



FOCUS

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Leasing in China

Deutsche Leasing (DL), Germany's biggest leasing group, is constantly pushing for investments abroad. Its latest target: China. This is a clear choice, since DL's main focus is machinery leasing and China is the world's third largest machinery market with only 1% of its fixed assets under lease. DL is the first to set up a Wholly Foreign Owned Entity (WFOE) in the Chinese leasing market. China Focus met with DL Board Member Rüdiger Freiherr von Fölkersamb to learn more about the market potential for leasing in China.

China Focus (CF): In March 2005, the first leasing regulation in China went into action. What did this change for DL?

Rüdiger Freiherr von Fölkersamb (RF):

The new regulation allowed us for the first time to open up a leasing company as a WFOE in China. Before this legislation was passed, a Joint Venture (JV) requirement for leasing companies was in place forcing international companies to cooperate with a local company. Furthermore, the required amount of registered capital for such a company was extremely high. Both these requirements changed, making it possible for Deutsche Leasing to successfully open a subsidiary in China to start offering services to clients in this market.

CF: How do you see the Chinese leasing market today?

RF: Leasing as a way to finance investments has existed in China since the early 80s. At the end of 2004, about 10.000 small Chinese leasing companies and only 40 foreign-Chinese JVs offered leasing services to the Chinese market. Even though this sounds like a lot, the full potential of leasing in China is hardly tapped. Currently, only 1% of all investments in China

in the field of machinery are financed by leasing. In Germany, the share of machinery funded by leasing reached almost 20% in 2005.

CF: So the green light for leasing in China has been given. How did DL become the first international company to set up a leasing WFOE in China?

RF: Well, the new regulations did not come by surprise. Since China's entry into WTO, the country is increasingly trying to open its financial sector to meet all WTO requirements. Opening the market for leasing companies was just another step in this process. We had our China plan ready 3 years ago and were just waiting for the right moment. We also gathered a lot of experience with other foreign expansions. Since 1993, we expanded to other countries in Europe and worldwide by adding at least one country each year to our portfolio list. Basically, we follow our customers.

CF: What are the most important success factors for you in China?

RF: One of the key factors, which proved to be critical in most foreign expansion and again proved very valuable in China is the selection of the right personnel. The investment in human resources is worth it. An international company has to acknowledge the national culture of the targeted country. To do that, we like to fill key management positions either with locals with a strong link to Germany or Germans with a lot of experience in local market. In the case of China, the top management is composed of a Chinese national who studied German languages and literature at a German university and a German national with strong roots and many years of experience in China.

CF: Who are your clients in China and what advantages can you offer them?

RF: Our clients are looking for a reliable and internationally experienced partner when making their investments. By offering leasing services which meet the high German quality standards and, at the same time, the local legislation, we are able to offer exactly that.

As the first step of our China engagement, we are focusing on mid-sized German companies. As an intermediary financier, we profit from their deals with industry partners. Additionally, we give them the chance to present a very appealing financing option to their clients. Often Chinese companies cannot pay for the ordered machines right away. To offer installment payments requires special governmental approval and so it is seldom done. In such a case, the leasing model can provide a valuable option for financing the transac-

tion and can prevent the deal from being cancelled.

CF: What are your future development plans?

RF: Our China office in Shanghai opened in March 2006. This marked the real start of our China business. In the first year, we invested about EUR 20 million for our clients -- this is a small share compared to our worldwide foreign investment of over EUR 800 million. We are optimistic that we can double our china investment annually for the next two years. After this period of adjusting to the unique market conditions, we will be able to fully establish ourselves on the Chinese market. Foreign investors will remain an essential component in the fast growing Chinese economy. We are part of this development by supporting our clients through our contacts and financial services.

CF: Thank you for this interview.

Unified Corporate Income Tax

On March 16, 2007, China National People's Congress fulfilled almost all its commitments to the World Trade Organization (WTO) since joining more than five years ago. It will meet one of these last pledges in 2008.

The law which sets the unified income tax rate for domestic and foreign companies at a level of 25% came after years of criticism that the original dual mechanism was unfair to domestic enterprises: these were charged with 33% while foreign invested companies only had to pay 15% income tax.

In fact, the proposed 25% are low compared to most other countries. Government data show the average corporate income tax rate in 159 countries and regions was 28.6% in 2005/2006, with the average rate in the Chinese mainland's 18 neighbouring countries and regions being 26.7%.

"The current tax regimes are too complicated", Finance Minister Mr. Jin Renqing recently told Xinhua. "A unified tax code will create a taxation environment that favours competition among all ventures registered in China."

