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This Week in China

China Seeks To Reduce Production Capacity From Position of Strength

China's State Council announced last week that it will restrict licenses for steel and cement production in an effort to clamp down on over-capacity, a move seen by many to signal the government's confidence that the economy is now strong enough to deal with an issue created by this year's record lending.

According to Bloomberg, the government also plans to "enhance management" of certain industries including flat glass, chemicals, wind power and polysilicon production, with measures that may include strict controls on market access, reinforced environmental supervision and tougher controls over land use. Banks will also be required to lend money to targeted sectors.

"The fact that policy makers decided to make the adjustment now signals they deem investment strength and growth momentum outside of these areas already strong enough to withstand this move," said Helen Qiao, an economist

at Goldman Sachs Group Inc. in Hong Kong. According to a report published by Bloomberg News, "...restraints on steel and cement output, as well as parts of the coal, glass and power industries, come as Chinese economic growth rebounded to 7.9 percent in the second quarter and Japan, France and Germany exited recession."

Last month, the China Iron & Steel Association warned that the risk of a "market glut is piling up." As Chinese local banks made a record \$1.1 trillion of new loans in the first six months of 2009, the country's fixed-asset investment increased 33.5 percent and fueled growth in steel production to record levels in July, contributing to a 12 percent drop in China's benchmark steel prices during the second and third weeks in August.

"Many countries, such as Australia, have been seeing significant increases in Chinese imports of raw commodities," said Joseph Tan, chief Asia economist at Credit Suisse Group AG in Singapore.

China's central bank this month said it would carry out "dynamic fine-tuning" of the nation's monetary policy. The People's Bank of China also said it will maintain a "moderately loose" monetary policy and guide "appropriate" loan growth.

Changes to China's lending policies won't hurt growth, which remains the top priority of policy makers, the Royal Bank of Scotland Plc said in a report.

"The current tweaking is aimed at reducing froth, rather than slowing growth," wrote Wendy Liu, Hong Kong-based head of China research at RBS ABN Amro.

Indeed, China's economic policymakers are now in the position where they can work to ensure that growth is not only strong in the short-term but also sustainable in the medium to long term.



Adam Roseman,
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This Week in China (cont'd)

China's Economy 'Looking Good' for 2010

Fan Gang, director of the China National Economic Research Institute and a member of the money policy committee of the People's Bank of China, is confident that the country can meet its GDP growth target of 8% this year and will keep the momentum of the economic recovery next year.

He attributed the strong economic growth to the stimulus package, rising investment in property and industrial sectors, and a growing trade surplus.

China's RMB 4 trillion (\$585 billion) stimulus package, mainly on domestic investment and consumption, is shoring up the economy, with manufacturing showing more signs of recovery, according to the State Council.

"Investment in real estate this year has almost fallen to its lowest level for years," Fan said, "yet money has started to flow into this sector and will increase quickly next year, making it a significant source of GDP growth."

From January to July, property sales have soared 37.1% year-on-year. Investment growth in real estate development has accelerated from 1% in January and February to 11.6% in July, according to Liu Shijin, deputy director and senior research fellow at the Development Research

Center of the State Council. He spoke at a meeting of National People's Congress.

Industrial enterprises, particularly in mechanics and chemical sectors, will resume investment in 2010, despite warnings of overcapacity among enterprises and manufacturers, Fan said.

The State Council vowed to "resolutely" curb overcapacity because the economy was still in a "critical period".

Restraints will be imposed on steel and cement output, as well as parts of the coal, glass and power industries, as Chinese economic growth rebounded to 7.9% in the second quarter.

Another contributor to the growth is trade surplus.

China's exports declined 22% year-on-year in the first seven months of this year. But its global market share is rising. The proportion of Chinese products among the total imports to the US and Japan has grown by 2.3% and 5.6% respectively from January to April, with an increase of 1.9% in the EU market.

To achieve the GDP growth, Fan suggested policymakers should maintain the pace of government-led investment. "The growth rate at 8% can be guaranteed as long as growth of government-led investment does not turn

negative."

However, some experts expressed worries about the impact of the stimulus package on the economy.

The stimulus index weakened significantly in the second quarter this year, contributing only 0.3% to the economic growth and will continue to shrink in July, according to Stephen Green, an economist with Standard Chartered.

About 80% of the money financed in infrastructure projects in the first half-year came from bank loans, instead of the finance budget, he said.

