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This Week in China

Latest Figures Spark Further Optimism in China's Speedy Economic Recovery and Future Prospects

Figures released last week show that China's economy is still showing very positive signs of recovery and shaping into positive forecasts for the nation's Q4 performance. According to a report released by *Reuters*, "A surge in construction and real estate spending, a double-digit increase in power use, a rise in foreign direct investment and a bullish export forecast" added to mounting confidence in China's quick rebound from the economic downturn.

"The barrage of figures came after data showed a marked improvement in imports and exports in September -- although they were still down from year-earlier levels -- as well as robust money and credit growth," the report said.

"Going into the fourth quarter, we expect that the pace of decline in exports will narrow further, and I think we'll quite possibly see positive annual growth in some months," said China Commerce Ministry

spokesman Yao Jian. He went on to say that the confidence of overseas firms in China is also likely to lead to a continued recovery in foreign direct investment, which grew by 18.9% from a year earlier with \$7.9 billion growth in September 2009.

The primary force behind China's continued growth this year has been the RMB 4 trillion (\$585 billion) stimulus package with its strong support for transport infrastructure, affordable housing and public works. However, as the real estate industry now accounts for more than 20% of total fixed-asset investment in China, private property developers are now stepping up to the plate. According to the National Bureau of Statistics, real estate investment grew by 17.7% from a year earlier in the January-September period, up from 14.7% reported for the first eight months of this year.

Economists at Bank of America Merrill Lynch reported an acceleration in the monthly property investment growth rate to 37% in September, year on year, from 34.6% in August. In a report released to the firm's clients, they predicted

property investment will continue to be a major growth driver through the rest of this year.

The Q3 GDP report set for release on Thursday is expected to show just how far China has come in its economic recovery since last quarter. A *Reuters* poll of economists predicted acceleration of the annual growth rate to 8.9% from 7.9% in the April-June period. If this proves to be the case, even the most optimistic forecasts may end up incorrect.

ING's chief Asia economist Tim Condon predicts that the People's Bank of China will continue to fine-tune the nation's monetary policy and respond ultimately with an interest rate increase in Q1 2010. Pressure for China to allow the yuan to appreciate once again is mounting as well. Clearly China's growth has caught the attention of the world and speculation has turned to what China will do post-recovery. Meanwhile most of the world's other major economies are still searching for recoveries of their own.

Adam Roseman,
Founder & CEO
ARC China



This Week in China (cont'd)

Domestic Spending To Hit RMB 12 Trillion

Consumer spending is expected to increase by 50% in China's top 25 cities in the next five years due to a rapid increase in the country's per capita disposable income, according to a new report from McKinsey & Company.

The report estimated that per capita spending in China's urban areas will rise to RMB 16,000 (\$ 2,344) per year in 2015, up from RMB 10,000 in 2008. The volume of domestic consumer spending is expected to total RMB 11.7 trillion.

"We anticipate consumption growth in China to

keep pace with GDP in the coming years, at a 10% CAGR by 2012," said Max Magni, partner and head of McKinsey's consumer practice based in Shanghai.

However, there are variations in consumer spending increases among different cities, with Beijing and Yantai and Weihai of Shandong province having the highest CAGR of 10.2% in 2008 to a projected 14% in 2015. Cities like Shanghai, Guangzhou and Shenzhen, with export-oriented economies, will have a CAGR as low as 6.5% during the same period.

Vinay Dixit, senior director of McKinsey's Asia Consumer Center, said

China To Input \$69 Billion For West Development In 2009

China plans to invest RMB 468.9 billion (\$68.65 billion) in projects to boost the development of the country's western region in 2009, said the National Development and Reform Commission (NDRC).

The investment will go to 18 projects, including rail-

ways, express ways, hydropower stations, shipping hubs, water control projects and airports.

These projects play a vital role in implementing China's West Development Strategy, promoting economic and social development there and improving people's livelihood in the region.