Old preferences cut

Certain tax preferences for foreign invested companies will be eliminated as follows:

1. *Tax holidays and preferential income tax rate for certain types of foreign invested enterprises (such as manufacturing enterprises, technologically advanced enterprises, export-oriented enterprises, service-oriented enterprises in Special Economics Zones)*
2. *Reinvestment tax refund of 40% to 100% for dividend reinvested*
3. *Special Economics Zones, Economic and Technological Development Zones, Pudong New Area, Suzhou Industrial Park, Open Coastal Areas.*



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New preferences added

The new law will be based more on sectors than regions. Tax preferences, which may be a combination of tax holidays, lower rates, super deductions, investment tax credits, accelerated deductions or depreciation, will be granted to firms in the following sectors:

- *High-new-technology*
- *Environmental protection*
- *Agriculture, forestry, animal husbandry and fishery*
- *Comprehensive utilisation of resources*
- *Infrastructure*
- *Energy saving, water conservancy*
- *Safety production*
- *Venture capital enterprises*
- *Projects in autonomous regions*

Mr. Jin Renqing also told NPC deputies that, "overseas firms, however, will enjoy a 5-year grace period, during which the new tax rate will be phased in". This will lower the impact on foreign companies.

Steve Bertamini, Chairman and CEO of General Electric (GE) North East Asia, packed the new series of products into the idea of "eco-imagination", saying the "green" business will become China's most booming industry in the future. In fact, some multinational companies have adapted their business plans to the policy change. GE China has announced that it will invest USD 50 million in its Shanghai-based technology centre for products serving environmental protection.

Liang Hong, Chief China Economist for Goldman Sachs Asia, said the massive influx of foreign investment in China will not stumble over an increased enterprise income tax rate.

Many experts call the tax change a commitment to the WTO by giving equal treatment to all enterprises. It is generally agreed upon that this will strengthen China's worldwide acceptance. A research report from the World Bank analysed that the stable political situation, sound economic development, broad market, rich labour sources as well as increasingly upgraded business infrastructure and government services in China are the major factors attracting foreign investment.

The new law is expected to help improve China's investment structure. It will provide incentives to encourage environmentally friendly businesses, increase research and promote high-tech enterprises. It will also help domestic companies invest overseas by easing their tax burden in the local market.

Branding Strategies

China's large consumer market with its often-quoted 1.3 billion potential buyers is per se a prime attraction for brands from all over the world. But in a country in which successful sales depend largely on how well a brand is known and trusted by consumers, imagina-

tive ideas are needed to build brand recognition within one's target groups before the sales start rolling in.

Creative and sporty

Creativity has been the key factor in many companies' branding campaigns – especially when targeting the highly attractive consumer group of the young and rich. Johnny Walker flies big name DJs into Beijing and Shanghai clubs to attract the cities' "young and hip". Major jewellers have developed partnerships with wedding planners and offer weekend honeymoon trips to Hong Kong to help drive their sales.

Sport sponsoring is also popular: According to Samsung research, 70 percent of Chinese pay attention to major sporting events. Firms such as UPS, a delivery service, are getting into China by linking with these major events, mainly the Olympic Games in Beijing 2008. And as China uses the Games to build its "brand" in the rest of the world, UPS is targeting Chinese businesses and consumers on the same track. The company opened its first retail outlet in Shanghai in 2005 and is now expanding its services across the country. Having your brand name and logo at the billboard of an Olympic stadium will help strongly in terms of recognition amongst local firms. An additional bonus comes from the image transfer delivered by healthy and successful athletes – an image many companies strive to be associated with.

Fighting brand pirates

For companies with an already established brand image, China offers a special obstacle: its infamous counterfeit industry. The old cliché, whereby "imitation is the most sincere form of flattery", was invented here - unlike Rolex and Louis Vuitton bags. Even though it is true to a certain extent that copies can help increase product exposure, counterfeits ultimately hurt sales by diluting a brand's image. Thus, many companies put at least as much effort into protecting their branded products as they do in promoting them.

Moët-Hennessey heavily markets its liquor at many nightclubs in Shanghai, Beijing and other parts of China. But bartenders don't throw away empty bottles. Instead, they are handed to Hennessey bottle smashers, who break the bottles into pieces in order to prevent the copying of labels and shapes.

Movie studios have taken a more traditional route: they have sued some of the larger DVD shops that sell counterfeit copies of their studio hits. One shop in Shanghai, KaDe Club, was sued by seven companies including Warner Bros, 20th Century Fox and Disney. But since the store representatives simply ignored the lawsuit and didn't show up in court, there is little chance the studios will see any of the RMB 25,000 they were awarded.

Companies such as Louis Vuitton have tried to make fighting piracy a more collaborative effort. They reward market vendors who don't sell counterfeit copies of their signature woman's handbags.

