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## This Week in China

### China to Aggressively Reduce CO2 Emissions Relative to GDP

Following a meeting presided over by China's Premier Wen Jiabao, the State Council said it had reviewed a national plan to address climate change and announced that China would reduce the intensity of carbon dioxide emissions per unit of GDP in 2020 by 40 to 45 percent.

The Council in Beijing also declared that Wen will lead the nation's charge for real climate change progress at the United Nations COP15 climate change conference in Copenhagen. The announcements came a day after the United States said it would cut carbon emissions by 17 percent by 2020 from the 2005 level.

The voluntary action on the part of the Chinese government was based on national conditions and places the country at the forefront of global efforts to tackle climate change. "Appropriate handling of the climate change issue is of vital interest to China's social and economic development and people's benefits, as well as the interests of all the people in the world and the world's long-term

development," the State Council said.

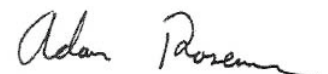
According to Greenpeace China's climate change campaign manager, Yang Ailun, Wen's presence at the summit will be an "important push" for substantial outcomes from the international negotiations and marks another challenge to the industrialized world to strive to match or at least come close to the hefty goals China has announced. "The carbon intensity target is a positive signal that China, the largest developing country and one of the largest greenhouse gas emitters, is willing to take a new development path that can decouple economic growth with increase of carbon emissions," Yang said. As the carbon intensity target is not the same as cutting emissions, China's economy is expected to double in size by 2020 if current growth rates prevail and its emissions will be considerably higher even if it meets the new target.

"The US commitment to specific, mid-term emission cut targets and China's commitment to specific action on energy efficiency can unlock two of the last doors to a

comprehensive agreement," said Yvo de Boer, the United Nations' top climate change official, who will head up the Copenhagen summit.

China is already making rapid gains in building up its domestic renewable-energy industries to help meet these targets. According to the Global Wind Energy Council, China is expected to install more new wind-generation capacity than any other country this year as well as become the world's biggest producer of wind energy by 2013. Within five years, China is expected to be the number one solar market, said Steven Chan, strategy chief for China's Suntech Power Holdings, the world's biggest maker of solar panels.

ARC China is pleased be highly focused on investing in alternative energy and energy recovery companies within China that will benefit from the Chinese government's efforts to achieve economic growth in a more environmentally responsible manner. We look forward to investing in a number of these opportunities in the future.



**Adam Roseman,**

**Founder & CEO**

## This Week in China (cont'd)

### China's Second- and Third-Tier Cities Draw Interest

Amid intense investor focus on where China lives and works, some real-estate professionals these days are looking at where it shops.

Hong Kong-based property investment firm Harvest Capital Partners Ltd. plans a push into shopping malls in China's second- and third-tier cities as a path to growth, said Chief Executive Ren Rong. The company, which is majority owned by the state-controlled China Resources conglomerate, manages two international real-estate funds that focus on commercial and residential projects in greater China, with total capital close to \$1 billion.

"Regional shopping centers will become the next winning property sector in China for another 10 to 15 years," Mr. Ren said.

China's commercial retail sector is also a target for other investors eager to benefit as mainlanders use their rapidly growing income to buy lifestyle products.

U.K. real-estate development and investment firm Grosvenor Ltd., which has been selling some residential property investments in China because the sector is producing less attractive yields than previously, has said it will focus on higher-yielding

projects, such as retail properties.

Blue-chip developer Hang Lung Properties Ltd.'s chairman, Ronnie Chan, recently said malls in big mainland cities are his favorite investments, adding "all provincial capitals are going to be good places to be at."

Retail properties can be a risky area for many investors. Following previous booms, many of China's big cities have a surplus of retail space. Real-estate firm Jones Lang LaSalle estimates Beijing had a third-quarter retail vacancy rate of 16%. It also expects more supply to come onto the market there, and sees little upside potential over the next 12 months in Beijing and Guangzhou.

