All time high in China confidence

Nordic companies are more bullish on China than ever

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THE SEB CHINA FINANCIAL INDEX REACHES 70, up from 66 in September

COMPANIES ARE INVESTING AGGRESSIVELY with one third of companies planning for significant investments in the next six months.

SKILLED LABOR SHORTAGE, COMPETITION AND HIGH RAW MATERIAL PRICES ARE MAIN CONCERNS in 2011.

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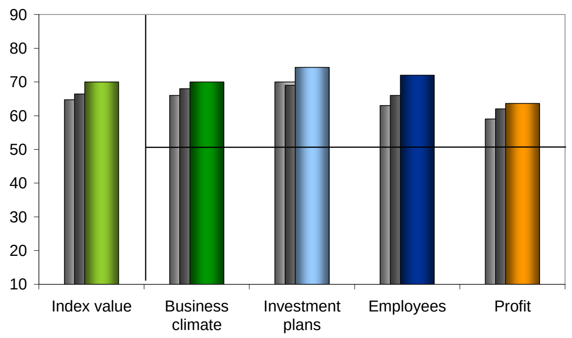
ALL TIME HIGH IN CONFIDENCE

Despite interest rate hikes and other tightening measures by the Chinese leaders, senior managers at northern European subsidiaries in China are more bullish than they have been in several years. 65% expect the business situation to improve further and 18% expect it to improve significantly. Furthermore, 58% expect profits to increase and 8% anticipate significant profit increases.

Continued growth in sales is leading to considerably more aggressive investment plans among companies with one third now saying that they are planning for significant investments in China in the coming six months. Another 55% will make modest investments during the period.

Nine of 10 companies are planning to recruit more staff and 22% say they will increase the number of staff significantly, as compared to 3% six months ago. Skilled labour shortage is raised as one of the main concerns for North European subsidiaries in China.

SEB's China Financial Index



Source: SEB Shanghai. Grey stacks show results in September and March 2010

In SEB's China Financial Survey, senior managers at 50 subsidiaries of major Nordic and German companies in China were asked about their expectations of their own business and the macro and financial environment.

A further indication that companies are positioning themselves for further growth is the fact that the need for both investment and working capital financing is up significantly among subsidiaries.

Still, it is a bit surprising that the sentiment among north European companies is increasing so much, since tightened monetary policies adopted by the central bank has had an effect on sentiment in other surveys. China's Purchasing Manager's index has for example fallen the last three months, as a sign that tightening monetary policies have started to have an effect on the overall economy.

Just as in the last survey, two thirds of companies expect their market shares to increase in the coming six months.

OUR CONCLUSIONS

China is hot, red hot. While Chinese authorities are fighting inflation with further tightening measures, and while China's leading purchasing managers' index (PMI) has fallen recently, Nordic and German companies remain bullish in China. And they are now turning their optimism into action, preparing for rapid expansion with more investments and hiring more staff. Profit expectations also increase in this survey but it remains to be seen if companies' concerns about higher raw material costs, labor shortage and increased competition will hit margins going forward.

Confidence still High

TIGHTENED MONETARY POLICY EXPECTED

Chinese growth ended at 10.3% for the full year of 2010, which is yet again the highest growth of all major economies. China will most probably continue to outpace other economies, but a slightly slower growth should be expected going forward as the country aims to tame rising inflation and avoid overheating in the property market. In China's 12th five year plan, the growth target has been lowered to 7%, although China historically has always overshot the previous target of 8%. Furthermore, the focus will be shifted to more energy efficient growth, consumer markets, and better distribution of wealth to China's inland.

Global GDP growth
Year-on-year percentage change

	2009	2010	2011	2012
United States	-2.6	2.9	3.6	4.0
Japan	-6.3	4.0	1.6	1.6
Germany	-4.7	3.6	3.1	2.5
China	9.2	10.3	9.5	8.5
United Kingdom	-4.9	1.4	1.5	2.5
Euro zone	-4.0	1.7	1.9	1.8
Nordic countries	-4.6	2.9	3.4	2.6
Baltic countries	-15.6	1.2	4.1	4.7
OECD	**-3.5**	**2.7**	**2.8**	**2.8**
Emerging markets	2.6	7.1	6.5	6.5
World, PPP*	**-0.6**	**5.0**	**4.5**	**4.6**
World, nominal	-1.3	4.3	3.8	3.9

