Strategy H2 2014

European Equities, when China stalls

June 2014

ALPHAVALUE

Paris London Frankfurt München New-York Brussels Milan Madrid Warsaw

European equities
Mid Year update
2014 eps growth: 13%
2014 PE: 16x

- **Slow macro & declining risks**
  - ✓ European pick up mostly slowed down by France
  - ✓ Safer financial system but over regulated banks remain a brake
  - ✓ Deflation / QE as current key worries
  - ✓ Oil shocks (Russia, Iraq) or non shocks (US shale oil surge)?

- **Markets**
  - ✓ Lasting low rates / cost of capital
  - ✓ Asset inflation, banks replaced by shadow banks
  - ✓ New systemic risks building up through dash for bonds, dash for yield, dis-intermediation, shadow funding

- **Equity markets**
  - ✓ Continental equity investors still reluctant to equity risks
  - ✓ Rather resilient and astonishing low volatility

European Equities Essentials

- **Earnings**
  - ✓ Earnings seen up 14% in 2014, 11% in 2015 (BNP is costing 1% to 2014 eps growth…)
  - ✓ Sadly, post Q1 releases led to slight downgrades
  - ✓ Across the board erosion + big one offs (BNP, Vod)
  - ✓ Underlying earnings: rather resilient, but …
  - ✓ … stream of unconnected profit warnings (Lufthansa, Vallourec, Tesco, Prada)
- **Valuation**
  - ✓ 2014 PE: 16x and rising on fund flows/cheap money/yearning for yield
  - ✓ 2014 yield at 3.2% vs. 10Y Bund: 1.5%
  - ✓ 2014 P/Book: 1.75x . Banks: 1x
- **Sectors**
  - ✓ Telecoms, Aerospace, Building & construction
  - ✓ Caution: Pharmas, Retail (Food & Non Food). Oils dominated by supply

2013 earnings growth erodes further, not 2014

EPS growth trend for AlphaValue Universe

As of 16-06-2014

2014 earnings growth hinges less on Banks

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Adjusted attributable net profit (€m)

In €m	2013	2014	2015	Chg. 14/13	Chg. 15/14
Total	**466 121**	**532 145**	**585 994**	**66 024**	**53 849**
Banks	60 030	80 335*	106 199	**20 305**	25 864
Metals & Mining	18 565	30 315**	33 115	**11 751**	2 800
Autos	25 392	33 937	39 004	**8 545**	5 067
IT Hardware	2 448	7 014	4 472	**4 565**	-2 542
Capital Goods	16 410	19 716	22 729	**3 306**	3 012
Insurance	40 188	42 601	46 760	**2 413**	4 160
Food & Beverages	39 882	42 192	44 820	**2 310**	2 628
Building & Construction	2 398	4 501	4 809	**2 103**	308
Transport	6 303	8 087	9 522	**1 784**	1 435
Food Retail	6 220	7 967	8 731	**1 747**	764
Consumer Durables	11 260	12 970	14 863	**1 709**	1 893
Chemicals	13 606	14 834	16 058	**1 227**	1 224
Pharma	41 765	42 793	44 396	**1 028**	1 602
Semi conductors	1 408	2 436	3 178	**1 028**	742
Others				**---**	
Oils	52 007	51 191	46 080	**-816**	-5 111
Utilities	23 163	21 648	23 017	**-1 516**	1 369
Telecoms	32 974***	30 252	29 884	**-2 722**	-368

As of 16-06-2014 – AlphaValue universe

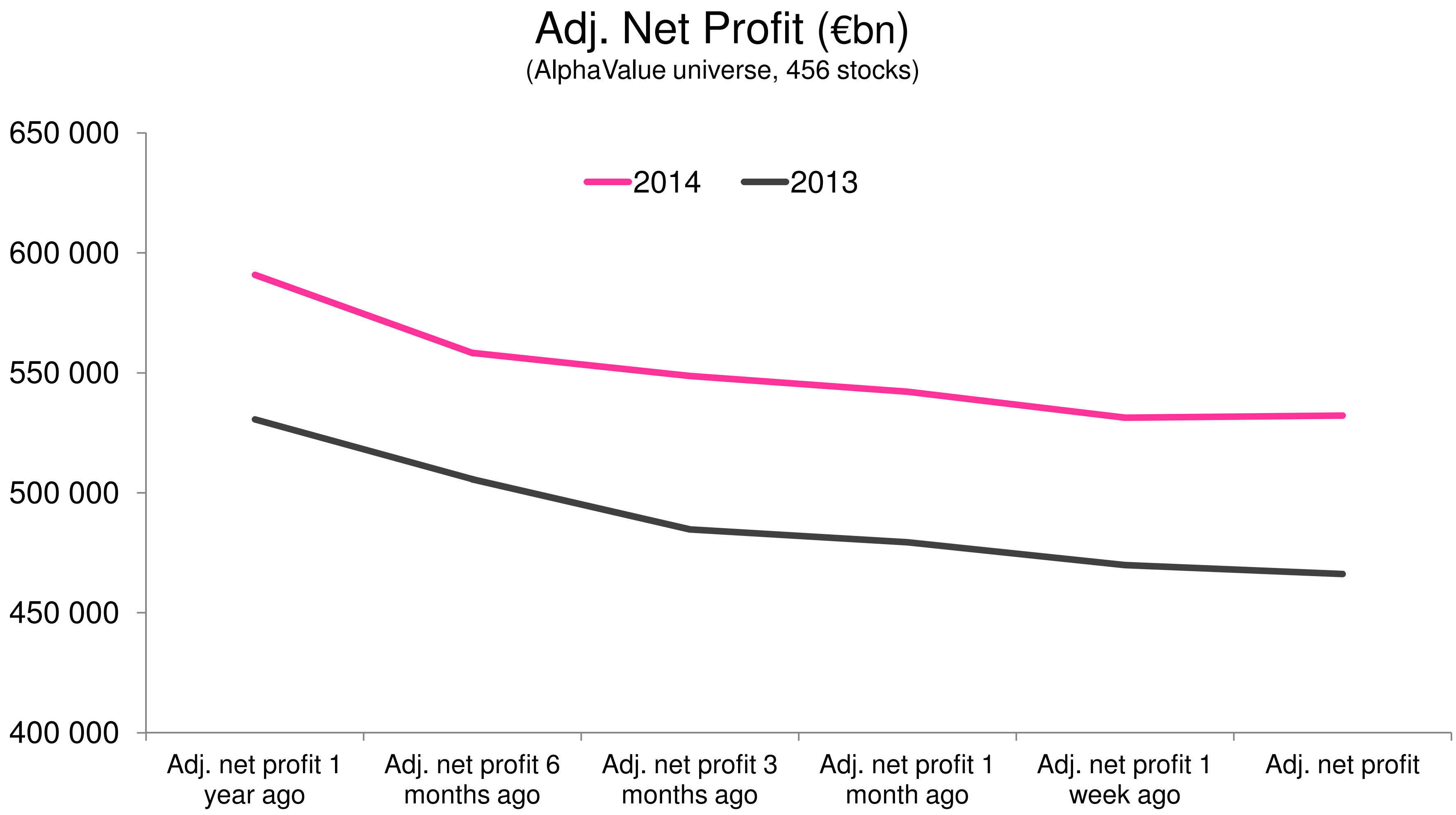
* BNP2014 earnings include $10bn fine
**Recovery of Steel + Xstrata merged in Glencore and excl. in 2013
*** Vodafone £47bn profit on Verizon Wireless regarded as exceptionals

2014 downgrades driven by Banks (BNP) and Pharmas
Autos and Transport pull earnings up

Earnings in €m	2014 3 months ago	2014	Delta	in % vs. 3 months ago
Autos	32 665	33 937	1 272	4%
Transport	6 909	8 087	1 178	17%
Metals & Mining	29 676	30 315	640	2%
Software	4 343	4 402	60	1%
Households	8 054	8 067	13	0%
other				
Building Prod. & Materials	6 017	5 494	-522	-9%
Food & Beverages	42 864	42 192	-672	-2%
Food Retail	8 816	7 967	-849	-10%
Chemicals	15 767	14 834	-934	-6%
Capital Goods	20 944	19 716	-1 228	-6%
Insurance	43 945	42 601	-1 344	-3%
Utilities	23 362	21 648	-1 714	-7%
Telecoms	32 170	30 252	-1 918	-6%
Pharma	44 868	42 793	-2 075	-5%
Banks	86 543	80 335	-6 208	-7%

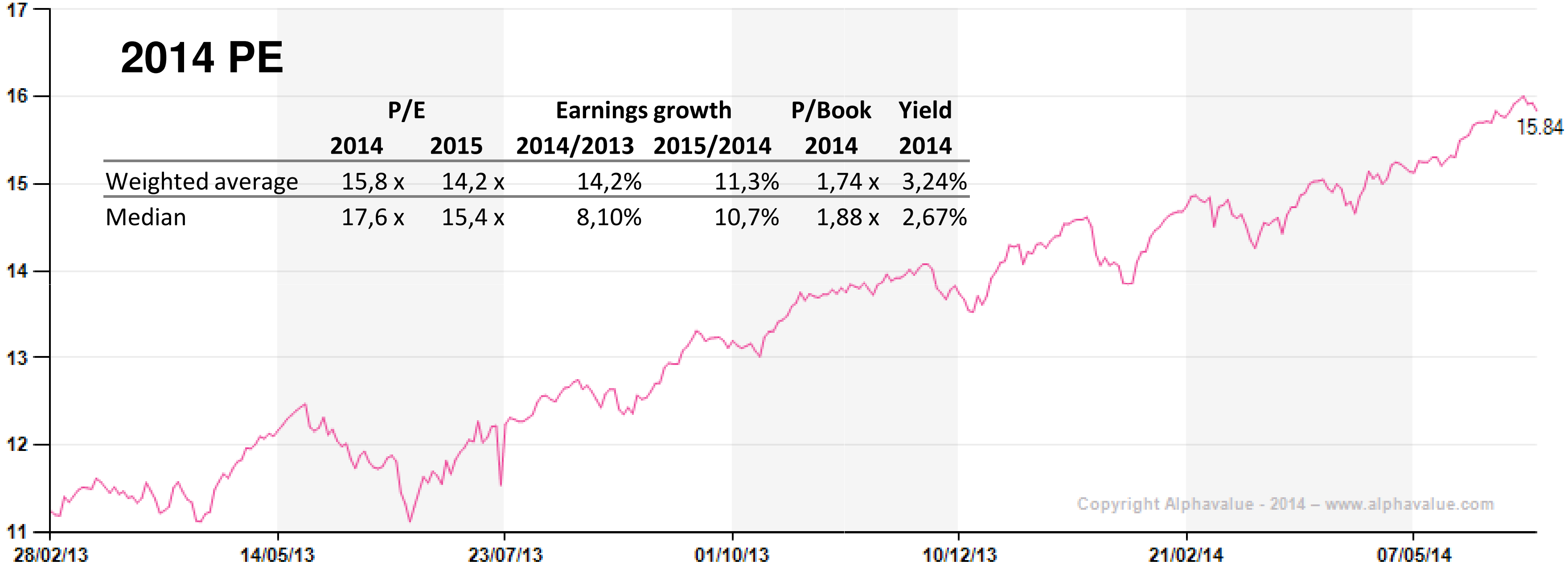
As of 16-06-2014

2014 still suffers from painful adjustments

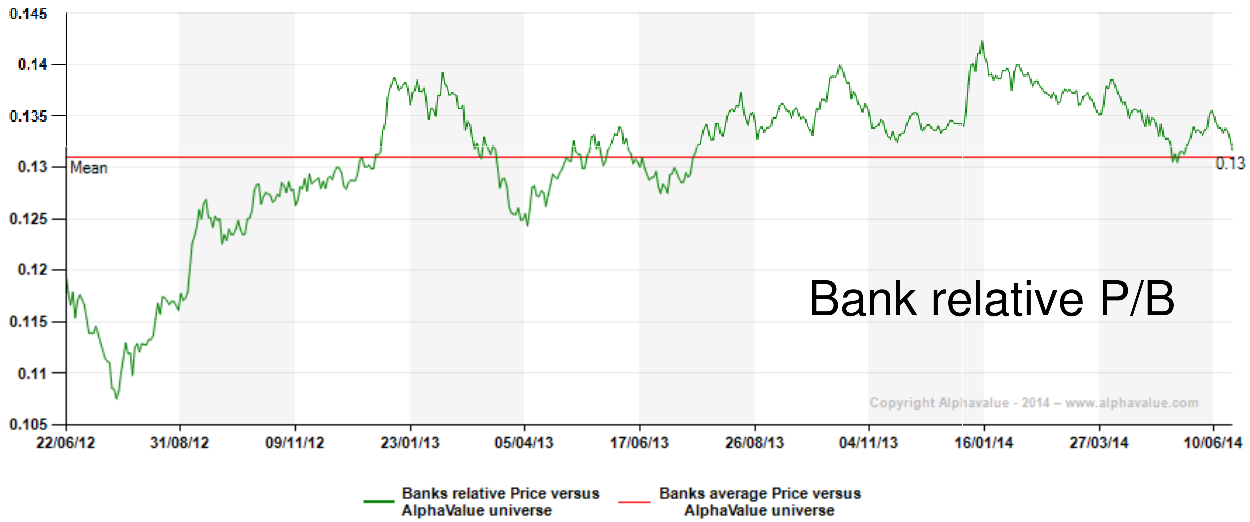


As of 16-06-2014

2014 PE extends to 16x. Banks revaluation completed



	P/E		Earnings growth		P/Book	Yield
	2014	2015	2014/2013	2015/2014	2014	2014
Weighted average	15,8 x	14,2 x	14,2%	11,3%	1,74 x	3,24%
Median	17,6 x	15,4 x	8,10%	10,7%	1,88 x	2,67%



As of 16-06-2014

Sector hierarchy, as of 16-06-2014. Current position

Sensible Sector selection

Caution required

Sector	Upside	Mom.	P/E 2014	P/E 2015	Earnings growth 2014/2013	Earnings growth 2015/2014	P/Book 2014	Yield 2014
Paper & Packaging	17,6%	++	15,4 x	12,9 x	6,6%	19,9%	1,31 x	3,5%
IT Hardware	16,8%	+	19,2 x	14,8 x	6,6%	28,9%	1,93 x	2,4%
Software	13,9%	+	20,0 x	18,1 x	8,6%	10,4%	3,59 x	1,8%
Telecoms	13,4%	+	16,0 x	14,6 x	9,1%	9,73%	1,87 x	4,3%
Aerospace-Defence	13,4%	++	14,4 x	12,7 x	21,2%	13,2%	2,88 x	2,7%
Insurance	10,3%	+	9,85 x	8,95 x	12,5%	10,1%	1,09 x	4,0%
Computer Services	9,57%	+	18,8 x	16,5 x	18,8%	13,5%	2,70 x	2,0%
Hotel, Catering & Leisure	7,78%	+	19,9 x	17,6 x	14,1%	12,3%	3,53 x	2,3%
Other financials	6,92%	+	15,9 x	14,2 x	11,8%	12,0%	1,16 x	2,8%
Media	6,76%	+	16,2 x	14,6 x	13,8%	10,4%	3,13 x	3,0%
Utilities	6,60%	+	15,4 x	14,5 x	-8,4%	6,10%	1,43 x	4,4%
Metals & Mining	6,24%	+	13,0 x	11,7 x	42,9%	11,5%	1,40 x	3,2%
Building Prod. & Materials	5,73%	+	18,9 x	15,2 x	24,5%	24,4%	1,30 x	2,2%
Health	5,32%	+	21,7 x	19,7 x	7,3%	10,4%	2,87 x	1,5%
Building & Construction	4,52%	++	15,2 x	14,2 x	28,6%	6,72%	2,07 x	3,3%
Banks	4,40%	+	14,1 x	10,8 x	33,1%	30,9%	0,96 x	3,4%
Consumer Durables	4,20%	+	20,4 x	17,9 x	6,9%	14,0%	2,94 x	2,0%
Chemicals	4,08%	+	17,7 x	16,5 x	7,7%	7,60%	2,52 x	2,7%
Food Retail	2,06%	-	15,0 x	13,4 x	12,0%	11,7%	1,66 x	3,6%
Capital Goods	2,00%	+	18,0 x	15,6 x	20,5%	15,3%	2,83 x	2,9%
Support Services	1,99%	+	21,3 x	19,0 x	15,3%	12,2%	4,17 x	2,9%
Concessions	1,96%	+	20,9 x	18,8 x	4,5%	10,9%	2,91 x	3,7%
Semi conductors	1,12%	+	26,2 x	21,1 x	67,0%	24,2%	3,16 x	1,3%
Transport	-0,22%	+	16,1 x	13,7 x	33,8%	17,7%	1,82 x	2,3%
Autos	-0,76%	++	10,9 x	9,65 x	33,2%	12,8%	1,32 x	2,6%
Property	-2,47%	+	19,2 x	17,9 x	5,7%	7,6%	1,14 x	4,4%
Food & Beverages	-3,12%	+	19,2 x	18,0 x	6,0%	6,4%	3,57 x	3,1%
Pharma	-3,47%	++	21,7 x	20,9 x	1,5%	3,8%	4,19 x	2,9%
Households	-5,47%	++	22,6 x	21,7 x	0,0%	4,1%	3,54 x	2,0%
Oils	-8,91%	+	13,6 x	15,3 x	4,0%	-10,7%	1,34 x	4,1%
Non Food Retail	-11,5%	-	22,3 x	20,3 x	9,70%	9,8%	4,70 x	2,7%

