INVESTING STRATEGIES

China's 'MIT' is why Wong of APS remains a bull

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'The best years of China are not behind, but ahead. And therefore, my view is that China is very likely to have entered a multi-year bull market' / Photo: Albert Chua

For veteran fund manager Wong Kok Hoi, the recent pickup in China's stock markets is a clear vindication. When Chinese stocks were beaten down over the past few years, he stuck to his guns and declared his optimism loudly.

"I've never seen this kind of value in China in the last few years. I am bullish not because I expect very high growth rates; I am bullish because the market has more than discounted the bad news out there," he told *The Edge Singapore* in an interview in November 2023.

Since then, China's stock market has gained more than 50%. In a recent interview, Wong reiterates his stance that this is just the beginning, and not the end. "If you look out for five years or 10 years, China's success will not be less than in the past. The best years of China are not behind, but ahead. And therefore, my view is that China is very likely to have entered a multi-year bull market."

The APS All China Alpha Fund, Wong's flagship fund, reported year-to-date net returns of 35.44% as of Aug 29, outperforming the MSCI China All Shares NTR Index, which is used as the reference index. Over one year, the disparity was bigger with APS at 63.08% vs MSCI's 43.54%. The firm's AUM has reached US$2.2 billion, up from US$1.4 billion when he last spoke to The Edge Singapore in late 2023.

As he has been consistently doing so, Wong spends half his time in China, visiting companies, including many repeat visits. During these visits, Wong was able to sense that more than half of them were able to show better results, despite the headlines of headwinds which China faces. "It is a matter of time that some of these companies will be able to either launch better products or report higher earnings," he reasons.

Wong says he is optimistic because of another fundamental reason. Numerous stocks were trading at significantly below their intrinsic value, at significant fractions of their book values. Despite the recent gains, many are still commanding deep value.

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One reason perhaps is that international investors were spooked by repor by the Western media that have been painting all kinds of dire scenarios, such as how China will go the way of Japan into a balance sheet recession, and so on. "Some of these really lacked analytical rigour, they just wanted to

smear China," says Wong, who held the view that the market prices then reflected a lot of these negative views.

M-I-T

Wong has summed up what he thinks are three key factors in China's favour: manufacturing, innovation and talent, or as he quips, M-I-T.

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With decades of hardcore experience as the world's manufacturing hub, China is today the maker of more than a third of manufactured products around the world. "Manufacturing is not about just factories, machines and workers. It is an ecosystem that includes infrastructure, power plants, your highways, airports, sea ports and so on," he adds.

China has built such a complete manufacturing ecosystem; no other country, not India, not Vietnam, not Japan, not the US, can duplicate China's manufacturing progress in the next ten to 20 or even 50 years, says Wong, adding that China has an additional advantage in the form of its "very disciplined" army of workers and engineers.

To widen its competitive edge, China is now in the midst of a Beijing-led push to introduce AI capabilities into manufacturing processes. For example, AI is used to design new models and new products, which will shorten the design process and also lower costs. DeepSeek, the homegrown AI platform, has not just gotten the US worried; it has also inspired a new generation of young Chinese to make their mark in AI as well.

Wong acknowledges that in the past few decades, there has been a comm view that the Chinese are not innovative, as they prefer to copy products already created by others and then try and produce cheaper versions of their own. He explains that it was because Chinese businesses dic

sufficient resources to spend on innovation and then wait out the eventual payback. This is different from saying they are not innovative.

He points out that a big proportion of R&D engineers in Silicon Valley are ethnic Chinese. For example, at least half of Facebook's recently assembled "superintelligence" team is made up of Chinese. "Why would US tech companies spend so much money on Chinese engineers?

China, of course, has recognised the need to innovate, for if not, the sustained success will hit a wall at some point. Wong, for a good measure, points out that the Chinese were behind key inventions throughout history, including papermaking, printing, the magnetic compass and gunpowder.

Another factor is talent, which Wong says refers to not just engineering talent but also entrepreneurial talent and even managerial talent — all of whom would be needed to come together to drive the economy up to the next level. Even policy-making talent is seen to be available in bigger numbers, he adds.

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Wong, drawing reference to China's traditional system of selecting bureaucrats via a series of examinations, believes that there is no lack of managerial talent to help formulate and implement effective economic policies.

At the core, meanwhile, would be the six million science and engineering graduates the country's universities produce each year, more than what the US, Japan, UK, Germany, France and Italy train in aggregate. With this large base, there is a bigger chance that there will be innovators and risk-taking entrepreneurs who will emerge successfully and make their mark in the ne fields, be it in semiconductors, biotechnology, humanoids and so on. "From here onwards, you'll get a lot of innovation in the country, and that's important for China's continued success," says Wong.

Lithography versus rare earths

China's push to develop its own capabilities has made several sectors such as semiconductors, biotechnology, drone technology and of course, artificial intelligence something investors ought to pay close attention to.

Specifically, Semiconductor Manufacturing International Corporation, the state-backed chip maker, is what Wong says is a company that is at the "core" of China's technological advancement — the kind of entity that "cannot fail".

To him, this is a stock that is "pretty well covered, but not well understood". By most common measures, this stock at current levels seems expensive, but Wong believes it is not. Due to various forms of trade and technical restrictions, the company is basically the only leading foundry that companies in China can tap into in the next five years or longer to manufacture seven-nanometre chips — not the most cutting-edge but a generation of chips good enough for most applications today. "There's a long queue," he adds.

Wong reasons that as SMIC gains more experience and expertise, it will be able to improve its technology and processes further and thereby its yield — a measurement of chips that are usable — and therefore the profitability. This will improve with both volume and margins, although generally the more advanced the processes, the lower the yield.

Wong readily agrees that the industry leader by far, Taiwan Semiconductor Manufacturing Corp, is "significantly superior" to SMIC in terms of technology, with a gap of three generations, but this is a gap that will narrow. For one, China has more talent than Taiwan. "We are also reaching the end of Moor[illegible] Law, which means it is very difficult for TSMC to move to even more advanced node chips," he adds.

One reason why TSMC can stay ahead for years is its access to th[illegible] cutting-edge capital equipment, the kind sold by ASML, which face[illegible]

restrictions on what it can sell to China.
In response, Chinese firms are actively developing their own machines — not as advanced as ASML's for now but good enough for more mature processes — and are steadily narrowing the gap.

Meanwhile, in this politics-fraught global economy and trading environment, China has a trump card in the form of its rare earths production capacities and processing capabilities.

Specifically, it is a key exporter of rare earths, where its various elements are critical materials needed in defence, medical and broader electronics industries of other nations. When other countries let their own rare earth mining and processing industries falter, China went the other way. It now controls 92% of the processing capacity, and the US imports 70% of its rare earth demand from China. Due to the lack of engineering expertise in this field, the US will take years to restart its own rare earths production and processing capacities. In the meantime, China can choose to play this card each time negotiations become difficult, says Wong.

He also points out that the US and China did not reach a trade agreement even after their third meeting in Stockholm. However, the doors are still open for either side; they are still talking, as they recognise they need each other in equal parts. "This is the reciprocity rule that must be respected," Wong adds.

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