

INVESTOR'S BUSINESS DAILY

MONDAY, MARCH 13, 2006

FRONT PAGE

Chinese Stocks Are Back Again, With New And Broad Leadership

State-owned giants and nimble high-tech firms riding red-hot economy

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China-based stocks have reawakened after two years of sleepy performance.

The 80 Chinese firms that trade as ADRs in the U.S. have gained 13% since Oct. 28, even with the recent overall market retreat.

Names such as PetroChina, NetEase and China Medical Technologies have landed on IBD performance lists such as the IBD 100 and the Weekly Review.

Why the revival? China's economy has been going strong for years — so strong that many U.S. investors worried it wouldn't last.

"The fear over the last year or so that China's economy was overheating and heading to a fall has now dissipated," said Donald Straszheim, who heads Roth Capital Partners' investment in and research on China.

Investors now realize "China has the capacity to grow at 9% a year for a long, long time," he said.

More Chinese ADRs Now

It's not just a handful of Chinese Web portals that grabbed so much attention in 2003.

Chinese energy giants such



as PetroChina and Sinopec Shanghai Petro continue to shine, thanks to soaring oil prices.

There's also a whole new crop of Chinese-based U.S. ADRs, many of which are charging ahead.

Ctrip.com debuted in December 2003. The Chinese Web travel site shot up in 2005, surging 84% from late April to early October.

After basing for several months, Ctrip broke out again last month.

Vimicro's U.S. ADRs debuted at \$10 in November. After basing for the past several weeks, it surged 15% Friday to a new high. The chipmaker enjoys triple-digit and accelerating profit and sales growth.

Mike Donnelly, vice president and senior portfolio manager with American Century, said U.S. investors have also benefited from the yuan's modest rise vs. the dollar.

"If you have an ADR, it's going to be the local price times the exchange rate," he said. "If the exchange rate appreciates . . . the value of the investment does too."

Pressure is growing in Washington for China to more aggressively revalue the yuan. But Donnelly notes a big appreciation would hurt Chinese banks' big Treasury holdings as well as Chinese exporters.

Romeo Dator, a manager at U.S. Global Investor's China Region Opportunity fund, agreed saber rattling over the yuan bears watching.

"If it actually results in anything that restricts free trade, that's definitely a negative," he said. "But at some point (the yuan) will become free floating."

Dator said Chinese financial firms such as China Life Insurance have fared well as the government promotes consumption.

Wireless firms such as China Mobile also should see increased demand from that shift, Dator said.

China's hot growth is benefiting Singapore, Korea, Hong Kong and Taiwan, Donnelly noted. "The region is growing very rapidly."

2 Kinds Of Chinese Stocks

The number of Chinese companies listed on U.S. exchanges has multiplied in recent years.

"The best companies in China don't list on the domestic exchanges in China, which are highly suspect," Straszheim said. "They want to list in America."

There are basically two types of Chinese ADRs in the U.S.

Big caps — like PetroChina, China Unicom and China Telecom — trade primarily on the New York Stock Exchange. They represent state-owned firms that Beijing has sold a piece of to investors.

Nasdaq-listed Chinese companies are a different breed. They have no state ownership, tend to be high tech and are typically run by managers who were educated and often trained in the U.S.

"They get a taste of American capitalism and they're smart and ambitious," Straszheim said. "They say 'I can do that' and they go home and form one of these companies."

State-owned firms have pluses and minuses, Straszheim said.

"They can grant you tax breaks or they can give you monopoly power," he said.

The state can also make moves without consulting investors.

"A couple of years ago (the Chinese government) removed the CEOs of a couple of these big telecom companies overnight," he said. "It just happened. There was no debate. It was just done."