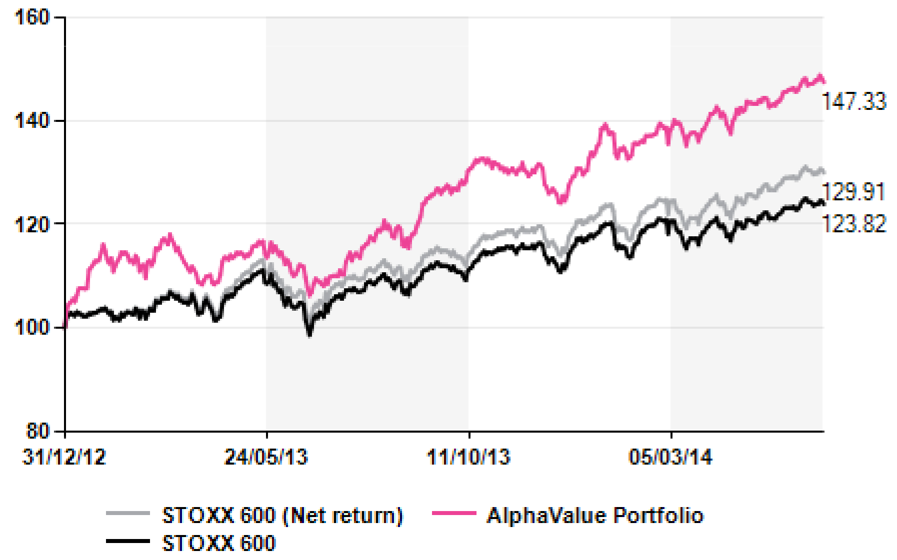
de-risking continues

AlphaValue Central Portfolio

LONG		Performance from entry	2 weeks	Since	Upside
Orange		32.7%	-8.31%	17/02/2014	29.8%
GBL		23.2%	-1.03%	12/11/2013	32.4%
Enel		20.0%	-1.11%	10/02/2014	11.4%
Saipem		14.3%	2.04%	20/01/2014	18.9%
E.on		11.9%	3.85%	07/04/2014	23.4%
Securitas		9.80%	-0.13%	31/03/2014	13.2%
Zurich Insurance Group		8.00%	-1.42%	18/11/2013	24.2%
Veolia Environnement		7.81%	2.94%	24/03/2014	13.7%
Telefonica		7.50%	2.20%	12/05/2014	24.1%
ENI		7.36%	4.39%	05/05/2014	17.0%
Heineken		6.13%	2.54%	05/05/2014	19.0%
DSM		5.46%	-2.21%	07/04/2014	20.2%
CNP		3.21%	-5.68%	10/03/2014	24.7%
LVMH		2.36%	1.43%	14/04/2014	15.8%
STMicroelectronics		1.94%	-3.90%	17/03/2014	29.2%
Finmeccanica	IN	0.00%	4.15%	23/06/2014	21.2%
Rexam		-0.75%	-0.75%	09/06/2014	21.6%
Syngenta Internation...		-1.73%	-5.92%	28/04/2014	32.9%
Nutreco		-1.85%	0.59%	19/05/2014	19.2%
Stora Enso		-3.75%	-4.62%	26/05/2014	27.0%
Airbus Group		-7.26%	-7.26%	09/06/2014	45.7%
Crédit Agricole		-7.74%	-7.74%	09/06/2014	26.5%
SHORT					
Carrefour	IN	0.00%	-2.07%	23/06/2014	-10.9%

Portfolio performance

Year	AlphaValue Portfolio	STOXX 600	STOXX 600 (Net return)
2014 YTD	12.8%	5.50%	7.55%
2013 A	30.7%	17.4%	20.8%



As of 24-06-2014

Europe is no longer the issue

Two nagging worries:

- Deflation
- China

When deflation looms

A bottom up view of deflation

- **Facts**
  - ✓ Falling cost of labour in Europe (unemployment, EM competition, IT led productivity gains)
  - ✓ Falling nominal cost of capital (QEs, China exports its wrong cost of capital)
  - ✓ « Hedonist » gains (IT in most consumer goods for instance)
  - ✓ Retail prices transparency
  - ✓ Drop in purchasing power

- **Can deflation set in: YES**
  - ✓ Happy few consumption/property bubble not enough to pull up prices
  - ✓ Above mechanisms here to stay

Deflation and markets

- **Bond bubble**
  - ✓ Dash for bonds means systemic risks building up- Crowded trade
  - ✓ "*Bond funds like shadow banking are giving people a liquid claim on illiquid assets*"
  - ✓ Banks will no longer lend their balance sheet due to regulation
  - ✓ Warning shot of IMF to ECB : go for QE

- **Risk**
  - ✓ Expansion of shadow banking where « any return is a good return »
  - ✓ Additional systemic risks

- **Sectors**
  - ✓ Best avoided: Consumers retail and manufactured goods, Banks,
  - ✓ Protection: Concessions, Utilities, Oils, Pharmas

If deflation sticks

Sector hierarchy, as of 16-06-2014.

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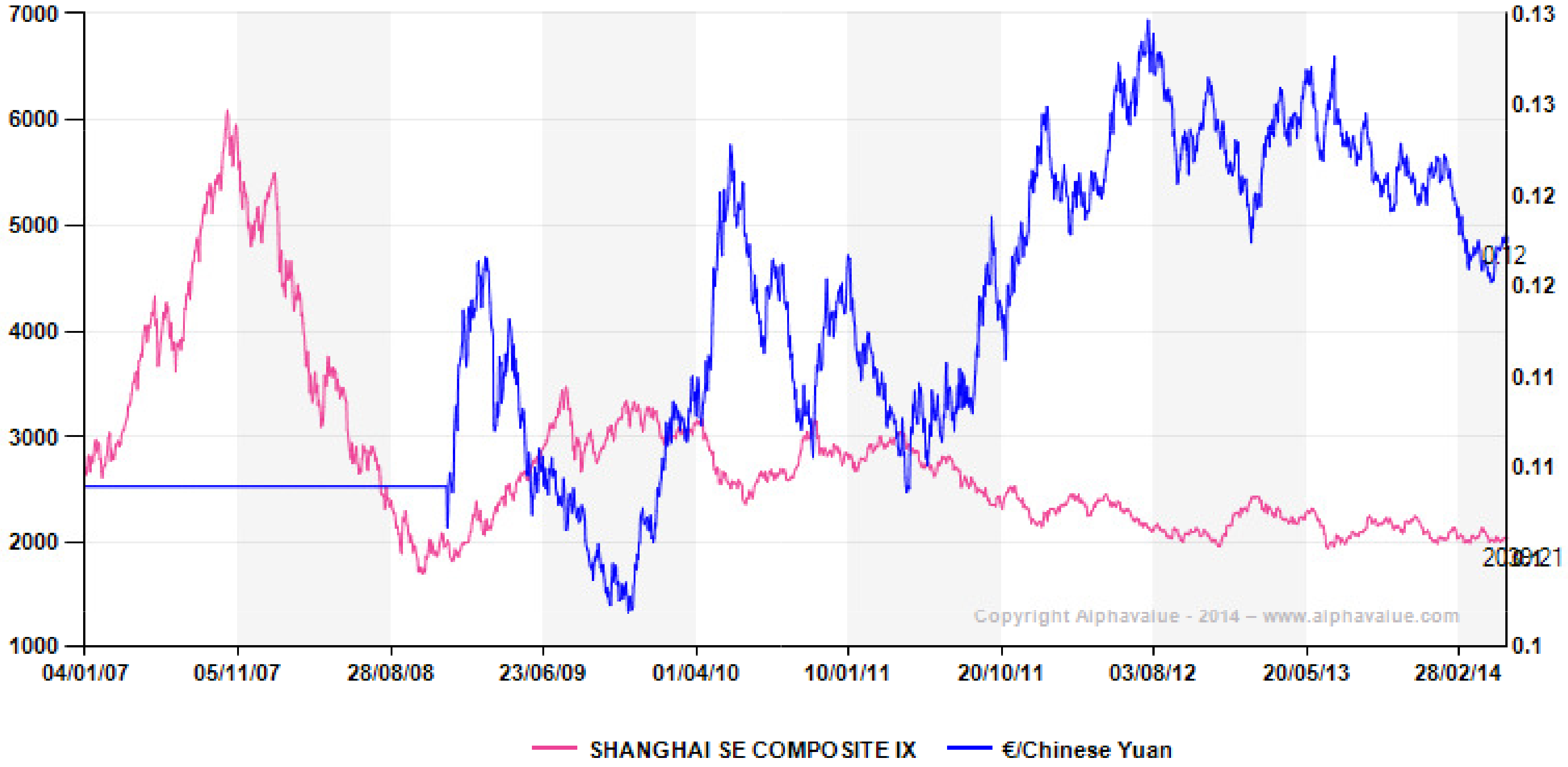
风险

When* China stalls

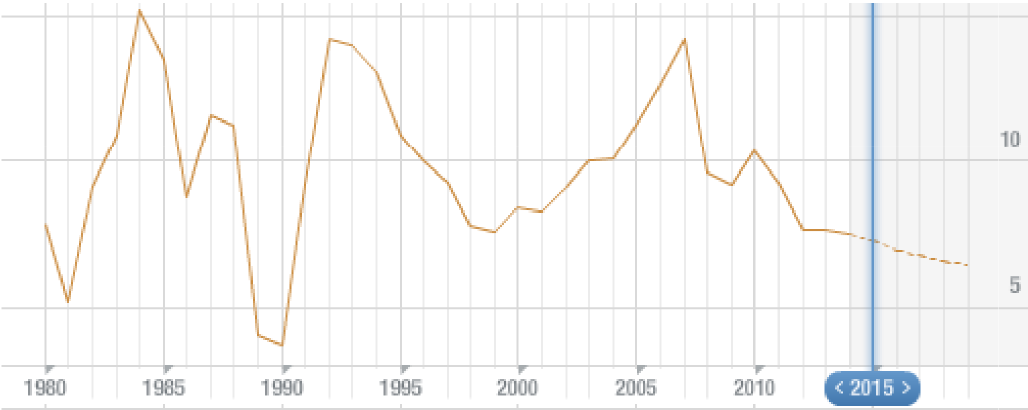
* Not if

"China grows at 7.5% and can manage at least 7%". Actually markets disagree since 2008. Even the Yuan is no longer a one way bet.

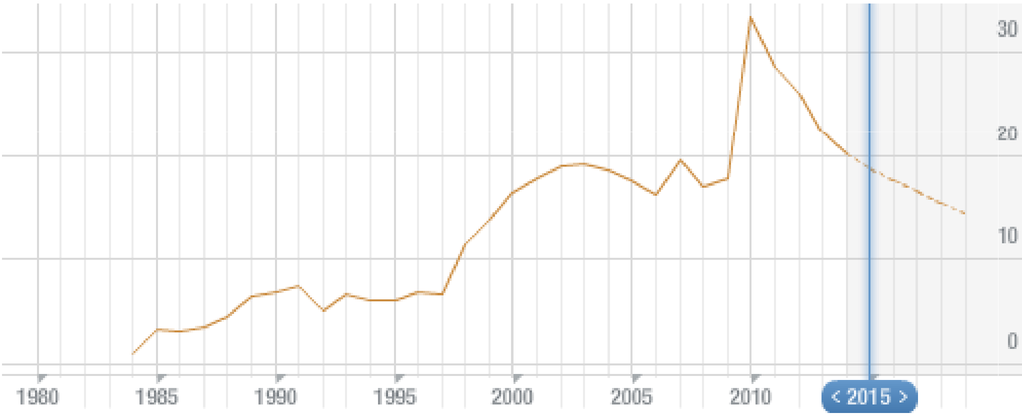


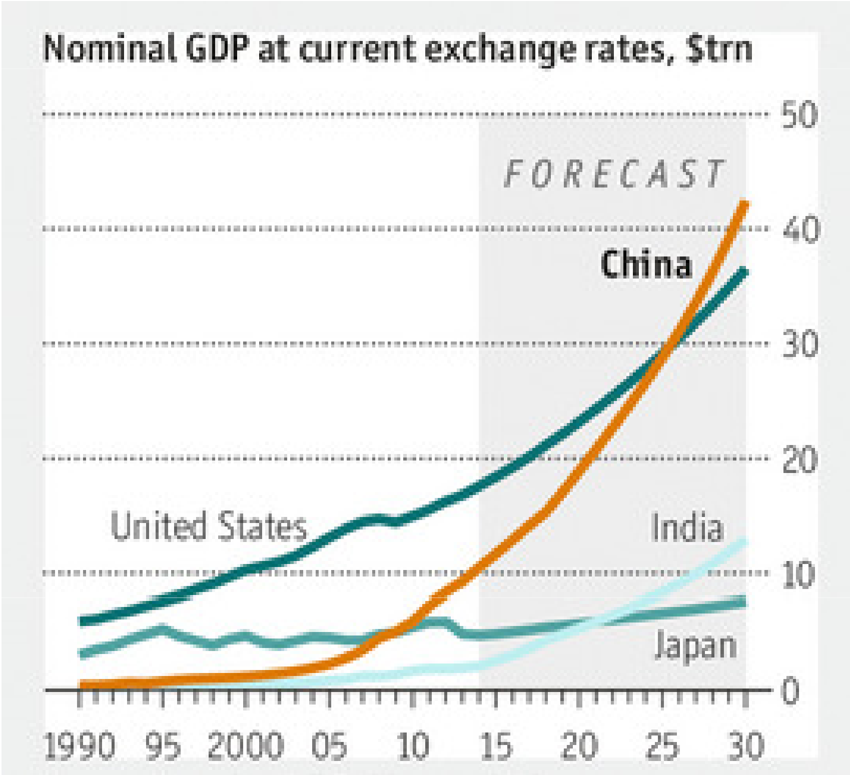
China growth data (IMF 2014)
China is sustaining growth with limited debt. Rosy picture?