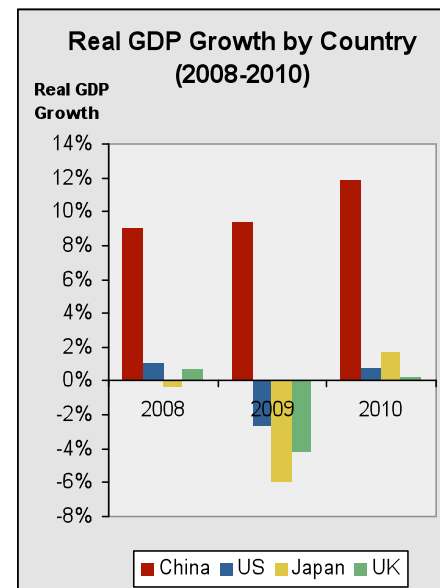
The Ministry of Finance said it would invest RMB 200 billion in the fourth quarter, after giving 80 billion to local governments in the third quarter.

People also questioned about the efficiency of government investment.

Jia Kang, director of the Institute of Research at the Ministry of Finance, urged the government to send inspection teams to supervise and monitor the ongoing or planned projects invested in by the government or in partnership with private investment.

"It is a top priority to ensure the quality of investment projects at every stage through timely checks and guidance," he said.

Source: China Daily



Source: Goldman Sachs; Euromonitor

"The growth rate at 8% can be guaranteed as long as growth of government-led investment does not turn negative."

Alternative Energy

China Racing Ahead of U.S. in the Drive to Go Solar

President Obama wants to make the United States “the world’s leading exporter of renewable energy,” but in his seven months in office, it is China that has stepped on the gas in an effort to become the dominant player in green energy, especially in solar power, and even in the United States.

Chinese companies have already played a leading role in pushing down the price of solar panels by almost half over the last year. Shi Zhengrong, CEO and founder of China’s biggest solar panel manufacturer, Suntech Power Holdings, said that Suntech, to build market share, is selling solar panels on the US market for less than the cost of the materials, assembly and shipping.

Backed by lavish government support, the Chinese are preparing to build plants to assemble their products in the United States to bypass protectionist legislation. Chinese solar companies are encouraging their United States executives to join industry trade groups to tamp down anti-Chinese sentiment before it takes root.

Since March, Chinese governments at the national, provincial and even local level have been competing to offer solar companies ever more generous subsidies, including free land, and cash for

R&D. State-owned banks are flooding the industry with loans at considerably lower interest rates than available in Europe or the United States.

Suntech is on track this year to pass Q-Cells of Germany to become the world’s second-largest supplier of photovoltaic cells, only behind First Solar in Tempe, Arizona.

Hot on Suntech’s heels is a growing list of Chinese corporations backed by entrepreneurs, local governments and even the Chinese military, all seeking to capitalize on an industry deemed crucial by China’s top leadership.

In addition to heavy Chinese investment and low Chinese costs, the global economic downturn and a decline in European subsidies to buy panels have lowered prices.

The American economic stimulus plan requires any project receiving money to use steel and other construction materials, including solar panels, from countries that have signed the WTO agreement on free trade in government procurement. China has not.

In response to this, and to reduce shipping costs, Suntech plans to announce in the next month or two that it will build a solar panel assembly plant with 75 to 150 workers in Phoenix, or somewhere in Texas.

Yingli Solar, another large

Chinese manufacturer, also had a “preliminary plan” to assemble panels in the United States.

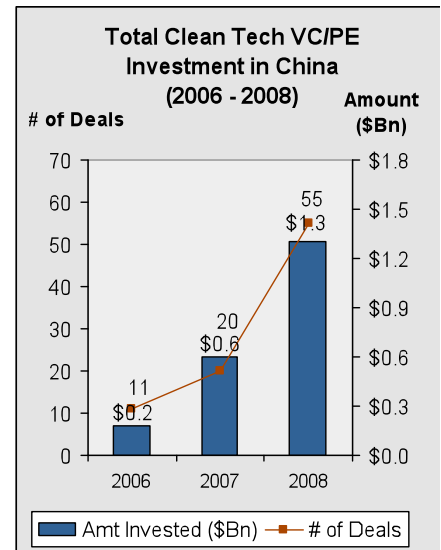
Western rivals, meanwhile, are struggling. Q-Cells of Germany announced that it would lay off 500 of its 2,600 employees because of declining sales. It and two other German companies, Conergy and SolarWorld, are particularly indignant that German subsidies were the main source of demand for solar panels until recently.

