Navigating the Belt and Road

Financial sector paves the way for infrastructure

August 2015
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In the first half of 2015, the roll-out of the “One Belt, One Road” initiative and the implementation of a series of reform measures have encouraged more Chinese enterprises to “go out” into the global market. Their investments have created new energy in the global market. Despite the short term impact resulting from the currency policy adjustment, we believe Chinese companies will continue to invest in different parts of the world given the strong government support. As these companies become more experienced in overseas investment, they will find new confidence, be better poised to leverage favorable policies and form a more global and long-term strategic vision, which will enable them to go even further on the road to internationalization and sustainable growth.

Albert Ng  
Chairman, China  
Managing Partner,  
Greater China

Foreword

In 2014, China’s outward FDI saw year-on-year growth of 14.1%, ranking it third in the world. In the same year, after several years of continual growth, China’s outward FDI almost surpassed its inbound investment, a clear sign of the country’s successful transformation from a popular investment destination to a powerful investor. During the first half of 2015, Chinese investors’ enthusiasm for outbound investment remained unabated. According to statistics released by the Ministry of Commerce, China’s non-financial outbound investment amounted to US$56b in the first half of 2015, a year-on-year increase of 29.2%, which indicates that China is likely to outperform the expected outbound investment growth target of 10% for the year.

Behind the impressive high growth, we can see the implementation of the “going out” strategy and the dreams of expansion of Chinese enterprises. The “One Belt, One Road” strategy has evolved from a general guidance to concrete projects, which will guide future China outbound investment, and lay a solid foundation for Chinese investment’s Big Navigation Era.

- **Stronger policies.** Frequent high-level visits and trade; governmental support in the financial sector; equipment “going out” and international production capacity cooperation.
- **Clearer development strategy.** New model of overseas cooperation: emphases on infrastructure and international production capacity cooperation, with financial collaboration and support.
- **Broader space expansion.** Across Siberia and the Pacific Ocean, and extending to Latin America, distance is not affecting the enthusiasm of Chinese investors. More and more Chinese enterprises are striding towards the global market. However, experience tells us that without long-term planning, the road to internationalization could be very long, winding and rocky. Enterprises need to improve their ability to establish and implement strategic planning, and then to integrate internationalization into their long-term development goals, conduct an assessment of their competitiveness, and consider the external environment and their practical needs in order to make the right move at the right time.

In the future, China’s outbound investment will continue to grow as Chinese enterprises are looking for a wider investment scope. There are many opportunities ahead, but we hope forward-looking Chinese enterprises will be cautious in their outbound investment, calmly deal with various challenges and achieve their dreams of internationalization.

Loletta Chow  
EY Global COIN Leader
Lead the tide with rising investment enthusiasm

Thriving in an ever-changing global economic environment: Intrim review of China’s outbound investment in 2015

During the past five years, China’s outward FDI compound annual growth rate averaged a remarkable 14%: In 2012, China became the world’s third-largest overseas investor; in 2013, China’s total outward FDI exceeded US$100b for the first time; and in 2014, China’s outward FDI grew level with inbound investment for the first time, indicating that China is on the verge of becoming a net exporter of capital, which will have an important and far-reaching influence on global capital movement.

In 2015, Chinese investors accelerated their “going out”. During the first half of 2015, China’s outward FDI totaled US$56b, a year-on-year increase of 29.2%, making it likely to outperform the expected outbound investment growth target of 10% for the year. China’s outward FDI is expected to continue to be about 10% in the next five years; and by 2025, China’s accumulated outward FDI is projected to have increased nearly three-fold to US$1.25t. China’s outward FDI is fully into the fast lane.

Chart 1: China’s outward FDI and inward FDI during 2005–2015*

This surging outbound investment is being fully supported by Chinese government policies. Since the government announced the “going out” strategy in 2000, China has issued policies that simplify administrative review, enhance financial support and improve public service support. With the acceleration of China’s economic transformation, “going out” is playing an especially important role in promoting the structural transition of the Chinese economy and easing downward economic pressure. This policy support has been developed to stimulate outbound investment.

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*China’s outward FDI (US$56b) from Jan to Jun of 2015 not included financial investment

Source: National Bureau of Statistics of China, Ministry of Commerce. Financial investment is not included in the data for 2006 or before; the data for 2015 is predicted by EY Knowledge.

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7 Source: National Bureau of Statistics of China
8 Source: Ministry of Commerce
9 Source: Ministry of Commerce
10 Source: “Seek sustainable development, the Asia-Pacific have wished dream - a speech at the APEC CEO Summit Opening Ceremony”
Meanwhile, with the enhancement of their capital and technical strength, more Chinese enterprises are seeking to use their resources worldwide, and to take advantage of the benefits of their global expansion. Outbound investment has become an essential method for enterprises to gain factors of production, improve innovation and core competitiveness, and realize an upstream shift in their industrial chain. In addition, after more than a decade of international expansion, many Chinese enterprises have gained experience in outbound investment strategies, risk management, post-M&A integration, and the development of management talent, all of which will provide them with more skills and resources in terms of “going out”. Supported by these developments, Chinese enterprises are expected to be able to expand their overseas operations more confidently and successfully, and become more active in the global capital market.

Global-focused optimization and diversification: The evolving spread of Chinese capital
With the gradual maturing of China’s outbound investment, the focus of this investment has shifted from neighboring countries, especially the developing ones, to developed countries further afield. Today, the footprint of Chinese investors covers 184 countries and regions, including resource-rich developing countries such as Brazil and South Africa, and developed countries such as the United States and the UK. In recent years, developed countries have had lower asset prices due to the European debt crisis, while Chinese enterprises’ investments have shifted to brand, technology and other high-end areas, making Europe and the US attractive destinations for Chinese investors looking for mergers and acquisitions.

11 Source: Ministry of Commerce
China's outbound investment

- North America (2)
  - Canada
  - The United States
  - 127.6

- Europe (1)
  - UK
  - Italy
  - France
  - 158.2

- South America (5)
  - Brazil
  - Argentina
  - 35.6

- Africa (6)
  - South Africa
  - 31.2

- Asia (3)
  - Singapore
  - Russia
  - Nigeria
  - Kazakhstan
  - India
  - 81.5

- Oceania (4)
  - Australia
  - New Zealand
  - 41.6

Source: Mergermarket, including outbound M&A in Hong Kong, Macao and Taiwan

Chart 3: Distribution of China's outbound M&A in 2005-2015 1H


Data Source: MergerMarket, including M&A deals of Hong Kong, Macau and Taiwan. Developed and developing country concept is in line with the United Nations’ World Investment Report is defined by UNCTAD in 2015.
The changes in the industrial distribution of the investment also show the gradual maturing of China’s outbound investment. China’s early overseas investments focused on acquiring energy, mining and other resource-oriented production factors. However, as the overseas investment has developed and Chinese enterprises have become more interested in investing further upstream in the industrial chain, the investment has become increasingly diversified. Industries such as technology, media and telecommunications, financial services, and the automotive industry have grown in popularity. The diversity in the outbound investment is increasing Chinese enterprises’ standing in these industries, and enhancing their influence in the global capital.

Chart 5: Overseas investment by Chinese companies is diversifying

Share of outbound M&A amount by industry in 2010

Share of outbound M&A amount by industry in 2014

Source: MergerMarket, including outbound M&A in Hong Kong, Macao and Taiwan
Leading by infrastructure, the “One Belt, One Road” initiative steadily moves forward

The “One Belt, One Road” action plan: From top-level conception to practical cooperation

Since President Xi Jinping proposed the idea of building the “Silk Road Economic Belt” and “21st-Century Maritime Silk Road” in 2013, the “One Belt, One Road” initiative has been upgraded to a national strategy and an important component of the new round of reform and opening up. At the end of March 2015, the guidance, Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road (“Vision and Actions”) was issued by the National Development and Reform Commission, Ministry of Foreign Affairs and Ministry of Commerce, indicating the official release of action plan of the “One Belt, One Road” initiative and marking the transition from top-level conception to practical cooperation.