Real China GDP growth in %

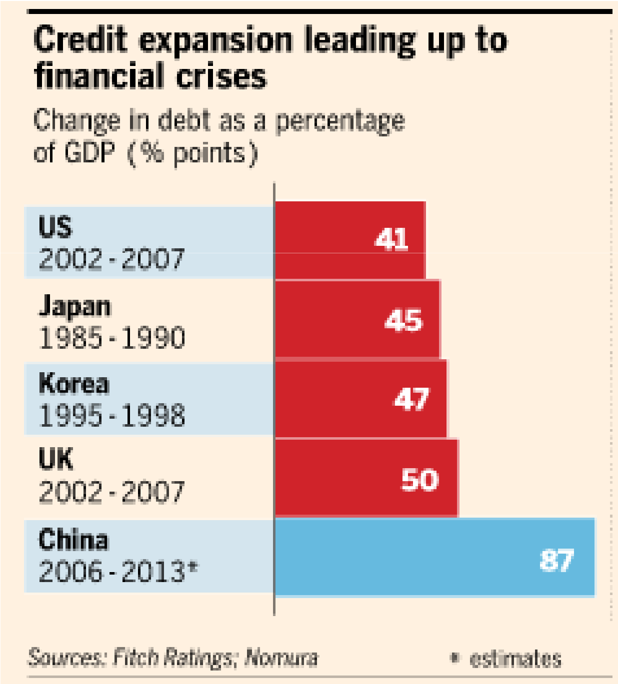


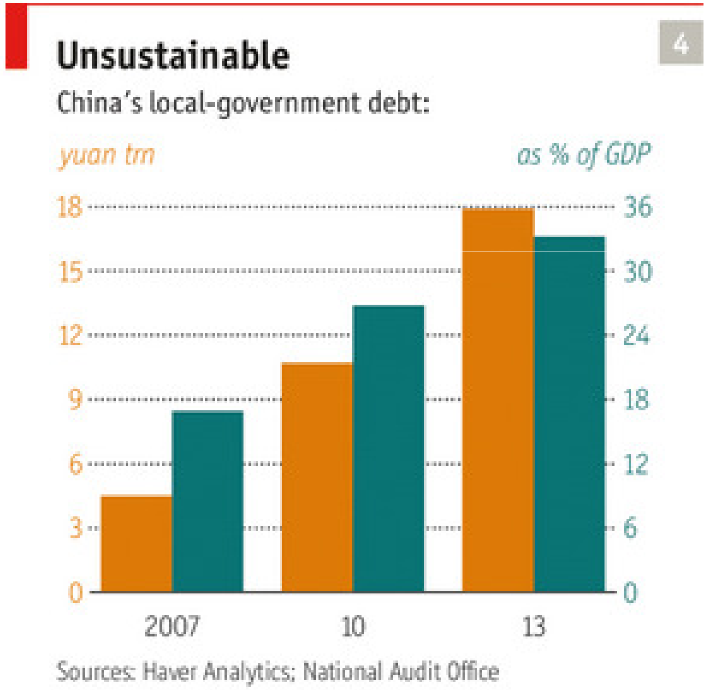
Gvt gross debt (% of GDP)

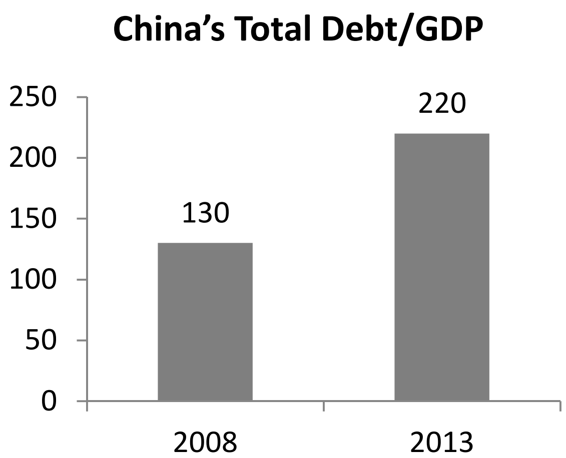




China is throwing more debt at its unsustainable growth. Not so rosy!

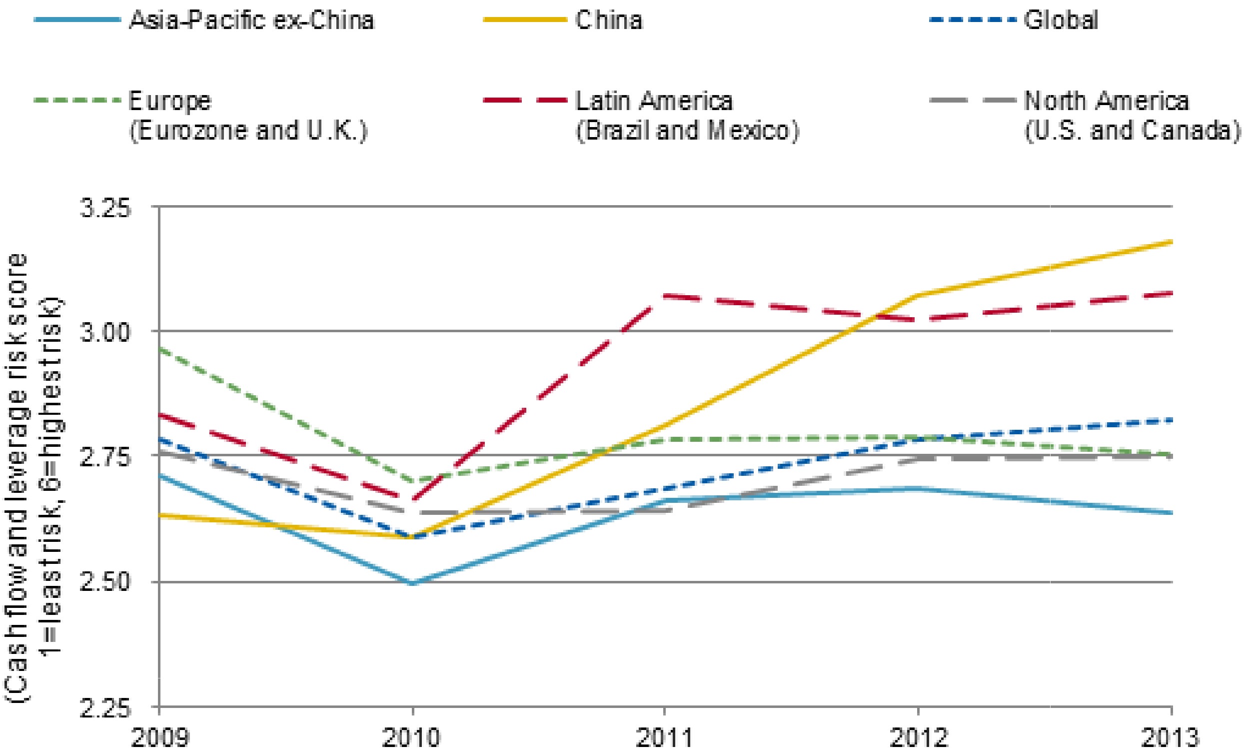






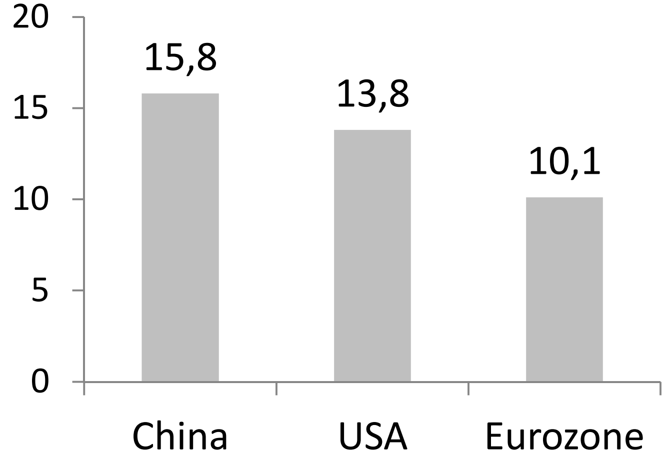
More debt than meets the eye

S&P risk score



Source: S&P Capital IQ.

2014 Non Financial corporate debt ($Tn) (S&P)



<u>LGFVs </u>(local gvt financing vehicle)

- c. 10,0000 LGFVs run total debt at RMB19Tn ($3Tn) or 31% of GDP
- Chinese shadow banking supplied $4.8tn worth of financing since 2007

From Communist Party to Communist Kleptocracy

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Communist Party to keep power

Engineer growth at all costs

~~Democracy & consumption = too complex, long, risky~~

Manage fast forward growth: fixed asset formation

State-owned enterprises + State-owned banks = cheap capital

Cheap labor

Internal migrants

"Pour concrete"

Policy boosted by cheap capital + cheap workforce + No pricing of externalities: environment, land, migrants without rights

WRONG COST OF CAPITAL

Growth through increasingly useless assets / fast declining returns

Misappropriation of profits through grossly inefficient financial system / wrong wealth distribution

Oligopoly / speculation / corruption type profits for happy few

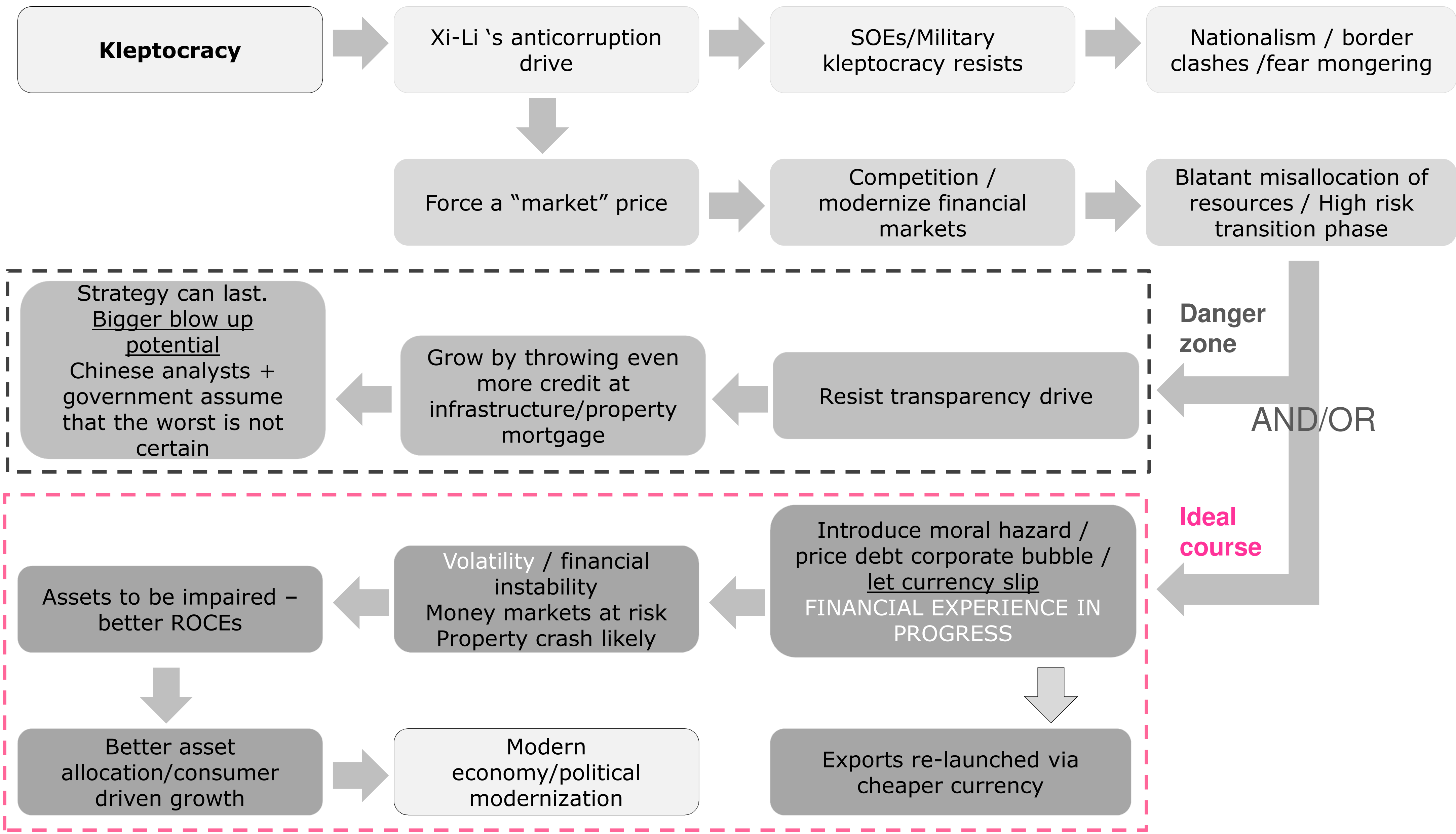
Many "unlucky" Lack of confidence / "save for rainy day"

Priority to hard asset/roof: Property demand

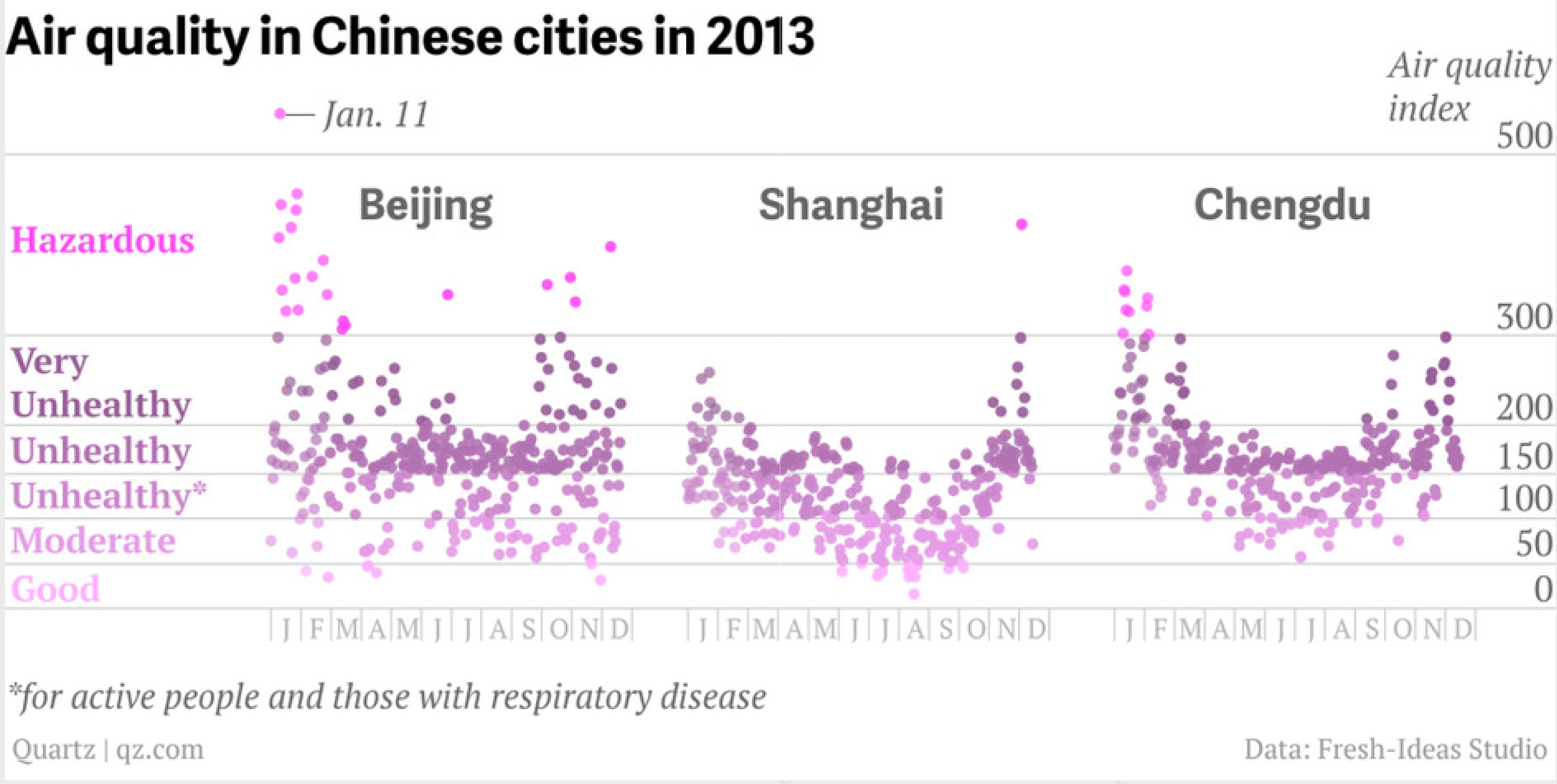
Local authorities seize land / corruption

Shift to kleptocracy

From communist kleptocracy to modern state



Wrong capital cost/no pricing of externalities. eg: air quality



Essential Chinese statistics

- **China**
  - ✓ Fixed investment accounts for 50% of GDP. Q1 growth: +18% to sustain 7% GDP growth
  - ✓ Credit/GDP : 180% (allowing for state owned banks and local gvt lending) vs 25% usually quoted
  - ✓ M2 at 3x the level of 3 years ago
  - ✓ Essentially China has geared itself massively to generate growth since 2011

- **China property accounts for**
  - ✓ 12% to 20% of GDP - 23% of 2013 GDP according to Moody's
  - ✓ 14% of workers (including migrants) or 90 millions staff
  - ✓ 60 m are dirt poor internal migrants

- **Prices**
  - ✓ Shanghai: 5.8k€/sqm. 28 years of income. Chengdu: 1.8k€/sqm. 19 years

GDP growth seen through M2 expansion

Property, the visible stress point in the Chinese dirigist growth

May 14th 2014 :

"China's housing market is slumping fast:

- Major developers have slashed prices as much as 15% since March, reports Bloomberg
- Housing starts fell 25% in the first quarter of 2014, according to Nomura.

