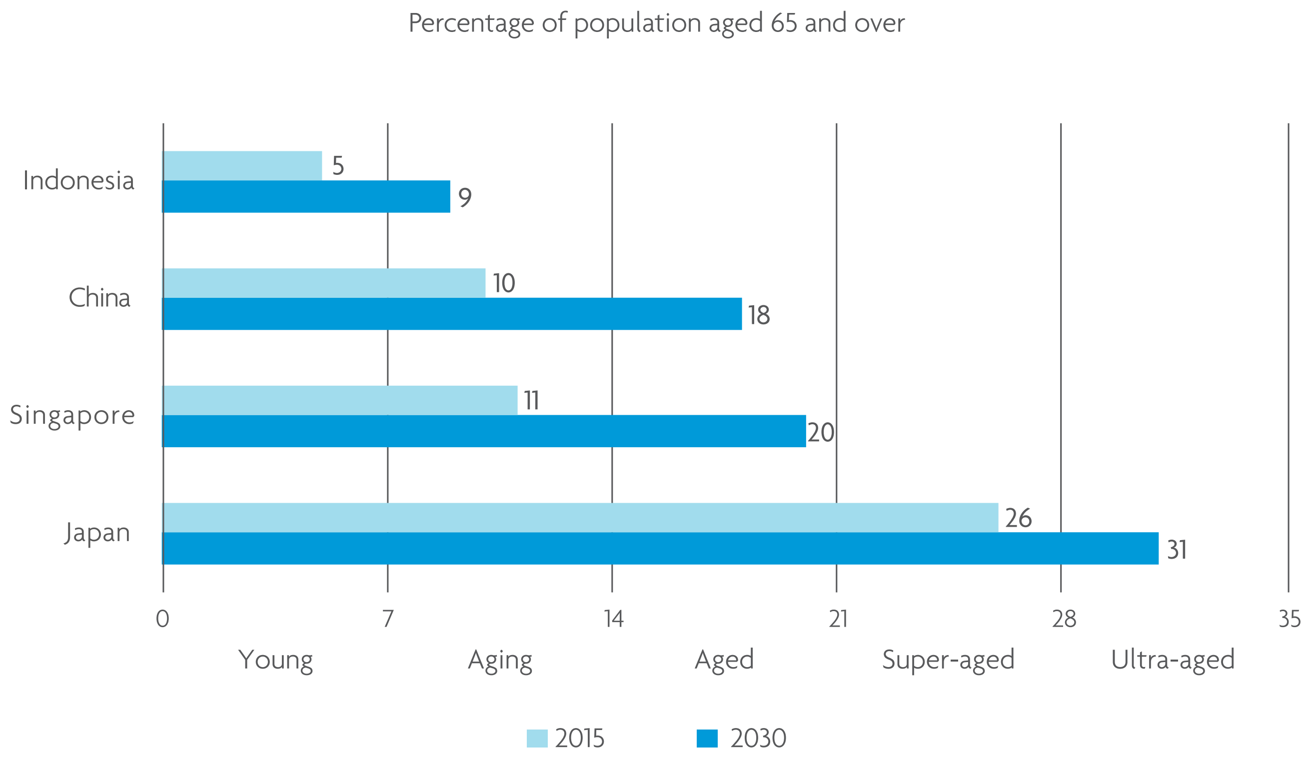
As elsewhere, Thailand's rapid aging is sounding alarm bells, but also opens up new avenues for growth. Economists have expressed concerns about the downward pressure on economic growth due to labour and capital shortages that become apparent when populations age. These labour market stresses were further exacerbated during Thailand's Covid outbreak.

It is also worth noting the different problems that wealthy and less wealthy nations may encounter. In a wealthy country, it is common for asset prices to fall as a growing cohort of older people seeks to support itself by liquidating investments. Fiscal problems arise because government coffers become strained by rising pension liabilities. In less wealthy nations like Thailand, there are fewer resources to overcome the challenges of individual aging. A particular issue confronting the country currently is the high cost of treating long-term chronic ailments associated with old age, such as cancer and cardiovascular disease.

To track the depth of the challenges and opportunities posed by old age, countries are now categorised according to the percentage of elderly in the population. Those with more than 21 percent of their population aged over-65 are now defined as "super-aged", and more than 28 percent as "ultra-aged". For example, Japan has long been a world leader in term of its old age population. In 2015, the country had close to 26 percent of its population aged 65 and over, triple the world average.