Chart 6: Gradual progress in “One Belt, One Road” initiative

- In late 2013: The “One Belt, One Road” initiative was proposed
- In October 2014: Preparation of the Asian Infrastructure Investment Bank (AIIB) and Silk Road Infrastructure Fund was started
- In February 2015: The leading task force was established
- In March 2015: The Vision and Actions plan was unveiled

In the first half of 2015, the gross exports and imports between China and countries along the Belt and Road totaled US$485.4b, or 26% of the gross value of foreign trade, and China’s outward FDI in 48 roadside countries amounted to US$7.05b, or 15.3% of total investment, up 22% year on year.

Under the guidance of the Vision and Actions plan, the deployment of the “One Belt, One Road” initiative is accelerating. Various ministries and commissions, including the Ministry of Commerce and the Ministry of Transport, have introduced supporting plans and measures. The State Council has requested 34 provinces, municipalities and autonomous regions to complete the development of a specific implementation scheme by October 2015. In April 2015, the Silk Road Infrastructure Fund announced its first investment: the construction of the Karot hydropower project in Pakistan. In May 2015, the total size of RMB100b is expected to fund the Gold Silk Road to help integrate the gold resources along the Belt and Road so as to enhance China’s gold pricing power in the world. In addition, the preparation of the China-led AIIB has been steady. In June 2015, 50 countries signed the Articles of Agreement of the Asian Infrastructure Investment Bank. And the AIIB is planned to be established by the end of 2015.

Source: Ministry of Commerce

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12 Source: Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road, National Development and Reform Commission, March 2015.
14 Source: “List of energy projects of the ‘One Belt, One Road’ initiative was unveiled, Economic Information Daily, 16 June, 2015
15 Source: “Silk Road Infrastructure Fund makes first investment in Pakistan and plans to start construction by the end of 2015”, People.cn, 21 April 2015
17 Source: Ministry of Finance
A new wave of outbound investment is spearheaded by infrastructure construction

The “One Belt, One Road” initiative runs through more than 60 roadside countries in Europe, Asia and Africa, and is aimed at promoting cooperation in policy coordination, facilities connectivity, unimpeded trade, financial integration, and people-to-people bond. The infrastructure construction, energy, cultural tourism, high-technology industries and finance collaborations are, in particular, positive.

Facilities connectivity is a priority area for implementing the “One Belt, One Road” initiative, especially in transportation, energy and information sectors. The lack of such infrastructures in many Asian countries provides opportunities for mutually beneficial cooperation. Meanwhile, for China, the facilities connectivity plays an important role in strengthening the industrial structure, absorbing excess capacity, and ensuring energy security. It is estimated that the infrastructure construction investment of the “One Belt, One Road” initiative will total US$6t.

Chart 7: Key industries of the “One Belt, One Road” initiative

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<tr>
<th>Infrastructure</th>
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<tr>
<td>The Asian Development Bank (ADB) has predicted that Asia’s infrastructure construction will see a financing gap of US$8.3t during 2010-2020. China’s advantages in infrastructure construction, such as capital and technical advantages, will be extended to less-developed Asian countries.</td>
</tr>
<tr>
<td>The construction of several projects will be accelerated, including the transportation channels linking Asia and Europe, the high-speed railway of Southeast Asia, Central Southeast Asia and South Asia ports and information infrastructure construction.</td>
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<td>According to government work reports of provinces, the value of the infrastructure construction investment related to the “One Belt, One Road” initiative has amounted to US$1.04t, while the amount of transnational investment has amounted to US$52.4b.</td>
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<td>In May 2015, the State Council decided to further boost international cooperation in production capacity and machinery manufacturing in railway and electricity infrastructure, thus bringing a new wave of outbound investment.</td>
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<tr>
<th>Energy &amp; power</th>
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<tr>
<td>Many countries along the Belt and Road are rich in energy resources but have financial and technological constraints. The joint exploration, development, and construction of energy pipelines and power facilities offer vast potential for future development.</td>
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<td>China will promote the construction of a national energy resource distribution system and accelerate the export of power generation machinery.</td>
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<tr>
<th>Cultural tourism</th>
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<td>Along the Belt and Road, there are approximately 500 world cultural and natural heritage sites, but the development of tourism has been restricted by problems such as transportation, visa approvals, promotion and security.</td>
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<tr>
<td>China is encouraging enterprises to invest in tourism and improve infrastructure in the roadside countries. The China National Tourism Administration is developing over 200 key tourism projects for the “One Belt, One Road” initiative for the next three years and expects to send 150 million tourists to these countries in the next five years, which could contribute more than US$200b in revenue.</td>
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<tr>
<th>Industry cooperation</th>
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<tr>
<td>China has advantages in information technology, new materials and high-tech manufacturing (such as high-speed railways and nuclear power), so some less-developed neighboring countries are expected to benefit from China’s manufacturing technology.</td>
</tr>
<tr>
<td>According to Ministry of Commerce statistics, Chinese entities are currently constructing more than 70 economic and industrial cooperation zone projects in roadside countries, with an annual production value of more than US$20b.</td>
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<tr>
<th>Financial cooperation</th>
</tr>
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<tbody>
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<td>The “One Belt, One Road” initiative will create a huge demand for financing, bonds, insurance and asset management.</td>
</tr>
<tr>
<td>The government has recently unveiled a series of policies to encourage the financial sectors to help enterprises to implement the “going out” strategy. In April 2015, the Silk Road Infrastructure Fund announced its first investment and in June 2015, 50 countries led by China entered into an AIIB agreement.</td>
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Source: STCN, www.gov.cn

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Recent developments: High-level visits and free trade zone construction to boost the “One Belt, One Road” initiative

From this year, taking full advantage of recent high-level visits, the Chinese government has kept promoting the “One Belt, One Road” initiative. According to statistics, in 2015, over 12 countries have participated in the “One Belt, One Road” initiative through research, investigation and project promotions. 

Chart 8: List of recent high-level visits and agreements

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<thead>
<tr>
<th>Date</th>
<th>Visit</th>
<th>Agreement or cooperation intention</th>
</tr>
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<tbody>
<tr>
<td>June and July</td>
<td>Premier Li Keqiang visited France and Belgium</td>
<td>China, France and Belgium advanced China-EU strategic development cooperation, including the “One Belt, One Road” initiative and the EU “Juncker Investment Plan” totaling EUR315b</td>
</tr>
<tr>
<td>June 2015</td>
<td>Foreign Minister Wang Yi visited Hungary</td>
<td>Hungary became the first European country to sign the “One Belt, One Road” cooperation documents with China, and will jointly promote the construction of major projects such as Hungary-Serbia railway</td>
</tr>
<tr>
<td>May 2015</td>
<td>Premier Li Keqiang visited four Latin American countries: Brazil, Colombia, Peru and Chile</td>
<td>China will set up a “special fund of Sino-Latin American production capacity cooperation” of US$30b to support cooperation projects in capacity and machinery manufacturing fields; China, Brazil and Peru started a feasibility study on the construction of a railroad linking the Atlantic and Pacific Oceans; and China Development Bank (CDB) signed Memorandums of Understanding on infrastructure cooperation with Brazil, Colombia and Chile, encouraging the machinery manufacturing industry to “go out”</td>
</tr>
<tr>
<td>May 2015</td>
<td>The Prime Minister of India Narendra Modi paid an official visit to China</td>
<td>China and India issued a joint statement to strengthen the cooperation in the implementation of the “One Belt, One Road” initiative and the construction of BCIM (Bangladesh, China, India and Myanmar) Economic Corridor</td>
</tr>
<tr>
<td>May 2015</td>
<td>President Xi Jinping visited Kazakhstan, Russia and Belarus</td>
<td>China and Russia signed Joint Statement on the cooperation of the Silk Road Economic Belt construction and the Eurasian Economic Union establishment; China and Kazakhstan decided to accelerate the economic strategy cooperation of the Silk Road Economic Belt and the “Shining Path”, (Kazakhstan's infrastructure development program in response to the global financial crisis); and China and Belarus agreed to make the China-Belarus Industrial Park project the landmark project of the Silk Road Economic Belt</td>
</tr>
<tr>
<td>April 2015</td>
<td>President Xi Jinping visited Pakistan</td>
<td>China and Pakistan signed an investment plan package including nuclear energy, the China-Pakistan Economic Corridor project and the construction of Gwadar Port, totaling around US$46b</td>
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Source: Online news, collected by EY