China has launched 102

China's Forex Reserve Hits Record \$2.27 Trillion

China's foreign exchange reserve hit a new high of \$2.27 trillion by the end of September, up 19.26 percent year on year, according to the People's Bank of China, the central

bank.

In the first three quarters, China's foreign exchange reserve increased \$326.6 billion, and the increase was \$50.7 billion less than the same period last year.

China's foreign exchange reserve added by \$43 billion in July, \$36.2 billion

export-dependent cities have suffered a harder blow from the global financial crisis, which means a longer recovery of consumer spending momentum.

McKinsey recently released the findings of a separate survey of 15,000 people in 58 cities that showed lower consumer confidence in the wake of the financial crisis, particularly among low-income earners and those living in export-reliant regions.

The consumer confidence index dropped to 86 points in March from 94.5 points in the same period last year.

Source: China Daily

projects for boosting western region development from 2000 to 2008, involving RMB 1.74 trillion of investment.

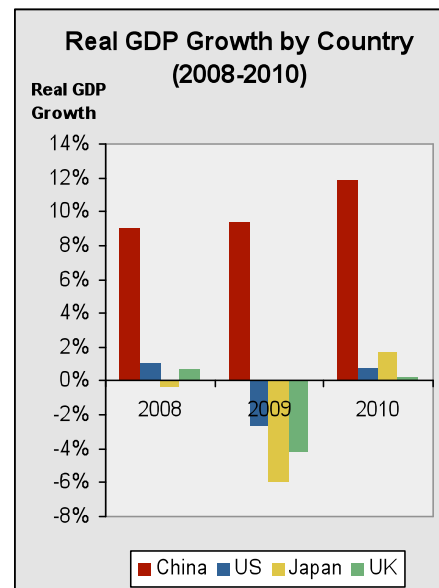
The West Development Strategy is a policy adopted by the Chinese government to help the underdeveloped western region catch up with prosperous eastern region.

Source: China Daily

in August and \$61.8 billion in September.

At the end of June, China's foreign exchange reserve surpassed \$2 trillion for the first time by \$131.6 billion.

Source: Xinhua News



Source: Goldman Sachs; Euromonitor

The report estimated that per capita spending in China's urban areas will rise to RMB 16,000 (\$2,344) per year in 2015, up from RMB 10,000 in 2008.

This Week in China (cont'd)

Third and Fourth Tier Cities Shine

China's so-called third and fourth-tier cities - those at county level - will be most targeted in the future by domestic enterprises, investment agencies and international companies.

Under the current situation of urbanization, consumption markets in the country's first and second-tier cities, for example Beijing, Shanghai and Guangzhou, tend to be saturated and people's spending power will not be enough to support the country's economic growth.

There are more than

4,000 third and fourth-tier cities in China. The retail sales of consumer goods at and below county level totaled RMB 3.48 trillion (\$510 billion) in 2008 compared with RMB 1.84 trillion in 2004.

To comprehend the size of the market outside major metropolises, it is worth considering that Yichun, a Chinese clothing brand hard to find in big cities, took in RMB 8 billion in sales in 2008. Lenovo released computers targeted at rural markets that cost just RMB 1,499. Ownership of the Nokia 1110 phone in China is reported to be

about 200 million.

Peng Gang, director of integration strategy at Bates 141 China, said the rules and principals of marketing and branding in third and fourth-tier cities are very different from those in big cities. "People in smaller cities usually put quality, durability and after-services first when they make consumption decisions." In addition, they have far more time and their consumption decisions are made more prudently rather than impulsively, Peng said.

Source: Xinhua News

China's Super-rich Bounce Back From Financial Crisis

China's super-rich have bounced back from the financial crisis with a vengeance, and China now has more known dollar billionaires than any other country except for the United States.

The annual Hurun Report said China has 130 known dollar billionaires, up from 101 last year. The number in the United States is 359 while Russia has 32 and India 24, according to Forbes magazine.

