

## **The Interview - Ezra Sun, Veritas Asset Management: “The Year of the Rabbit is likely to be dominated by a tussle between a deflationary environment in the West and inflationary pressure in the East”**



Ezra Sun, manager of the [Veritas China Fund](#) [1] and head of Far East at Veritas Asset Management, believes that consumption is a strong structural theme that over time will yield great returns, while capital investment also offers opportunities as infrastructure spending continues unabated amid continuing capacity expansion and upgrading.

### **GFM: What is the background to the Veritas Asset Management China Fund?**

**ES:** The [Veritas China Fund](#) [1] was launched beginning of October 2009 and is listed on the Irish Stock Exchange. I am manager of the fund, along with the Veritas Asian Fund and Real Return Asian Fund. The fund currently has USD140m in assets under management.

The [Veritas China Fund](#) [1] is a long/short fund investing in companies located in China or companies located elsewhere that derive more than 50 per cent of their income from the country. It targets annual returns of between 15 and 20 per cent on a rolling three- to five-year basis.

The fund’s investment strategy uses specific macro themes to drive a bottom-up stock-picking process. In analysing companies we focus on the business model, the quality of management (or lack of it) and sustainability of the business. Particular attention is paid to free cash flows.

Our return target is an annualised return of 15-20 per cent with roughly half the daily volatility of the market. Our investment horizon is long-term and we are prepared to tolerate the short-term volatility prevalent in the Asian markets.

### **GFM: Who are the fund’s key service providers?**

**ES:** The fund’s auditor is PricewaterhouseCoopers, the administrator is HSBC Securities Services (Ireland) and legal counsel is A&L Goodbody.

### **GFM: What is the fund’s client base?**

**ES:** The fund is registered for sale in the UK, Ireland and Switzerland. The client base consists predominantly of discretionary wealth managers, family offices, asset management firms and

pension funds.

**GFM: How have the recent global financial crisis and economic downturn affected your business?**

**ES:** Over the last three years the assets of Veritas Asset Management have grown from GBP900m to GBP4.5bn, of which Asian strategies account for GBP1.5bn. The Veritas China Fund was launched following the financial crisis.

**GFM: How do you generate ideas for your fund?**

**ES:** The idea generation process starts with a top-down approach focusing on identifying trends, dynamics and possible changes in the macro economy as well as in different sectors.

We utilise a broad range of intelligence sources, including industry research and outside experts in academia and government who have influence on formation of policy as well as a clear understanding of the fundamentals of the economy and the industries they are involved in.

Our stock research focuses on macro issues as well as company and industry fundamentals and our top-down analysis leads to the identification of themes. Our fundamental research focuses on the quality of the business, the value chain of the market or sector, obtaining industry research, conducting company visits, and establishing our valuation of the company under analysis.

**GFM: What is your approach to managing risk?**

**ES:** Given the main tenet of our philosophy is real return investing, the greatest risk is loss of capital rather than underperforming an index. There are two areas of risk control embedded within the investment.

It is our belief that risk can only be taken when it is controllable, and when it is fully understood. In areas where we think we have the requisite skills, our entry position is 1 to 2 per cent, with an individual stock representing a maximum of 5 per cent at cost for long positions, and a maximum of 3 per cent at cost for short positions. Net sector exposure is generally no more than 25 per cent.

We aim for lower volatility in the fund, monitor the efficiency of risk/return performance through the Sharpe and Sortino ratios, and make use of the Excerpt risk analytics tool from EM Applications. These are only tools, however, and do not drive the investment process.

**GFM: How has recent performance compared with your expectations and track record?**

**ES:** Between the fund's launch in October 2009 and the end of January this year, the fund's USD A Class shares have returned 19.9 per cent with half the daily volatility of the market.

**GFM: What events do you expect to see in your sector in the coming year?**

**ES:** We believe that 2011, the Year of the Rabbit, is likely to be dominated by a tussle between two conflicting forces: the deflationary environment in the West and inflationary pressure in the East. The abundant liquidity will tend to push asset prices up, while inflation fears may from time to time push asset prices down. It is highly likely we will see a re-enactment of 2010, where the norm was a frequent shift between risk-on and risk-off.

From a sector point of view, we see opportunities in two areas, consumption and capital expenditure. The consensus has been very bullish on consumption, but performance last year in the sector was varied. There have been disappointments in some segments, particular the mass-market staple sector, as we have warned about before. This means investors are less enthusiastic about the sector now.

**GFM: How will these developments affect your own portfolio?**

**ES:** The momentum in economic growth is such that we can reasonably expect good returns from China, provided that inflationary pressures are tackled and contained. We remain optimistic on China and would view any significant pullback as a good buying opportunity.

**GFM: What opportunities are you looking at right now?**

**ES:** We continue to believe that consumption is a strong structural theme that over time will yield great returns, and capital investment is another strong theme. Infrastructure spending continues unabated, while capacity expansion and upgrading also proliferate. There are great opportunities in machinery, power equipments, IT, oil and gas, alternative energy, environmental protection and new materials.

**GFM: What differentiates you from other managers in your sector?**

**ES:** The Veritas China Fund is a long-short strategy managed in accordance with Ucits III regulations and protection. We have a successful track record of running long/short money in Asia. The fund also capitalises on our expertise and experience in China, which I have followed for the past 16 years.

**GFM: How do you view the environment for fundraising over the coming 12 months?**

**ES:** Given the US Federal Reserve’s ambition to “target” equity markets to create the “wealth effect”, according to Ben Bernanke’s Jackson Hole speech, we expect flows into equities to continue.

**GFM: Do you have any firm plans for further product launches?**

**ES:** There are no immediate product launches in the pipeline, but we are always looking at new opportunities in line with our investors’ needs.

- [Fund Manager Interviews](#)

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**Links:**

[1] <http://www.veritas-asset.com/veritas-china-fund.aspx>