The growing interest in retail property also comes amid broad uncertainty about China's outlook. The nation's economic growth has roared back since the global financial crisis, thanks in part to a huge stimulus package. Property prices across 70 large and midsize cities rose 3.9% in October from a year earlier, the fastest annual growth rate this year and a fifth month of rising prices. That has led to concerns that prices will weaken once the stimulus ebbs.

Harvest believes its connections with China Resources, as well as research into local

markets, will help it find properties that would hold up despite economic uncertainty.

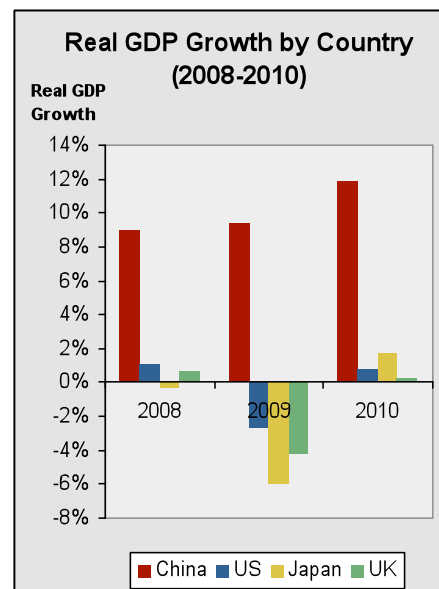
George Agethen, Harvest's head of capital raising and business development, said the fund generally prefers China's tier-one cities when investing in commercial property such as retail and office space.

"But we see specific opportunities in regional shopping malls, mainly in second- and third-tier cities," Mr. Agethen said. "We see opportunities to take advantage of the strong urbanization trends, rising disposable income and the relative lack of well-designed organized retail centers."

During the first nine months of 2009, year-on-year income growth in households in second-tier cities, such as Chongqing, surpassed that of first-tier cities, such as Beijing and Shanghai.

Mr. Ren said also said fund raising is easier than in recent years because foreign investors now favor local managers for their funds. "Different sources of domestic capital are emerging strongly. That will provide us with additional exit possibilities in both the domestic private and public markets," Mr. Ren said.

Source: Wall Street Journal



Source: Goldman Sachs; Euromonitor

*During the first nine months of 2009, year-on-year income growth in households in second-tier cities, such as Chongqing, surpassed that of first-tier cities, such as Beijing and Shanghai.*

## This Week in China (cont'd)

### Fidelity's Bolton to Start China Fund as West Slows

Fidelity International's Anthony Bolton said China's "attractive" economic growth lured him to move to Hong Kong to set up a fund focusing on the country as recovery in the U.S. and Europe "runs out of steam."

Bolton, Fidelity's first fund manager in Europe, will relocate from London in the first quarter of next year and return to managing money after stepping down from day-to-day portfolio management in 2007.

"The center of gravity is shifting to this part of the world," Bolton, 59, president of investments at Fidelity International, which manages \$210.1 billion of global assets, said at a media briefing in Hong Kong. "I want to play a bit of a part in it while I still get the chance to do it."

Goldman Sachs Group Inc. has predicted China's gross domestic product may surpass the U.S. by 2027. Bolton, who began investing in China in 2005, forecast the country would overtake Japan as the world's second-largest market "if not this year, almost certainly next year."

"There were very few things that would persuade me to come back to money management, but China is the only thing," Bolton said. "That's why I've decided

to give up sitting on the beach. This is why I've decided to delay my retirement."

He favors shares related to China's domestic economy, and may invest in Chinese stocks listed in Hong Kong, Shanghai, and New York, declining to be more specific about his new fund.

China has cut interest rates five times since September 2008 and encouraged \$1.3 trillion of lending to boost domestic spending as the global recession curbed demand for the country's exports. Hong Kong's Hang Seng China Enterprises Index has surged 67 percent this year on the credit expansion, driving its price to 16.8 times estimated earnings, up from 10.2 times at the start of the year. The mainland's Shanghai Composite Index has rallied 74 percent in the same time.

"It would have been lovely if we could have launched this fund at the beginning of this year," Bolton said. "The bargain stage is over. But I don't think valuations are yet in the expensive phase where one should be more shy or more cautious."