China's rich are getting richer, with the average wealth on the list \$571 million, up almost one-third from last year, said compiler Rupert Hoogewerf. "With the greatest wealth destruction in the west of the last 70 years,

we've seen China buck the trend and the wealth seems to be still growing."

"They've put the credit crunch behind them," he said. "The key driver has been urbanization. You've got all these cities being built, and that requires property developers, iron and steel manufacturers. The latest thing is cars."

Topping the list was Wang Chuanfu, chairman of electric car and battery maker BYD Co Ltd in which U.S. billionaire Warren Buffett holds a stake, with an estimated personal wealth of \$5.1 billion. He was also the fastest riser from last year, up 102 places.

Second place went to Zhang Yin and family, owner of paper recycler Nine Dragons Paper, while in third place was Xu

Rongmao and family, owner of Shimao Property Holdings Ltd.

Hoogewerf said the actual number of dollar billionaires could be higher than estimated. "Either they are super-discreet, or perhaps they haven't come to the surface," he said. "Having said that, the transparency of wealth...is now very much in the open. There's many more listed companies."

China's ruling Communist Party once condemned entrepreneurs and private business people as capitalist exploiters, but now welcomes them since the landmark economic reforms in the 1970s. One third of the people on the 1,000-name rich list are estimated to be Party members.

Source: Yahoo News

This Week in China (cont'd)

China's Housing Prices rise 2.8% in September

Housing prices in 70 of China's large and medium-sized cities rose 2.8 percent in September compared with the same month last year, according to the National Bureau of Statistics.

Prices were up 0.7 percent from August,

Strong Trade Figures Export New Optimism

China reported surprisingly good trade figures, offering fresh evidence that the world's third-largest economy is well on the road to recovery and suggesting global demand is improving.

Exports from China fell in September by 15.2 percent compared to the same period last year, which was much better than analysts had expected. Forecasters were braced for a 21 percent fall.

And there was more good news, with imports falling by just 3.5 percent compared to September 2008, far better than the anticipated 15.3 percent decline.

Brian Jackson, an economist with Royal Bank of Canada in Hong Kong, said the slower pace of decline bodes well for China's recovery because growth this year had depended too much on the government's RMB 4 trillion (\$586 billion) stimulus package. He said there is now hope that

when they rose 2 percent from the same month in the previous year.

Prices of new houses in September rose 2.7 percent from the same month last year, and 0.8 percent from August.

Housing prices in certain cities rose more quickly than in other cities. September prices in

growth can also be encouraged by increased demand.

Indeed, the news was even better than it first appeared because, after adjustments are made taking into account the number of working days each month, exports rose by 6.3 percent compared to August and imports rose by 8.3 percent during the same period.

The strong trade performance was beyond the expectations of some analysts who insisted it was not sustainable in the long term.

Analysts said it was too soon to be overly optimistic but they said there will likely be positive growth in exports during the final quarter as manufacturers benefit from both the worldwide economic turnaround and the low benchmark set last year.

While the high unemployment rate is likely to persist for several months and while the consumption confidence index is not encouraging, most American economists believe the US has

Guangzhou and Yinchuan rose 7.3 percent and in Kunming 6.1 percent from the same month last year.

In September, prices of second-hand homes in the 70 cities rose 3.8 percent from a year earlier, and 0.5 percent from August.

Source: China Daily

emerged from the economic recession.

China's purchasing management index (PMI), another indicator of the economic health of the manufacturing sector, rose to 54.3 percent in September, 0.3 percentage points higher than it was in August. It was the seventh consecutive month that the index had risen above 50 percent.

Imports in September were worth \$103 billion. That represented a 17 percent increase on the volume of imports in August, according to the Customs data.

Exports totaled \$115.9 billion, up 11.8 percent from August.

Total foreign trade reached \$218.94 billion in September, down by 10.1 percent year-on-year.

"The improvements (among both exports and imports) were much larger than expected. The worst is over," said Denise Yam from Morgan Stanley.