The People's Bank of China finally took action earlier today, ordering big banks to start churning out more mortgages to homebuyers"

Chinese looming property crash, a well identified issue indeed but:

When? What outcome?

Minsky Moment or Zombie Economy ?

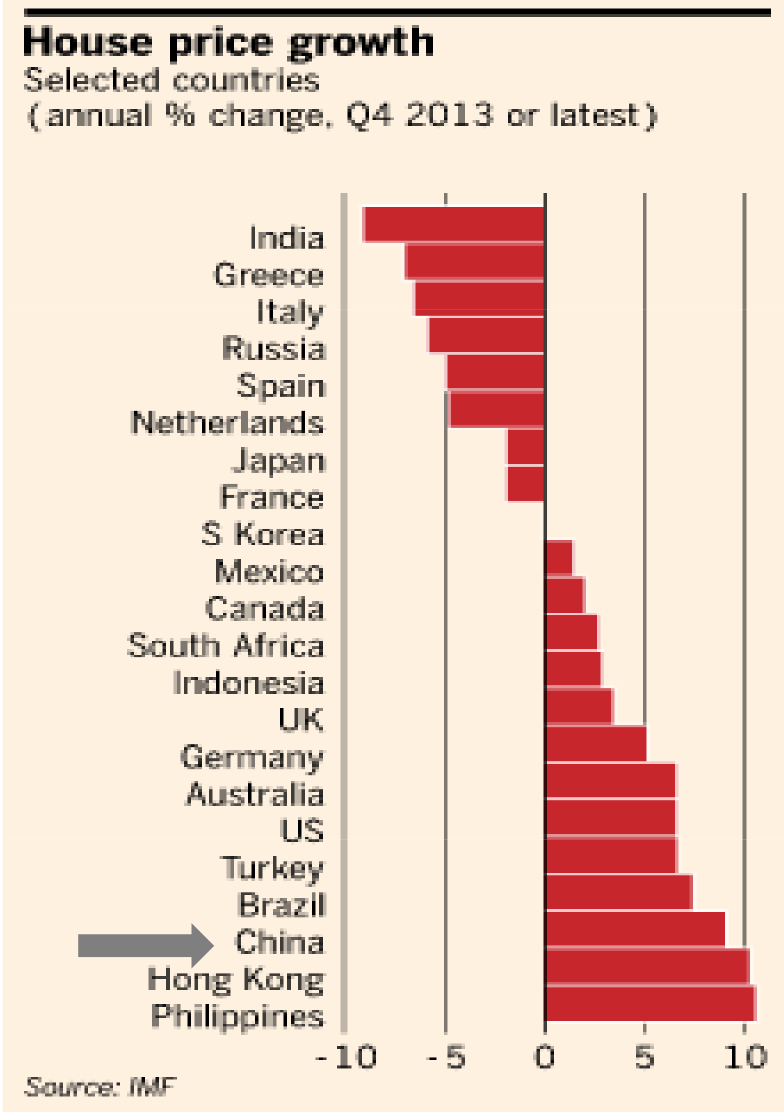
Chinese blow up potential

- **Triggers to a potential blow up**

  ✓ A repeat and prolonged liquidity squeeze like in June 2013.

  ✓ Re-pricing of credit risks in LGFV debt once credit defaults begin. Stop to issuance, domino type collapse

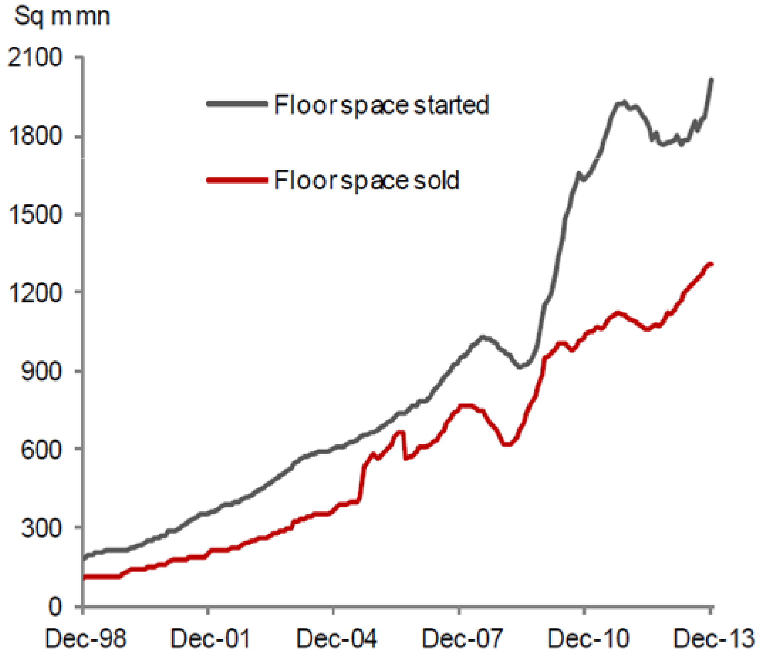
  ✓ Property prices collapse, impact on local fiscal revenues, domino type collapse, impact on central government



GDP growth slowing anyway, even with more property

Excess property supply, no doubt

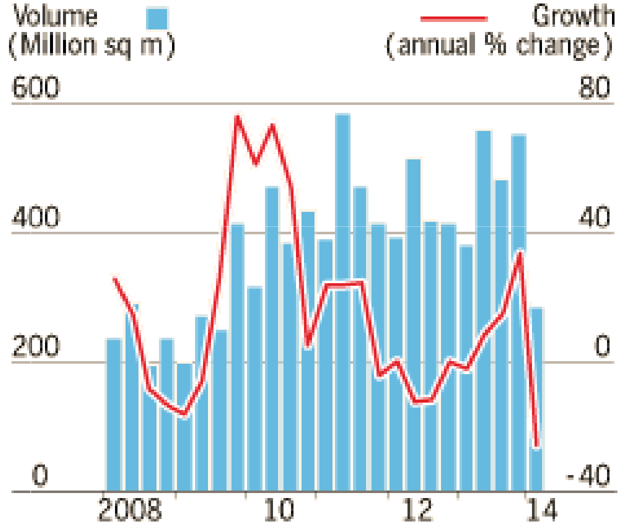
Floor space started and sold (12m rolling sum)



Source: CEIC and Nomura Global Economics.

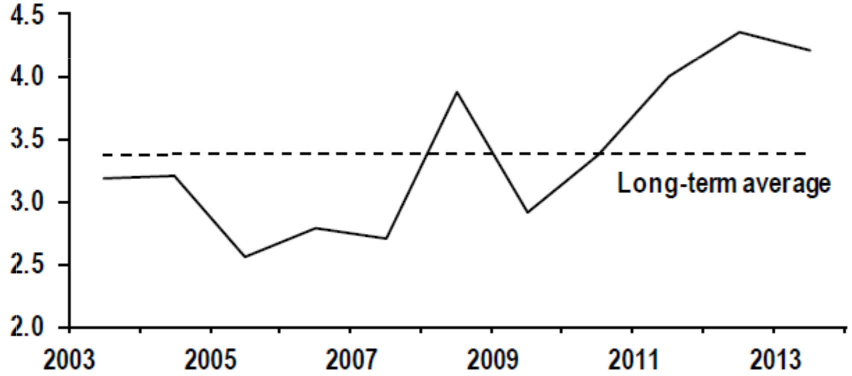
China housing

New housing starts



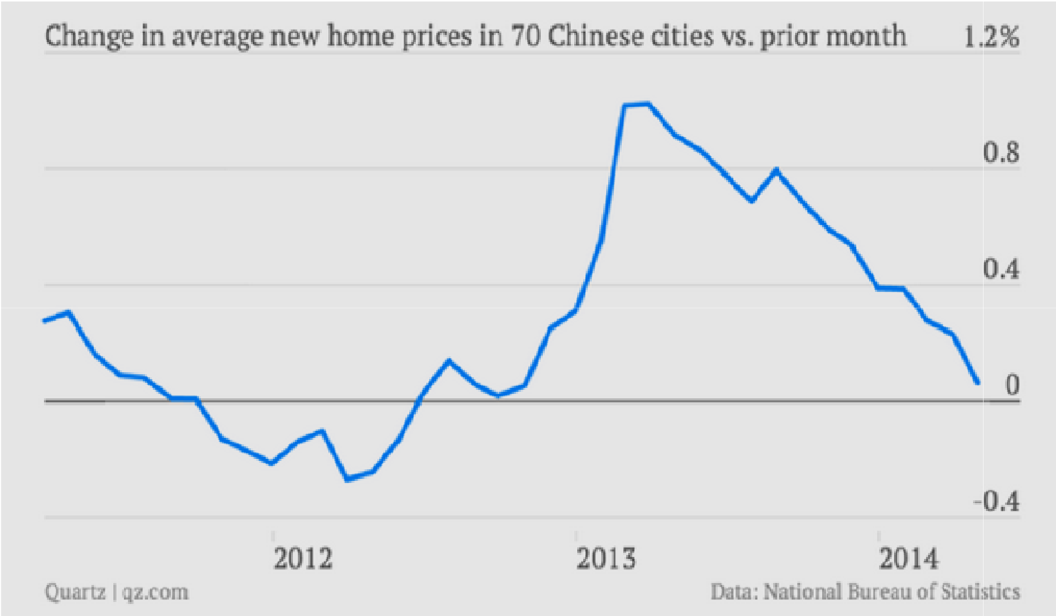
Housing supply conditions

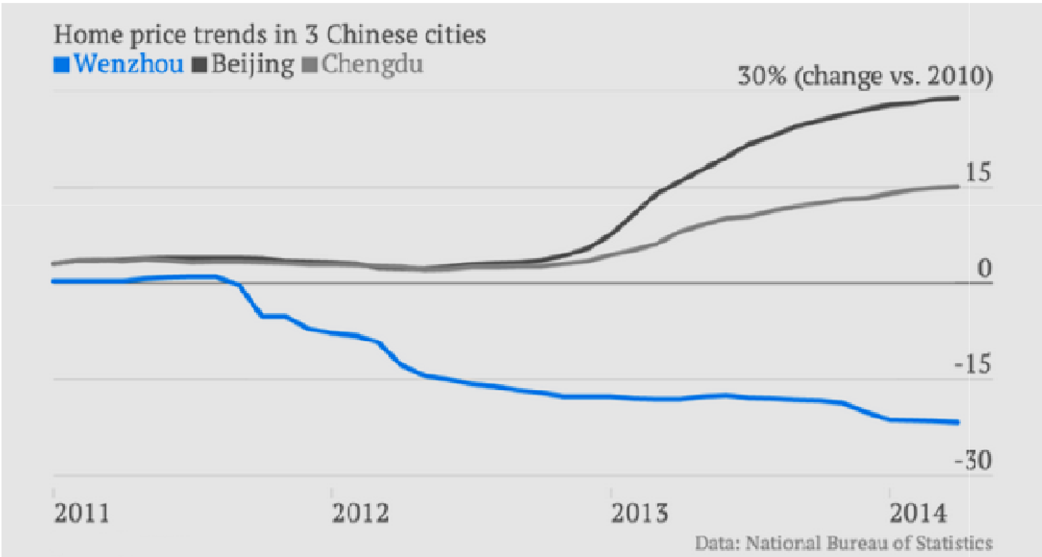
Housing under construction/12-month sales



Source: CEIC, J.P. Morgan reseach by Haibin Zhu, Grace Ng and Lu Jiang

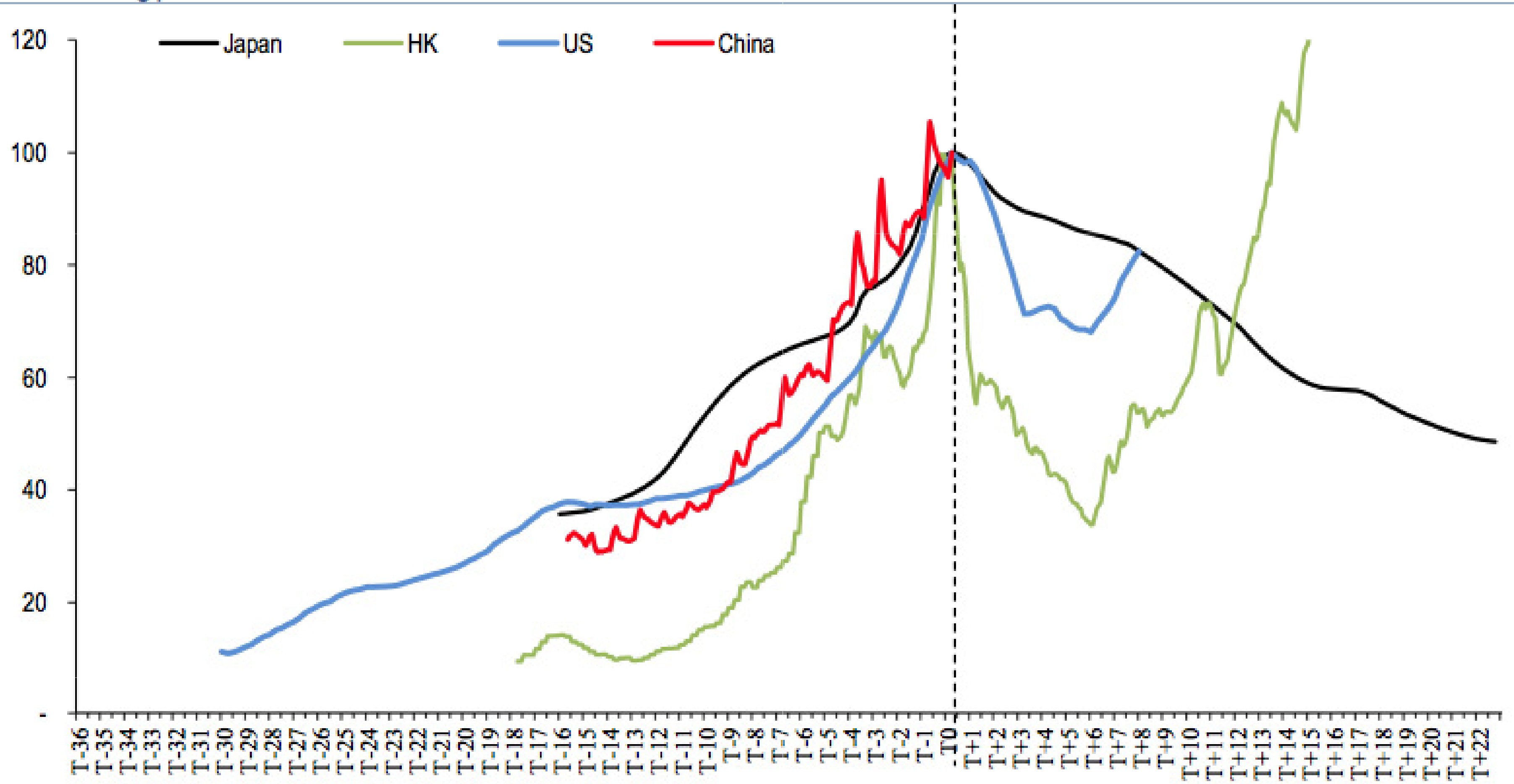
Property crash in progress, excl. Beijing, Shenzen, Shanghai