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15 Source: “More than 12 countries responding to the “One Belt, One Road”, project promotion is the main method”, People.cn, http://finance.people.com.cn/n/2015/0610/c1004-27128806.html, 10 June 2015
16 People.cn, Sina, CRonline, CHINA ECONOMIC NET, Hexun.com, April-July 2015
China outbound investment is being supported by frequent high-level visits. During Premier Li Keqiang’s visit to Brazil in May 2015, several major initiatives were commenced: The Industrial and Commercial Bank of China (ICBC) and Caixa Economical Federal, the top mortgage lender in Brazil, established a US$50b investment fund for infrastructure projects; the China Development Bank (CDB), the Export-Import Bank of China (EXIM bank), ICBC and Petrobras signed a US$10b financing agreement; and the Bank of Communications is acquiring an 80% stake in Banco BBM SA (Brazilian bank) for US$174m22. During the visit to China of India’s Prime Minister Narendra Modi in May 2015, CDB, ICBC and Bharti Airtel, the telecom service provider in India, agreed to provide US$2.5b in long-term credit to Bharti Airtel23. Moreover, the construction of free trade zones, as important vehicles that drive trade cooperation along the Belt and Road, is accelerating, and China has signed 13 free trade agreements involving 21 countries and regions24. In May 2015, the State Council issued a document with the intention of strengthening top-level design between the building of free trade zones and the “One Belt, One Road” initiative. The Ministry of Commerce also expressed it would advance the negotiations on the China-ASEAN Free Trade Zone upgrade, China-Sri Lanka Free Trade Zone, and China-GCC Free Trade Zone25. The acceleration of the free trade zone development will boost the economic and trade exchanges among the countries more effectively, and facilitate Chinese enterprises’ “going out”.

Risk prevention: An ambitious strategy also requires cautious planning

With the blueprint of the “One Belt, One Road” initiative unveiling a clear vision for the future, enterprises should however not neglect the possible challenges when making their overseas investments. Because of the complex geopolitics and widely different political, economic and regulatory environments in the countries along the Belt and Road, the “going out” journey contains tremendous risks. These risks include the uncertainty in the target country’s political security as well as the corporate operational risk. Chinese enterprises have learnt from the following incidents: The Sino-Thai Railway has been affected by the instability in Thailand, the construction of the Myitsone Hydropower Project in Myanmar was suspended due to NGO opposition, and the new Sri Lankan government suspended the Colombo Port City project approved by the former government. Chinese enterprises, before going overseas, should be fully aware of the political and economic environments of the countries along the Belt and Road, and assess the risks and be prepared at the institutional level to respond to all kinds of difficulties.

Chart 9: Enterprises need to respond cautiously to avoid risks

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22 Source: “The first achievement of the Premier’s visit to Latin America: US$27b orders were signed covering railway, hydropower, etc.”, China Daily, 21 May 2015
23 Source: “India’s largest telecom operator was guaranteed a US$2.5b loan by Chinese-funded banks”, China Economic Net, 16 May 2015
24 Source: “China has signed free trade agreements with 13 countries”, Xinhuanet, 16 June, 2015
26 Source: Ministry of Commerce

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9
Financial sector help pave the way for overseas expansion

Enterprises need financial support for overseas expansion

Obtaining appropriate financial support is crucial for enterprises when making outbound investments. Overseas investments, especially large ones such as infrastructure investments, require substantial financial support; and financing difficulties and insufficient financing channels can act as a constraint. Furthermore, as these outbound investments mature, the needs for financial demands broaden from traditional services such as loans, deposits, and settlements to investment banks and intermediary business, risk control and financial management. Financial institutions will not only help enterprises establish a global presence, but also perform the important task of guiding and protecting them when they enter foreign markets.

As China will develop into a capital exporter, enterprise demand for financial services will increase. With the gradual implementation of the “One Belt, One Road” initiative and the acceleration of international capacity and equipment cooperation, the projects with high financing and other service demands are moving forward, highlighting the importance of financial support.

Numerous policies encourage the financial system to assist enterprises’ “going out”

Outbound investment even if supported by the internationalization of the financial sector cannot be realized without vigorous financial system reform and policies. In recent months, policies encouraging the financial system to support “going out” have been introduced. In December 2014, the State Council required the financial system to support enterprise “going out” through three core aspects: simplifying approval procedures, expanding access to funding, and perfecting the policy system. In March 2015, the China Banking Regulatory Commission revised its Guidelines for the Risk Management of Merger and Acquisition Loans Granted by Commercial Banks, relaxing the multiple restrictions on lending merger and acquisition loans. The paper Made in China 2025 and Guiding Opinions of the State Council on Promoting the Cooperation between International Capacity and Equipment Manufacturing issued in May 2015 also required institutions to strengthen financial support and improve the export credit insurance, thereby providing strong support for the “going out” of made-in-China items and the machinery manufacturing industries. Meanwhile, China is actively promoting the development of the Asian Infrastructure Investment Bank, the Silk Road Fund and other policy-based financial institutions. Furthermore, free trade zones in Shanghai, Guangdong, Tianjin and Fujian and the pilot Qianhai financial zone have been set up, and the implementation of pilot financial reforms in these zones will give strong impetus to financial innovation and “going out”.

Chart 10: Three core financial support-measures to accelerate the “going out” of enterprises

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<th>Simplify approval procedures</th>
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<td>Remove the registration system for foreign exchange management for overseas investment (handled directly by the banks instead)</td>
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<tr>
<td>Lift the geographic restrictions for Renminbi bonds issued overseas</td>
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<tr>
<td>Simplify the approval procedures for overseas listing, merger and acquisition, and the establishment of bank branches</td>
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<th>Expand access to funding</th>
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<td>Encourage banks to increase financial support for major machinery design, manufacturing and the whole industry chain</td>
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<td>Promote the multiple use of foreign exchange reserves, let policy banks play their roles, and absorb social capital to provide long-term financial support by means of bond and fund issuance</td>
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<th>Perfect policy and system</th>
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<tr>
<td>Improve the Renminbi cross-border payment and settlement system</td>
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<td>Steadily release short-term export credit insurance, and increase the number of business entities</td>
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<tr>
<td>Innovate in export credit insurance products, develop overseas investment insurance, reduce premiums appropriately, and expand policy insurance coverage</td>
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Source: Executive meeting of the State Council, 24 December 2014
**Chart 11: Chinese-led multilateral development financial institutions and development, policy banks power the “One Belt, One Road” initiative**