Bolton said China, whose economy grew by 8.9 percent from a year earlier in the third quarter, is "much too early for a bubble," countering comments by China's central bank adviser Fan Gang, who on Nov. 18 said the nation is among the emerging markets

facing risks of property and commodity-market bubbles.

"The fact he has gone for China is a major vote of confidence in the new economic superpower at a time when people are questioning whether that market has become a little frothy," Darius McDermott, managing director of financial advisers Chelsea Financial Services, said.

Economic recovery in the U.S. and Europe will "run out of steam" in the first half of 2010, Bolton said. China, with the world's largest foreign-exchange reserves of \$2.3 trillion, is the U.S.'s biggest creditor, holding \$798.9 billion of Treasuries as of September.

"The economies of the western world, particularly America, the U.K., and Europe, are going to see lower growth than they saw before the financial crisis because of the cost of solving the financial crisis," Bolton said. "They have, to a certain extent, mortgaged the future, so there'll be a cost that they will have to over time increase taxes or reduce spending to put their own balance sheets back in order."

Bolton's China fund will be the fourth in Fidelity's portfolio focused on the country. The others are: Fidelity Funds China Focus Fund with \$4.08 billion and Fidelity Funds Greater China Fund at \$366 million.

Source: Zero2IPO

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## This Week in China (cont'd)

### Consumer Spending on the Rise in China

Chinese consumers are now buying bigger flat-screen televisions and more vehicles than Americans. China Mobile's customer base recently crossed the half-billion mark. And the country is now among the world's fastest-growing luxury markets.

The headline stories suggest consumers are shifting gears from recessionary behavior to recovery mode.

Indeed, while recession-hit consumers in the United States and Europe are scaling back on showy purchases, Chinese consumers are flocking to domestic retailers, spurred by government stimulus measures such as rebates on home appliances and tax cuts for low-emission cars.

Retail sales increased in real terms by 15.3 percent in the first 10 months year-on-year, which is at least two percentage points higher than in the previous nine months.

According to a consumer confidence survey released recently by Nielsen Co, consumer confidence in China in the last quarter reached its highest level since mid-2007, driven by a strong improvement in local job prospects in western China and in second-tier cities, as well as personal income increases across the country.

Fifty-seven percent of Chinese consumers who were surveyed described local job prospects as "good" or "excellent" for the next 12 months, a figure 14 percent higher than the second-quarter response.

"In the previous survey conducted in July, we saw that consumers were beginning to feel that the economy had bottomed out and was on the road to recovery. In the third quarter, we see an extension of this optimism," said Mitch Barns, president of Nielsen Greater China.

"Consumers are gradually feeling more comfortable with their situation and feel that the economy is moving in the right direction," Barns said.

The World Bank China Quarterly Review late last month pointed out that continued increases in government transfers are likely to support income growth somewhat in 2010, including a 10 percent rise in pension commitments.

Moreover, in much of 2009, households benefited from negative inflation, which boosted their purchasing power. This will likely change next year with inflation expected to turn positive again, according to the World Bank.

The Nielsen survey also showed that there is still a willingness to spend on new products.

"Companies that focus on innovation and introducing new products to the market will be the ones to drive consumption throughout China," Barns said.

It's not just the well-off consumer on a spending spree. Experts said that affluent Chinese consumers are spending a smaller proportion of their income than the poor.

"The poorer people tend to consume higher proportions of their income than richer people," said Athar Hussain, director of the Asia Research Center at the London School of Economics and Political Science.

"So if China shifts the distribution of income in favor of lower-income groups, consumption will increase," Hussain said.

In many economists' views, China must significantly reform its social programs before more people will part with their money.

However, Hussain described building such a social security system for a country with 1.3 billion people as "a bigger task than building the Great Wall".

Chinese families save for buying apartments, their children's education and medical expenses. And many save for the marriages of daughters or sons.

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## This Week in China (cont'd)

"You cannot subsidize marriage, but you can certainly subsidize education costs. You can also increase the proportion of health expenditures which is refunded," said Hussain, who has been watching the Chinese economy for the past 20 years.

Hussain added that the government also should increase the country's minimum wage and minimum pension levels.