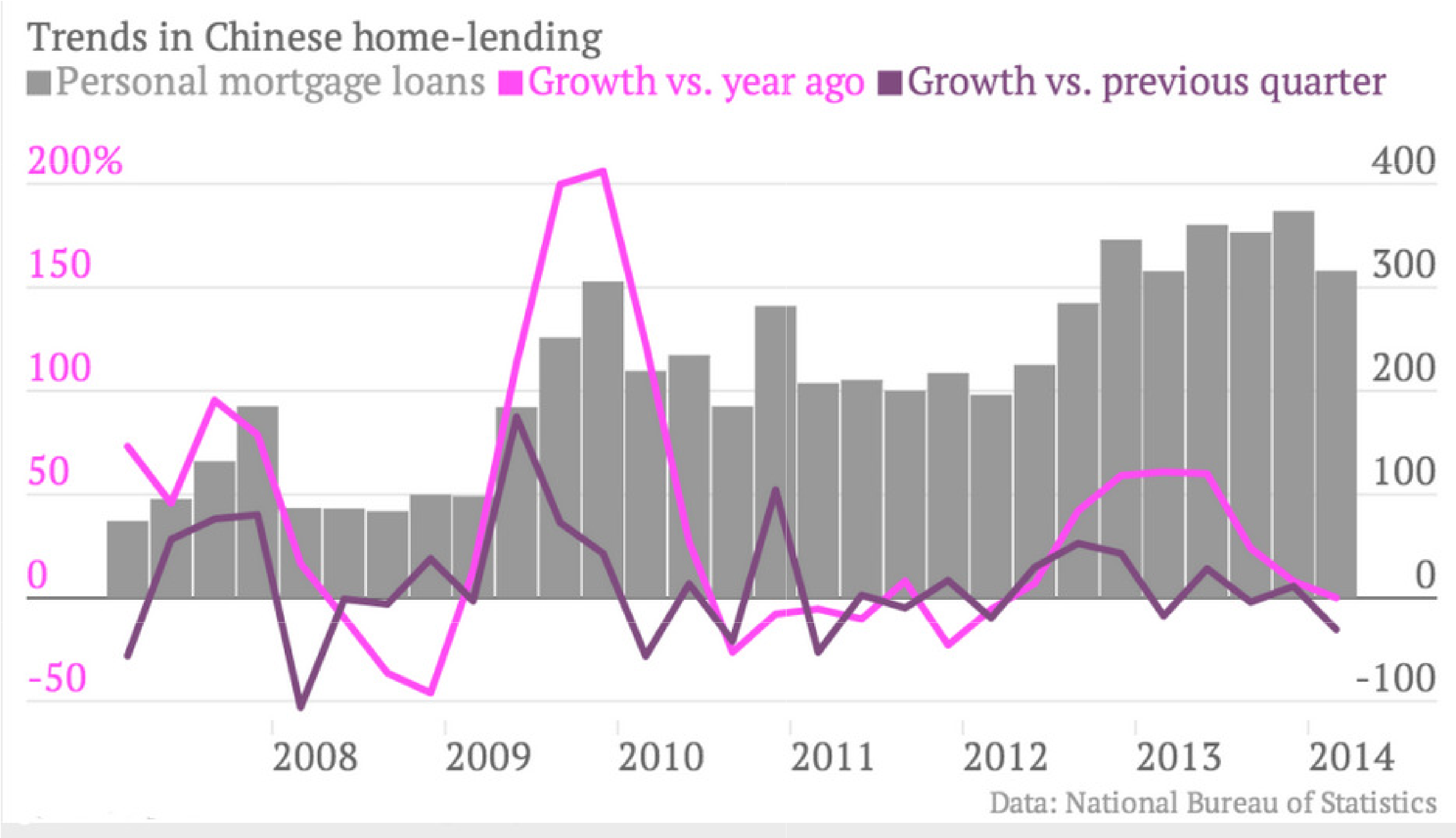
Property "cycles" have similar profiles. When is the Chinese peak? Now

Chart 1: Housing price: China vs. other bubble countries

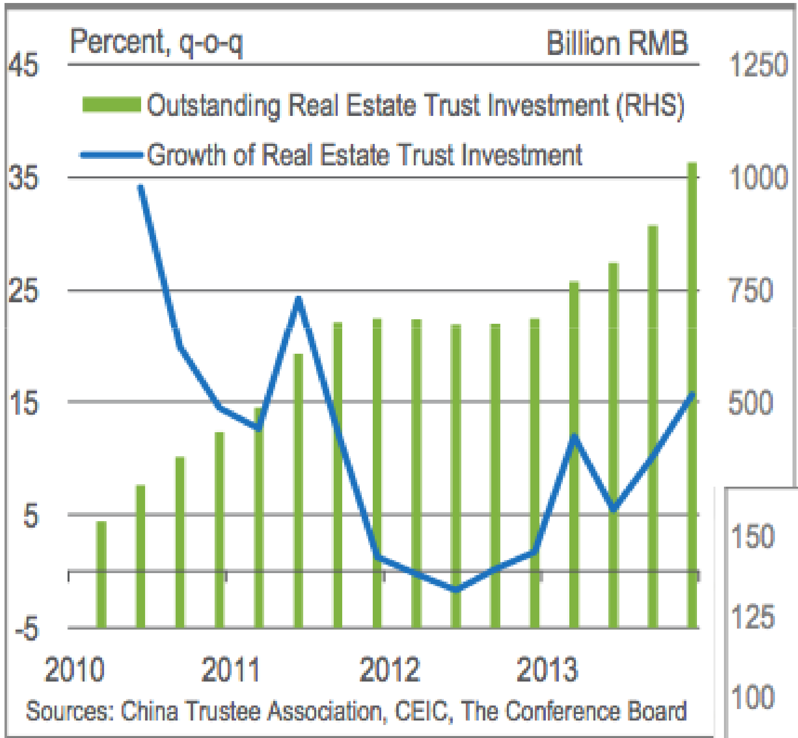


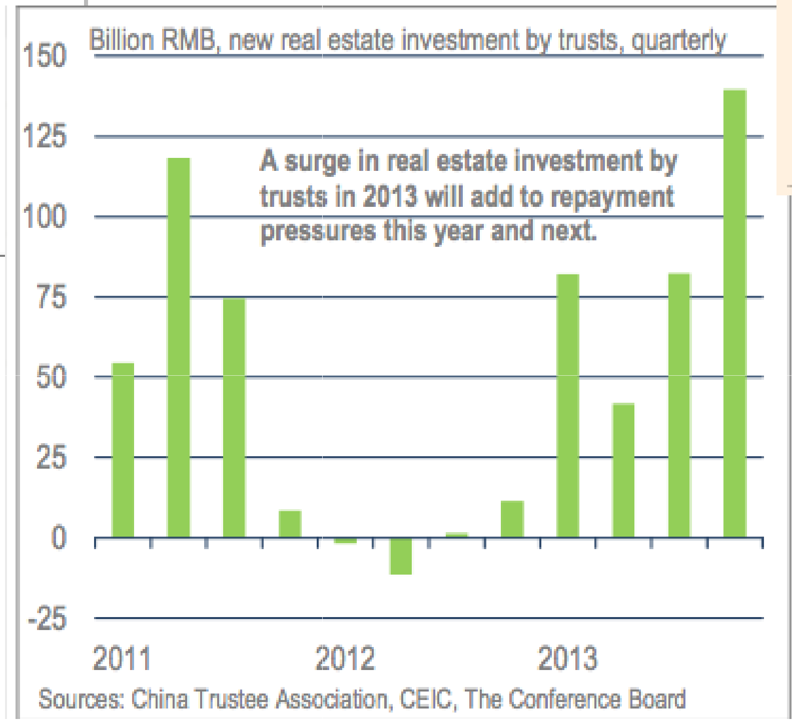
Source:
Japan: house price index: Japan (SA, 1999 4Q = 100) (Source: Federal Reserve Bank of Dallas/ JREI)
HK: all dwelling property price (Index, 1999 = 100) (Source: BIS)
US: all existing dwelling property price (Index, 2000 Jan = 100) (Source: BIS)
China: overall residential property price (Index, 2000 Jan = 100) (Source: Economy Research Institute of Chinese Urban and Rural Construction/ NBS)

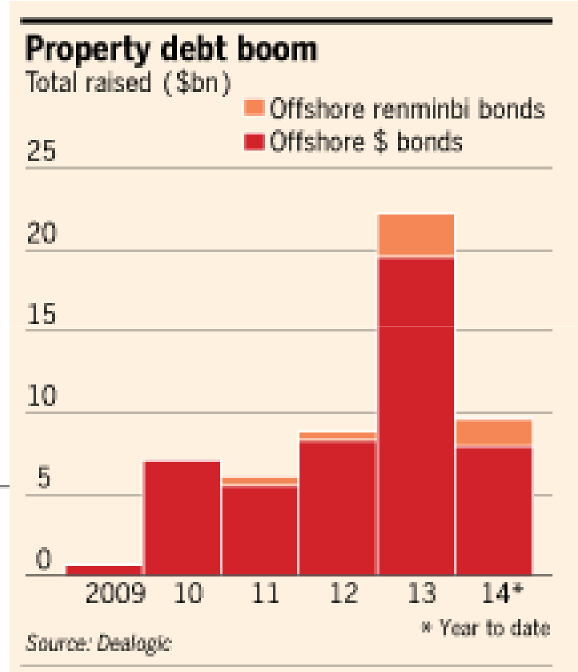
Chinese property crash avoidance: throw even more money (mortgages) at the problem



Throw more "shadow" credit to developers



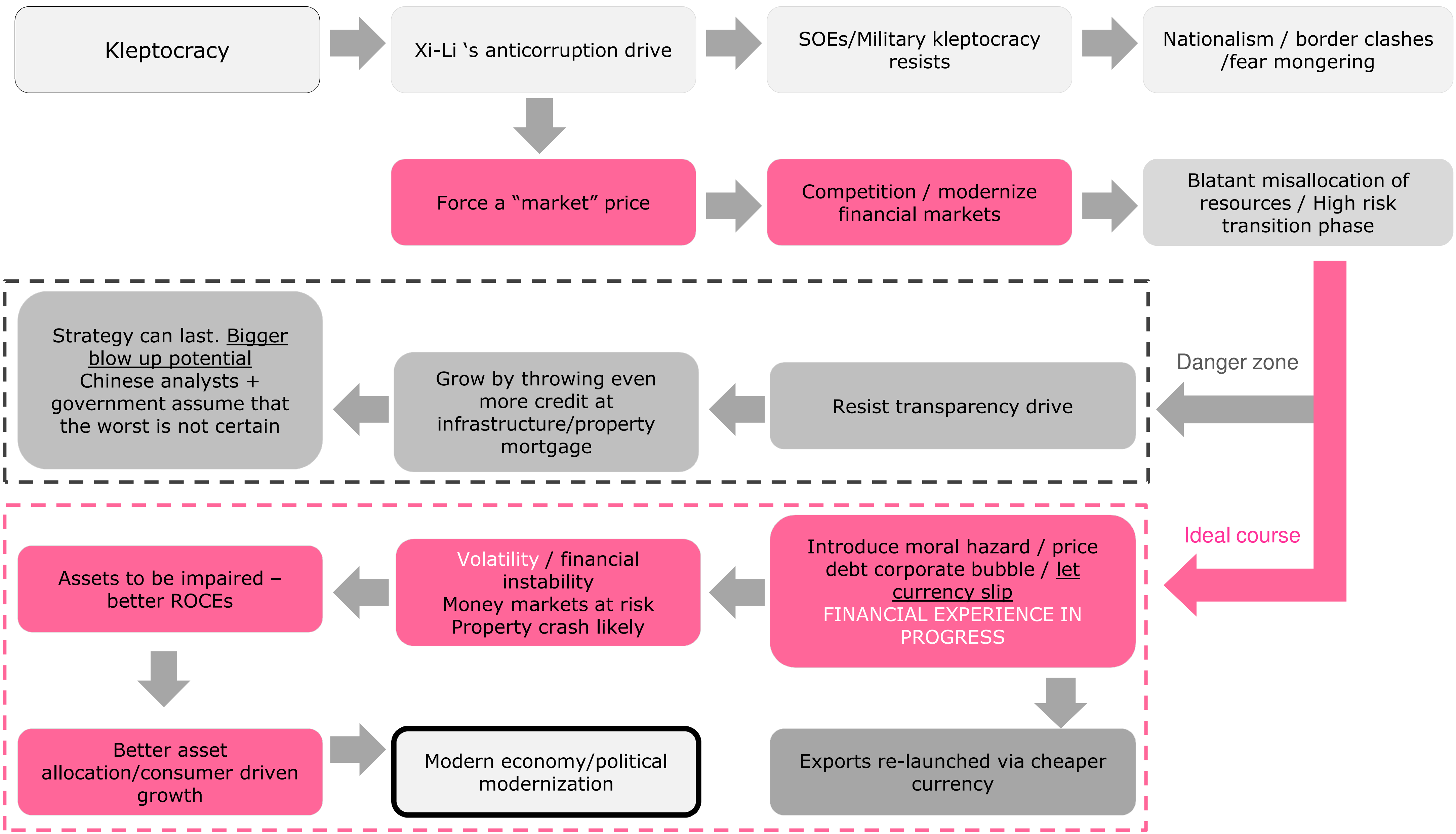




The obvious consequences of a property slump:

- **Capital investment cycle**
  - ✓ Lesser demand for energy, cement, steel (coal, iron ore, nickel), aluminium, copper, etc
  - ✓ Lesser demand for heavy machinery (Metso, Atlas Copco, Caterpillar etc)
  - ✓ Lesser financing/ lesser guarantees – options from banks
- **Banking collapses**
  - ✓ Booking loan losses / Worthless collaterals (if they exist at all)
  - ✓ Shadow financing hurt – shedding of assets
- **Consumer hurts**
  - ✓ Unfinished property / Financial assets at risk /money market instruments?
  - ✓ Slower discretionary consumption

Experimenting with financial markets



Experimenting with financial markets: From state owned banks to Alibaba's Yu'E Bao, an overnight money market transformation. Even more "shadow" credit?

Mr. Ma

Zhejiang Alibaba E-commerce Co.