*Purchasing power parties

Source: OECD, SEB

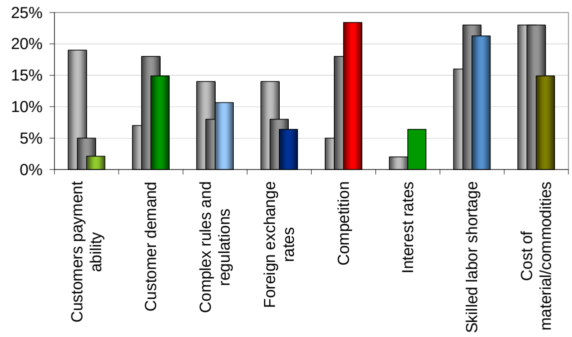
COMPETITION, RAW MATERIAL COSTS AND LABOR SHORTAGE ARE MAIN CONCERNS IN 2011

While almost all indicators in this survey point in the direction of improved business conditions, slightly higher profit expectations and aggressive growth plans among Nordic companies in China, there is also a clear trend change as regards the challenges facing the same companies. While companies saw customer demand as their main concern a year ago, competition was mentioned as the main worry in our last two surveys. In this survey, over 40% mention competition as one of their top two concerns in China in 2011.

As both foreign and domestic investors in China are planning a faster expansion in the Chinese market, access to skilled labor risks becoming a bottleneck. Anecdotal evidence from discussions with SEB clients show that many companies can't grow as fast as they would wish to due to lack of available staff in the market, but also due to loss of existing qualified staff. 44% of companies think that skilled labor shortage is one of their top two concerns in the coming six months, up from 27% six months ago. This will undoubtedly risk spilling over in increased labor costs going forward.

A total of 38% listed high raw material costs as the most important or second most important concern which is slightly up from the last survey. As China is a net importer of raw material, global price increases have a direct effect on North European companies' subsidiaries in China, just as in other markets. The Chinese Producer Price Index, PPI, was up by 7.2% in February.

Picture: Major Concerns in the coming six months



Source: SEB Shanghai, colored stacks show companies choice as major concern, grey stacks show second and third largest concern

THE RMB WILL CONTINUE TO APPRECIATE AND RATES WILL MOVE UP FURTHER

China continues its monetary tightening and the one year PBOC policy rate has been raised in three steps to 6.06%. Many analysts expect 2-3 more hikes in 2011, along with further currency appreciation. Since late June last year, when the appreciation of the RMB against the USD was resumed, the RMB has strengthened by close to 4%.

As many as 88% of respondents expect interest rates to continue to go up in 2011 and 82% believe that the RMB will continue to appreciate against the US-dollar.

Survey Results

INFORMATION ABOUT THE SURVEY

The SEB China Financial Survey is based on input from CEOs and CFOs at 50 subsidiaries of major Swedish, Danish, Finnish, Norwegian and German companies. Most of the companies have a global turnover of over EUR 500 million. The survey is web- based and confidential and was carried out during the period March 1 – 7, 2011.

SUBJECT: BUSINESS CLIMATE / PROFIT EXPECTATIONS

Northern European subsidiary managers in China have a more positive view of the business climate for the coming six months, compared to six months ago. 65% (54% in September) of companies expect business conditions to be favourable over the coming six months and 18% (21% in September) believe they will be very favourable. No company believes that conditions will be unfavourable or very unfavorable. One year ago 8% of companies had a negative view and, eighteen months ago the figure was 11%.

When asked about profit expectations, 58% expect profits to increase as compared to 59% six months ago, but today as many as 8% of companies believe profits will improve considerably (compared to 3% in September). 6% expect falling profits (3% in September.

Growth in 2010 reached 10.3 and most figures point at continued strong growth in China during 2011. Chinese exports (of which approximately 60% are produced by foreign-invested companies) are now back at levels seen before the financial crisis. As the global economic outlook continues to improve, there is reason to believe that Chinese exports continue to grow also in 2011. Retail sales increased 18.4% in 2010, which was slightly higher than market expectations.

(See graphs 1 and 3, p. 5)

SUBJECT: EMPLOYMENT STRUCTURE

Northern European companies are recruiting more in China than in any of the previous China Financial Index Surveys. The pace has picked up significantly in the past six months. As managers in northern European companies become increasingly bullish, they are now planning to further increase staff numbers. 88% are planning to increase staff in China, out of which 22% are planning significant increases (the latter figure was only 3% six months ago).