In addition, the government should more strictly enforce the regulation to ensure people living on a minimum wage salary are getting paid on time, he said.

Urban demand, meanwhile, is being boosted as millions move into the \$4,000 to \$6,000 income bracket in China and shift from spending only on essentials to buying more expensive goods such as apartments, cars and electronic appliances.

The next 10 years will witness a boom in the number of small and medium-sized enterprises (SMEs), said Zhou Tianyong, deputy director of the Research Office of the Party School of the Communist Party of China Central Committee.

Such a trend will bring more people up to the wealthier echelon, as SMEs tend to provide more job opportunities than capital-intensive State-owned companies.

Since more residents of

rural communities are moving to the cities, their spending patterns will be influenced by their fellow urban dwellers, he said.

In the coming decade, Zhou said, people will continue spending to improve their living standards, and they will continue buying cars, electronic devices, healthcare products and beauty products.

In addition, they will start consuming more service products provided by educational institutions, domestic workers, travel agents and the entertainment sector, he said.

Therefore, economists and experts are arguing that China should try to keep migrant workers in the cities, as they will be the future spenders.

Fan Jianping, a senior analyst at the State Information Center, suggested that China should issue certain residence policies to give migrant workers incentives to buy apartments and to include them in the social security safety net enjoyed by their counterparts born in cities.

These efforts are needed to encourage migrant workers to stay in the city where they have been working, Fan said.

Much of China's rural markets remain untapped. In his recent field trip to the countryside in Hebei province, Wang Bin, an official with the Ministry of

Commerce, found that the consumption patterns of the local rural people are 10 years behind their urban counterparts and that sales network development is at least 20 years behind.

"China should improve its sales network, especially in the countryside," Wang said.

However, Ji Xinyu, general manager of the strategic development division of Hainan Airlines Retailing Holding Co Ltd, said his company encountered problems when trying to move business to the rural area. The company recently set up a few branches in some counties and townships to sell travel services to rural residents.

"The sales revenues in rural areas are not stable, as rural people's shopping patterns are unpredictable. In addition, the cost to set up a vendor store in rural areas is rather high because the company has to pay more compensation to send their more experienced city-based staff to work in the countryside," Ji said.

Spending by Chinese households as a percentage of GDP is roughly half the US consumption rate and remains significantly below consumer spending levels in Europe and Japan.

Source: China Daily

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# Alternative Energy

## China's Prominence in Alternative Energy Gaining Momentum

China Longyuan Power Group's imminent sale of \$2.3 billion in shares to the public and its listing on the Hong Kong exchange could hardly have been better timed by what is the country's largest investor in wind power farms.

The government in Beijing announced on November 26, days after Longyuan Power's listing plans were made public, that it aimed to boost the country's energy efficiency as part of its contribution to the fight against global warming. China pledged to cut carbon dioxide emissions per unit of gross domestic product by 2020 compared with 2005 levels. With coal still playing a predominant part in the country's energy mix, that means an increased role for less-polluting means of energy production - such as wind power.

Longyuan Power will list on December 10 after closing its heavily oversubscribed book to investors on December 2. The retail tranche was more than 29 times oversubscribed.

The State Council announcement also came ahead of the December 7-18 Copenhagen climate summit, which aims to set international targets for climate-changing

pollutants. Prospects of internationally binding agreements emerging from the summit remain slight, but the event itself will increase public and investor interest in manufacturers involved in less-polluting forms of energy production, particularly those, such as Longyuan Power, based in the world's largest country and fastest-growing economy.

China's energy demand is rising rapidly and it will overtake the US as the largest consumer of energy by 2015.

China's willingness to raise the profile of alternative energy sources was already made clear in its 11th Five-Year Plan (2006-2010), where it committed to increase the use of alternative energy resources to 20% of total energy production by 2020, from 7.86% in 2006. Hydropower makes up as much as 5.9% of China's energy production, but extensive water pollution, dwindling water resources and growing concern about the negative effects of large dams will limit expansion of traditional hydropower generation.

At the same time, massive government investment has boosted the importance of less controversial wind and solar technology and helped manufacturers in these sectors become leading players in the global market.

