BARRON'S INTERVIEW

8 China Stock Picks from Atlantis' Liu Yang

The outspoken hedge fund manager profits from Beijing's policy cues and isn't afraid of triple digit PEs.

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By
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Liu Yang is in pain. The Atlantis hedge fund manager put her back out playing golf and has an acupuncturist coming over after her sit-down with *Barron's Asia* in Hong Kong. "I'm getting to that age," says the vociferous 49-year old, who manages about USD1 billion in Greater China stock funds.

Pain is gain, as they say though: Especially when you run China's first and biggest dedicated healthcare stock fund. "Ten years ago people didn't even realize you could invest in healthcare. Who cared about China at that time?," Liu recalls. Well, they certainly do now. Her healthcare fund invests in everything from online drug platforms to stem cell companies and in the last five years has consistently outperformed the MSCI Asia-Pacific ex Japan Healthcare Index. "Nowadays healthcare's as sexy as the internet. This is a must-own and must-overweight sector," she says.

Liu Yang - CIO and fund manager at Atlantis Investment Management.

It's going to get even sexier, she claims. Liu doesn't mince words when she says China needs to spend more on healthcare, with this being one obvious spur for the market. "The GDP per capita the Chinese government is spending on healthcare is just 5% - that's pathetic." For reference, that's less than other emerging markets like Russia, Brazil and South Africa. That means there's plenty of room to grow and there are signs it is: Deloitte reckons that market will grow 12% annually until 2018, hitting USD900 billion. The Chinese government has made healthcare reform a major policy focus in recent years, shaking up everything from access to drugs, health insurance and foreign investment in the sector.

Liu's current healthcare holdings include drug promoter China Medical System (ticker: 867.HK), a stock which is up more than 20% since *Barron's Asia* wrote positively about the stock in September. Beware though: some of her picks require a strong stomach. SeaRainbow Holding (000503.CN) could leave some reaching for a sedative: It started life as a chemical fiber maker before moving into online games. It now sells drugs over the internet. The stock was temporarily suspended from trading twice last year and its forward PE ratio is a nauseating 270 times. Still, it's up about 22% since September. Traditional medicine firm Nantong Jinghua Pharmaceutical (002349.CN) is another one she owns. This area of healthcare has high barriers to entry, according to Liu. "Traditional Chinese medicine can't be learned - it stays within the Chinese community," she reasons. Regardless, it's up over 80% in the last three months and at 80 times forward earnings it's a 'cheaper' alternative.

She's not willing to give the Chinese market a totally clean bill of health, though. After running up almost 60% between New Year and June, the Shanghai Composite then endured a 45% selloff over the summer. The index recovered to close about 10% higher for the year. That rebound didn't impress Liu much though: she described the rebound as a technical one that "doesn't really matter much." Liu says the smart money is waiting on the sidelines for now, with fresh catalysts likely to come from the next session of the National People's Congress in March. "Until you see clear policy and clear direction, would you really dare to put money into the market?" she asks.

Liu makes a full-time job out of following the scent of policy clues, and she's made a lot of money for herself and clients doing just that. Her investment approach is predominantly top-down, Liu says. She hones in on the Communist Party's next big policy push and parks money in companies that benefit from it. It took her a while to figure this out though, she's all too happy to admit. "I lost a lot of money before because I didn't understand the government policies. There's no textbook that tells you how to invest in China." Based on this approach, she likes stocks in biotech, environmental energy, and internet sectors. Her picks include sewage treatment play China Water Affairs Group (855.HK), which is up more than 20% in the last couple of months. "We've made a fortune out of it already," Liu enthuses. Biotech small cap Golden Meditech (801.HK) is another holding. The stem cell storage company has more cash on the books than its HKD3 billion market cap, suggesting it's undervalued by the market. "That stock's going to fly high for sure," she beams.

A selection of China's onshore blue chips looks cheap as well, she reckons. Liu's enthusiastic on Midea Group (000333.CN), China's largest seller of electrical appliances. The stock was trading for more than CNY41 over summer, but has come way off since investors began euthanizing their A-share portfolios from June onwards. Shares are currently priced at a touch under CNY30 and Liu says it's been oversold. Midea trades at an inexpensive 10 times trailing earnings, not too far off its five-year low. "With this company in ten years I've made a return of ten times," Liu claims.

She points to other stocks going cheap. Windshield maker Fuyao Group Glass's (600660.CH) stock price was shattered earlier in the year, falling from a high of CNY18 to as low as CNY11. The shares have staged a recovery since, but still trade at a reasonable 13 times earnings. Yunnan Baiyao Group (000538.CN), a big traditional Chinese medicine company, has been misdiagnosed by investors. The shares have a PE ratio of 27 times trailing earnings – not a bargain on first glance – but not far off the stock's five-year basement. "The market leaders with big brands names - these are the ones that look really cheap," Liu believes. "They've been oversold."

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