(See graph 4 on page 5)

SUBJECT: FIXED ASSET INVESTMENT PLANS

One third, of companies in this survey is planning for major investments in the coming six months in China, up from 18% in the latest survey in September. 55% are planning for modest investments. Only 12% are planning no further investments and no company is divesting.

Hence, it is obvious that the strategy to “carefully expand”, which was prevailing in previous SEB China Financial Index surveys, has now developed into a more aggressive investment mode among northern European companies. China saw some USD 108.7bn in foreign direct investment last year, an increase by 7.4% from the year before and most surveys point in the direction of China continuing to be a prime FDI destination for western companies.

(See graph 2 on page 5)

SUBJECT: AVERAGE OUTSTANDING ACCOUNT RECEIVABLES DAYS

Foreign companies often highlight payment terms and the issue of actually being paid on time as one of the main challenges in China. Based on this survey, only a small minority of Nordic and German corporates have average outstanding account receivable days greater than 90, but the number has increased somewhat. 12% of respondents now have 90-120 days average payment terms compared to 6% in the last survey. 4% have over 120 days (2% in the last survey).

(See graph 5 on page 5)

SUBJECT: FUNDING NEEDS

Funding needs are on the rise. Today, 62% of managers are expecting funding needs to increase in the coming six months, as compared to 46% six months ago and 42% 12 months ago. Only 33% of managers expect funding needs to remain unchanged, whereas 6% expect funding needs to decrease. Considering that companies continue to invest in China, this seems logical. At the same time, the improved business situation with increased sales leads to a greater need for working capital.

(See graph 6 on page 5)

SUBJECT: FX AND INTEREST RATES

The view that the Chinese economy is expanding quickly can be seen from managers' views of interest rates and the RMB exchange rate. No company believes that interest rates will fall, whereas 88% believe that rates will go up (compared to 51% six months ago). 12% expect rates to stay at current levels in the coming six months (six months ago, 49%

thought they would be unchanged). Both deposit rates and lending rates are regulated in China and the current lending rate for a 12-month bank loan is 6.06%. The 12-month deposit rate is 3%. The Chinese Central Bank, PBOC, has already hiked rates three times since November, by totally 0.75%, and considering that inflation, measured as CPI, was reported at 4.9% in December, further rate hikes are probable. Most market forecasts point at a further 2-3 hikes during 2011. At current levels, deposit rates are highly negative. Although the government will move cautiously, most economists expect further tightening of the Chinese economy during the year.

Almost all managers expect the RMB to continue appreciating against the US dollar after the RMB finally started to move in July last year. 82% expect the RMB to appreciate over the coming six months compared to 85% in September. 16% still believe that the RMB will be stable against the US dollar. A fairly stable RMB/USD exchange rate is one of the main reasons why many companies have traditionally invoiced their China trade in USD, but the trend seems to have changed in the last six months. As many as 30% of the respondents now use the Euro as their main currency. This is up from 22% in the last survey. 9% use one of the Scandinavian currencies. An interesting question in coming surveys will be to see how many companies will start to use the RMB as their cross border settlement currency, as China has started to allow that. Between June 31 and March 7, the RMB appreciated by 3.3% against the USD, and depreciated by 10.7% against the EUR, 11.9% against the NOK, 9.5% against the DKK and 16.3% against the SEK. The fact that so many companies are expecting the RMB to start moving against the USD this year may be one reason why as many as 49% are hedging some or most of their FX flows on the on-shore forward market and another 24% are hedging via their head offices through NDF-contracts or the CNH market.

(Please see graphs 7 and 8 on page 5 plus graphs 9 and 10 on page 6)

Subject: MAIN CONCERNS

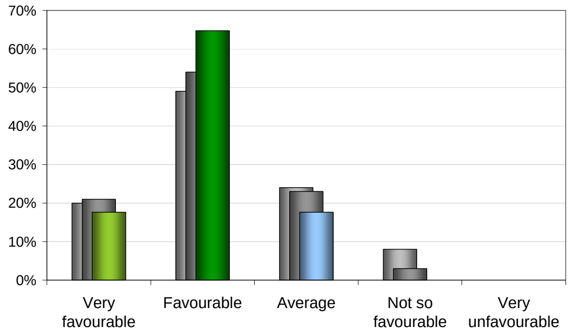
Competition continues to be the major concern for local management. Now 23% mention this as their main concern and another 18% say it is their second largest concern. Skilled labor shortage is also a top concern (mentioned by 21% as the main concern and 23% as the second largest concern) as well as raw material costs (15% and 23% respectively). Customer demand was the main concern a year ago but is now only mentioned by 18% of companies as a main concern.

