

SCHECHTER + CHOU, INC.

嘉 质 策 略 • www.splusc.com



S+C NEWSLETTER Volume 1, Issue 14, August 5, 2008

GREETINGS...

Greetings to our colleagues, contacts, friends and associates in the US, China and Asia. We all look forward to a very exciting Olympic Games in Beijing. Let the Games begin! We at Schechter + Chou wish our readers around the world a great Olympics and summer season.

Sincerely,

Aaron Schechter and Frances Chou

HOT TOPICS...

Speculative capital flows into China....

Even with strict capital controls, China has been hit with the largest wave of speculative "hot money" ever to hit an emerging economy. Using a variety of calculations, experts estimate that between US\$90 – 300 billion of speculative capital has poured into China during the first 5 months of the year. Even with China's trade surplus starting to shrink this year, China's foreign-exchange reserves are continuing to grow ever faster. Hot money can come into China through various ways including companies overstating foreign direct investment (FDI) and through over-invoicing exports. Additionally, other loopholes exist, such as resident individuals can bring in \$50,000 annually into China



from abroad, and they may be using their friends and relatives' quotas as well, and Hong Kong residents can transfer US\$11,600 a day into China's banks. While trying to crack down on the inflows, the Chinese government is concerned that if they block the channels, they risk that the activity will simply be driven to underground money exchangers. The bulk of the capital flows into standard bank deposits. With an interest rate of 4% on yuan deposits versus 2% on dollars, plus expected appreciation in the yuan, success in bringing money into China offers what seems like a risk-free profit.

The potential risks to China's economy for all the hot money are two-fold; one, the capital could suddenly flow out, thus affecting its banking system with an abrupt withdrawal. Additionally, there is a concern that capital inflows will fuel inflation. Attempts by the Chinese central bank to curb inflation by allowing the yuan to rise at a faster pace versus the dollar, by an annual rate of 18% in the first quarter of this year, ended up encouraging investors to bet on future appreciation, thus creating even more capital inflows. Additionally, the Chinese government is under pressure to slow the rate of appreciation of the yuan versus the dollar, from Chinese exporters who have seen their profits squeezed. We shall see what will happen to this "hot money" trend.

Chinese outbound investment....

Spurred on by its appetite for natural resources and commodities, Chinese firms this year have acquired overseas assets of approximately US\$42 billion. This total represents nearly double what China invested overseas for all of 2007, according to Dealogic data. While this represents a large increase, as a percentage GDP, Chinese company's acquisition of foreign assets is still far below the levels of France, Germany and the United Kingdom. The largest Chinese companies, most of which are publicly traded state-owned enterprises where the Chinese government still holds substantial stakes of 70-80%, are leading the charge overseas. Chinese companies are sitting on large cash balances built up over the last few years and have the support of the Chinese government to go abroad, given the need to access raw materials and new markets.

In February, Aluminum Corp., of China, ("Chinalco"), teamed up with US giant Alcoa Inc. to buy 12% of Rio Tinto for more than US\$14 billion. In July, Chinese metals trader Sinosteel Corp., won a battle for the controlling interest in an Australian iron-ore company, Midwest, which marked corporate China's first successful hostile acquisition of an overseas company. Also in July, a subsidiary of CNOOK agreed to buy Awilco, a publicly listed Norwegian oil-service company, for US\$2.5 billion. Chinese companies are choosing their targets carefully. In the acquisition of Awilco, given that Norway has plenty of its own oil in the North Sea, and where Awilco is not a household name and does not own any oil fields, it did not stir up much scrutiny.

In some other cases, the heavy Chinese government ownership of companies has raised some concerns in the Western countries in more sensitive areas involving technology and natural resources. For example, Chinese telecom giant Huawei recently teamed up with US private equity firm Bain Capital to acquire 3Com but failed because of US regulators' concerns over technology transfer. A number of deals in Australia have reportedly been delayed as well. A recent McKinsey report estimated that Chinese government shares of the largest Chinese enterprises will continue to fall and be almost entirely sold off by 2012. Once this occurs, it should act to reduce fears that the Chinese companies will be driven to act on behalf of the Chinese government, and not the company's shareholders. As for now, less high profile deals in highly competitive industries have a higher likelihood for success.

Let the Games Begin...

With a price tag of US \$43 billion, the Beijing Olympics are the most expensive in history, far surpassing the US\$15 billion spent on the 2004 Games in Athens, Greece. In all, 37 competition and 56 training venues

1

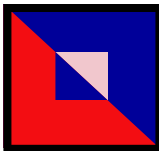
Schechter + Chou, Inc. 嘉质策略 • 10960 Wilshire Boulevard, Suite 1225, Los Angeles, CA 90024, USA

tel: 310-479-8600 • fax: 310-479-0699 • email: info@splusc.com • website: www.splusc.com

All rights reserved. Copyright 2007, Schechter + Chou, Inc.

Schechter Plus Chou, Inc., does not share your email address or any other information with other parties.

To remove your name from the mailing list, contact us at the above-referenced address or at frances@splusc.com.



SCHECHTER + CHOU, INC.

