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"All In" on Chinese Assets:

Optimistic About Hard Tech's Investment Potential

– Interview with Wong Kok Hoi, Founder and co-CIO of APS Asset Management

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Since entering the Chinese market in 2002, APS Asset Management has navigated through many cycles of bull and bear markets, maintaining a steadfast and rising conviction in Chinese equities. Recently, Wong Kok Hoi, founder and co-CIO of the Singapore-based asset management firm, shared his enduring belief in, and insights about, investing in China during an interview with Xinhua Finance. Wong emphasized that currently, the valuation of China's stock market is highly attractive, and is optimistic about investment prospects in hard tech sectors such as semiconductors and auto components.

Becoming the "Patient Capital" Investing in China

Rewinding to 2004, China's capital markets were in their early stages of development, and many international investors keenly recognized the enormous investment potential driven by China's rapid economic growth. Against this backdrop, APS launched its first offshore China A-share fund, building a bridge between international capital and China's growing investment opportunities. Today, APS manages approximately CNY15 billion in China equity strategies.

As investors with the "patient capital" mindset in China, APS' equity strategies have consistently been nearly fully invested, even amidst frequent fluctuations in China's stock market. When asked why the firm remains so committed to being "All In" on Chinese equities, Wong provided three key reasons:

1. China has built a manufacturing eco-system that has both scale and efficiency, contributing roughly one-third of the world's manufacturing output.
2. China's rapid technological ascent is spectacular, achieving global leadership or parity with Western nations in many critical technological areas.
3. Finally, the dedication, hard work, and resourcefulness of Chinese employees, researchers, and engineers remain a significant driving force behind China's economic progress.

In recent years, some foreign private fund management firms have struggled to adapt to the nuances of China's market, resulting in stagnating fund raising and poor investment performance. Wong highlighted that the stability of a firm's core investment team is crucial for the firm's long-term development. Currently, APS' core portfolio managers have worked together at APS for 29, 28, and 20 years, respectively. This long-term and close collaboration fosters a high degree of constructive synergy among team members and results in a consistent application of its investment framework.

Investment is More Than Just Reading Financial Statements – It Requires Active Research

APS applies the Four Alpha-Hats® framework to all its investments. The framework categorizes target companies' investment theses into Structural, Economic, Dynamic, and Opportunistic Alpha groups. Structural Alpha companies are driven by long-term industry trends and companies' core competitiveness. Economic Alpha stocks are characterized by stable cash flows and market sell-offs that lead to mispricing. Dynamic Alpha stocks are influenced by fluctuations in the business or economic cycle, while Opportunistic Alpha stocks are often propelled by special events such as mergers or corporate restructuring.

Wong shared that for most stocks in his portfolio, he does not just analyze financial reports in the office. Instead, he conducts on-site due diligence visits at companies multiple times to gain deeper insights. "Spending hours in face-to-face discussions with company founders often reveals details and critical information that are hard to glean from public sources," Wong remarked.

During busy seasons, Wong might meet with four to five companies in a single day, maintaining this pace for as long as two weeks at a time. Over the past two years, his research journeys have taken him across cities like Beijing, Shenzhen, Wuhu, Hefei, Hangzhou, Nanjing, and Fuzhou, and even to Xinjiang for first-hand information.

One intriguing anecdote from Wong's research experience involves a listed company's founder who rarely interacted directly with investors but unexpectedly agreed to Wong's request for a one-on-one meeting. When asked why, the founder candidly admitted that while the company's recent performance had been subpar, the fund managed by Wong consistently appeared on the company's shareholder list.

This unwavering support piqued the founder's curiosity – what kind of investor had such steadfast confidence in the company? In their subsequent in-depth discussion, Wong and the founder exchanged valuable insights. Over time, the company's stock price began to rebound, affirming Wong's judgment and vision.

"A miss is as good as a mile". Wong believes that in the field of investing, the ability to detect subtleties and nuances is critical. APS leverages in-depth analysis of alternative data to meticulously score the quality and growth potential of its portfolio companies. In APS' investment framework, ESG (Environmental, Social, and Governance) is a key consideration and plays an increasingly significant role in investment decisions. However, challenges such as data transparency and uniformity of data standards persist in China's ESG landscape. To address these issues, APS collaborated with an AI company to develop a bespoke AI-enabled fundamental ESG research system. This system assigns scores to every company in the portfolio, using AI technology to extract and process alternative data, effectively supplementing standardized financial information. This cutting-edge tool empowers APS to gain deeper insights into companies, enabling informed investment decisions and enhancing the overall rigor of its ESG considerations.

A "Turning Point" Approaches: Investment Potential in Hard Tech

Looking ahead, Wong believes that Chinese assets prices are poised to exhibit stronger upward potential. First, after a prolonged bear market, the Chinese stock market seemed to have reached a turning point, with investor sentiment bottoming out. Current market valuations are also highly attractive because of the massive sell-down over the past four years. At the same time, China's relatively high real interest rates leave room for further rate cuts by the central bank, paving the way for improved liquidity in the future. Crucially, proactive fiscal policies and moderately accommodative monetary policies are expected to provide solid support for corporate earnings growth. These factors combined are likely to drive the stock market higher.

In this market environment, Wong suggests that investors should focus on three categories of stocks:

1. **Hard tech companies**: Sectors such as semiconductors and electric vehicle components are expected to emerge as leading drivers of economic growth in the coming years. These industries stand to benefit from advancements in technological innovations and improved profitability, positioning them for standout performance.
2. **State-owned enterprises (SOEs) and central government-controlled listed companies**: These companies offer compelling investment opportunities due to policy support, reform initiatives, market capitalization management, and dividend policies. They have demonstrated strong stability and resilience.
3. **Deep value stocks**: These are companies with stable business models and robust balance sheets. While their growth rates may be modest, they are characterized by low capital expenditures and high dividend payouts. These stocks are often ignored and undervalued by the market.

Overall, Wong highlights hard tech sectors – including semiconductors, auto components, and defense – as well as pharmaceuticals, healthcare, consumer goods, software services, and cybersecurity, as the areas offering rich pickings. Investors should pay close attention to stocks in these industries.

This interview was translated from Chinese into English. The original interview can be found here.

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