Source: China Daily



Metal & Mining

China and Miners Lock Horns on Annual Pricing

Miners will demand hefty price increases for iron ore and coking coal during the annual contract negotiations that start in China this week, opening the door for a clash with Beijing on the cost of the commodities.

The demand comes amid a rally in commodities prices, from crude oil to copper, on the back of strong China growth and a weak dollar, and is likely to boost miners' shares, which have surged since January.

Vale of Brazil, Rio Tinto and BHP Billiton will ask for a 30-35% increase in iron ore prices for 2010-11, partially reversing the 33% cut agreed for 2009-10, according to mining executives familiar with

the negotiations.

They will ask for a 40-50% rise in coking coal prices, after a 58% fall this year.

The rosy outlook is due to the miners' belief that an economic recovery is under way, with steel production rising in China and elsewhere.

Analysts and brokers agree prices will rise, but they are less bullish, forecasting increases for iron ore of 10-20% and 30-40% for coking coal.

The 40-year-old benchmark system, in which the first deal between a miner and a steelmaker sets a yardstick to be followed by the rest of the industry, is under threat after China rejected the miners' 2009-10 settlement with Japan, opting to buy on the spot market.

But analysts believe a

benchmark deal is likely to be struck for 2010-11, although it is months away.

China and the miners are facing off for what could be a contentious negotiating round, with differences not just on the magnitude of any price change but even on whether prices should rise or fall.

The China Iron and Steel Association has sent clear signals that it wants a price cut. In recent days it has talked of oversupply in iron ore imports and declared its intention to cut back on overcapacity in the steel industry. The fresh negotiations come after this year's talks ended in stalemate as China refused to accept a deal between Rio and Japanese mills for a 33%, insisting instead on a 40-45%

Source: Financial Times

China's Zijin considering up to \$1 Billion in gold and copper projects in the Philippines

China's Zijin Mining Group (2899.HK) is eyeing up to \$1 billion in investments in gold and copper projects in the Philippines within five years, the Philippine environment secretary said.

China's largest listed gold company signed an MOU with the Philippine government to signify their interest to enter into min-

ing ventures in the Southeast Asian country.

"It's an MOU where their intention to invest was clearly stated," said Jose Atienza, environment and mining secretary.

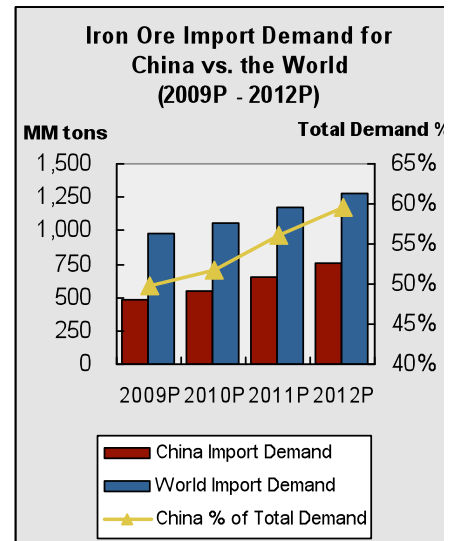
"They can look for a local partner," Atienza said, adding Zijin has initially linked up with local mining firm NiHAO Mineral Resources International Inc (NI.PS: Quote).

Zijin has been actively pursuing acquisitions of mineral resources outside

China and had made initial investigations into various overseas projects. In July, it ended share acquisition talks with a Kazakhstan gold company.

The global downturn has hurt the Philippines' mining sector, with the government cutting its investment target for this year to just over \$600 million, down from an initial target of up to \$1 billion.