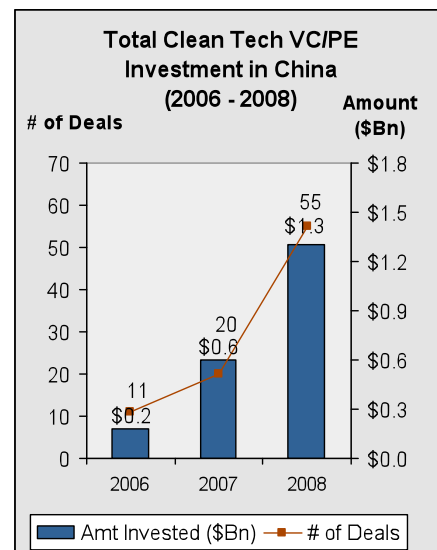
China now ranks fourth in

the world for total wind power capacity, and installed capacity may jump tenfold to 100 gigawatts by 2020, from 10GW next year, according to a 2008 plan by the National Energy Administration.

At the core of this growth, the government in 2006 started to establish wind farms in the far-west region of Xinjiang, neighboring Gansu, northern Inner Mongolia, Hebei province around Beijing, and coastal Jiangsu province, with the aim of doubling installed capacity for four consecutive years. As a result, the country has already exceeded its 10GW target for 2010, reaching 12.2GW of installed capacity.

Solar power is also an increasingly important component of China's energy strategy. More than two-thirds of China's land area has 2,200 hours of solar radiation annually, especially in western provinces, such as Inner Mongolia, Xinjiang and Yunnan. Installed capacity to capture this is expected to reach 20GW of installed solar PV (photovoltaic) power capacity by 2020, up from only about 0.07GW in 2005. Recently, China announced plans to install more than 0.5GW of solar power projects over the next two to three years.

Source: Asia Times



Source: Zero2IPO

*China has already exceeded its 10GW wind power capacity target for 2010, reaching 12.2GW of installed capacity.*

## Consumer / Retail

### China's Biggest Car-Maker Expects 30% Surge in Sales this Year

China's leading automotive corporation, the SAIC Group, expects to sell 2.65 million vehicles this year, a roughly 30 percent rise from a year ago.

The SAIC Group, or Shanghai Automotive Industry Corporation, sold a total of 2.17 million vehicles in the first ten months this year. "Sales for the whole year will likely hit 2.65 million units, surpassing Suzuki and

Fiat to become the world's eighth largest car company," said Group vice chairman Chen Hong.

Chen said due to the impact of the global financial crisis, multinational car companies had not fared well this year, while the SAIC group benefited from the booming car market in China.

In January this year, the Chinese government approved a series of industrial support packages including tax cuts and subsidies for car purchases in a bid to spur consumption. This had

driven car sales to record highs.

In the first ten months of this year, auto sales in China broke the 10 million mark and reached 10.89 million units, up 36.23 percent from a year ago, surpassing the United States as the world's largest auto market.

Chen forecast the country's total sales would reach 13.4 million units this year, and 20 million by 2014.

Source: China Daily

### Xinyu Hengdeli To Open 30 New Stores In Greater China In 2010

Hong Kong-listed luxury watch retailer Xinyu Hengdeli has announced plans to open at least 30 new stores in Greater China in 2010.

According to Zhang Yuping, chairman of Xinyu Hengdeli, the company has achieved its goal of opening 20 new stores in Greater China in 2009 and

the company currently has 250 retail outlets in this market.

He said that due to the increase of consumer confidence, sales from its individual stores in the second-tier Chinese cities increased by double-digits in October 2009.

With regard to the Taiwanese market, Zhang revealed the company will invest more resources in the future to improve its retail

network in Taiwan, especially in tourism cities on the island.

Prior to this, Hengdeli renewed its strategic alliance with LVMH Watch & Jewellery Shanghai Commercial Limited to continue to distribute the latter's watch brands of TAG Heuer and Zenith in mainland China.