But organizing resistance to Chinese exports could be difficult, particularly as Chinese discounting makes green energy more affordable.

Even with Suntech acknowledging that it sells below the marginal cost of producing each additional solar panel, any antidumping case, in the United States, for example, would have to show that American companies were losing money as a result.

Even organizing a united American response to Chinese exports could be difficult. Suntech has encouraged executives at its United States operations to take the top posts at the two main American industry groups, partly to make sure that these groups do not rally opposition to imports.

Source: *New York Times*



Source: Zero2IPO

Chinese companies have already played a leading role in pushing down the price of solar panels by almost half over the last year.

Metals and Mining

China Makes Move on Iron Ore Prospector

Baosteel Group, China's biggest steelmaker, agreed to invest \$240 million for a minor stake in Australian iron ore explorer Aquila Resources, underscoring China's huge appetite for Australian assets.

The deal comes at a tense time for Australia and its biggest trading partner, with an Australian mining executive detained in China on a commercial espionage charge, Beijing canceling a top-level visit to Australia, and the recent collapse of a \$19.5 billion investment.

But analysts said this latest deal was likely to be approved by Australia's foreign investment watchdog, noting it would give state-owned Baosteel only 15 percent of Aquila, and the fact that Aquila was still only a prospector and not yet in production.

The latest deal, which sent Aquila shares surging 11 percent to near a 10-month high, would give Baosteel the right to directly invest and co-develop most of Aquila's projects and give the Australian miner access to cheap loans from Chinese banks.

Baosteel plans to buy up to 43.95 million Aquila shares at \$6.50 a share, Aquila said, adding that Baosteel Vice President Dai Zhihao had been nominated to its board.

"I'd like to think this agreement with Baosteel

will help take Sino-Australian relations off the bottom," Aquila Executive Chairman Tony Poli told Reuters by telephone from Perth.

Baosteel has agreed to acquire no more than 19.9 percent of Aquila. Anything over that would require Baosteel to declare a formal takeover attempt under Australian securities regulations.

Further cash could come via Brazilian mining giant Vale, which holds an option starting in December to buy out Aquila's 24.4 percent stake in the Belvedere coal project in Queensland.

Analysts have suggested Aquila would use proceeds from the sale for development of iron ore mines in Australia. Alternatively, the funds could go towards Aquila's Eagle Downs coking coal project, also in Queensland.

Aquila has enough reserves to annually mine 32.5 million tons of iron ore and 11.4 million tons of coal, with production of both expected to begin in mid-2013, according to a recent presentation it made at a conference in China.

Aquila's deposits lie in the West Pilbara iron ore belt, home to the massive operations of Rio Tinto and BHP Billiton, the world's second- and third-largest producers of iron

ore.

Australia's relations with China soured in June when a then-indebted Rio Tinto ditched a planned \$19.5 billion equity partnership with China's state-owned Chinalco and instead agreed a joint venture with rival BHP Billiton.

Soon after, Rio Tinto's top iron-ore salesman in China, Stern Hu, was detained along with three other Shanghai-based Rio Tinto staff and later charged with commercial espionage.

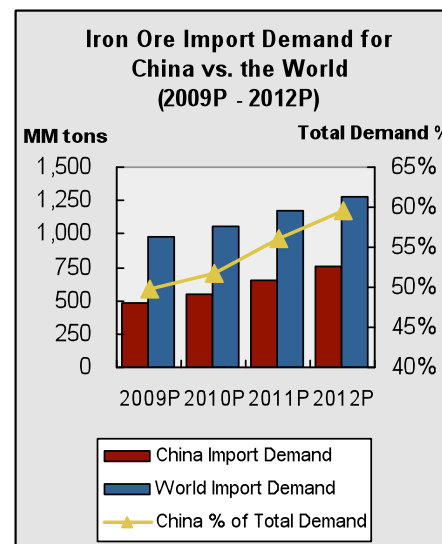
Despite the recent political tensions, investment ties have proven resilient, with Australia last week agreeing to a \$50 billion deal to sell liquefied natural gas to PetroChina from a yet-to-be-built project.

"Trade is still going to occur," said Steven Robinson, senior investment manager at Alleron Investment Management.

"The Chinese are looking to secure raw materials for the longer term. The main thing is the security of supply."