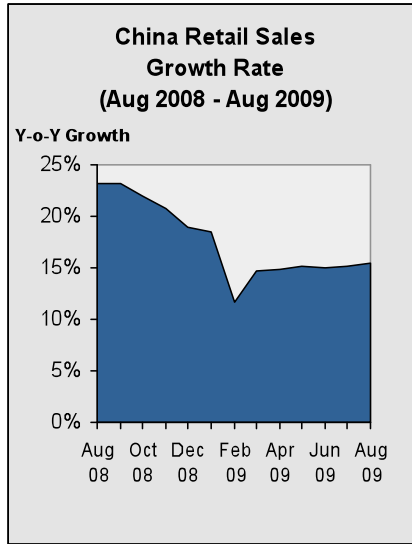
Source: Reuters



Source: Morgan Stanley

Vale of Brazil, Rio Tinto and BHP Billiton will ask for a 30-35% increase in iron ore prices for 2010-11, partially reversing the 33% cut agreed for 2009-10

Consumer / Retail



Source: Bloomberg

China has a rapidly growing number of rich people – 825,000 with a personal wealth of more than RMB 10 million.

Versace Leaves Japan and Courts China

Tucked away on the lower ground floor of a Shanghai shopping mall is a modest boutique that could represent the future for Versace.

While the Italian designer label this week announced its retreat from Japan, the largest luxury goods market, it signaled grand ambitions in China.

Versace has opened 20 boutiques in the country and is planning more.

Soon its clothing range – items in which price up to RMB 25,000 (\$3,700) – will be displayed in premises in Shanghai's Plaza 66 mall, where it hopes to catch the eye of China's wealthy entre-

preneurs. But potential customers are not just the rich. Shanghai's women office workers are renowned for spending a month's salary on a handbag or pair of shoes.

China has a rapidly growing number of rich people – 825,000 with a personal wealth of more than RMB 10 million, according to The Hurun Report, a luxury-business research group known for its annual China rich list. They are just as obsessed with high-end brands as the Japanese, and their love affair with luxury is in its infancy.

"China will become not just a market you hope to sell into but one you design your strategy around, just as Japan has been," says

Yuval Atsmon, a luxury-industry expert at McKinsey in China.

But luxury brands have a lot to learn about the Chinese consumer. More than 55% of Chinese consumers only started to buy luxury products in the past four years, according to a McKinsey study.

Their traits differ from those of the Japanese. "The Chinese wealthy consumer is 20-30% younger than in Japan," Mr Atsmon says.

McKinsey expects the growth in luxury goods consumption to come from cities that are not well penetrated by international businesses.

Source: Financial Times

Gap Aims to Crack China Market

Gap, one of the world's biggest clothing retailers, is to open its first store in China next year in a push for international growth that will include selling online in the European Union and Canada for the first time.

Glenn Murphy, chief executive, said that the company intended to "step up" investment to regain market share and expand international operations after two years working on improving performance.

The China store will be the first new market that Gap has entered directly for more than a decade,

rather than through the franchising model, launched in 2007, that it is using in the Middle East, Asia and Eastern Europe.

"It's a big opportunity... Chinese consumers love American brands," Mr Murphy said at Gap's annual investors' meeting.

Mr. Murphy contrasted the new approach to Gap's initial international expansion in the 1990s, when it tried to apply a standard US store blueprint.

Gap's online sales delivered revenues of more than \$1 billion in 2008.

The clothing retailer said that it would continue efforts to increase the profitability of its store

operations by reducing its total store base square footage by 10% over the next five years, while maintaining store numbers.

Its more than 1,000 Old Navy stores in North America reported positive year-on-year comparable sales gains in August and September, its first two months of consecutive positive numbers for more than five years. Old Navy's sales account for 40% of Gap's total sales. Comparable sales at Banana Republic and Gap brands have remained negative.

Source: Financial Times



Recent Transactions

PearlinPalm Reaps \$10 Million Investment

PearlinPalm, a leading mobile game producer in China, garnered over \$10 million from China Broadband Capital Partners and DT Capital Partners.

