SEB Shanghai Branch 16 March 2010

Investments up as business climate improves

- But profit expectations fall as margins deteriorate

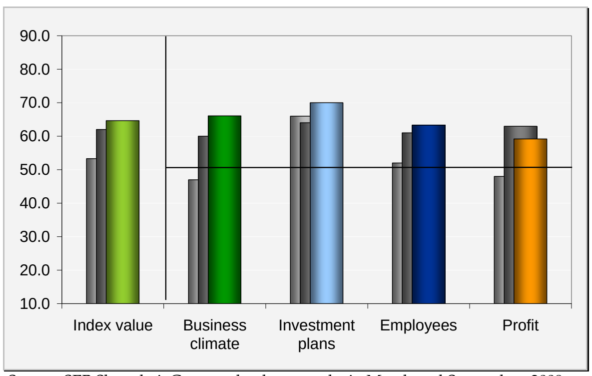
Senior managers at Northern European subsidiaries in China foresee a continued improvement in business prospects on the Chinese market. Almost half of the respondents expect their business situation to improve further and 20% expect it to improve significantly.

Companies are now starting to invest in China again with 65% planning modest investment and 18% planning major investments in the coming six months. Recruitment plans also continue to increase.

However, profit expectations are lower than previously, indicating falling margins as higher manufacturing costs cannot be completely passed on to clients and domestic competition increase.

SEB's China Financial Index reached 65 in September, up from 62 in September.

SEB's China Financial Index



Source: SEB Shanghai. Grey stacks show results in March and September, 2009

In SEB's China Financial Survey, senior managers from around 50 subsidiaries of major Nordic and German companies in China were asked about their expectations of their own business as well as the macro and financial environment. Overall, managers believe that the economy will continue to improve and are moving from the previous "carefully expand" strategy that many companies adopted in September towards a more aggressive expansion in China.

In the meantime, monetary policies are expected to be tighter. More than two thirds expect interest rate hikes and half of the respondents expect the RMB to start to appreciate against the US-dollar.

Our conclusions

Multinational companies are moving back to an expansion mode on the Chinese market as the country continues to report high growth. With higher raw material prices, and a stronger RMB, manufacturing companies are expecting to face rising input costs, while overcapacity and competition in almost every manufacturing sector limits the ability of firms to raise final goods prices. That should be the most logical reason behind dampened profit prospects among respondents in this survey.

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Confidence High

China leading growth in 2010

China's economy grew by 8.7% in 2009 and SEB's forecast is that China will grow by 10.5% in 2010 and by 9% in 2011. China will thereby show the highest growth pace of all major markets in the world. This is in stark contrast to the US, Europe and Japan which are all still struggling in the wake of the financial crisis. The key to growth has been fiscal stimulus financed by huge bank lending. At the recent National People's Congress, the government assured markets that it will maintain its expansionary monetary and fiscal policies, even as the government attempts to tackle risks of overheating in the economy by fine tuning policies and controlling infrastructure investment

GDP growth
Year-on-year percentage change

	2008	2009	2010	2011
United States	0.4	-2.4	3.4	2.2
Japan	-1.2	-5.0	1.5	1.8
China	9.6	8.7	10.5	9.0
Euro zone	0.5	-3.9	1.7	2.0
United Kingdom	0.6	-4.6	1.8	2.6
Sweden	-0.2	-4.5	3.1	2.7
Norway	1.8	-1.0	2.3	2.4
Denmark	-0.7	-4.8	1.4	1.8
Finland	1.1	-7.4	2.5	2.7
Nordic countries	0.5	-4.1	2.4	2.4
Baltic countries	-1.0	-15.9	-0.1	4.2
Emerging markets	6.1	2.1	6.3	6.0
OECD	**0.6**	**-3.5**	**2.4**	**2.3**
World, PPP*	**3.0**	**-0.7**	**4.5**	**4.3**
World, nominal.	2.0	-1.4	3.7	3.6

