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New Asian dividend culture lures investors

By Steve Johnson
Cash-rich Asian business have long been a byword for profligacy and waste. All too often stories have emerged of companies frittering away their surplus cash in ill-conceived non-core operations – corporate golf courses a regional speciality – or funnelling it into a headlong rush for market share and revenues, at the expense of profit.

Investors keen on actually receiving some of their money back in the form of dividends – long shown to be the key driver of long-term returns – largely chose to stick to developed markets.

But a growing band of intrepid equity income investors are now charting a course for Asia in the belief that these stereotypes no longer apply.

"Asia is a very good market for yield but is ignored by investors. There has been a different approach from many companies in terms of their acceptance that they should pay dividends," says Mark Williams, whose Liontrust Asia Income fund, with a target yield of 4.5 per cent, is due to launch next month.

Steve Thornber, whose Threadneedle Global Equity Income fund now has 25 per cent of its holdings in Asia, well ahead of the benchmark weighting of 10-12 per cent, adds: "The income culture has been growing. [A decade ago] I would not have had as much in Asia because there wouldn't have been so many income opportunities. In the last four or five years more and more companies have started rewarding shareholders with dividends. It has changed and it's still changing."

The figures give credence to these perceptions. According to data from Thomson Reuters, the payout from the Chinese equity market has jumped from 0.79 per cent to 3.15 per cent in the past five years, with dividend yields also rising in Hong Kong, Taiwan, Singapore, Malaysia, the Philippines and India, although the latter, along with South Korea, remains a laggard with yields of just 1.3-1.5 per cent.

The yield across Asia ex-Japan is now 3.16 per cent, according to FTSE Group, above the US, Japan and the global average of 2.7 per cent, although a little below that available in the UK and continental Europe.

"Five years ago you didn't get any income, it was all about capital growth, but there has been a levelling out of yield across markets," says Andrew Green, who leads the investment services team at Deloitte. "So many more Asian-based companies are just much more mature global companies. That means they have to pay dividends of some nature to be treated as mature companies."

Jason Pidcock, manager of the £1.3bn Newton Asian Income fund, says pay-out ratios in Asia have risen to 40 per cent of net earnings, in line with the global average, a trend he assigns to a maturing of Asian markets.

With Asian companies, on average, perhaps in ruder health than those elsewhere, this means that 26 per cent of stocks yielding 3 per cent or more are now in Asia-Pacific ex-Japan, he says, more than in any other region. In 1995, Asia lagged behind North America, Europe and the UK on this measure.

The seeds of this development are widely attributed to the Asian financial crisis of 1997, when Asian companies found themselves cut off from the capital markets. Many companies found they needed to treat their shareholders better to regain that access.

Mr Pidcock believes the change in mindset was more profound still. "After the Asian crisis a lot of families that had very high ownership levels of their listed companies saw their wealth massively marked down.

"The easiest way to take wealth out was through dividends and they saw there was a virtuous cycle. The return on equity picked up, they weren't frittering money away and the p/es [price/earnings ratios] were re-rated. Even though they had taken cash out the value of their remaining stock was not any lower, so they kept it up."

Mr Pidcock points to the growth of Asian domestic institutions, such as pension funds, that require income. Moreover the Chinese government, a big domestic shareholder, has made it clear it would rather like to receive a little more income.

There are some countervailing factors, with Mr Williams accepting that some companies may increase capital expenditure, possibly at the expense of dividends, when the global economy improves, although he does not believe that will be enough to reverse the trend for higher pay-out ratios. "It's long term, it's not due to the crisis because companies can't find anywhere to invest their money," he argues.

For the time being, he is happy there are fewer opportunities for reinvestment. "One of the problems in Asia has been a misallocation of capital. If they do it on a more sensible basis, rather than the Asian disease of just looking at market share or revenue, it's more of a sign that companies are well managed."

And while Mr Thornber sees plenty of opportunity in high-yielding technology and telecoms plays, he is wary of "quasi government organisations", such as the big Chinese oil companies, which may be run more in the national interest than in the interests of minority shareholders.

Perhaps the strongest argument for the concept is the suggestion that it can generate market-beating returns.

Mr Pidcock's fund has delivered 82.7 per cent after fees over the past five years, comfortably outstripping the 24.1 per cent total return of the FTSE Asia Pacific ex-Japan Index. Most other Asian income funds have also beaten the index, although typically by a smaller margin.

Mr Pidcock sees plenty of scope for others to join the party. "It's definitely not a saturated area. The amount of money that is chasing high-yield stocks in particular in Asia is still a tiny proportion of all the money coming into Asia," he says.