嘉 质 策 略 • www.splusc.com



S+C NEWSLETTER Volume 1, Issue 14, August 5, 2008

HOT TOPICS—Continues...

were completed in time. Additionally, Beijing boasts a futuristic new airport at a cost of about \$3 billion that is said to be one of the largest buildings in the world. The most visible challenge remains air pollution, and the China Daily, China's official English-language newspaper warned in a recent article that officials may force additional vehicles off the streets and temporarily close more factories in an effort to improve air quality. Additionally, with approximately 20,000 journalists accredited to cover the Games, concern has been raised by the International Olympic Committee to Chinese government officials that there has been some blockage of web-sites at Beijing's newly opened Main Press Center.

REGISTER NOW...

Schechter + Chou is proud to serve on the planning committee for the inaugural **Pacific Rim Entrepreneur Summit (the "Summit")** to be held in Shanghai, China, from October 23-25. We would like to invite you to be a participant in **this Summit**. USC Marshall's Greif Center for Entrepreneurial Studies and its Center for International Business Education and Research (CIBER) are the co-developers of **the Summit**, in partnership with entrepreneur programs/centers from 17 business schools at the leading universities: Cheung Kong Graduate School of Business, Cornell University, Nanjing University, National Taiwan University, National University of Singapore, Northwestern University, Shanghai Jiao Tong University, Stanford University, Tsinghua University, University of Chicago, University of Colorado at Boulder, University of Malaya, University of Maryland, University of Sydney, University of Virginia, Waseda University and Zhejiang University. For detailed information on **the Summit** and for registration for **the Summit**, please go to <http://www.pacrimentrepreneursummit.com/>. We are seeking participants who are entrepreneurs or the leaders of innovative divisions of large global firms. Each of the partner schools is responsible to recruit participants and panelists from its network of internationally-focused alumni and friends. Thus, a major benefit for the participants of **this Summit** is that they will be able to develop new personal networks with alumni from the participating schools. Given the unique structure of **this Summit** and the strategic alliance of 18 prominent business schools, we feel confident that each participant can realistically expect to develop serious new friendships with 20 to 25 potential business partners from at least 3 to 4 Pacific Rim economies. **We hope to see you at the Summit in Shanghai this October!**

LEGALLY SPEAKING...

The following is provided by Y.F. Chou, Prof. Corp. For questions, please contact info@yfchou.com.

New Development in IPR in China

On June 5, 2008, the State Council of China issued the "Outline of National Intellectual Property Strategy" (the "Outline") setting forth Chinese government's new strategy to deal with the IPR issues. The Vice Premier of the State Council, Wang Qishan, commented that the implementation of the strategy "will open a new chapter of IPR protection in China." The Outline states that it is formulated for the purpose of, among other things, "improving China's capacity to create, utilize, protect and administer intellectual property". Its goal is to China "a country with a comparatively high level" related to all aspects of IPR by 2020. The focuses of the strategy is to improve the intellectual property regime, to promote the creation and utilization of intellectual property, to strengthen the protection of IPRs, to prevent abuses of IPRs and to foster a culture of IPRs. The strategic measures to take include, but are not limited to, increasing the capacity to create intellectual property, encouraging the commercialization and utilization of IPRs, expediting the development of the legal system, law enforcement and administration related to intellectual property, promoting a culture of IPRs and expanding international exchanges and cooperation in intellectual property. The failure of Chinese government to implement any meaningful IPR protection in China has always been the major complaint of Western companies. In the past, the Chinese government seems to be too distant and uninterested in providing any IPR protection, and the culture seems to be too resistant to the idea of IPR. However, there has been a significant rise of home grown intellectual property in China in the recent years. It seems that finally, the Chinese companies with established brand names and self-developed products have some intellectual property to defend against, and they start to demand more protection for their own IPR from the Chinese government. Since 2003, the number of trademark applications in China has grown by 60%, and the currently active patents are around 850,000. China now has about 50 courts that solely handle IPR cases. These courts are staffed with judges trained in dealing with IPR cases. The number of IPR related lawsuits has more than doubled. More and more Chinese companies are bringing lawsuits at these courts to protect their IPR. Even though the damages awarded in Chinese courts are lower in comparison to those jury awards in the US, the low cost in bringing lawsuits and the recoverable legal costs in lawsuits increase the willingness of Chinese companies to go to courts in China to protect their IPR. It seems that finally, there is some hope that Chinese government will take the protection of IPR issue more seriously in order to protect the IPR owned by, not just foreign companies, but Chinese own citizens and domestic companies. With the rise of IPR awareness by domestic companies in China and the announcement of the Outline, hopefully, some of the strategies and measures mentioned in the Outline will be implemented. The effect of this Outline still remains to be seen.

Schechter + Chou, Inc. 嘉质策略 • 10960 Wilshire Boulevard, Suite 1225, Los Angeles, CA 90024, USA

tel: 310-479-8600 • fax: 310-479-0699 • email: info@splusc.com • website: www.splusc.com

All rights reserved. Copyright 2007, Schechter + Chou, Inc.

Schechter Plus Chou, Inc., does not share your email address or any other information with other parties.

To remove your name from the mailing list, contact us at the above-referenced address or at frances@splusc.com.