

# JESA INVESTMENT & MANAGEMENT CO. LTD.

NEWSLETTER

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## NEWS FROM JESA!

*By Saro Capozzoli, Founder and GM of JESA Investment & Management Co., Ltd*

The end of June is on the doorstep and it is worth to start summing up the results of the first semester of this year.

As far as our company can report about its analysis, two different behaviours and perspectives can be drawn up: the foreign companies' side and point of view and their subsidiaries' one in China.

Observing China from abroad, as a perspective of a new investor there have been a slow down in the decision making processes. Several projects have been postponed or slowed down.

Despite the efforts of the Central Government to ease the procedures, delegating some powers to provincial level for the approval, establishment and administration of foreign invested enterprises, the Ministry of Commerce announced that the FDI in China plunged of 21% year on year in the first four months of 2009. On the other hands, for an observer from China,

these decisions are lost chances to enjoy internal favourable conditions.

Besides the governmental efforts to ease the investment approval, there are several data that is worth to consider. The cost of the land is decreased of 30% and the rent fees of productive buildings and offices decreased as well. Generally speaking this is the best time to find more reasonable prices and exploit these advantages to put the right foot into China.

For those companies mainly committed in outsourcing activities in the Mainland this is the right time to negotiate with suppliers for better conditions. Moreover it has sense start to refresh the pool of suppliers and look for new reliable ones.

Those companies whose financial situation and risk sustainability allow them to think about it, can look to the Chinese companies as potential targets for acquisition. The main targets are those companies in interesting industries that can speed up the path of market penetration of the Investor.

A stable presence in the market is one of the most important factors of success or failure of a foreign company. In this period, that sees harsh

and dry domestic markets in the mother countries, the Chinese internal demand could represents a breath of fresh and new air, despite Chinese pollution of course.

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## ITALIAN VERSION

La fine di giugno è alle porte e si può quindi cominciare a dare un occhio ai risultati ottenuti durante il primo semestre dell'anno.

Per quanto la nostra società possa riferire solo delle proprie analisi è possibile delineare due differenti prospettive e comportamenti: il punto di vista delle società straniere e quello delle loro filiali in Cina.

Osservando la Cina dall'esterno, nell'ottica di un nuovo investitore, si riscontra un rallentamento del processo decisionale. Alcuni progetti vengono posticipati o subiscono ritardi.

Nonostante gli sforzi del governo centrale per snellire le procedure, delegando a livello provinciale alcuni poteri per l'approvazione, la costituzione e l'amministrazione di società straniere, il Ministro del Commercio ha annunciato che gli investimenti esteri in Cina

sono diminuiti su una base annua del 21% solo nei primi quattro mesi del 2009. D'altro canto, per coloro che osservano la Cina dall'interno, queste decisioni sono un'occasione mancata per godere di favorevoli condizioni interne.

Oltre agli sforzi del governo per sveltire gli iter, ci sono numerosi altri dati che val la pena di considerare.

Il costo della terra è sceso del 30% così come l'affitto di capannoni e uffici. In generale, questo è il momento migliore per trovare prezzi ragionevoli, vantaggio che andrebbe sfruttato per entrare in Cina.

Per le società maggiormente concentrate sull'outsourcing in Cina questo è il momento giusto di trattare con i fornitori condizioni migliori. Inoltre, sarebbe opportuno approfittare per cercarne di nuovi e affidabili.

Le società la cui situazione finanziaria e propensione al rischio lo permettono possono guardare alle società cinesi come possibili target di acquisizione.

I target principali sono le imprese che appartengono a settori particolarmente interessanti che possano velocizzare il percorso di entrata sul mercato da parte dell'investitore.

Una presenza stabile nel mercato è uno dei più importanti fattori di successo o fallimento per una società estera.

In questo periodo, che vede i mercati delle nazioni madri rigidi e fermi, la domanda interna cinese può infatti rappresentare una boccata di aria fresca e nuova... nonostante l'inquinamento cinese, ovviamente.

### Notice for Italian Tax Payers

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## Chinese Overseas Direct Investments

While business around the world may suffer the ongoing financial crisis, Chinese biggest companies are looking abroad for investments.

The Ministry of Commerce has released a guideline for overseas investment to help Chinese companies seek overseas opportunities.

This guideline comes as a consequence of the eager commitment of Chinese companies to invest overseas. It includes investment laws, regulations and statistics of more than 20 countries but it is expected to cover 160 countries by the end of June.

China's overseas investment has been increasing rapidly in recent years. In 2008, the country outbound investments in non-financial sector soared by 63.5% to USD 40.65 billion. The contract value of projects in foreign countries went up by 39.4% to USD 56.6 billion.

The fast-growing domestic market is not stopping the Companies in their "going-global" path. The most obvious reason behind this is to acquire technology and know-how. Chinese companies aim to reach the quality level and

R&D capability to compete with more mature US and European companies.

Another reason to make overseas acquisition is the market diversification and the acquisition of global consumers, to gain distribution overseas and penetrate new markets.

Moreover Chinese are pulled by developed economies that are facing increasing needs of funds to boost the recovery of a host of their companies.

Three are the main kinds of investment that are driving China abroad.

The first types of deals involve Chinese State Owned Enterprises that are taking stakes in overseas commodities firms. Since 2005 many cases have been concluded successfully, allowing China to enter and participate in foreign companies capitals. In 2005, China National Petroleum Corp acquired Canadian-owned Petro Kazakhstan for US \$ 4.2bn. Three years later, in 2008, China Petrochemical Corp (Sinopec), the second-largest Chinese oil producer, acquired Canada's Tanganyika Oil, operating in Syria, for US \$ 1.9 bn. The state-owned Aluminum Corp of China (Chinalco) offered US\$19.5bn for an 18% participation in Rio Tinto, an Anglo- Australian

mining company but the whole deal is delayed by an infinite series of regulatory checks.