(See graph 11 on page 5)

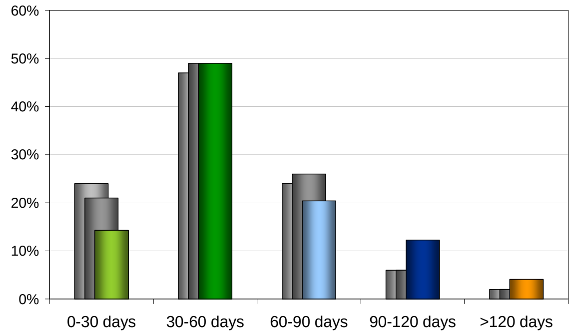
CHINA FINANCIAL INDEX – COMPOSITION

The SEB China Financial Index in March had a value of 70, indicating a positive attitude. A value of 50 would indicate a neutral view. The index is based on four components with the following ranking in this survey: General Business Situation – 70, Profit Expectations – 64, Investment Plans – 74, and Employment Plans – 72. (see the graph on page 1)

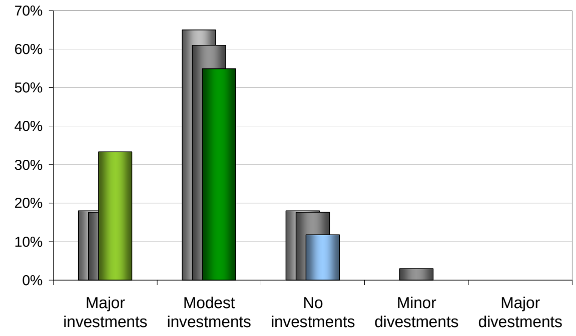
1. BUSINESS CONDITIONS



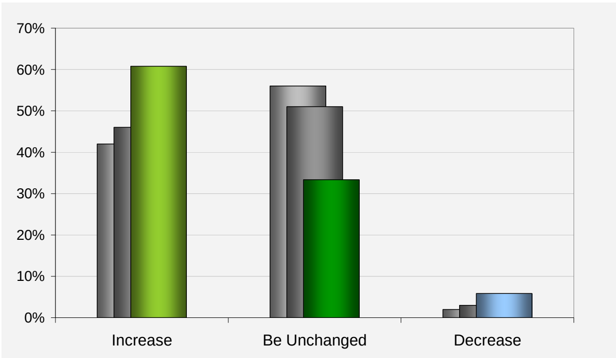
5. AVERAGE OUTSTANDING A/R



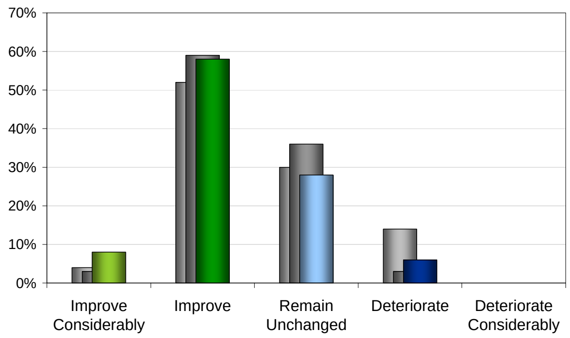
