

APS ASSET MANAGEMENT: Fundamental research is key

BY EILEEN LIAN

APS Asset Management is bullish about China's A-share market, forecasting strong earnings growth over the next few years, with at least a 15 to 20 per cent jump in earnings this year.

The Singapore-based investment management firm is expecting a 3 to 5 per cent appreciation in the Renminbi per annum over the next five years and a tax unification, likely to be ratified by China's National People's Congress in the first half of this year, which will bring the corporate tax rate for many A-share companies down from 33 per cent to 25 per cent.

Both these spell good news for investors. "Valuation of the market is still quite reasonable taking into account all these factors," said James Liu, deputy chief investment officer at APS.

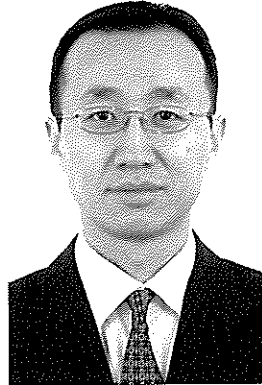
The company won *Asia Asset Management's* 2006 Best of the Best award for Best China Equity (1 year). It is currently one of the largest foreign players in the Chinese A-share market with more than US\$500 million assets under management and two research offices in China, one in Shanghai and the other in Dongguan, Southern China.

However, the company sees last year's strong rally in the A-share market, which had the Shanghai Stock Exchange A-share index move up by 130.6 per cent and Shenzhen's by 96.4 per cent, as a signal for vigilance.

"Investors may see a short-term correction and we have started to take caution over the market," remarked Mr Liu.

Still, the non-tradable share reform, which had about 95 per cent of A-share companies convert their non-tradable state-owned shares into tradable stocks as of end-2006, has paved the way for a healthier stock market in China, Mr Liu added.

He also expects that a larger number of quality Chinese companies will seek listing on the domestic bourses, enlarging



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the shopping list of investors going forward. And once the full flotation is in place for all companies this year, corporate governance, installation of management incentive schemes and the facilitation of mergers and acquisitions should be enhanced.

At the moment, corporate governance is a key issue with some Chinese A-share companies and APS is careful to stay clear of companies that are badly managed and with poor track records in terms of corporate governance.

The boutique house considers itself a pure stock picker with a very bottom up strategy. "In other words, we kick the tyres by ourselves," said Mr Liu. "We rather spend more time on

the companies, conducting our ground research than to work intensively on the macro numbers."

The firm would first identify long-term structural and business trends and then pick up individual stocks that can ride on these trends, which could last for a few years.

It also likes the out of favour stocks that are not garnering any buy recommendations and whose earnings have been depressed in the past few quarters or longer for various reasons.

"As long as the fundamentals are still sound, valuations are attractive and management are honest and competent, we will have the conviction to incorporate them into our portfolio," Mr Liu explained. "Our decisions are not affected by their short-term performance since we are a long-term investor."

APS recognises the private sector as one of the engines of growth in the Chinese economy, as private companies have been expanding fairly rapidly relative to the state-owned sector.

"There are many private enterprises listed on the China A-share market. We like them a lot as they can deliver a fairly high "g" to us, usually in the high 20s or in the 30s," elaborated Mr Liu.