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<tr>
<th>Organization Name</th>
<th>Introduction</th>
<th>Recent news</th>
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| Asia Infrastructure Investment Bank      | • This is an inter-governmental Asian regional multilateral development institution, focusing on infrastructure  
• China proposed it in 2013; 50 countries formally signed the agreement in June 2015; it is expected to start by the end of 2015  
• The authorized capital is US$100b, and China is committed to providing an initial investment of US$50b | • In June 2015, 50 countries signed the “Agreement on the Asian Infrastructure Investment Bank” in Beijing. China accounted for 30% of the subscribed shares, has 26% of the voting rights |
| Silk Road Fund                           | • It’s a long-term development investment fund dedicated to promoting economic and social development and interconnection among the countries along the “One Belt, One Road”  
• It was established by the Chinese government at the end of 2014 and launched the first phase of funding of US$10b, co-financed by China’s foreign exchange reserves, China Investment Corporation, the Export-Import Bank of China, and China Development Bank  
• It was positioned as open-end funds, taking equity, debt, loans, funds and other diversified investment and financing method | • In April 2015, the Silk Road Fund, the Three Gorges Group and the Private Power and Infrastructure Committee of Pakistan signed an agreement to jointly develop Pakistan Card Lott Station with a total investment of US$1.65b. This is the first foreign investment project funded by Silk Road Fund, and is expected to start construction in 2015, and be in operation in 2020 |
| BRICS New Development Bank               | • This is an international multilateral financial institution, mainly providing funding for developing countries’ infrastructure needs, and is also a supplement of the existing international financial security system  
• In July 2014, the BRICS countries signed an agreement to initiate the establishment, and it was opened in the same month.  
• The initial capital is US$100b, funded by the member states evenly, and headquartered in Shanghai | • In July 2015, the BRICS New Development Bank opening ceremony was held in Shanghai. It is expected to start operation by the end of 2015 or early 2016 |
| China Development Bank (CDB)             | • This is a Chinese government development-oriented financial institution, dedicated to finance infrastructure development, construction and development of basic and pillar industries  
• It was founded in 1994. By the end of 2014, its total assets exceeded Rmb101t, making it the largest development-oriented financial institution in the world | • In April 2015, the State Council announced CDB reform program, positioning CDB as a development financial institution and pledged the Central Bank will inject supplementary capital to the CDB. In July 2015, it was reported that the Central Bank injected US$48b  
• The CDB has set up a project library for the “One Belt, One Road” initiative, involving 64 countries, about 900 projects, investment over US$800b. By the end of 2014, the CDB had funded more than 400 projects related to the initiative, totally lending loans US$125.9b |
| The Export-Import Bank of China          | • It’s a Chinese governmental policy financial institution, providing financial services for mechanical and electrical equipment, high-tech product import and export, foreign project contracting and foreign investment  
• It was founded in 1994, with more than 20 business branches in China, and a Paris branch, and representative offices in St. Petersburg and Eastern & Southern Africa | • It was reported that in July 2015 the Central Bank injected US$45b into the Export-Import Bank of China. This strong capital support is to boost the “One Belt, One Road” initiative.  
• Over the past year, the Export-Import Bank of China significantly increased the capital investment to countries along the Belt and Road, with more than 300 new projects signed in 2014, an increase of 68% of the contract amount, and the cumulative amount of payments increased by 15% |

Source: People’s Daily reports (March-July 2015), China Development Bank, Export-Import Bank of China
In addition, the deeper intergovernmental financial cooperation and the internationalization of the Renminbi will help reduce the resistance from host regulators and create a good environment for financial internationalization. China attaches great importance to promoting financial cooperation between governments and actively participates in the development of the international financial regulatory systems and policies. In 2016, China will hold the G20 presidency, and is expected to play an expanded role in promoting international financial cooperation. In the meantime, Renminbi internationalization has seen rapid progress, with Renminbi settlement amounts in 2014 up 41.6% year-on-year, and Renminbi settlement amounts for foreign investment and attracted foreign investment up 117.9% and 92.4%, respectively. By the end of 2014, the Chinese Renminbi had become the world’s second most-used currency in trade finance, the fifth most-used currency for payment and the sixth most-used currency for foreign exchange transactions.\(^\text{26}\) In 2015, the pace of Renminbi internationalization has further accelerated, except Hong Kong, Macao and Taipei, the number of offshore Renminbi clearing banks has risen to 14 in July 2015. In early July, the Central Bank eased the restrictions on foreign institutions’ investing in the interbank market, and is considering promoting a Shenzhen-Hong Kong Stock Connect program, and modifying the regulations for exchange control and other measures\(^\text{27}\) With the progressive development of the Asia Pacific free trade zone, the regional economic and financial cooperation represented by the “One Belt, One Road” initiative, and China’s financial liberalization reform, Chinese financial institutions will experience a smoother road to overseas investment.

**Chart 12: List of offshore Renminbi-clearing banks**

Source: The People’s Bank of China, Annual Report on the Internationalization of Renminbi (2015); collected by EY Knowledge, excluding Hong Kong, Macao and Taiwan areas


Financial institutions join hands with enterprises in overseas expansion

Enterprises’ increasing financial service needs and the policy support are driving Chinese financial institutions to accelerate their overseas expansion. In 2015, all the major banks have quickened their establishment of overseas branches. For example, the Bank of China (BOC) plans to increase the number of branches in the countries along the Belt and Road from 20 to 36, which means a presence in over 50% of them. The China Construction Bank established four European branches in the first half of 2015 and is applying to establish branches in Chile, Switzerland, Malaysia and other countries. Meanwhile, all the financial institutions are innovating so as to provide better financing support for enterprises. For example, the BOC announced that it will strive to support the “One Belt, One Road” initiative with loans totaling US$100b in the next three years. In June 2015, it issued offshore bonds totaling US$4b, which is the largest-ever bond issued by Chinese banks.

Overseas M&A activity in the Chinese financial industry is also surging: M&A activity in the first half of 2015 amounted to US$3.71b, almost 100% year-on-year growth. Insurance companies and other non-bank financial institutions are also actively expanding overseas. Recently, China Minsheng Investment Co., Ltd. planned to acquire 100% shares of Sirius International Insurance Group for US$2.2b, Fosun Group acquired 20% shares of Ironshore (an insurance company in the USA) for US$0.5b, and Anbang Insurance Group acquired 63% shares of Tong Yang Life Insurance for US$1b. Insurance capital’s “going out” will help to facilitate more comprehensive financial services such as overseas investment insurance, export credit insurance, and specific contract insurance for other Chinese companies doing overseas investment and will efficiently decrease the foreign exchange risks and set up a better financing platform for them.

Chart 13: M&A deals of financial services in mainland China (1H of 2014 vs. 1H of 2015)

Source: MergerMarket, EY Knowledge analysis

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31 Source: MergerMarket, Collected by EY Knowledge
However, the reform of the Chinese financial system moves slowly and the internationalization and specialization level of financial institutions is far lower than their peers in developed countries, making it difficult to provide strong support for the enterprises’ global expansion and even constraining enterprises’ outbound investment. Chinese overseas investment has spread to over 184 countries and regions around the world; however, Chinese-funded banks currently have a business presence in only 53 countries or regions. Furthermore, domestic financial institutions mainly provide traditional services such as guarantees, making it almost impossible for them to meet the demands of outbound investment and satisfy the needs for long-term wholesale financing, and engage in M&A and capital operations. In addition, the international influence of Chinese financial institutions is limited, resulting in low credit ratings and high financing costs for enterprises.

