

## Investing in China a tricky business at the best of times, experts say

Craig Wong, The Canadian Press, On Thursday June 9, 2011, 3:15 pm EDT

OTTAWA - Investing can be a tricky business at the best of times, but investing in Chinese companies takes the concept of buyer beware to a higher level.

Kai Li, a finance professor at UBC's Sauder School of Business, characterizes the Chinese stock market as something "worse than a casino" where insider trading, poor corporate disclosure and lousy shareholder protection are just the beginning of the list of potential pitfalls.

"It is not a fair game," said Li, who has strong connections to China.

"I am proud of the Chinese economy, but I don't think the Chinese stock market represents the Chinese economy."

Canadian investors can gain exposure to China in a number of ways. Investing in Canadian-based companies that have operations in China or sell goods into the country is the most common and lowest-risk method, but it lacks the bang some investors are expecting from one of the world's hottest economies.

Mutual funds that invest in Chinese companies may be another, while investing in Chinese companies that obtain listing on major international exchanges such as the Toronto or New York markets also give exposure to the world's fastest-growing market.

There are more than 50 Chinese companies listed on the Toronto Stock Exchange and the TSX Venture Exchange.

While most are listed on the junior exchange, more than a dozen are listed on the senior market and a handful have a stock market value of more than \$1 billion, including China Gold International Resources Corp. (TSX:CGG) and Silvercorp Metals Inc. (TSX:SVM).

Li said an overseas listing offers some comfort for investors because it means the company must meet the same accounting and disclosure standards as Western companies. But even then, Li said, investors need to be cautious.

Last month, Yahoo Inc. was stung after Chinese Internet company Alibaba Group, in which Yahoo holds a 43 per cent stake, spun off its online payment service Alipay into a separate company controlled by its CEO, Jack Ma, without giving Yahoo anything in return.

In Canada, shares in Toronto-listed Sino-Forest (TSX:TRE) plunged last week after a little-known U.S. financial analyst trashed the Chinese company in a report that accused the timberland owner of exaggerating its assets and sales.

The stock lost three-quarters of its value in the days following the report and debt ratings agency Moody's raised concerns about the company even if the allegations are eventually proven false.

Dan Ondrack, a business professor at the University of Toronto's Rotman School of Management, noted the Chinese legal system should be of special concern for outside investors.

"The legal system is actually an agency of the government and so you can't depend on the legal system on being impartial," he said, though he noted that China is evolving.

"A lot of the businesses in China are adopting the international accounting standards, because it is important for them to be able to operate internationally."

Li said investors should look to see who is underwriting a Chinese company as one indicator of the company's legitimacy and seek out those backed by major Western investment banks such as Goldman Sachs and Morgan Stanley.

But she said even the big Chinese companies listed overseas don't have solid track records.

"It is always high risk, high return," she said.

U.S.-based Interactive Brokers recently published a list of more than 100 Chinese stocks listed on stock exchanges around the world that it would no longer allow lend against.

The broker-dealer noted it made the move, which will be phased in by the end of the week, "as a result of elevated risk concerns."

Toronto-listed companies on the list included Boyuan Construction Group (TSX:BOY), GLG Life Tech Corp. (TSX:GLG), Hangfeng Evergreen (TSX:HF), Migao Corp. (TSX:MGO) and Minco Silver Corp. (TSX:MSV).