* Purchasing power parities

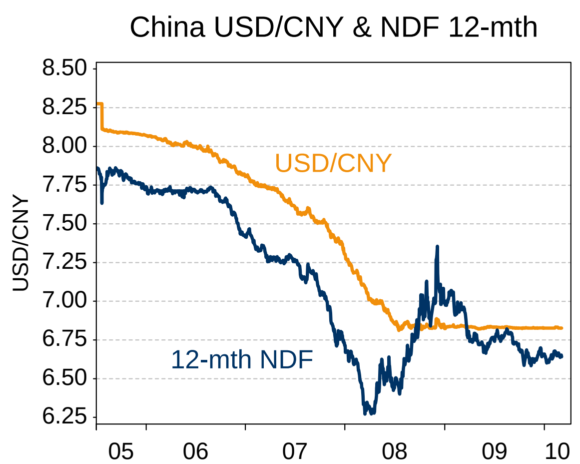
Source: OECD, SEB

Source: SEB, Nordic Outlook, September 2010

While all indicators in this survey point at a continued improving business climate in China, profit prospects have fallen since September. Anecdotal evidence from discussions with our clients within the manufacturing industry indicates that this is mainly due to rising input costs. As fierce competition and oversupply in many manufacturing sectors are keeping final goods prices down, this results in falling margins which seems to be a rising concern for companies. This is further proven by statistics: The Markit PMI index for manufacturing input prices has been climbing steadily, to 69.9 in December from 44.3 in May. More than half of the respondents in our survey have manufacturing in China.

The RMB will appreciate vs. the USD again; interest rates are on their way up

Although Chinese officials have emphasized that a stable (i.e. not appreciating) RMB is in China's interests and that the country will not give in to pressure from other countries to let the currency strengthen, there are many signs that the RMB will in fact start to strengthen during 2010. Recently, Zhou Xiaochuan, governor of China's Central Bank, described the current peg to the US dollar as temporary, leading to market conclusions that China will in fact continue to let the currency strengthen against the US dollar after a halt in appreciations since August 2008. Half of the respondents in this survey expect an appreciation and the 12 months price in the NDF market is at 6.63.



68% of managers are expecting interest rates to increase in the coming 6 months. The inflation figure for February came in at 2.7%, up from 1.5% in January. Most economists believe that this in combination with overheating in the property market will lead to several rate hikes by the People's Bank of China during 2010. The one year lending rate today is 5.31%.

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 – 10, 2010.

Subject: Business Climate / Profit Expectations

Northern European subsidiary managers in China have an increasingly positive view of the business climate for the coming six months, compared to six months ago. 48% (46% in September) of companies expect business conditions to be favorable over the coming six months and 20% (7% in March) believe they will be very favorable. Only 8% believe that conditions will be unfavorable. This can be compared to 11% in September and 35% one year ago. No company expects very unfavorable conditions.

When asked about profit expectations, 52% expect profits to increase as compared to 61% six months ago, and no companies believe that profits will improve considerably (compared to 4% in September). 14% expect falling profits (4% in September).

Growth in 2009 ended at 8.7% and most figures point at continued strong growth in China. Chinese exports (of which approximately 60% are produced by foreign invested companies) rose 45.7% in February compared to the same month last year. Although the significant increase is mainly due to base effects, most analysts expect export figures to gradually recover during 2010. Retail sales increased 22.1% in February which is 4% higher than market expectations. Possible reasons behind falling profit expectations are discussed on pages 1 and 2.
(Also see graphs 1 and 3, p. 5)

Subject: Employee Structure

Even in the middle of the financial crisis, there were no major lay-offs among foreign companies in China. As managers in North European companies become increasingly bullish, they are now planning to increase staff further. 55% plan to increase staff numbers and 6% are planning significant increases. This can be compared to 43% and 7% respectively in September last year.
(See graph 4 on page 5)

Subject: Fixed Asset Investment Plans

The number of companies planning investments has finally started to increase. In this survey, 65% are planning modest investments as compared to 50% in September, and the percentage of companies planning significant investments has increased to 18% from 11% in September. This is indicating a shift in China strategies among North European companies that seem to be moving from "carefully expanding" to a more aggressive strategy. Investment decisions are mostly taken on headquarter level and when multinational companies compare market prospects for 2010, emerging markets are expected to show the highest growth in 2010. China is in a class of its own, leading the recovery.
(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 of more than 90 days. The only statistically significant change is that payment terms seem to be shorter than previously. 24% of respondents now have 30 days average payment terms compared to 16% six months ago.
(See graph 5 on page 5)

Subject: Funding Needs

Funding needs are on the rise. Today, 42% of managers are expecting funding needs to increase in the coming six months, as compared to 33% six months ago. 56% of managers expect funding needs to remain unchanged, whereas only one single company expects funding needs to decrease. Considering that investment plans are increasing, this seems logical. At the same time, the improved business situation with increased sales should lead 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 fast can be seen from managers' views of interest rates and the RMB exchange rate. No company believes that interest rates will fall, whereas 68% believe that rates will go up. 32% expect rates to stay at current levels in the coming six months. Both deposit rates and lending rates are regulated in China and the current lending rate for a 12-month bank loan is 5.31%. The 12-month deposit rate is 2.25%. Given that China had a CPI of 2.7% in February, deposit rates are now negative again. Although the government will move cautiously, most economists expect one or more interest rate hikes in the coming six months.