In light of the enormous opportunities produced from the enterprises’ “going out” strategy, Chinese financial institutions are required to speed up their expansion overseas, develop multiple financing channels, tailor their services and products for industry needs, and provide all-round financial services including financing, investment banking, risk control, and financial management. In this way they can become powerful enablers and partners for enterprises’ “going out” and develop into strong global companies alongside these enterprises.

**Chart 14: Soundly prioritize the development of financial institutions for serving Chinese enterprises’ globalization**

<table>
<thead>
<tr>
<th>Define the international strategy, improve expansion overseas</th>
<th>Optimize the business structure, quicken financial innovation</th>
<th>Adapt to the regulatory environment, strengthen risk prevention and control</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Define the international strategy, steadily select appropriate regions and build financial channels along “one Belt, One Road”</td>
<td>• Develop asset management, investment banking and other emerging business and enhance the professional abilities so as to provide more financing channels and higher level financial services</td>
<td>• Enhance the abilities for risk management, innovate risk management tools, adapt to international standards and regulatory environment and develop differentiated business processes and risk strategies specific to the market and industry</td>
</tr>
<tr>
<td>• Improve the system of global RMB clearing network and support construction of the offshore RMB market</td>
<td>• Innovate financial products and provide more and more complicated structured products and targeted products tailored for industry investment needs for customers</td>
<td></td>
</tr>
<tr>
<td>• Properly select the expansion method and enter the market step by step through establishing branches, M&amp;A or other methods according to the host countries market and regulatory environment</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Expand overseas to realize coexistence and co-prosperity of emerging markets

Invest in Latin America—with bright cooperation prospects in infrastructure and other sectors

China and Latin American countries have always had good relationships in economy, trade and investment. In 2010, China’s outward FDI in Latin America exceeded US$10b. Since then, except for year 2012, China’s outward FDI in Latin America has been increasing, and exceeded US$10b every year. According to the report “Economic cooperation between China and LAC (Latin America and Caribbean) has entered a new era” released by the United Nations Economic Commission for Latin America and the Caribbean (the “LAC Economic Committee”), between 2010 and 2013, 90% of China’s direct investment in Latin America are energy and resource projects. In 2014, China’s investment in Latin America continued to grow, and also has increasing number of M&A deals. China Minmetals Cooperation acquired Las Bambas of Peru for US$7b, and CNPC acquired Petrobras Peru for US$2.6b.

Chart 15: 3×3 Mode

Aim at promoting the transformation and upgrade of China-Latin America cooperation with production capacity cooperation as a breakthrough.

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36 Source: Ministry of Commerce, National Bureau of Statistics
In 2013 and 2014, China’s President Xi Jinping visited Latin America, unveiling a new era of China-Latin American cooperation. In January 2015, in the first ministerial meeting of the China-CELAC Forum, President Xi Jinping said that China will invest US$250b in Latin America over the next decade. By the end of 2014, China’s direct investment stock in Latin America was US$98.9b. The meeting also approved the Planning for China-CELAC Cooperation (2015-2019), stating that China and Latin America will cooperate in 13 key areas, including politics & security, trade & investment, infrastructure construction, energy, agriculture, technology, education, culture & tourism, environmental protection, etc.

In May 2015 China’s Premier Li Keqiang made a successful visit to four Latin American countries, and explored new prospects of China-Latin American cooperation in economy and trade. During his visit, China and the four Latin American countries proposed “3×3 mode”, initiated the “Railroad linking Atlantic and Pacific Oceans” project and further discussed cooperation in “Tunnel linking Atlantic and Pacific Oceans” and other projects. China also signed nearly 70 cooperation framework agreements in energy, minerals, infrastructure, and technology sectors, and proposed to establish a mutual fund for China-Latin American production capacity cooperation. Infrastructure construction and production capacity cooperation will become key areas for future China-Latin American economic cooperation.

However, Chinese enterprises need to recognize there will be challenges in investing in Latin America. Imperfect laws and regulations in some areas, lack of effective governmental supervision, plus Chinese investors’ less experience in local economic environment, policies and culture will all cause potential investment losses.

China has established a sound relationship with some countries in Latin America at the government level, and built in a bridge for investment. Chinese enterprises should extend their investment focus beyond the energy and resource sectors to include manufacturing, services, and infrastructure construction, so as to maximize China’s investment effects on Latin America. At the same time, they need to pay more attention to the laws and regulations related to the local environment, to strengthen their social responsibility, and to employ a larger number of local people with more training programs provided, in order to achieve a win-win result for both investors and investment destinations.

**Chart 16: Railroad linking Atlantic and Pacific Oceans and Tunnel linking Atlantic and Pacific Oceans**

**Railroad linking Atlantic and Pacific Oceans:** It’s a railroad cross the South American continent linking the Atlantic and Pacific coasts. In May 2015, China and Brazil signed a joint action plan for the next five years and decided to initiate a basic feasibility study on the project.

**Tunnel linking Atlantic and Pacific Oceans:** It’s also called “Aconcagua Bi-Oceanic Center”, refers to the railroad and tunnel through the Andes linking Chile and Argentina. The Chinese government will support Chinese enterprises to cooperate with Chile in the project and start to perform a feasibility study as soon as possible.

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40 “3×3 mode”: China-Latin America production capacity cooperation “3x3” mode, refers to Chart15.
Brazil, China’s largest investment destination in Latin America

Brazil is the world’s seventh largest economy. Like China, it is an important emerging country, a G20 member, and one of the BRICS countries. It is also the first Latin American country to establish a comprehensive strategic partnership with China. In March 2015, Brazil became a member of AIIB, making it the first AIIB founding member from Latin America. Since 2011, the changing international environment, economic stagnation in developing markets like the Euro zone, falling prices of raw materials and decreasing trade demands, coupled with problems such as high interest rates, high taxes and insufficient investment in Brazil’s economy, have restricted its economic growth. Nevertheless, its economic and market scale make it the largest investment destination on the continent. In the mid and long term, Brazil has huge economic development potential.

The Brazilian government is also promoting policies to attract foreign investment to boost domestic construction and economic development. In 2010, it introduced the second phase of the Growth Acceleration Program (PAC 2), which stated the following: During 2011-2014, investment of BRL1.59t (US$950b) covered public healthcare, urban street construction, medical and educational facilities, residential construction, utilities; highway, railway, port, airport and other transportation projects; as well as energy projects such as power generation, oil and natural gas. To make preparations for the upcoming Rio 2016 Olympics, it is expected that governments at all levels will invest BRL24b (US$11b) to improve urban transportation infrastructure and sustainability. In June 2015, the Brazilian government announced further transport infrastructure investment, including a number of franchised roads, airports, railways, ports and other large projects, of up to BRL198.4b (US$64b), aimed at benefiting more than 130 cities in 20 states in Brazil.

Brazil’s infrastructure market is currently going through a very unique period. Although the Brazilian government urgently needs to improve infrastructure construction, and they have launched a series of investment plans, due to the higher financing costs, the pace of infrastructure development in Brazil is slow. As Brazil’s economy develops, the gap between supply and the actual infrastructure needs widens. Brazil has recently established many long-term franchise programs in airports, roads, ports and power-generation facilities. These programs allow both private and foreign capital to be invested and operate, and financial support is given to investors through policy banks in Brazil at a lower interest rate. Also considering the currency devaluation led to a lower value of the assets for foreign investors, investing in Brazil is undoubtedly a good choice.