Alibaba
To be listed

Alipay (48% owned)
"Yu'E Bao" short term wealth mgt/**saving** product
$87bn AuM (03-2014)

51%

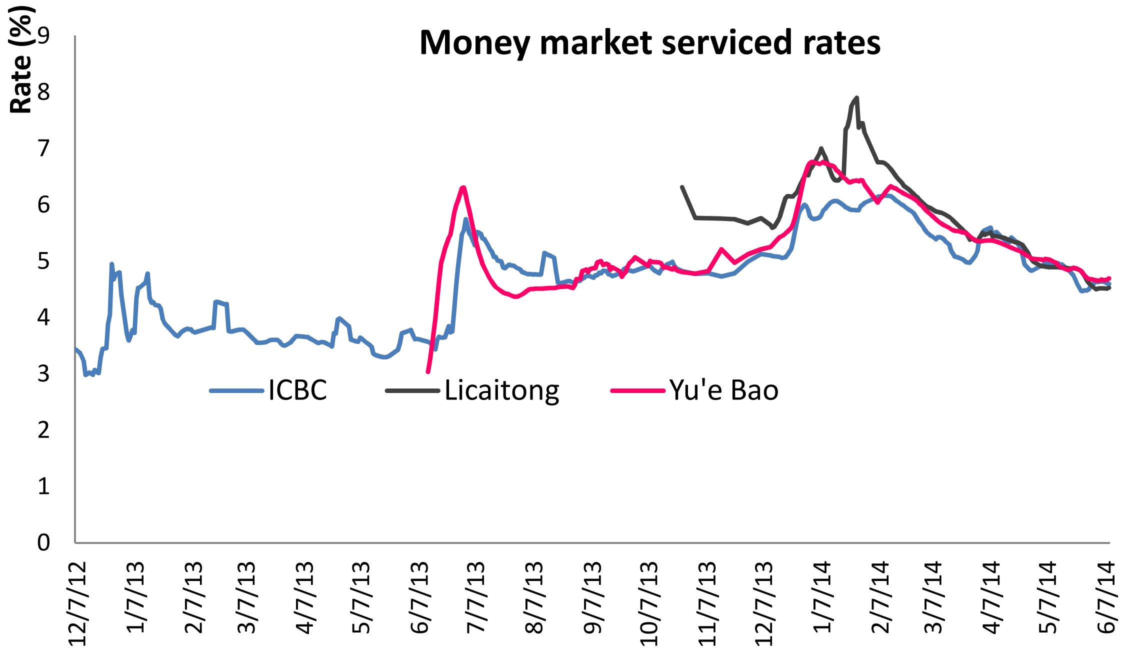
Tian Hong Asset Mgt
Actual fund manager.
Largest in China

People's Bank of China reserve requirements

92% invested in « bank deposits »

Rates driven by interbank rates

?



Risk zone

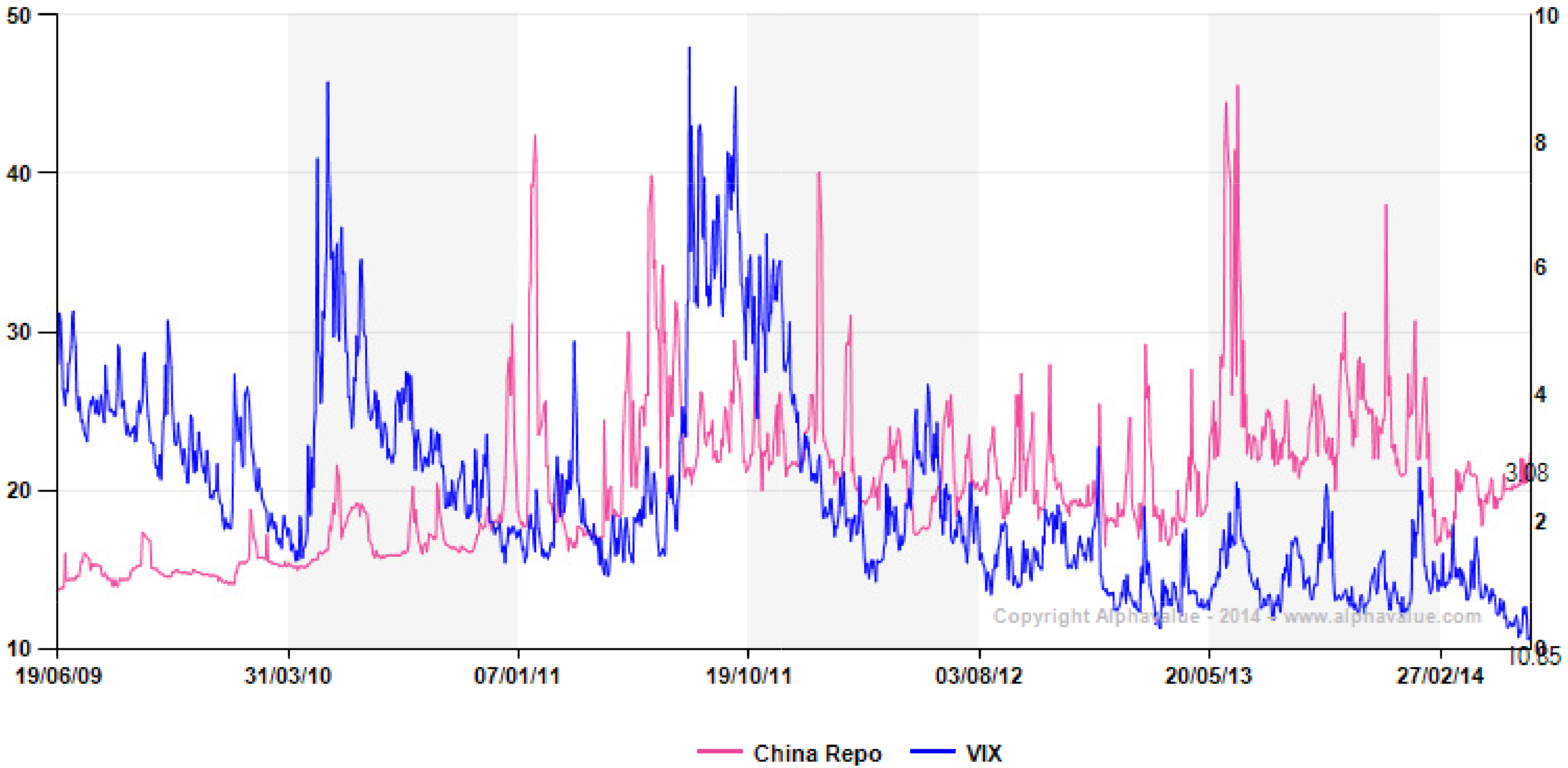
Local authority may provide guarantees

State owned banks channel loans in « trusts » as WMPs

Property company raises liquidity funding at 12-18%

China experiments with « more markets » appear under control for now

China Repo vs VIX



If China stalls, a map of consequences

Basic industries

Sector/ industry	Direct impact	More Chinese exports ?	Second degree Impacts	Key impacted EU players	Earnings Downside
Oils	Lesser crude demand	Unlikely	Lower energy prices across the board	All primary energy groups	-15%
Metals	Less imports	No	Australia, Sth Africa, Chile, Brazil, all weaker GDP growth	All miners, even better balanced BHP (lesser oil demand)	-50%
Chemicals	JVs, zombie Chinese partners	Yes using technology transfers	Chinese exports	All large chemical groups	-20%
Coal	Lesser demand	No	Australia, Sth Africa, US	Rio, BHP, Anglo Am.	-20%
Paper & Pulp	Lesser demand for paper and packaging	No	Cheaper pulp a positive	UPM, Stora, Homen, Mayr	Neutral
Cement	None, cement markets are not opened to foreigners	Unlikely	Less upward pressure on energy	None	Neutral

If China stalls, a map of consequences

Manufacturing industries & Services

Sector/ industry	Direct impact	More Chinese exports ?	Second degree Impacts	Key impacted EU players	Earnings Downside
Capital Goods aimed at construction & energy	Massive	Likely	Cuts in miners demand	Atlas Copco, Metso, Fl Smith, Danieli, Alstom etc	-20%
Lifts	Enormous, dependent on new installations	Unlikely	Local pure Chinese players likely to suffer even more	Schindler, Kone, ThyssenKrupp	-30%?
Capital goods aimed at industry	Less China imports then China needs to shift for quality	Likely	Positives of a Chines drive for productivity capex	ABB, Siemens	0%
Autos +parts	JVs + components exports	No	More competition in Europe and US	VW, BMW, Daimler, PSA, Renault -Nissan	-15% to -50%
IT Hardware	Limited as shift to IT based Chinese growth set to be encouraged	Yes	Expensive Chinese mftg assuming no devaluation	Alcatel, Ericsson, Nokia, Logitech	0%
Aerospace	No	No	More local mftg	Airbus, RR, Safran	0%
Transport	Yes	No	Possibly more east west flows	AP Moller, Airlines	-20%

If China stalls, a map of consequences

Consumer related

Sector industry	Direct impact	More Chinese exports ?	Second degree Impacts	Key impacted European players	Earnings Downside
Luxury	Self funded direct demand is pretty limited	No	none	All luxury players	-20% as the anticorruption drive has bitten already
Food	None	No	No		0%
Drinks	Trading down on spirits, no impact for beer	No	No	Pernod, Diageo, Remy et al.	-10%
Electricals	No	Yes	More competition in Europe/US/Japan	Electrolux, Seb, Husqvarna	-20%
Textile/shoes/ sporting goods	Slower local demand	Yes provided RMB devaluates sharply	Positive for buyers of Chinese products	Adidas, H&M, Next	0%
Leisure & Hotels	Small	No	Less Chinese travellers	Melia, Millenium	-10%

If China stalls, a map of consequences: -11% on earnings at first sight

ALPHAVALUE

Sector (in €m)	2014 earnings	Impact of a slowdown	
		in %	in value
Total	532 180	-11%	472 333

Sector (in €m)	2014 earnings	Impact of a slowdown	
		in %	in value
Mining	27 400	-50%	13 700
Autos	33 937	-33%	22 738
Capital Goods	19 716	-30%	13 801
Chemicals	14 834	-20%	11 867
Consumer Durables	12 970	-20%	10 376
Oils	51 191	-15%	43 512
Food & Beverages	42 192	-10%	37 973
Hotel, Catering & Leisure	4 805	-10%	4 324
Pharma	42 793	-10%	38 514
Banks	80 335	-5%	76 318
Building & Construction	4 501	-5%	4 276
Building Prod. & Materials	5 494	-5%	5 220
Households	8 067	-5%	7 664
Media	9 928	-5%	9 432
Non Food Retail	7 629	-5%	7 248
Other financials	10 270	-5%	9 756
Paper & Packaging	2 333	-5%	2 217
Support Services	2 077	-5%	1 974
Transport	8 087	-5%	7 682

Sector (in €m)	2014 earnings	Impact of a slowdown	
		in %	in value
Aerospace-Defence	9 560	0%	9 560
Computer Services	1 681	0%	1 681
Concessions	3 153	0%	3 153
Food Retail	7 967	0%	7 967
Health	5 323	0%	5 323
Insurance	42 601	0%	42 601
IT Hardware	7 014	0%	7 014
Steel	2 950	0%	2 950
Property	4 633	0%	4 633
Software	4 402	0%	4 402
Telecoms	30 252	0%	30 252
Utilities	21 648	0%	21 648
Semi conductors	2 436	5%	2 558

Chinese JVs with European issuers a learning curve

SWATCH

SWATCH	The Swatch Art Peace Hotel (90%)	Jin Jiang International (Group) Co., Ltd. (10%)
Sales in China	**Chinese subs**	**Chinese partners/suppliers**
37.9%	Hengdeli Holdings Limited (listed in HK)	***Swatch owns 20.57% of Hengdeli. LVMH holds 6.37% of Hengdeli. EXL Holdings, LLC holds 5.19%. EXL Holdings, LLC engages in the development and exploration of oil and gas resources, based in the US. No more other information.

Swatch has 6 wholly-owned subsidiaries in Mainland China, 4 in Hong Kong, 1 in Macau, and 1 in Taibei, in the field of retail, customer service, distribution, and assembly electronic components. Hengdeli is specialized in retaling renowned branded watches including Breguet, Bulgari, Cartier, Gucci, IWC, Longines, Mido, Omega, Rolex, etc. Hengdeli 2013 retail sales (USD 1.6 billion) up 11.4% on 2012, but net (USD 75.1 million) down 50.4% owing to higher labor and rental expenses and impact of the crackdown on corruptions. Swatch has two JVs with Hengdeli: Beijing Xin Yu Heng Rui Watch & Clock Co., Ltd. (Swatch holds 50%) and SMH Swiss Watch Trading (Shanghai) Co., Ltd. (Swatch holds 90%). Jin Jiang International Group is one of the largest tourism enterprise in China owned by the state. It has 4 listed companies: Shanghai Jin Jiang International Hotels (Group) Co., Ltd. (2006.HK), Jin Jiang Hotels Development (600754.SH/900934.SH), Jin Jiang Investment (600650.SH/900914.SH), and Jin Jiang Travel ((00929.SH). Jin Jiang International Hotels (50%) and Thayer Lodging Group (50%) acquired Interstate Hotels & Resorts, Inc. in 2011. The revenue of Jin Jiang International Hotels in 2013 was USD 1.5 billion. It also has JVs with Sofitel and Thomson.

BMW

Sales in China	Chinese subs	Chinese partners/suppliers
21% (20.2% by sales, 19.9% by sales volume)	BMW Brilliance Automotive Ltd. (50%)	Brilliance China Automotive Holdings Ltd. (incorporated in Bermuda) (50%)

The profit for Brilliance China in 2013 was $532m while the net profit contributed by BMW Brilliance was$ 552m (+47%). The sales volume of BMW Brilliance was 206,729 vehicles, up 28.5%. BMW Brilliance has three plants in China. The development of the Brilliance China's own brand is very slow, with 83,747 minibuses sold in 2013. Brilliance China is controlled by Brilliance Auto Group (officially Huachen Group Auto Holding Co., Ltd.) with 2013 total assets at $11.7bn and revenue at $20.5 bn, up 20%. Its sales volume in 2013 was 777,000 passenger vehicles up 15.7%. With the help of BMW, other self-owned brands (Jinbei & Zhonghua) of the Brilliance Auto Group have had a better development. The group has 4 listed companies. Over-capacities in China is a risk factor.

RICHEMONT

Sales in China	Chinese subs	Chinese partners/suppliers
26% (24.1%)		Chow Tai Fook Jewellery Group Ltd.

Chow Tai Fook listed in Hong Kong, is the world's largest pure play jeweller by market capitalisation. 2013 revenue $ 7.4 bn only up 1.5%, with earnings down to $ 733 m vs $ 848m. Watches only account for 6% of revenues. Because of its huge sales network, rapidly expanded retail channels, and frequent exposure from media, Richemont chose Chow Tai Fook as the partner to develop Baume & Mercier instead of Hengdeli. Different from Swatch, Richemont only has one wholly-owned subsidiary: Richemont Commercial Co. Ltd.

Chinese JVs with European issuers a learning curve

ALCATEL-LUCENT

Sales in China	Chinese subs	Chinese partners/suppliers
7.81%	Alcatel-Lucent Shanghai Bell (50%)	China Huaxin Post and Telecommunication Economy Development Center (50%)

Alcatel-Lucent has 2 production sites in Shanghai. Alcatel Shanghai Bell (ASB) was established in 1983, and remains the first sino-foreign joint venture in China's telecom industry. At the early stage of ASB's development, the former Ministry of Posts and Telecommunications supported the group.ASB is now less competitive than Huawei and ZTE. China Huaxin Post and Telecommunication Economy Development Center was transferred to be under control of China Reform Holdings Corporation Ltd. in 2012. According to the State-owned Assets Supervision and Administration Commission of the State Council (SASAC), China Reform took over the companies who did not belong to important industries or key areas, who were smaller and weaker, and who had little correlation with large central enterprises. The main mission of China Reform is reshuffle and management of some SOEs. China Reform also has 2.5% stake of China Minmetals Co., Ltd.. ASB had 2010 revenue at $2.93bn and $3m profit. The acquisition 85% of Alcatel-Lucent Entreprise by China Huaxin will be completed by Q3-2014. China Huaxin (37.5%) also has a joint venture (Yangtze Optical Fibre & Cable Co., Ltd.) with Prysmian Group. TCL (55%) and Alcatel (45%) established a joint venture: Alcatel Mobile Phones in 2004, and TCL acquired Alcatel's 45% in the JV in 2005. Alcatel Shanghai Bell has 14 subsidiaries including Radio Frequency Systems. China Mobile released the bid results for second-phase TD-LTE centralized procurement in May 2014: ZTE 34%, Huawei 31%, Ericsson 9%, Alcatel Shanghai Bell 9%, Nokia 8%, New Post Com 1.5%, Putian 1%, FiberHome Technologies 0.5%. Alcatel and FiberHome Technologies built a joint venture in 2002 to develop business of optical fiber. There is no other information about this JV.