A second type of overseas direct investment is the state-to-state, loans-for-oil deal. Last February, to ensure energy supplies from different countries, the Chinese government provided billion in loans-for-oil deals to Russian, Brazil and Venezuela oil companies in return for interest and the right to buy hundreds thousands barrels per day of oil for 20 years. Funding for these loans has come from the China Investment Corp (CIC), a sovereign wealth fund created in 2007.

A third type is the investments that both state-owned and private companies do in non-resource sectors such as computers, automobiles and engines. Among these the most important cases are the US\$1.7bn purchase by Lenovo, a leading Chinese computer manufacturer, of US-based IBM's personal computer business in 2005 and a US\$2.4m acquisition in February 2009 by diesel engine giant Weichai Power of Moteurs Baudouin, a French marine diesel-engine maker.

This picture doesn't exclude that the internationalization process is without risks and limits for Chinese investors. First of all, a foreign

currency restriction is in force and this makes hard the approval process for the convertibility of the Renminbi. For the record, it is worth to say that this is now changing as the Government encourages the overseas investments.

The limits and risks are also represents by the political consequences of some of previous bids that have made many potential acquirers more cautious. When in 2005 China National Offshore Oil Company Ltd (CNOOC) offers to purchase an American Company, Unocal Oil Company, a political storm was triggered and CNOOC withdrawn the offer. The Global economic crisis is impacting as well on this process causing the decreasing of attractiveness of overseas markets, due to the state of flux entire industries are suffering.

Lastly it cannot be forgotten the host of management issue brought by an overseas acquisition and Chinese companies are ill-equipped to address differences in management style, legal systems and cultural gaps. The overseas thirsty is however newly confirmed by the Chinese Prime Minister Wen Jiabao that announced that a new purchasing delegation will be sent to Europe very soon to

increase imports from the area and reinforce the positive results of the previous one.

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### China Recovery

At the end of May, the Government announced that the Chinese economy will reach in 2009 8% of growth. In the Chinese culture eight is a lucky number because the pronunciation sounds like the word prosperity. Reminding to the ancient traditions and combining a massive financial stimulus the Government's target might be feasible. At the beginning of this year, such a growth was considered to be impossible due to the deep global recession that causes astonishing plunge in the export, the fall of the growth rate to 6.1% and 20 million of unemployed around the Country.

The same economists that doubted so much about the Government's target feasibility are now revising their forecast. There are evidences that China is turning the corner and is leading out itself – and the rest of the world? – of the global economic crisis.

For the record, economists often doubted the credibility of Chinese data regarding the growth of its GDP and even if they still think that the Government might be up to this kind of tricks, it is reasonable believe that data are correct.

Paul Cavey, an economist at Macquarie Securities, explains that this year the GDP growth is 6.1% higher then the last year, even if the electricity production (two variables that historically are used to grow together) was 4% lower than it had been a year earlier. This discrepancy is due to the fact that energy-guzzling heavy industries (steel and aluminum) bore the brunt of the slowdown last year. Steel output fell by more than 10% to the fourth quarter, so it is hardly surprising that energy use dropped.

In April, the PMI (Purchasing Manager Index) reported the largest month on month increase in the PMI's five-year history, breaking into expansion territory for the first time since July 2008. This demonstrated that the manufacturing sector has begun a sustainable recovery.

Moreover for the first time in nine months, Chinese Manufacturers are raising their staffing level. This situation may also improve customer

sentiments toward the consumption boosting home and retail sales growth.

According to analysis on the car sales during April, unit sales for top 25 car assemblers were up 23.6% year on year, compared to the 2% rate of growth registered in the first quarter.

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### China is strengthening the intellectual property protection

China has launched a national plan for intellectual property rights and it is strengthening the protection of intellectual investments, increasing the compensation for infringements.

PRC officials are increasingly aware of the importance of the intellectual property protection for an innovative economy and, as demonstrated by revisions to the IPR law, seek to improve legal frameworks and channels through which companies can protect their intellectual property investments.

For this reason the Supreme Court has stressed in several occasions that shall be adopted a

flexible and practical method to calculate the damages in case of infringement in order to adequately compensate the right owner.

It is moreover foreseeable that in 2009, the Court will place stronger evidence on the balance between the interest of the rights owners and the interest of the public, and prevent the rights owners from abusing their power. This means that the standards applicable to patent infringement determination may be tightened.

China is both trying to protect foreign companies' rights from increasingly sophisticated Chinese counterfeiters (and enforce the international treaties signed) and Chinese companies that are enforcing even more patents against foreign firms.

Chinese companies are in fact just as eager as Western firms to protect their investments aiming to be the brain of the world as they already are the factories. The applications for patents in the country's patent office have reached the biggest volume in the world with more than 800.000 applications filled in 2008. Most of them are technologies that undergo minimal review and receive only a 10-year term.

In the other hand Chinese companies are increasingly filing for "invention" patents that receive 20 years of protection. Chinese companies in 2009 will surpass foreign ones in receiving "invention" patents in the country.

Chinese firms are also increasingly protecting their patent abroad, a sign that they want to protect them when exporting products to rich countries.

Revision of the patent law that is taking into effect in October strengthens the requirements for the patent's novelty, bringing it up to global standards.

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