More managers expect the RMB to start appreciating against the US dollar after over a year and a half of stable RMB/USD rates. 50% expect the RMB to appreciate over the coming 6 months compared to 33% in September. However, an equally large percentage– 50% - still believe that the RMB will remain stable against the dollar. A stable RMB/USD exchange rate is one of the main reasons why as many as 74% of Northern European companies use the USD as their main trading currency in China, which is actually up from 70% in our last survey. 24% use the EUR and only 2% answered that they use Scandinavian currencies. Since exactly six months ago, September 11, up until March 11, the RMB has appreciated by 7.04% against the EUR, 1.99% against the SEK, 6.70% against the DKK and depreciated 0.34% against the NOK. 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 46% are hedging some or most of their FX flows on the on-shore forward market, and another 16% are hedging via their head offices through NDF-contracts .
(Please see graphs 7 and 8 on page 5 plus graph 9 and 10 on page 6)

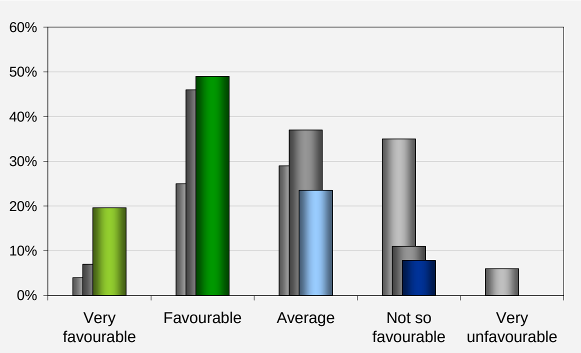
Subject: Main Concerns

The major concern for local management remains "customer demand", which is slightly up from the last survey six months ago. In September, 48% rated it as their main concern compared to 45% in March. The biggest change from our last survey is that as many as 13% now see "labor shortage" as a main concern (up from 5% six months ago). This would be logical considering that so many companies are now investing and recruiting, which was not so clearly the case six months ago. Other issues that were mentioned were "complex rules and regulations", "cost of raw material" and "foreign exchange rates". As discussed above, higher raw material costs and an expected appreciation of the RMB are negative factors for manufacturing companies. (See graph 11 on page 5)

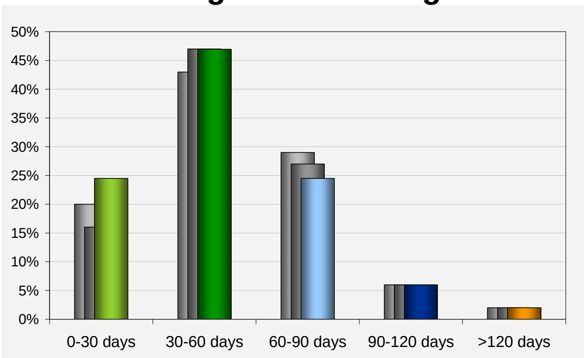
China Financial Index - Composition

The SEB China Financial Index in March had a value of 65, 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 – 66, Profit Expectations – 59, Investment Plans – 70, and Employment Plans – 63. (see the graph on page 1)