However, by 2030, this number is expected to reach 31 percent, making Japan the first in the world to be termed an "ultra-aged" nation. That said, over the next two decades, it is thought that 29 countries and territories will join Japan in this category. Europe is following in Japan's footsteps and the US is not that far behind.

Figure 5: Asian super-aged and ultra-aged societies



Source: Marsh & McLennan, Oxford Economics, World Bank, UN Population Division

At the same time, many Asian countries will enter the super-aged category. To prepare for this eventuality, governments are considering a number of age-defying policy measures. These include the extension of working lives, increasing the participation of women in the workforce, opening the doors to migrant workers, and upskilling workers to achieve productivity gains.

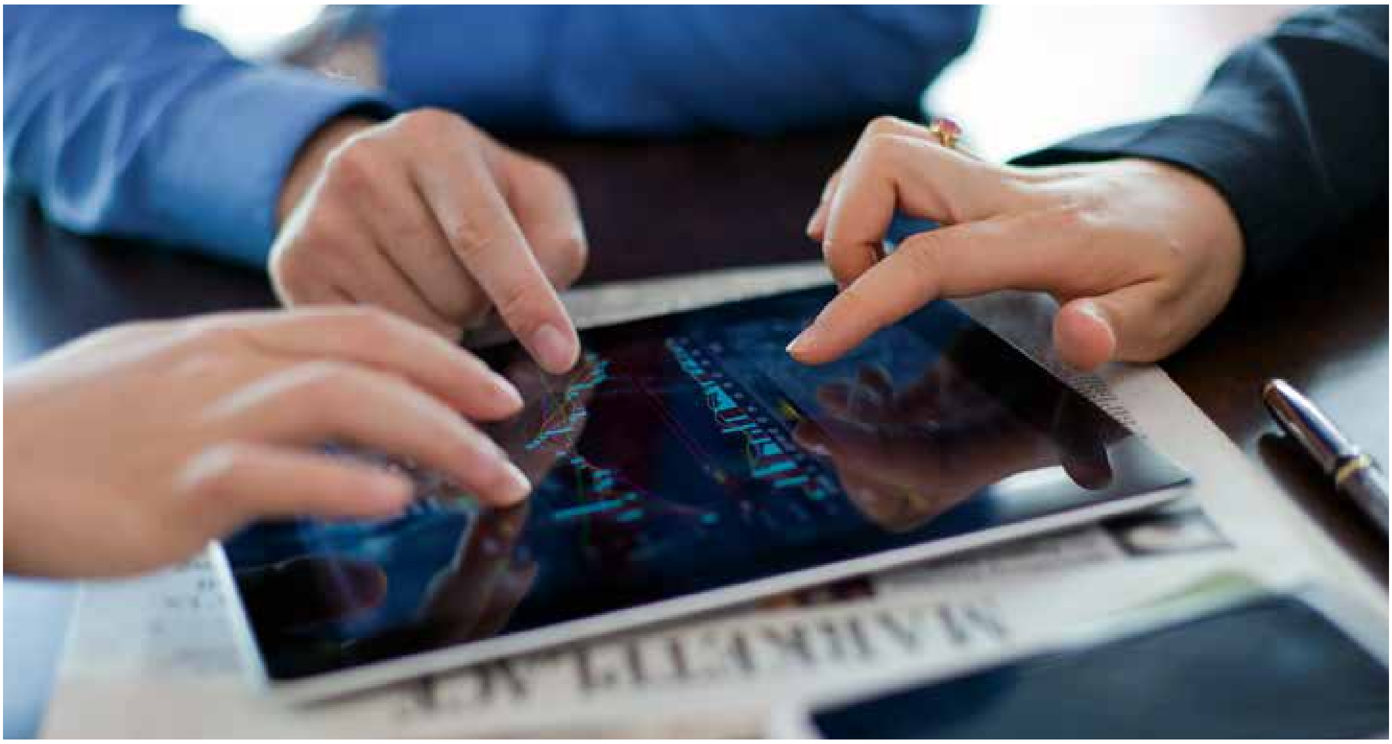
Technological innovations can also help ameliorate the effects of population aging. These include new drugs to slow the process of aging, the invention and deployment of assistive devices such as robots, and new models of home health care, public transportation systems, and urban design.