He pointed to a recent deal whereby China would provide up to \$6 billion in funding to Fortescue Metals Group in exchange for buying Fortescue's iron ore at a price discount.

Source: ABC news



Source: Morgan Stanley

"The Chinese are looking to secure raw materials for the longer term. The main thing is the security of supply."

Recent Transactions

Siemens Buys Two Chinese Metal Companies

German industrial conglomerate Siemens AG bought majority stakes in two small Chinese metal companies recently. One is Yangtze Delta Manufacturing, a metal-working company, and the other is aluminum foundry GIS Steel & Aluminum Products.

Siemens said the two companies had a total

Everlearn International Group Receives \$8 Million Capital Injection

DT Capital Partners, CID Group and iD TechVentures announced a joint investment of \$8M into Everlearn International Group, the top-ranking childhood education institution for children aged 3-6. It will increase the total PE investment in Everlearn to \$15 mm after an upfront investment of \$7 mm made by DT Capital Partners and CID Group in 2007.

Fortune VC Channels RMB 70 Million into Premium Household Furniture

"We started approaching this enterprise two years ago. We have seen the great potential of its business model, which solves the low-cost issue posed by the mass production of made-to-order furniture," said Fu Zhonghong, GM of

workforce of 600 employees, with combined revenue of 65 million euros (\$93 million) in 2008, but it did not release how much it paid to buy these two companies

Siemens made these two acquisitions to expand its global production network for high-voltage circuit breakers in China and its foundry capabilities from machining through final product assembly, as China is now the world's

Everlearn offers Genius Baby children's MBA training course, Little Earth children's English, Soong Chingling International Kindergarten and China Children's Summer Camp Service Center. Genius Baby has 20,000 trainees and 1,200 employees to date. It has 40 teaching centers in 20 Chinese cities by seeking local shareholders to build joint ventures and engage in chain operation. Its annual revenue has reached RMB 200 mm.

Shanghai Branch of Fortune VC based in Shenzhen, before signing an agreement with Premium Household Furniture. Customized furniture took up a share of about 10% in the Chinese furniture market and is growing at an annual rate of 20%, indicating great development prospects for the sector. Fortune VC has pumped roughly RMB 70

million in the enterprise this time with an objective of building it into an industry leader in customized furniture.

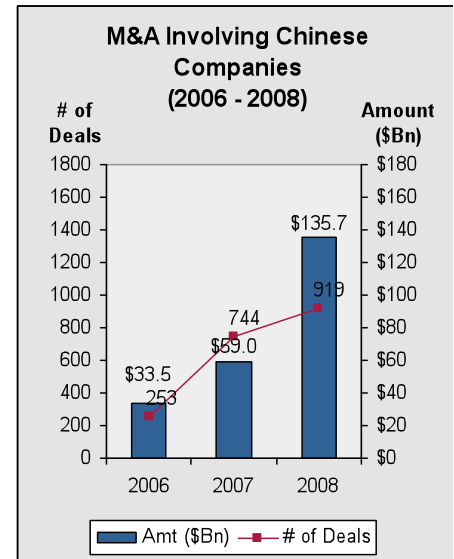
Mr. Fu noted that his company is a player in an emerging service sector. He hopes this company would make an IPO on the Growth Enterprise Market.

Source: China Daily

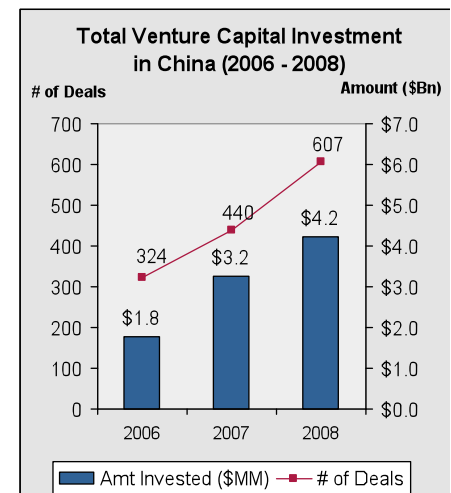
Liu Huiqin, CEO of Everlearn, said her group will use the proceeds to accelerate the development such as Soong Chingling International Kindergarten and Children's Summer Camp, to integrate the industrial chain between children's educational institutions and kindergartens, and capture a larger share in some of the children's educational segments.

Source: Zero2IPO

Source: Zero2IPO



Source: Capital IQ



Source: Zero2IPO