Chart 17: Profile of Brazil

- **Location:** Central and coastal South America
- **Population:** 202m
- **Major cities:** The capital-Brasilia, the largest city-São Paulo, and the 2nd largest city-Rio de Janeiro
- **Official language:** Portuguese
- **GDP of 2014:** BRL5.529t (approximately US$1.77t), **per capita GDP of 2014:** BRL27, 200 (approximately US$8,700)

Source: Instituto Brasileiro de Geografia e Estatística (IBGE)

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43 Source: Brazil’s implementation of the new round infrastructure investment planPeople’s Daily, 11 June 2015
Brazil is China's tenth largest trading partner globally, and is China's largest trading partner, and the largest investment destination and second largest engineering contracting market in Latin America. By the end of 2014, China's investment in Brazil totaled US$18.94b⁴⁴. In May 2015, during Chinese Premier Li Keqiang's visit to Brazil, the two governments signed the 2015-2021 Joint Action Plan as well as several cooperation documents related to railway, electricity, agriculture, petroleum equipment, shipping, quality control, nuclear energy, finance, technology, aerospace, sports, and the internet. They also signed a memorandum of understanding for a project feasibility study for the “Railroad linking Atlantic and Pacific Ocean”⁴⁵. With the implementation of these projects, China’s investment in Brazil will begin a new chapter.

**Chart 18: Brazilian major taxes**

<table>
<thead>
<tr>
<th>Tax category</th>
<th>Taxation jurisdiction</th>
<th>Tax nature</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate income tax</td>
<td>Federal tax authorities</td>
<td>Brazilian companies are required to pay corporate income tax and social expenses on global revenue.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- For the corporate income tax, the total amount of taxable income of BRL240,000 (approximately US$117,000) or less, the rate is 15 percent; more than BRL240,000 section above, additional levy of 10%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- For general corporate social expenditure fee, the rate is 9%; for the financial, personal insurance companies and capital companies, the rate is 15%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Based on the above, the actual tax burden of enterprises that made profits is about 34%</td>
</tr>
<tr>
<td>Social expenditure costs</td>
<td>Federal tax authorities</td>
<td>Brazilian tax residents from all over the world are required to pay personal income tax. Brazilian non-tax residents are only subject to personal income tax on their income from Brazil; personal income tax in Brazil uses a progressive system (0%, 7.5%, 15%, 22.5% and 27.5%)</td>
</tr>
<tr>
<td>Personal income tax</td>
<td>Federal tax authorities</td>
<td>According to general rules, there is a levy on imported goods and transactions involved in the production of products. Exported goods are exempt from the industrial products tax; depending on the product, the tax rate ranges from 0-365%</td>
</tr>
<tr>
<td>Industrial products tax (i.e., federal VAT)</td>
<td>Federal tax authorities</td>
<td>There is a levy on imported goods, the local sales of goods and provision of transport, telecommunications and electricity services. Interstate transactions are also subject to goods and services tax. Exported goods and services are exempted from the general circulation tax; but there is a tax rate ranging from 0% -25%, depending on the state of the trading parties</td>
</tr>
<tr>
<td>Circulation of goods and services tax (i.e., state VAT)</td>
<td>State tax authorities</td>
<td></td>
</tr>
</tbody>
</table>

Source: EY Tax analysis based on Brazil tax laws and regulations

**Chart 19: Brazil's need for infrastructure investment in the next ten years (US$billion)**

- **Power:**
  - 32,971 megawatt power supply
  - 23,200 km transmission line
  - **Total: 64.4**

- **Railway:**
  - 10 railway lines
  - covering 12,000 kms
  - **Total: 39.6**

- **Urban transportation:**
  - Growth acceleration plan of urban transportation funded by federal government
  - São Paulo metro program
  - Rio de Janeiro urban transportation system
  - **Total: 35.4**

- **Oil and Gas:**
  - 3 franchised projects
  - **Total: 34.8**

- **Ports:**
  - Invest in ports in 16 states covering franchised operation of public ports and management and trawlers of private ports
  - **Total: 23.8**

- **Expressway:**
  - 9 federal expressways covering over 7,500 kms
  - **Total: 18.3**

- **High-speed rail:**
  - Rio to Campinas via São Paulo
  - Galeo International Airport
  - Confins International Airport
  - **Total: 15.5**

- **Airport:**
  - **Total: 8.1**

Source: Ministry of Finance of Brazil

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⁴⁴ Source: Ministry of Foreign Affairs of the People's Republic of China
Natural resources and vast domestic market draw Chinese Investment to Russia

Russia, the world’s largest country by area, and one of the world’s largest economies, bridges Europe and Asia. China and Russia are both permanent members of the UN Security Council and BRICS members. After the 2008 global financial crisis, Russia is making good progress in its economic recovery. And currently its increasing industrial capacity, infrastructure construction and privatization are offering opportunities for global investors. Russia, which formally joined the WTO in 2012, has been relaxing its restrictions in both domestic and foreign investments to attract and encourage foreign and private capital investments in Russia\(^46\). Recently, Russia has been showing more interest in economic development in Asia and its leadership is seeking better relations with its eastern neighbors and new partnerships. According to data from China’s Ministry of Commerce, in 2013 Russia was the sixth-largest destination for China’s outbound investment, and based on data from the Central Bank of Russia, China’s outbound investment in Russia totaled US$1,280m in 2014. For 2011 to 2014, the CAGR of China’s investment in Russia was 117\(^%\)\(^47\).

<table>
<thead>
<tr>
<th>Source</th>
<th>Date of Publication</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central Bank of Russia</td>
<td></td>
<td>Source of statistical data</td>
</tr>
<tr>
<td>Ministry of Commerce, China</td>
<td></td>
<td>Source of statistical data</td>
</tr>
<tr>
<td>EY survey Perspectives from China</td>
<td>June 2015</td>
<td>Source of survey data</td>
</tr>
</tbody>
</table>

Historically, China has been Russia’s biggest trading partner in Asia: Trade between the two countries has grown steadily, and in 2014 totaled US$88.4b\(^48\). Russia and China have increasingly used the ruble and yuan in bilateral trade, and this trend is expected to continue as the yuan moves towards becoming one of the world’s reserve currencies and the relationships between the two countries deepen. According to the EY survey Perspectives from China: How concerns about the Russian market influence Chinese investment strategies, published in June 2015, 91\% of Chinese businesses with annual revenue over US$33m consider the Russian market attractive for investment. 66\% of respondents are attracted by Russia’s natural resources, while 62\% see potential in the domestic market\(^49\).

Chart 20: General information

- Territory: 17,125,407 sq.km
- Population: 146.3m
- Inflation (2014): 7.8%

Sources: Federal State Statistics Service of Russia, Oxford Economics; yellow highlight areas are special economic zones.
Thanks to its location, Russia is able to become an integral part of the “One Belt, One Road” initiative. Russia has already taken steps in this direction by introducing 17 special economic zones for business. Additionally, there are plans to set up 14 advanced development zones in Russia, which are meant to drive Asian investment into the region.50

**Special economic zones (SEZ)**

There are 17 special economic zones of four types in Russia: industrial, technological, tourist and logistical. They offer the following benefits:

- Income tax rate is 0-13.5% instead of 20%
- Property, transport tax exemption (up to 15 years)
- Land tax exemption (up to 10 years)
- Income tax exemption (to cluster companies residents)
- Special customs regime

**Advanced development zones**

Additionally, there are plans to set up 14 advanced development zones in Russia. Significant tax benefits will be offered to the residents of these zones in the Russian Far East:

- Zero profits tax rate (federal portion) for 10 years
- The regional portion of profits tax will be capped at 5%
- Social taxes will be cut to 7.6% of payroll (vs the standard rate of 30%)
- Exemption from regional assets tax and land tax
- Preferential treatment in connecting to infrastructure in these zones

The management of the advanced development zones will be via a management company set up for this purpose and controlled by the Ministry for Development of the Russian Far East

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50 Source: Russian Ministry of Far East Development
As part of the “One Belt, One Road” strategy, progress is being made on several major infrastructure projects in Russia. During Chinese Premier Li Keqiang’s visit to Russia in October 2014, the Russian Ministry of Transport, Russian Railways Corporation, China’s National Development and Reform Commission (“NDRC”), and China Railway Company signed a memorandum of understanding regarding high-speed rail. In addition, the railway companies from China and Russia signed a research and a design contract for a 770 km high-speed rail project between Moscow and Kazan in June 2015, which is China’s first “going out” high-speed rail contract. This indicates that high-speed rail cooperation between China and Russia has taken a substantial step forward.