NESTLE

Sales in China	Chinese subs	Chinese partners/suppliers
7.18%	Shanghai Totole Food Ltd. (80%) Shanghai Totole First Food Limited (80%) Guangzhou Refrigerated Foods Co., Ltd. (97%) Sichuan Haoji Food Co., Ltd. (80%) Yunnan Dashan Drinks Co., Ltd. (70%) Xiamen Yinlu Foods Group Co., Ltd. (60%) Anhui Yinlu Foods Co., Ltd. (60%) Hubei Yinlu Foods Co., Ltd. (60%) Shandong Yinlu Foods Co., Ltd. (60%) Hsu Fu Chi International Limited (60%) Wyeth	

Nestle acquired 80% of Totole in 1999. As the dominant brand in the chicken essence market, Totole has had a 42% of market share for many years. Nestle bought 97% of Guangzhou Frozen Food in 1999. "Wuyang" brand of Guangzhou Refrigerated Food is the largest ice-cream brand in Guangdong, which focuses on the lower-end market. Nestle has kept this brand and also developed its own brand of ice-cream. Nestle just started to introduce Wuyang ice cream on Nestle China website in 2012. Nestle bought 60% of Sichuan Haoji in 2001. Haoji is the second largest chicken essence producer. Nestle acquired 70% of Yunnan Dashan in 2010 to fill its gap in bottled water market in China. Yunnan Dashan covers more than 95% of the market share in Yunnan. Nestle bought 60% of Xiamen Yinlu in 2011. Xiamen Yinlu specializes in the production and management of canned food and beverage. Sales of Yinlu Peanut Milk is more than USD 801.63 million in 2013. Xiamen Yinlu is the producer of Nestle coffee. Nestle acquired 60% of Hsu Fu Chi in 2011. Hsu Fu Chi is a candy producer who has been the first in the sales volume ranking since 1998, and its sales in 2013 was USD 962 million. Wyeth, the infant nutrition division of Pfizer, was acquired by Nestle in 2013. Wyeth had the biggest market share in milk powder industry in China in 2013.

Chinese JVs with European issuers, a learning curve

VOLKSWAGEN

Sales in China	Chinese subs	Chinese partners/suppliers
18% (31.2% by sales volume)	Shanghai Volkswagen Automotive Co., Ltd. (50%) FAW Volkswagen Automobile Co., Ltd. (50%)	SAIC Motor Corporation Limited (50%) FAW Group Corporation (50%)

Total 2013 sales volume of the two JVs in 2013 was 3 million vehicles (locally produced), up 16.4%. SAIC Motor 2013 volumes up 13.7% to 5.1 millions vehicles, among which, Shanghai Volkswagen contributed 1.5 millions vehicles (third largest, after Shanghai GM and SAIC-GM-Wuling Automobile) with an increase of 19.14%. Nanjing Automobile, a subsidiary of SAIC, acquired MG Rover in 2005. FAW Group has built joint ventures with Volkswagen, Toyota, Mazda, GM. 2013 revenues of FAW Group $66.9bn. 2013 sales volume of FAW-Volkswagen in 2013 around 1.5 million vehicles.

KINGFISHER

Sales in China	Chinese subs	Chinese partners/suppliers
3.78%		China National Building Material Co., Ltd. Beijing New Building Material (Group) Co., Ltd.

Kingfisher has 39 stores (2013 sales up 8% at £412m, loss £-6m) and 3997 employees in China but is looking for strategic partner in China. Kingfisher has at least 2 JVs with China National Building Material Co., Ltd. (03323. HK) (revenue in 2013: $18.8 billion, +34.9%; net profit: $1.3bn, +7.4%), which is a subsidiary of an SOE China National Building Materials Group Corporation (revenue $41 bn, +18%; net profit $2bn, +10%). Beijing New Building Material (000786.SZ) (revenue $1.2bn, +12.04%) is also a subsidiary of China National Building Material Group Corporation. Kingfisher has had a lot of payment disputes with suppliers.

SABMILLER

Sales in China	Chinese subs	Chinese partners/suppliers
Not consolidated	China Resources Snow Breweries Ltd. (49%)	China Resources Enterprise (51%)

NING Gaoning was once the Chairman of China Resources, but now he is the Chairman of COFCO, China's largest food processing, manufacturer and trader. COFCO has 16.3% stake of Mengniu Dairy. Danone has 9.9%, and Arla Foods has 5.3%. So COFCO Dairy Investments, the JV between COFCO, Danone, and Arla Foods, holds 31.5% of Mengniu Dairy. Vanke (CR is the biggest shareholder 15%), established a joint venture with COFCO. Vanke bought 70% of 201 Folsom Street, a mainly high-end residential project owned by Tishman Speyer. Canada Pension Plan Investment Board has formed a JV with Vanke in March to develop business in Chinese real estate market. CR Enterprise has been involved in beer since NING Gaoning looked at Tsingtao Brewery. 2013 CR revenue was $64.53bn. CR has 10 listed companies. CR Snow was incorporated in British Virgin Islands in 1984. It has 13 breweries in China. In the news in China, it is reported that CR Snow has more than 95 breweries. CR Enterprise (60%) also established a Non-Alcohol Beverage joint venture with Kirin Holdings Company (40%) (a member of Mitsubishi Keiretsu). Kirin holdings also holds 100% of Lion Nathan. Anheuser-Busch InBev acquired full control of Liaoning Dalian Daxue Brewery Co. in China from Kirin Holdings in 2011. The market share of CR Snow was 23% in 2013, a leader since 2006. The market share of the biggest five beer producers (CR Snow 23%, Tsingtao Brewery 17.19%, Anheuser-Busch 13%, Beijing Yanjing Brewery 11.3%, and Carlsberg 10%) in China was almost 75% in 2013. CR Snow acquired Kingway Breery Holdings Ltd. in 2013 with an 8% production capacity increase. 2013 sales of CR Enterprise $19bn (up 16%) profits down 52% to $ 341m. Beer accounts for 22% of CR Enterprise's sales, dominated by retail (80% JV with Tesco). Mr. Andrew Y. Yan (Non-Executive Director of CR Land) is also non-executive director of Fosun International Limited (partner of Alibaba), Mengniu Dairy, and Sinopec (partner of Linde, Bayer, BASF, etc.). There are three joint ventures between CR Cement (50%) and HeidelbergCement (50%): China Century Cement Limited, Easy Point Industrial Limited, and Squareal Cement Limited. A subsidiary of CR had a joint venture with Fresenius, but Fresenius acquired the stake back. A subsidiary of CR holds 0.69% stake of Beijing Yanjing Brewery.

Chinese JVs with European issuers a learning curve

GLAXOSMITHKLINE

Sales in China	Chinese subs	Chinese partners/suppliers
	Sino-American Tianjin Smith Kline & French Laboratories Ltd. (55%)	Tianjin Zhongxin Pharmaceutical Group Co., Ltd. (25%) Tianjin Taiping Group Co., Ltd. (20%) Shenzhen Neptunus Interlong Bio-Technique Co., Ltd.

Tianjin Zhongxin Pharmaceutical (600329. SH) is a subsidiary of a wholly state-owned enterprise Tianjin Pharmaceutical Holdings Ltd (TJPH). TJPH holds 44% of Zhongxin. Revenue from JVs account for 1/3 of the group's total revenue. The 2012 annual revenue of TJPH in 2012 was $4.2bn. Tianjin Taiping Group is a joint venture between the Tianjin government and a foreign company. There is a joint venture between GSK and Shenzhen Neptunus Interlong (8329. HK), which is a subsidiary of Neptunus Group. Neptunus Group is not a state-owned enterprise. Its revenue in 2012 was $2.6 bn. It has another 2 listed companies: China Nepstar Chain Drugstore Ltd. (stock code: NPD), and Shenzhen Neptunus Bioengineering Co., Ltd. (000078. SZ).

ARCELORMITTAL

	Valin ArcelorMittal Automotive Steel (49%)	Hunan Valin Steel Co., Ltd. (51%) (000932.SZ)
Sales in China	**Chinese subs**	**Chinese partners/suppliers**
	China Oriental (47.01%) (00581.HK) Hunan Valin Steel Co., Ltd. (15.05%)	

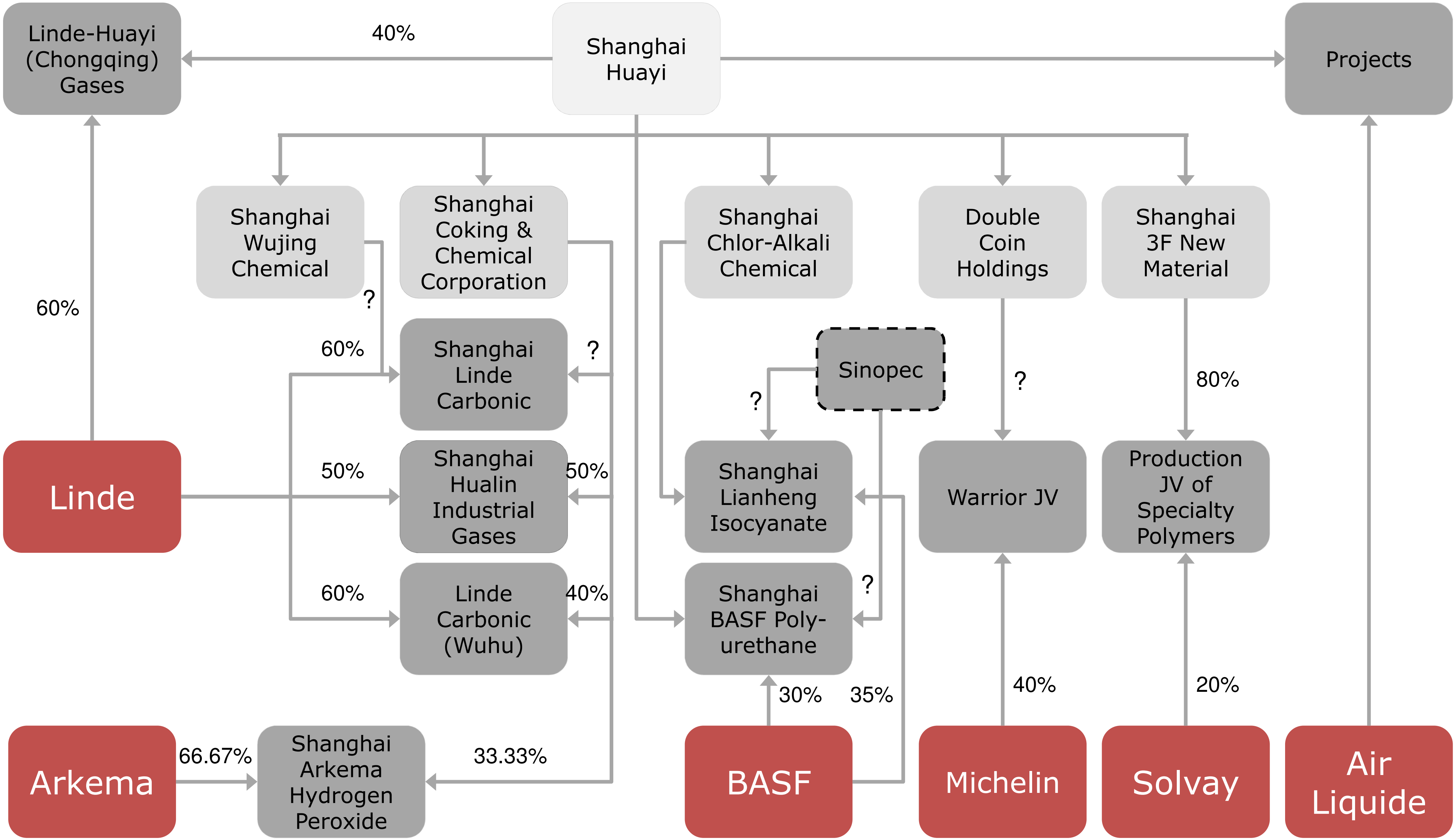
2013 revenue of Hunan Valin in 2013 was $9.6bn with earnings at $27m. ArcelorMittal and Valin Group agreed on a share swap arrangement based upon a put option mechanism. ArcelorMittal will decrease in two years its holding in Hunan Valin Steel from 29.97% to 10.07%, and in return, ArcelorMittal will increase its stake in Valin ArcelorMittal Automotive Steel (JV) from 33% to 49%. 2013 revenue of China Orientalat $5.23bn (-10%) and profits down 57% to $10m.

CARREFOUR

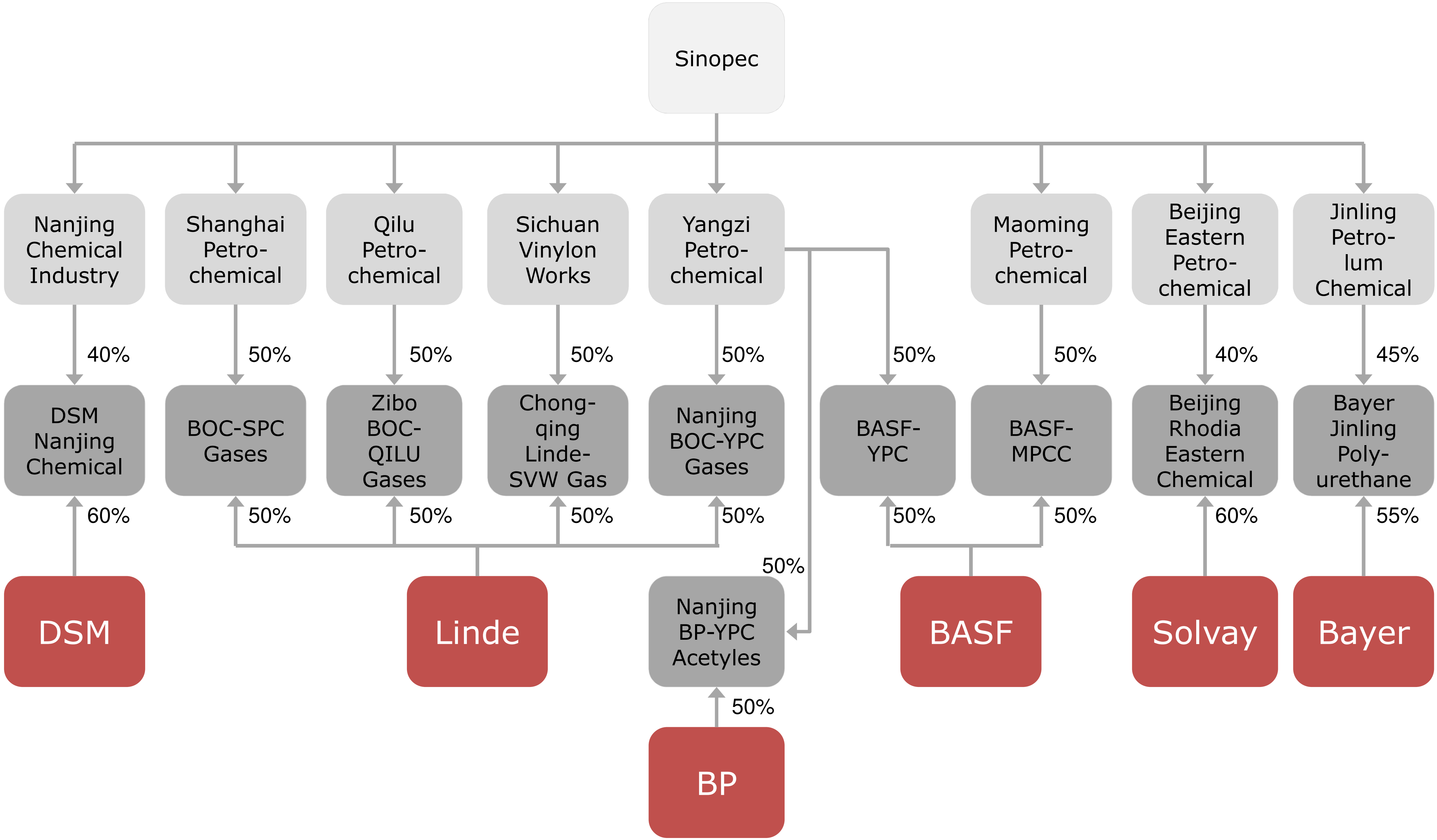
Sales in China	Chinese subs	Chinese partners/suppliers
6.7% by net sales		Yueda South Lianhua Supermarket Holdings Co., Ltd. Tianjin Quanye Bazaar (Group) Co., Ltd.

