# Michael Liang

✲ CIO ✲ Foundation Asset Management

Liang helped establish Foundation in Hong Kong in 2006 with UOB and Britain's CIM Investment Management. The Foundation China Opportunities Fund launched in early 2007 and now has $13 million of assets.

**What is the fund's objective?**
We're looking to generate value-based absolute returns with a China focus, and we do that through four related sub-strategies: Garp (growth at reasonable price), recovery, deep value and alpha shorts.

Value investing is now interesting. There are strong macro headwinds, rising inflation and slowing global demand. Investor psychology is uncertain and edgy, but valuations have become more reasonable.

**How do you see valuations?**
There seem to be reasonable valuations for long-term investors with a two-to-three year investment horizon. Of course running an absolute-return fund makes timing all the more important. We don't have the luxury of looking at a three-year time horizon.

Most China funds are focusing on growth, which is good but not sufficient. We also need to figure out entry points and have a good understanding of market dynamics in order to decide the overall portfolio exposure. Stocks that have been beaten down because of macroeconomic policy uncertainties can offer short-term opportunities as well as long-term value.

**Where do you find such stocks?**
There are downstream and mid-stream industrial companies that have been hammered down because of price controls in China. We think those policy risks won't diminish entirely but may reduce after the Olympics.

We see value in certain consumer names. Investors who want to be in China should be there for one simple reason, and that is its people. In my opinion, Chinese people are natural born capitalists. Rising domestic consumption in China is a growth driver that we have to focus on. There are some firms there which already have very substantial share of a new market segment it operates; I think they have the potential to become highly successful companies.

**What about financials?**
For banks, NPLs are on the rise, but from a low base. However, the market is very smart in trying to discount what is going to happen in six months to a year's time, where there may be rising risks.

**Can you give an example of how you play recovery stocks?**
Coal companies face limits on coal prices because of price controls on electricity tariffs. In my opinion it's a nice idea but it's very hard to implement as China is so reliant on coal for its energy, and so demand for coal will increase. In the meantime the price of some coal companies have been beaten down due to policy risks. Therefore I see some core value in that sector.

**How do you approach 'growth' companies?**
As value investors, we have to understand what makes a company an organic-growth company and the differences between them and cyclical companies. We want to pay for companies that can continuously deliver growth over a prolonged period, and those companies are very rare in China. Once you find them though, you don't want to let them go.

**For how long do you retain your holdings?**
Our absolute returns are defined by a calendar year.

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When we enter into a new position, we estimate a target price which is usually very different from sell-side brokers' targets, and seek a margin of safety in the entry price. Then we feel more comfortable holding on for longer periods. To do this though you need very rigorous risk controls. We manage those risks using hard stop-loss limits.

Given the current volatility, we have narrowed our hard stop-loss band, from 8% to 5%. We are happy to crystallize our losses. The visibility of the market is very low and we don't want to risk "falling in love" with our stocks.

**What has performance been?**
Down about 9.6% year to June, so that's a little better than our peer group average. Last year we made 36%. Of course, I'm not satisfied being down and we are striving to recoup those losses in the second half of the year. It is our big challenge. Our net exposure can range from negative 30% to positive 90%. Right now we are about 35% positive exposure. That exposure will fluctuate depending on the way that we think markets are heading.

More important though is our bottom-up analysis of the companies we buy. I think we have a reasonable chance to make a comeback.

**What is your outlook for the market?**
Given the mixed picture of macro policies and decelerating earnings growth, it's understandable for people to worry about comes next. However if you look at valuations a lot of potential bad news has been factored in, so I am optimistic.

Where the market goes from here I think depends on continuation of policy reforms, which are positive for the country as a whole. The equity risk premium has not lowered, though, and I think this means that people are concerned about the continuation of reforms.

You cannot decouple a bottom-up analysis from the rest of the market. That would make for an extremely painful way of running an absolute-return fund.

**In what areas are you short?**
We only try to make money from company-specific shorts, not the market in general. We use the index to hedge but try to generate profit from shorting individual stocks, say H shares in Hong Kong.

Take, for example, fertilizer companies: people like these stocks because of the rising food prices and likelihood of more fertilizers being used. What people may not understand is the supply side of this business and the existence of price caps on domestic selling prices.

Many of these individual companies may not enjoy rising fertilizer prices because they act as distributors, they don't actually produce the fertilizer.

Some of the mid-sized Chinese banks have gone through a tremendous period of earnings growth and there may be some negative impact on margins and NPLs. Some of their large valuation premiums might need to come back.

**What is the mood amongst investors towards China?**
Very cautious. They might like China for the next 20-30 years but would prefer to stay out at the moment, even if that means missing the first 10-15% of profit. It's hard to raise new capital, but we are on the verge of closing a couple of investments and hope to grow our assets to $30 million this year. ■

**PERSONAL CV**

**CAREER**
2007-present: Foundation Asset Management, CIO

2003-06: UOB Kay Hian, director

2000-03: DBS Vickers, vice president

1998-2000: Daiwa SMCB, vice president

1997-98: SG Securities, vice president

1993-97: Macquarie Equities (Australia)

**EDUCATION**
2006: Peking University, EMBA

2001: CFA

1993: University of Wollongong, BCom