In May 2015, Chinese President Xi Jinping visited Russia, and during his visit, the two sides issued a joint statement regarding the connection and development of the special economic zone of the Silk Road and the Eurasian Economic Union. President Xi Jinping said China would promote mutual investment facilitation and cooperation in capacity transition and build industrial parks and cross-border economic cooperation zones. China and Russia will enhance their interconnection in logistics, transport infrastructure, multimodal transport and other areas, and the two countries will also strengthen their financial cooperation and achieve currency swap to promote regional economic integration. According to forecasts by the Russian Ministry of Economic Development, Chinese outbound investment in Russia will rise six-fold by 2020. With the acceleration of the implementation of the “One Belt, One Road” strategy, we have reasons to foresee further developments in bilateral cooperation.

**Chart 21: 32 deals signed with total value of US$25b during President Xi’s visit to Russia**

- **Infrastructure**: China provides Russia billions of dollars in infrastructure loans, including financing of Rubles 300b (about US$6b) for Moscow - Kazan high-speed railway construction projects; China Civil Engineering Group, a subsidiary of China Railway Construction signed MOU on railways and Far East port projects with Tuva Energy Industrial Corporation.
- **Energy**: Gazprom and China National Petroleum Corporation signed an MOU to build a gas pipeline to China, with the sales volume of 30 billion cubic meters of natural gas per year.
- **Finance**: Sberbank and China Development Bank reached a Rmb 6b of credit agreement; Russian Direct Investment Fund and CITIC Investment Management Co., Ltd. signed an agreement to establish Russia-China Investment Bank.
- **Aviation**: Russian Helicopters Company and China Aviation Industry Corporation signed a cooperation framework agreement for heavy helicopter project; Russia Joint Investment Fund, the United Aircraft Manufacturing Corporation will cooperate with Chinese investor to establish a leasing company to promote 100 Russian-made civil aircraft in China.

Source: People.cn

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51. Source: “China is willing to give priority to the implementation of the Moscow Kazan high-speed rail project”, Xinhuanet.com, http://news.xinhuanet.com/world/2014-10/16/c_127106395.htm, 16 October 2014


The Chinese and Russian governments are cooperating closely, but the main parties involved still need to work hard in order to implement deeper cooperation. Foreign investment in Russia may also encounter some obstacles. According to a recent survey conducted by EY, the rule of law, uncertain macroeconomic environment, lack of investment guarantees, corruption, sanctions by the West and geopolitical complexities are issues of concern to Chinese investors. These investors also consider the labor costs, access to technology, regulatory and tax environment, and infrastructure are less attractive elements for foreign investors. Investors should be fully prepared before entering the Russian market, and seek professional advice when necessary.

Chart 22: Five tips for investing in Russia

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1</strong></td>
<td><strong>Thoroughly research Russian laws, taxes and practices of doing business in the target segment</strong></td>
</tr>
<tr>
<td></td>
<td>It is vital to study the legal and taxation system of Russia prior to investing in order to understand how to do business in a certain industry and to explore the potential limitations, e.g., investing in strategic targets, or the available liberalizations such as tax relief for investors in priority development territories and zones. Also, it is worth analyzing the current trends in the legal and tax spheres due to the frequent changes in Russian law to foresee possible amendments and avoid losing capital in the near future.</td>
</tr>
<tr>
<td><strong>2</strong></td>
<td><strong>Establish dialogue with local authorities and partners</strong></td>
</tr>
<tr>
<td></td>
<td>The principle “it's not what you know, but who you know” holds true for Russia. For successful investment and further business development, it is essential to communicate with Russian counterparts regularly, listen carefully, and be clear and concise about your plans; this should lead to solid business relationships based on mutual trust and respect.</td>
</tr>
<tr>
<td><strong>3</strong></td>
<td><strong>Think over divestment strategies beforehand</strong></td>
</tr>
<tr>
<td></td>
<td>Anyone interested in investing in Russia should think over all the possible ways of divesting and getting back their capital when structuring their investment, as changing a business structure in Russia requires money, time and effort.</td>
</tr>
<tr>
<td><strong>4</strong></td>
<td><strong>Create a detailed business plan and integration approach</strong></td>
</tr>
<tr>
<td></td>
<td>Some Chinese investors expect they can operate in Russia using the business plans and integration approaches they have successfully used elsewhere. However, Russian business has its specifics which have to be taken into account ranging from the law to cultural differences, which means a proper business plan for investing in Russia may take months, not days to draft.</td>
</tr>
<tr>
<td><strong>5</strong></td>
<td><strong>Think long-term</strong></td>
</tr>
<tr>
<td></td>
<td>Chinese investors should be prepared for long-term investment as in the end it might not only offer better returns but also help stabilize financial markets, promote global economic growth and bring wider social benefits. The purchase prices of target companies in Russia might now be lower than usual, which makes targets in Russia exceptionally attractive. However, to ensure further successful work in in Russia, investors should be willing to carry such costs as external advisors fees, and integration costs.</td>
</tr>
</tbody>
</table>

55 Source: Perspectives from China: how concerns about the Russian market influence Chinese investment strategies, EY, June 2015
Prioritize strategy to promote Chinese enterprises’ international transformation

In the previous EY China Outbound Investment Report, we proposed the “EY Overseas Investment Growth Navigator”, focusing on the challenges in strategy, financing, cooperation, risk, company governance, social responsibility and enterprise culture, and the corresponding response strategies when enterprises invest overseas. Prudently developing an international strategy helps enterprises go global and provides significant assistance to the enterprises trying to achieve a strategic transformation and global business growth.

**Determine a long-term vision, and develop an international strategy based on enterprise’s competitiveness**

Chinese enterprises’ outbound investment development is still immature. Due to the lack of systematic strategic planning, many enterprises that expand overseas face two issues: They are going global only for internationalization purposes, to pursue very high margins and pick the low-hanging fruit; in addition, hasty decision-making and insufficient assessment result in a large number of overseas projects failing. In the new round of outbound investment, the enterprises have to be prudent and learn from experience. Many Chinese enterprises are now focusing more on upstream factors such as technology and branding, rather than market expansion and resource acquiring; however, the investment environment is more complex, and thus these enterprises need to do more systematic and dynamic strategic planning.

Global development aims to improve the enterprise competitiveness, and therefore outbound investment should be subject to an enterprise’s long-term strategic objectives, and these should be set based on the enterprises’ core competitiveness and considering the business structural adjustment and transformation needs in order to enhance the enterprises’ long-term competitiveness in the international market. When setting the strategic objectives, enterprises need to not only understand the industry development, market environment and their positioning in the industrial chain, but also assess the enterprise’s existing core competitiveness and consider how to obtain the required competitiveness and thus plan the investment orientation and method.

**Chart 23: Three key elements for developing an international strategy**

1. Assess the existing competitiveness so as to prioritize the investment direction. Understand the market dynamics and the competitive position in the domestic market and various international markets so as to determine the development priorities and time to enter the market.