But sometimes even collaborating with a Chinese partner can backfire. Eastman Kodak had to make this experience with China based firm Lucky Film. Kodak has a 20 percent stake in Lucky, but the com-

panies are independent and the original technology is not used in the Chinese company's manufacturing process. However, photographic paper from Lucky began to appear in Kodak's China photo studios in 2004 with logos that looked very close to Kodak's.

All-in-all, branding in China can be a tricky business. But aren't 1.3 million potential buyers worth the risk?

Consulting Co-operation

Adrian Loyd of global strategy consulting firm Marakon Associates, writes about a successful collaboration project with Fiducia Management Consultants.

Earlier this year, Fiducia partnered with Marakon to advise the Association of International Chemicals Manufacturers (AICM), an organisation which represents the world's largest MNC chemical manufacturers to the Chinese government and consumers. Together we helped AICM's board to develop and adopt a new vision, set of priorities and organisational model. This new form of collaboration between our two firms leveraged the China expertise of Fiducia and the global advisory expertise of Marakon.

Our work included benchmarking against other associations, in-depth analysis, and around 30 interviews with the leaders of member companies. We also conducted a conjoint survey of 270 individual members to understand their needs and willingness to pay for different AICM offers.

The outcome of the work was the board's approval of a new vision and an enhanced set of offer components, coupled with a new pricing structure. These changes were underpinned by a new simplified and streamlined management model, where key changes included: introduction of executive accountability; creation of a smaller, more accountable ExCo; unification of AICM to enable communication with 'one voice'; and simplification of the complex committee structure into three core 'policy groups'.

AICM's Chairman presented the new strategy to the AGM in January and secured agreement in principle to an increase in membership fees to fund the improvements to the association's offer and operations. The restructuring is currently taking place.

China Province Reports

Every month, Fiducia features one of China's Provinces in a comprehensive overview including major industries, investment environment and development potential of the region. This month's issue covers the **Guangxi Zhang Autonomous Region**.

You can download the report from our website at <http://www.fiducia-china.com/CPR>.

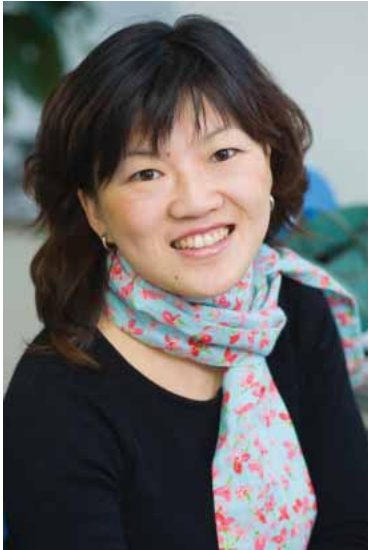
Fiducia Staff Profile



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This month we profile **Helen Gui**, Consultant in Fiducia's Beijing Office.



CF: What is your position and how long have you been with Fiducia?

HG: I work as a consultant in the China Consultant Department in Beijing and I've been with Fiducia for four years.

CF: What is your particular focus or area of expertise?

HG: Our department provides China market entry or market expansion strategy consulting service to European and U.S. clients. My other working fields include market research, competitor benchmark analysis, M&A target search & negotiation support and commercial and financial due diligence services.

CF: What is your educational background?

HG: I graduated from the University of Melbourne with a Master degree in Applied Finance and a BA degree in English from the People's University, Beijing.

CF: What previous work experience have you had?

HG: Prior to working at Fiducia, I worked for Toshiba Electronics Asia as an in-house business analyst for three years. I was also employed at Howard Consul-

tants in Melbourne, where I did similar professional consulting. Both jobs prepared me well for Fiducia in terms of manufacturing practices in China as well as the necessary methodology and experience professional consultants needed to serve their clients.

CF: What do you regard as the greatest challenge in your job?

HG: The most challenging part to me is "putting the puzzle together" and work out a practical solution for our clients. We need to help our clients, who compete in fragmented and price-sensitive markets, to find way to leverage their international capability and use their own core competencies to achieve their strategic goals in a given time frame.

CF: What do you find exciting about your job?

HG: We have a wide industry coverage for our projects, which allows me to learn more about how various types of industries function. The chance to "explore" each different industry also makes my work feel fresh and exciting.

CF: What is particularly interesting and challenging about working in the China market?

HG: One of my colleagues once said "China is a continent rather than a country". The vast geographic territory and complicated cultural background makes China very diversified per se. At times, both myself and my clients feel challenged but at the same time excited to find the different "gold mines" in the different regions.

CF: What projects are you working on now?

HG: Currently I'm working on the China entry strategy of protective packaging products for a top-tier U.S. packaging company.

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