Investment Implications

Logistics, construction and transportation

US-China tensions and Covid-induced supply chain disruptions are a big plus for Asia's large and young workforce. The deepening of US-China tensions is having positive consequences for Asia. In an attempt to sidestep both these superpowers, investments are starting to flow instead to non-partisan countries such as ASEAN nations, Japan and South Korea. Labour-intensive businesses in particular, including electronics and consumer sectors, are most likely to shift their operations given their limited ability to cope with higher tariffs or geo-political shocks. ASEAN countries like Indonesia and Malaysia offer a stable investment climate and a ready pool of workers to capitalise on companies looking to diversify beyond China.

The pandemic-related disruptions to global supply chains are also favouring Asian economies. Few could have foreseen the travel restrictions, quarantine requirements and export bans imposed during the pandemic and many companies were caught short. But there are now concerted efforts to ensure that the resulting shortage of critical goods and raw materials is not repeated. This includes reducing an over-reliance on a few suppliers, switching to more digitalised trade and logistics processes, and the establishment local sales networks. Asian logistics, construction, transportation sectors offering digitised solutions and a productive workforce are the primary beneficiaries of these supply chain relocations and diversifications.



Consumer services and wealth management

Asia's growing affluence bodes well for the consumer and wealth management sectors
As Asia's middle-class individuals progress through their careers and working lives, they are having families, buying houses and cars and spending on education, recreation, culture, arts and entertainment. At the same time, they are thinking forward and planning to provide for their families' future savings, wealth management, insurance, and needs.

Given the speed of growth of this middle class market, companies still have the opportunity to capitalise on first-mover strategies for many consumer and financial products and services. For example, it is estimated that 73 percent of Southeast Asians remain unbanked or underbanked. Furthermore, there are now opportunities to overcome adoption barriers via the use of digital solutions. A report by Google, Temasek Holdings and Bain & Company suggests that up to 40 million people in six ASEAN countries - Singapore, Malaysia, Indonesia, the Philippines, Vietnam and Thailand - came online for the first time in 2020 as a result of the Covid pandemic. This puts internet penetration at nearly 70 percent of the population and paves the way for the growth of digitally-enabled middle class consumption.

Healthtech, edtech and greentech

Asian millennials will drive the demand for innovation and sustainability.

The one billion millennials in Asia provide the market scale for technological innovations. Meanwhile, the pandemic crisis has caused these innovations to come thick and fast. Health concerns, social restrictions and lockdown conditions have all acted as catalysts for sustainable tech advances aimed largely at the digitally initiated.

Within HealthTech, the priority has been to make healthcare more accessible via the use of data, telemedicine and robotics. As infrastructure improves and these services become more familiar, the demand for remote diagnostics, online mental healthcare, virtual fitness, and robot-enabled home palliative care looks set to grow.

Within EdTech, eyes are opening to the potential for non-classroom based learning. While remote schooling is nothing new, EdTech capabilities now extend to e-attendance of even the most prestigious of global educational institutions, made available to students from around the world.

Within GreenTech, post-Covid initiatives have been boosted by millennials' greater sensitivity to social and environmental issues, and heightened awareness of global connectivity. For many, it is not good enough to simply recover to pre-Covid standards. Millennial consumers want more green real estate, green transport, green food production and green infrastructure.

Travel, recreation and health services

Older segments of the population have different needs than their younger compatriots

This is even more apparent for those who live longer, are better educated, and have higher wealth reserves. As these individuals move towards and beyond their retirement age, their spending is likely to veer away from the mass market. In fact to date, the older generation are the key drivers of "experiential commerce" within the more developed markets. Given that they are no longer working but financially secure, this group are making more expensive lifestyle choices, including on big ticket travel, recreation and cultural pursuits.

However, across the wider elderly population, it is healthcare spending that is the biggest concern for governments and biggest opportunity for the private sector. Asian healthcare experts see a strong need for better integration across public-private boundaries to deal with the rapid growth of the elderly population. This collaboration can extend beyond primary and secondary care to training and sharing of medical expertise. Over the next decade, significant organisational and operational changes in Asia's health services for the elderly will throw up the potential for exciting new business models.

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