There are more than 50 hypermarkets established by Yueda South and Carrefour. Yueda South is a subsidiary of Yueda Group. The turnover of Lianhua Supermarket Holdings in 2013 was $5bn. Reports suggest that partners of Carrefour do not care whether supermarkets are profitable or not. It is easier for them to get loans from the bank if they say they are partners of Carrefour. A lot of supermarkets of Carrefour in China are not very well organized.

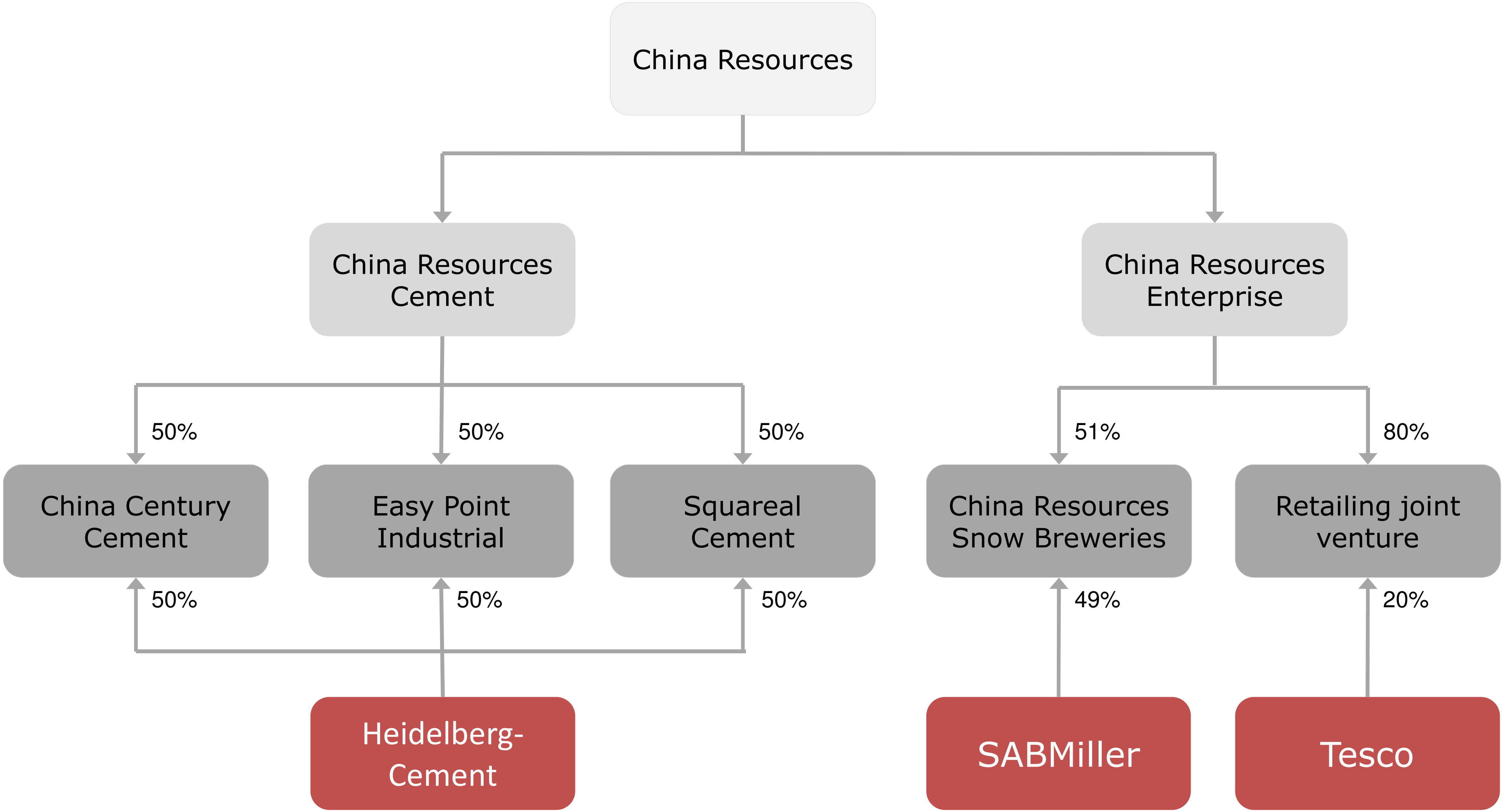
Chinese JVs, a map of consequences. eg: Chemicals



Chinese JVs, a map of consequences. eg.: Chemicals, cont'd

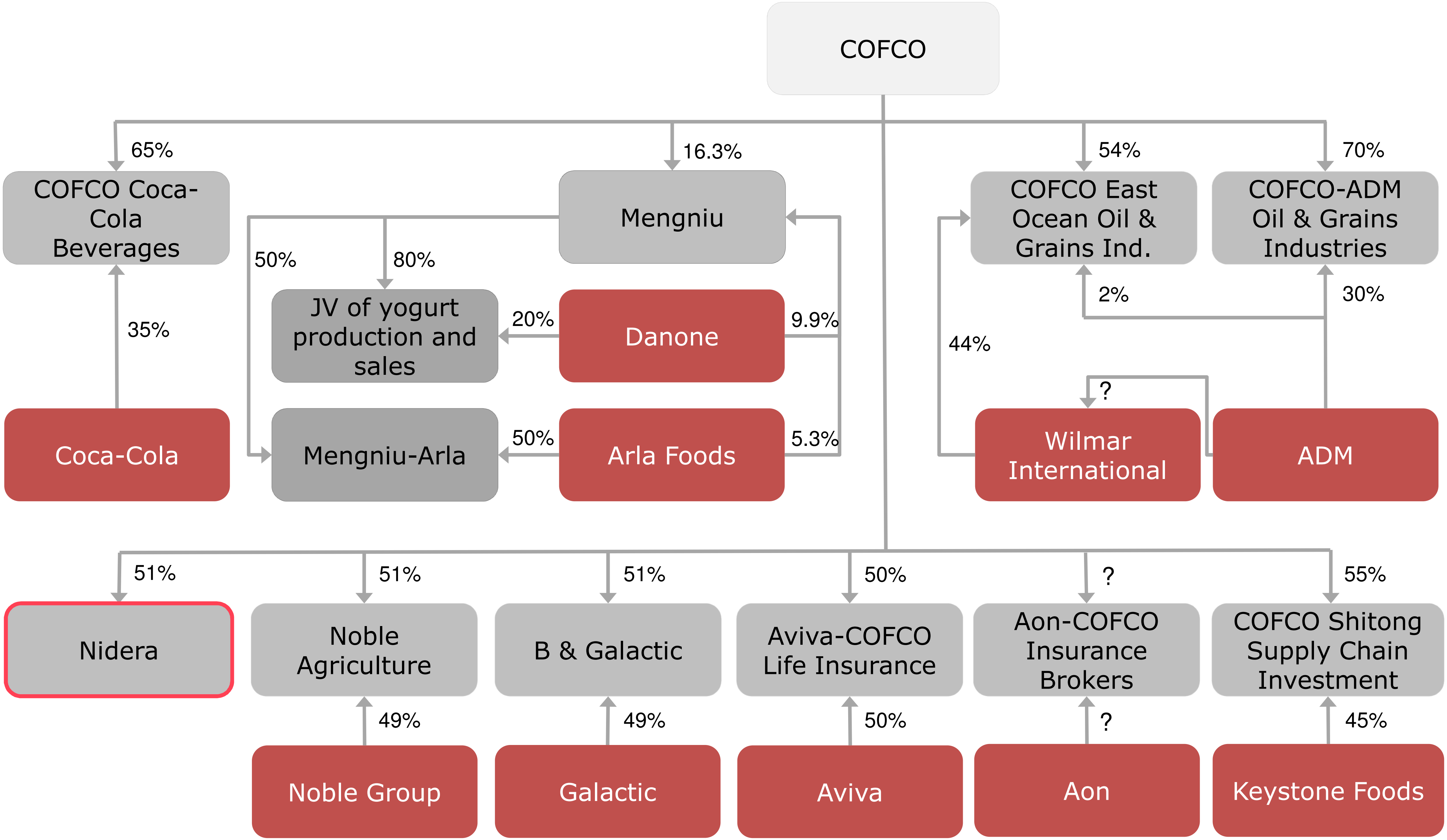


Chinese JVs, a map of consequences



Chinese JVs, a map of consequences

ALPHAVALUE



Sector hierarchy, as of 16-06-2014.

Sensible Sector selection

Caution required

Sector	Upside	Mom.	P/E 2014	P/E 2015	Earnings growth 2014/2013	Earnings growth 2015/2014	P/Book 2014	Yield 2014
Paper & Packaging	17,6%	++	15,4 x	12,9 x	6,60%	19,9%	1,31 x	3,59%
IT Hardware	16,8%	+	19,2 x	14,8 x	6,65%	28,9%	1,93 x	2,46%
Software	13,9%	+	20,0 x	18,1 x	8,66%	10,4%	3,59 x	1,84%
Telecoms	13,4%	+	16,0 x	14,6 x	9,13%	9,73%	1,87 x	4,38%
Aerospace-Defence	13,4%	++	14,4 x	12,7 x	21,2%	13,2%	2,88 x	2,78%
Insurance	10,3%	+	9,85 x	8,95 x	12,5%	10,1%	1,09 x	4,00%
Computer Services	9,57%	+	18,8 x	16,5 x	18,8%	13,5%	2,70 x	2,08%
Hotel, Catering & Leisure	7,78%	+	19,9 x	17,6 x	14,1%	12,3%	3,53 x	2,36%
Other financials	6,92%	+	15,9 x	14,2 x	11,8%	12,0%	1,16 x	2,86%
Media	6,76%	+	16,2 x	14,6 x	13,8%	10,4%	3,13 x	3,08%
Utilities	6,60%	+	15,4 x	14,5 x	-8,47%	6,10%	1,43 x	4,44%
Metals & Mining	6,24%	+	13,0 x	11,7 x	42,9%	11,5%	1,40 x	3,20%
Building Prod. & Materials	5,73%	+	18,9 x	15,2 x	24,5%	24,4%	1,30 x	2,22%
Health	5,32%	+	21,7 x	19,7 x	7,34%	10,4%	2,87 x	1,52%
Building & Construction	4,52%	++	15,2 x	14,2 x	28,6%	6,72%	2,07 x	3,35%
Banks	4,40%	+	14,1 x	10,8 x	33,1%	30,9%	0,96 x	3,45%
Consumer Durables	4,20%	+	20,4 x	17,9 x	6,99%	14,0%	2,94 x	2,00%
Chemicals	4,08%	+	17,7 x	16,5 x	7,71%	7,60%	2,52 x	2,73%
Food Retail	2,06%	-	15,0 x	13,4 x	12,0%	11,7%	1,66 x	3,66%
Capital Goods	2,00%	+	18,0 x	15,6 x	20,5%	15,3%	2,83 x	2,92%
Support Services	1,99%	+	21,3 x	19,0 x	15,3%	12,2%	4,17 x	2,99%
Concessions	1,96%	+	20,9 x	18,8 x	4,50%	10,9%	2,91 x	3,73%
Semi conductors	1,12%	+	26,2 x	21,1 x	67,0%	24,2%	3,16 x	1,37%
Transport	-0,22%	+	16,1 x	13,7 x	33,8%	17,7%	1,82 x	2,35%
Autos	-0,76%	++	10,9 x	9,65 x	33,2%	12,8%	1,32 x	2,64%
Property	-2,47%	+	19,2 x	17,9 x	5,72%	7,60%	1,14 x	4,49%
Food & Beverages	-3,12%	+	19,2 x	18,0 x	6,09%	6,49%	3,57 x	3,14%
Pharma	-3,47%	++	21,7 x	20,9 x	1,54%	3,87%	4,19 x	2,97%
Households	-5,47%	++	22,6 x	21,7 x	0,05%	4,10%	3,54 x	2,08%
Oils	-8,91%	+	13,6 x	15,3 x	4,02%	-10,7%	1,34 x	4,17%
Non Food Retail	-11,5%	-	22,3 x	20,3 x	9,70%	9,87%	4,70 x	2,73%

Sector hierarchy, summary view as of 16-06-2014.

Sensible Sector selection

Caution required

Sector Current	Sector Deflation	Sector China	Upside	Mom.
Paper & Packaging	Paper & Packaging	Paper & Packaging	17,6%	++
IT Hardware	IT Hardware	IT Hardware	16,8%	+
Software	Software	Software	13,9%	+
Telecoms	Telecoms	Telecoms	13,4%	+
Aerospace-Defence	Aerospace-Defence	Aerospace-Defence	13,4%	++
Insurance	Insurance	Insurance	10,3%	+
Computer Services	Computer Services	Computer Services	9,57%	+
Hotel, Catering & Leisure	Hotel, Catering & Leisure	Hotel, Catering & Leisure	7,78%	+
Other financials	Other financials	Other financials	6,92%	+
Media	Media	Media	6,76%	+
Utilities	Utilities	Utilities	6,60%	+
Metals & Mining	Metals & Mining	Metals & Mining	6,24%	+
Building Prod. & Materials	Building Prod. & Materials	Building Prod. & Materials	5,73%	+
Health	Health	Health	5,32%	+
Building & Construction	Building & Construction	Building & Construction	4,52%	++
Banks	Banks	Banks	4,40%	+
Consumer Durables	Consumer Durables	Consumer Durables	4,20%	+
Chemicals	Chemicals	Chemicals	4,08%	+
Food Retail	Food Retail	Food Retail	2,06%	-
Capital Goods	Capital Goods	Capital Goods	2,00%	+
Support Services	Support Services	Support Services	1,99%	+
Concessions	Concessions	Concessions	1,96%	+
Semi conductors	Semi conductors	Semi conductors	1,12%	+
Transport	Transport	Transport	-0,22%	+
Autos	Autos	Autos	-0,76%	++
Property	Property	Property	-2,47%	+
Food & Beverages	Food & Beverages	Food & Beverages	-3,12%	+
Pharma	Pharma	Pharma	-3,47%	++
Households	Households	Households	-5,47%	++
Oils	Oils	Oils	-8,91%	+
Non Food Retail	Non Food Retail	Non Food Retail	-11,5%	-

Thank You

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COVERAGE

STOXX 600
by market cap covered

Source Bloomberg
as of April 2014