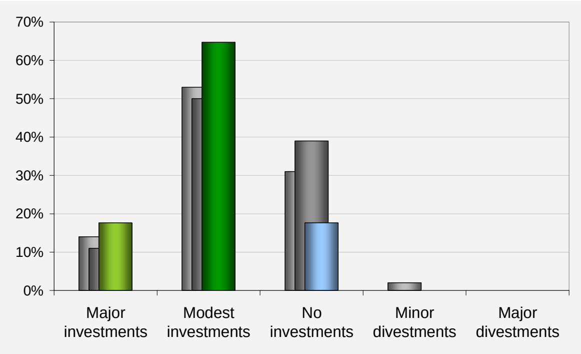
1. Business Conditions



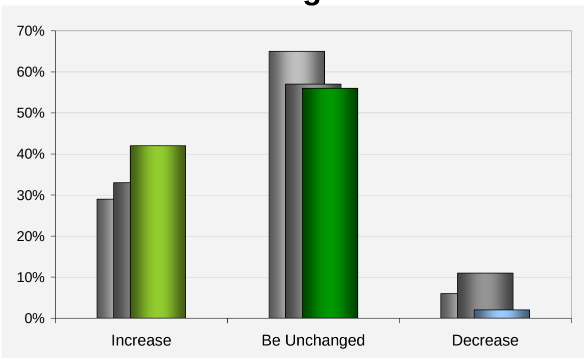
5. Average Outstanding A/R



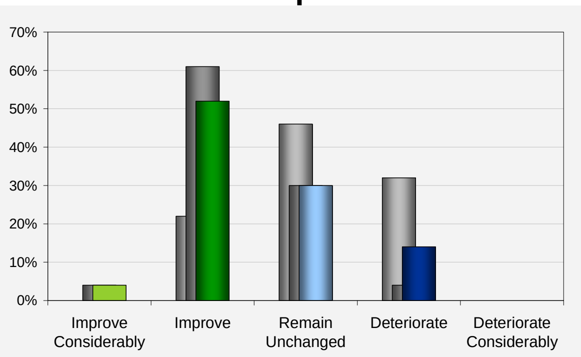
2. Fixed Asset Investment Plans



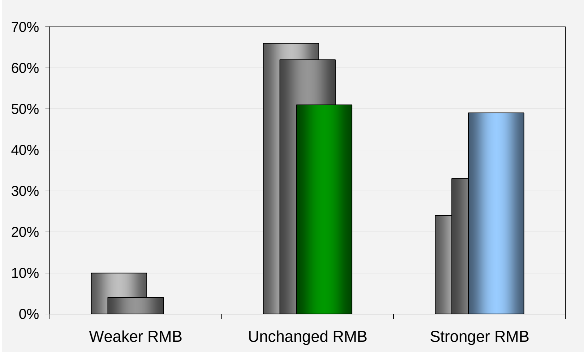
6. Funding Needs



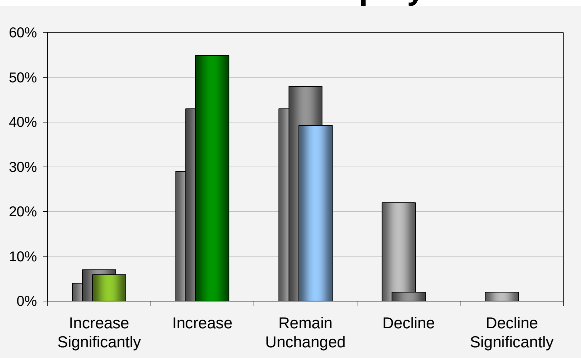
3. Profit Expectations



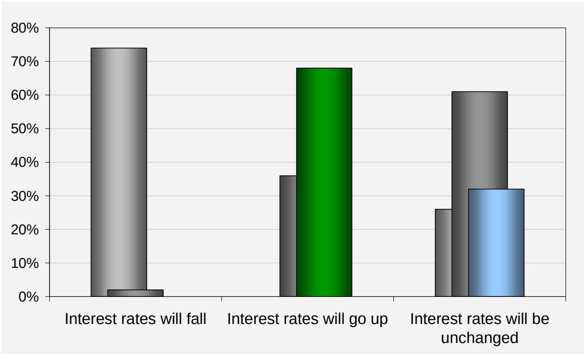
7. RMB against USD



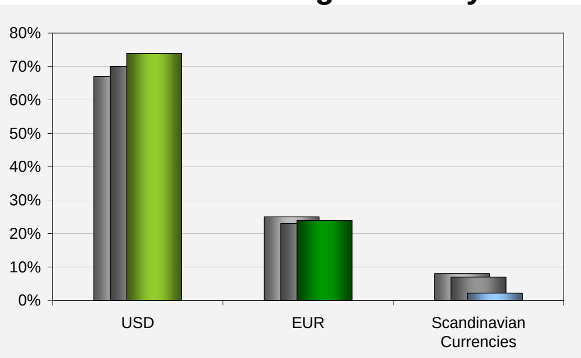
4. Number of Employees



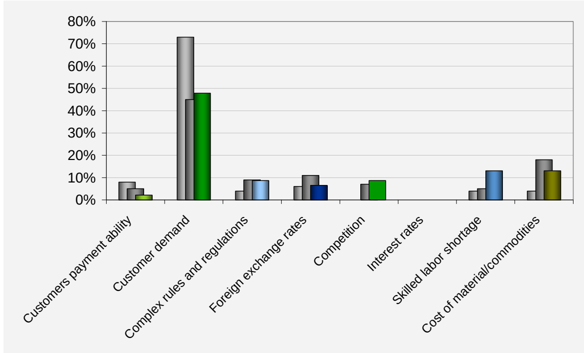
8. RMB Interest Rates



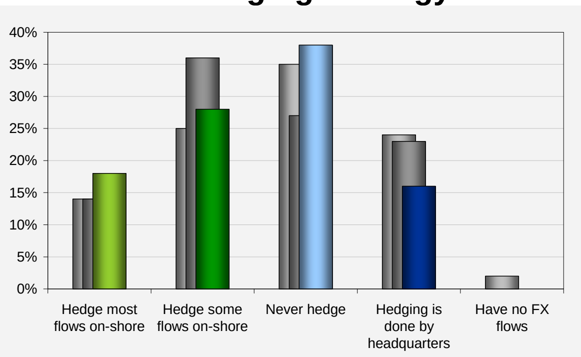
9. Main Trading Currency



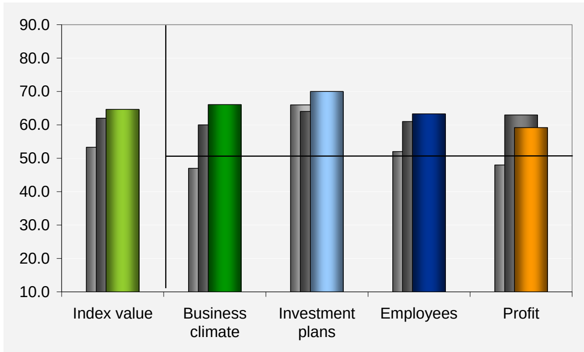
11. Main Concerns



10. Hedging Strategy



12. Main Index



Source: SEB Shanghai. Grey stacks are indicating companies' answers in March 2009, and September 2009

Financial Data

Macro Data (% changes)	2005	2006	2007	2008	2009
GDP	10.4	11.6	13.0	9.6	8.7
CPI	1.8	1.5	4.8	5.9	-0.7
Industry Output	16.4	16.6	18.5	12.9	11.0
Exports	18.2	24.7	21.7	17.3	-16.0
Imports	22.2	13.9	25.7	18.5	-11.2