PearlinPalm, a foreign-

Far Eastern Receives Investment from KKR, GIC and CICC

An investor consortium including affiliates of Kohlberg Kravis Roberts & Co., Government of Singapore Investment Corporation and China International Capital Corporation Limited (CICC) announced an investment of \$160 million for a significant minority stake in International Far Eastern

Coca-Cola Invests in China's Largest Still Beverage Plant

Coca-Cola (KO.N) said that it has opened a RMB 600 million (\$88 million) bottling plant in China, its largest single investment in still beverage production in the country, to meet growing demand from Chinese consumers.

The world's biggest soft drinks maker said in a statement that still beverages accounted for 30 percent of Coca-Cola China's business.

The plant, based in the central industrial city of Wuhan, is Coca-Cola's

owned enterprise boasting advanced technologies, has been dedicated to top-notch R&D and services of mobile games and application products for China's wireless value-added service market.

As of the beginning of 2009, PearlinPalm has

Leasing Company Ltd. (Far Eastern), the leading provider of financial leasing in China and a subsidiary of Sinochem Group (Sinochem). The investment will support Far Eastern's future growth as it moves to capitalize on the attractive potential in the underdeveloped financial leasing space in China. Sinochem is retaining a controlling stake in Far Eastern.

39th in China and the third it has opened this year in China, the world's second-largest beverage producer in the world after the United States.

Coca-Cola has committed to investing \$2 billion in China over the next three years.

"We are dedicated to providing Chinese consumers with a diversified portfolio of high-quality drinks and we will continue to invest in the full spectrum of the beverage business", said Doug Jackson, president of Coca-Cola China, in the statement.

successfully developed and operated more than 200 mobile games and application products on a variety of subjects, such as martial arts, fairy tales, history and leisure, some of which are familiar to the public.

Source: Zero2IPO

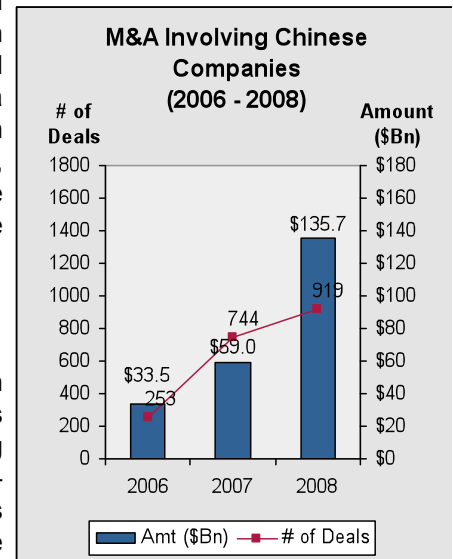
Headquartered in Shanghai, Far Eastern is focused on providing innovative and industry-tailored financing solutions for its clients. The company targets sectors with stable cash flow and sustainable growth potential, including those in the medical, printing, education, infrastructure construction, shipping, machine tool sectors, etc.

Source: Zero2IPO

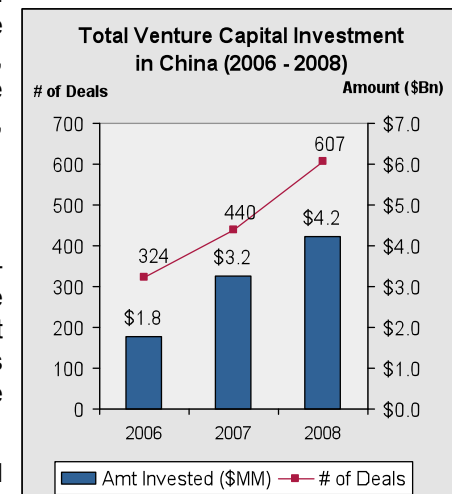
Earlier this week, Cola-Cola launched a Minute Maid "Pulpy Milky" fruit dairy product in China, its first dairy beverage offering in the market.

In June, the company said it would establish a still-beverage production base in Sanshui, Guangdong. The facility is scheduled to start operating in 2010. With the completion of the Sanshui operation, Coca-Cola's total investment in China's still-beverage market would reach RMB 2.8 billion, according to the company.

Source: Reuters



Source: Capital IQ



Source: Zero2IPO