Source: China Retail News

### Chow Sang Sang Invests HKD50 Million In New Stores In China

According to Vincent Chow, general manager for the Hong Kong-based jewelry company Chow Sang Sang, the company plans to invest about HKD50 million this year in opening new stores in mainland China.

Chow told local media because its business network in Hong Kong is

almost complete, the company plans to focus on the development of the mainland market. At present, its mainland business accounts for 30% of the company's total businesses.

He also pointed out that in Hong Kong, the company's revenue from mainland tourists accounts for 35% to 40% of its total revenue. However, due to H1N1 flu, the number of tourists

decreased in May.

Due to cost increases and a decrease in securities profits, Chow Sang Sang reported that its net profit decreased by 8.8% to HKD470 million in 2008 while its revenue increased by 25.5% to HKD9.881 billion, with the revenue from the jewelry retail sector increasing by 30% to HKD5.359 billion.

Source: China Retail News



Source: Bloomberg

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# Recent Transactions

## Baosteel Buys 15% Stake In Aussie Miner

Baosteel Group, China's leading steelmaker, announced its acquisition of 15 percent stake in Aquila Resources, an Australian iron ore and coal company.

The A\$286 million (\$265 million) has made Baosteel the second largest shareholder of Aquila.

## CIC Said To Buy \$400 Million Of Stock In Longyuan IPO

China Investment Corp., the nation's sovereign wealth fund, agreed to buy \$400 million of shares in the Hong Kong initial public offering of China Longyuan Power Group Corp. CIC's investment in the IPO of China's largest wind power producer will be locked up for 12 months.

The accord marks the latest of a string of recent CIC investments into the energy and resources industries to hedge against inflation and to meet the needs of the Chinese economy.

## "Mr.China" Perkowski's Auto Components Firm Up For Sale

Asimco Technologies, an automotive components maker founded by Wall Street veteran Jack Perkowski in Beijing 15 years ago, is up for sale in a deal that could fetch over \$200 million.

Asimco is currently the largest independent manufacturer of automotive and

The transaction is an important strategy for Baosteel's overseas expansion by securing long-term supply of critical raw materials for its steel making business.

The deal will help the Australian company source low-cost financing from Chinese institutions to support its projects.

Tony Poli, executive

The fund, which held almost \$300 billion in assets at the end of last year, has spent more than \$4 billion since September on resources to support expansion in the world's fastest-growing major economy. Earlier this month, it bought a \$710 million stake in GCL-Poly Energy Holdings Ltd., China's biggest producer of polysilicon.

Beijing-based Longyuan may raise up to HK\$17.5 billion (\$2.3 billion) in the Hong Kong share sale. It would be the world's third-largest alternative energy IPO since at least 1999, according to data compiled by Bloomberg.

heavy-duty truck components in China. It became famous following the publication of Tim Clissold's best-selling book, "Mr. China," which was based on Perkowski's experiences in the country.

U.S. boutique investment bank Houlihan Lokey has been hired to advise on the sale and about 15 global private equity funds including the Carlyle Group and TPG Capital

chairman of Aquila said, "The company now looks forward to developing its relations with Baosteel to the mutual benefit of both companies."

Under the terms of the deal, Dai Zhihao, a vice president of Baosteel, will step in as a board member of the Australian coal-miner.

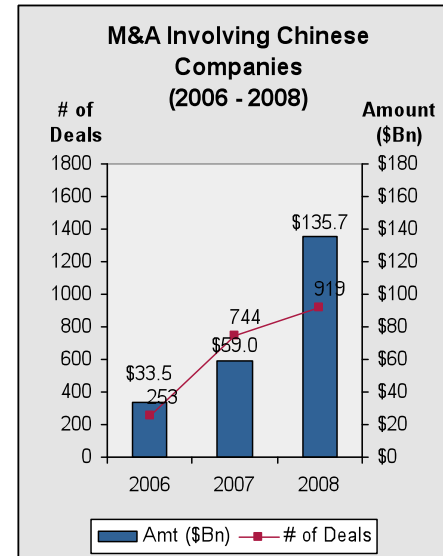
Source: China Daily

Four other so-called cornerstone investors have been guaranteed a combined \$330 million worth of Longyuan IPO shares in return for a promise not to sell the holdings for 12 months.