On-shore deposit rates, major currencies, below 3m USD equivalent

On-shore interest rates (%)	Current	3M	6M	9M	12M
USD	0.0500	0.1600	0.7500	0.8500	1.0000
EUR	0.1000	1.0000	1.1250	1.1875	1.2500
JPY	0.0001	0.0100	0.0100	0.0100	0.0100
HKD	0.0100	0.1500	0.5000	0.6250	0.7500

RMB Interest Rates (PBOC Regulated)

PBOC Rate 100311 (%)	< 6M	6M-1Y	1Y-3Y	3Y-5Y	> 5Y
Lending Rates	4.86	5.31	5.4	5.76	5.94
PBOC Rate 100311 (%)	**Current**	**3M**	**6M**	**1Y**	**2Y**
Deposit Rates	0.36	1.71	1.98	2.25	2.79

FX Indicative Spot and Forward Rates

		11/Jun/10	11/Sep/10	11/Dec/10	11/Mar/11
FX	**11/Mar**	**3M**	**6M**	**9M**	**12M**
USD/CNY	6.826	6.824	6.812	6.792	6.753
EUR/CNY	9.320	9.323	9.315	9.272	9.224
GBP/CNY	10.226	10.221	10.201	10.168	10.105
JPY/CNY	7.551	7.553	7.544	7.526	7.490
HKD/CNY	0.880	0.879	0.878	0.875	0.870
SEK/CNY	0.957	0.957	10.955	0.953	0.947
DKK/CNY	1.253	1.250	1.250	1.246	1.239
NOK/CNY	1.162	1.163	1.161	1.157	1.150

All indicative rates as per 2010-03-11

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