2. FIXED ASSET INVESTMENT PLANS



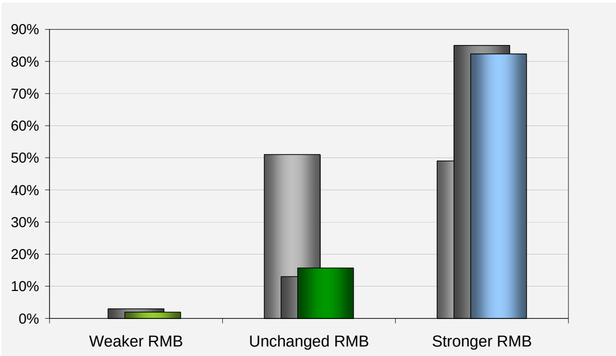
6. FUNDING NEEDS



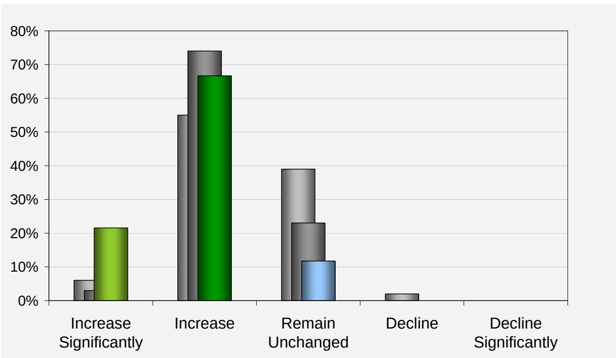
3. PROFIT EXPECTATIONS



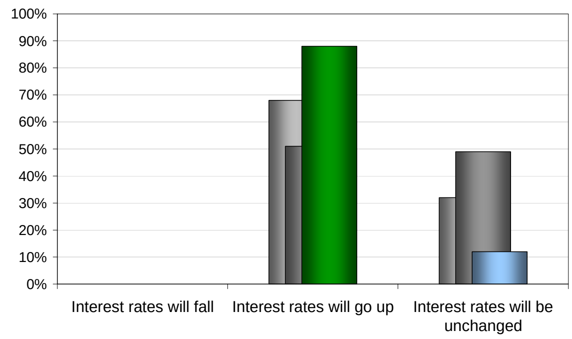
7. RMB AGAINST USD



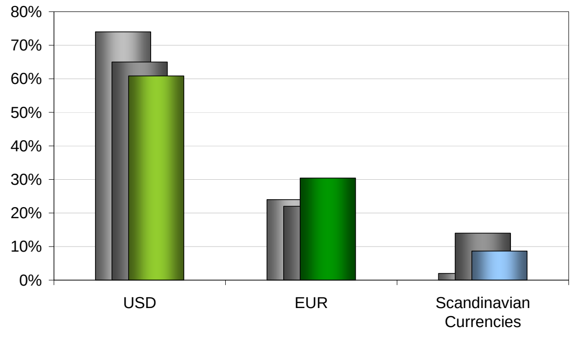
4. NUMBER OF EMPLOYEES



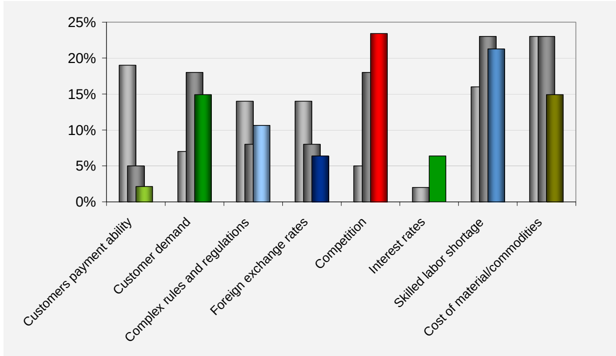
8. RMB INTEREST RATES



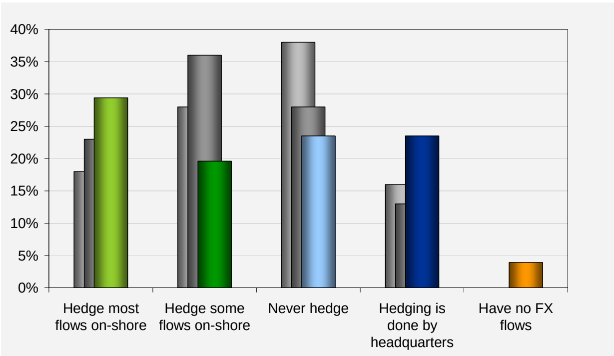
9. MAIN TRADING CURRENCY



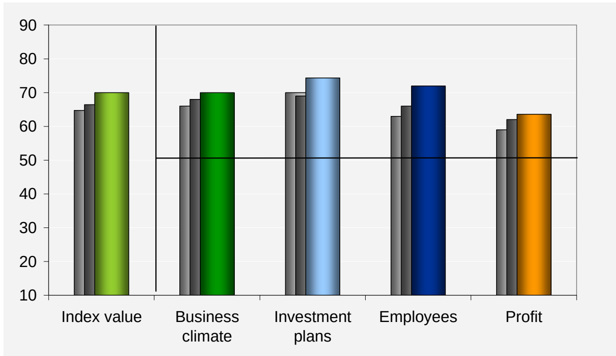
11. MAIN CONCERNS



10. HEDGING STRATEGY



12. MAIN INDEX



Source: SEB Shanghai. Grey stacks are indicating companies' answers in the last two surveys in September and March 2010