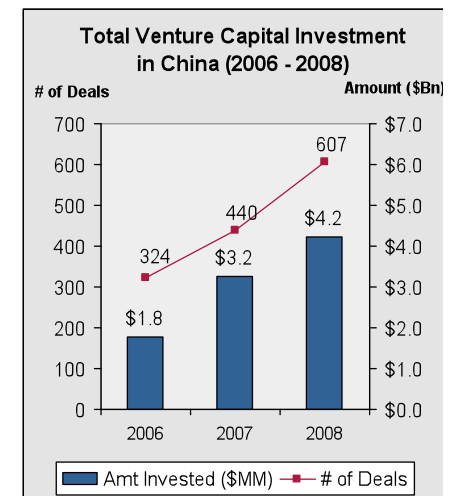
The four include WL Ross & Co. LLC, founded by billionaire Wilbur Ross, and companies linked to China Life Insurance Co., Bank of East Asia Ltd. Chairman David Li and Hong Kong-based asset manager Value Partners Group Ltd.

Morgan Stanley and UBS are managing the IPO.

Source: Bloomberg



Source: Capital IQ



Source: Zero2IPO

## Recent Transactions (cont'd)

widely ranging from piston rings to alternators and operates 900 service stations across China, is now controlled by a U.S. private equity fund Key Principal Partners (KPP).

KPP, based in Cleveland, Ohio, led a \$100 million investment in Asimco in March 2004 and later won control of the company, which has regional offices in the United States,

### Investment Firms Buy Into Sina

Three investment firms, including Sequoia Capital, are joining Sina Corp.'s management to invest \$180 million in the company as they attempt to reinvigorate China's largest internet portal.

FountainVest Partners, and Citic Capital Holdings Ltd. are backing the Sina management team's purchase of new shares that will give the group a 9.4% stake in the company. Sina's management, led by chief executive Charles Chao, will put in around \$50 million and the three investment firms will provide the remaining roughly \$130 million, with each taking stakes of a similar size.

In September, Sina said it was planning to sell the new shares to its management in a "private equity placement" to fund acquisitions and its working capital needs. Since that announcement, Sina has been hammering out terms with the investor group to provide the financing.

The investment agreement

Europe and Japan for its non-Chinese corporate clients.

Asimco was launched by Perkowski in 1994 in Beijing as one of the first few foreign direct investments in the capital city. Now the company, still headquartered in Beijing, has sales of more than \$500 million.

"As big as you think the

comes as Sina dropped a plan to acquire assets from Focus Media Holding Ltd. The deal would have given Sina access to a huge network of television screens playing advertisements in office buildings across China.

Sina's management is building a stake in the company with the aim of showing investors its confidence in the future prospects of the business. The deal represents a "management buy-in," giving the management a bigger stake in the company's future and greater say over its operations.

The new investors are betting the management can engineer a turnaround in Sina's business. Sina was an early mover in China's competitive internet market, but has failed to keep pace with competitors in recent years.

Unlike some competing portals like Sohu.com Inc. and Tencent Holdings Ltd., it never moved into online games, which has proven to be highly profitable and also resilient during an economic downturn. Sina's

Chinese market is," Perkowski said, "It's bigger."

Global carmakers such as Volkswagen and General Motors are stepping up their presence in China, which has overtaken the United States as the world's largest auto market this year.

*Source: Forbes*

heavy exposure to the highly cyclical online advertising has hurt its performance since the onset of the global financial crisis.

Still, Sina's internet portal remains a valuable franchise that has wide recognition among Chinese internet users. Sina earns advertising revenue from its main news portal supported by its own in-house news gathering operation and portals for consumers shopping for apartments and automobiles. In its third quarter results, the company said it is now seeing signs of a strong recovery in online advertising.

Sina combined its real-estate portal with part of E-House (China) Holdings Ltd. to form China Real Estate Information Corp., which raised \$231 million in an October listing on Nasdaq. Sina owns a 33.4% stake in China Real Estate Information.

*Source: Wall Street Journal*