2. Determine the objectives and mode of overseas investment according to a company’s required core competitiveness. For example, in the period of a company’s transformation to high value chain business, it requires companies to have highly synergistic integration, innovation and brand management capabilities; and these capabilities can be developed through...

3. Set international objectives according to the enterprises’ actual needs. Determine the significance of internationalization to self-development, and evaluate whether the objectives meet the needs at this stage. International objectives should be organically integrated into the group’s mid- and long-term strategies so as to improve the enterprise value from the group level.
Break through blindness and misunderstanding, and encourage strategic planning and implementation

For the planning and implementation of the enterprises’ international strategies, the enterprises must comprehensively plan and construct a system including management’s preparation and performance evaluation of specific projects. The enterprises need to prepare well, improve their strategic planning and implementation, and seek help from a third-party professional body when they need to plan and implement international strategies when laying the foundation for internationalization.

Chart 24: Five steps of planning and implementation of international strategies

<table>
<thead>
<tr>
<th>Step 1</th>
<th>Step 2</th>
<th>Step 3</th>
<th>Step 4</th>
<th>Step 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management’s preparation</td>
<td>Comprehensive assessment</td>
<td>Strategy design</td>
<td>Strategy implementation</td>
<td>Control and evaluation</td>
</tr>
</tbody>
</table>

- **Step 1: Management’s preparation**
  - Empower senior management with an international vision to design an international strategy
  - All departments within the enterprise fully communicate and reach a consensus on the strategy
  - Management should realize that strategic planning is a long-term and gradual process and make preparations

- **Step 2: Comprehensive assessment**
  - Make adequate assessment on international and domestic market environment
  - Understand the enterprises’ competitiveness and international needs
  - Make a comprehensive assessment with the help of a third-party professional body with rich experience

- **Step 3: Strategy design**
  - Set definite international strategic objectives
  - Develop a detailed strategy plan and make adjustments based on changes in the environment
  - Assess the profits and risks involved in a specific strategic plan so as to ensure financial soundness

- **Step 4: Strategy implementation**
  - Develop specific implementation plans, determine main objectives and break down specific implementation
  - Determine a position statement and provide the required support
  - Ensure adequate strategic clarifications, communication and collaboration

- **Step 5: Control and evaluation**
  - Establish and perfect performance evaluation and accountability mechanism, set specific indicators and timely assess the execution result
  - The evaluation system should be dynamic and can be timely adjusted according to changing external environment and enterprises’ strategic objectives

Compared with the multinational enterprises of developed countries, Chinese enterprises have less experience in areas such as global market, strategic planning and implementation, which will impact the formulation and implementation of the enterprises’ international strategies. In practice, the most prominent issue relates to the lack of mechanisms and tools for the formulation, management and control of international strategies; meanwhile, the lack of an international vision and talent and insufficient information also result in short of professional abilities, fewer information channels, and challenges in efficient global expansion and operation.

To act on these challenges, the enterprises need to strengthen the construction of an internal strategy management department, and improve their systems, tools and talent development with the help of knowledge and experience of a third party that is familiar with the overseas market.

Chart 25: Common problems and solutions during planning and implementation of international strategies

<table>
<thead>
<tr>
<th>Problems</th>
<th>Solutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategy management team lacks international vision and cannot efficiently perform long-term systematic and overall planning in multiple regions</td>
<td>Strengthen international exchanges to cultivate the management’s global vision; include international strategy in the entire group’s mid- and long-term development strategies and set globally consistent objectives and develop supporting and integrated solutions</td>
</tr>
<tr>
<td>Imperfect strategy management and control mechanism and lack of quantization tool and management system for assessing investment</td>
<td>Improve strategic decision-making and management and control system; establish professional management system, process and assessment mechanism; and establishes specific and quantitative system for providing decision support and make timely adjustment according to changes of the market</td>
</tr>
<tr>
<td>Few information channels and lack of international talents result in inadequate execution abilities</td>
<td>Take full advantage of services and network of third-party professional body to form reliable cooperation resource reserves including talent and gradually improve the execution abilities</td>
</tr>
</tbody>
</table>
Case study: Huawei

Analysis of Huawei’s Globalization Strategy

Founded in 1987, Huawei Investment & Holding Co., Ltd. (“Huawei”) is a 100-percent employee-owned private company headquartered in Shenzhen, China, that manufactures, sells and markets ICT (Information & Communication Technology) equipment and related services. It divides its business into three operating segments: carrier business, enterprise business and consumer business.

Business sectors

<table>
<thead>
<tr>
<th>The carrier business</th>
<th>The enterprise business</th>
<th>The consumer business</th>
</tr>
</thead>
<tbody>
<tr>
<td>develops and manufactures a wide range of wireless networks, fixed networks, carrier software and core networks, as well as services solutions to telecommunications operators</td>
<td>develops ICT products and solutions including enterprise network infrastructure, cloud-based green data centers, enterprise information security and unified communication and collaboration, and delivers these solutions to vertical industries such as governments, public utilities, enterprises, energy, power, transportation and finance</td>
<td>develops and manufactures mobile broadband devices, home communication devices, smartphones, as well as the applications on these devices, and delivers them to consumers and businesses</td>
</tr>
</tbody>
</table>

Huawei – A great Chinese company

Huawei is committed to building a “Better Connected World” with innovative ICT products, services, and solutions, thus creating value and global progress. In its vision “to enrich life through communication”, Huawei focuses on customers’ market challenges and needs by providing ICT solutions and services to create maximum value. Huawei is striving to become a global leader in the ICT industry by acting as a responsible corporate citizen, an innovative enabler for the information society, and a collaborative industry contributor. After nearly three decades of development, Huawei has grown from a small to a global company with 170,000 employees, revenue of over US$46b, and a business presence in over 170 countries, thanks to the tireless efforts of its staff and the company’s global-mindedness. About two-thirds of Huawei’s revenue in 2014 was generated from outside China. In 2015, Huawei has climbed to 228th in the “Fortune Global 500” from 285th in 2014, leading the privately owned companies from mainland China on the list.

Chart 26: Global business layout

Source: Huawei Annual Report 2014

Huawei’s Road to Globalization

In 1996, Huawei recorded a turnover of US$2.6b, but realized that the incremental demand in mainland China was slowing down. Therefore, Huawei decided to go global. Its first step was to cooperate with Hutchison Telecom in Hong Kong by launching “Business Network” products, of which narrowband switches were the main product. Through this cooperation, Huawei gained its first international experience, and also moved closer to global quality and service standards due to Hutchison Telecom strict requirements.

In late 1990s, Huawei entered into African market. Shortly after that, Huawei set up training centers in Nigeria, Tunisia, Egypt and Kenya for the purpose of developing local ICT experts. Furthermore, Huawei launched the “Future Telecom Seed” plan, in which Huawei collaborates with local governments and universities and offers internship programs to local college students, and even invites them to Huawei headquarters in China for further training. In 2014, Huawei declared that it would help the world-leading transportation solution provider Bombardier with the...
construction of the communication and signal systems for Zambia Rail’s Chingola-Livingstone project. Once it is finished, Zambia will be the first country in Africa that owns ETMMS Regional Signal System and GSM-R Wireless System59.

In 1997, Huawei established joint ventures in Russia and Brazil, and started to develop local markets through localization. In 2006, Huawei signed up contracts with Rostelecom, the leading operator in Russia, in relation to VOT and FPV businesses. In the same year, Huawei provided test message services to five Latin American countries from only one system center in Mexico.

Huawei entered the market in Western Europe in 2001 and its products successfully penetrated to developed countries. By 2006, Huawei’s products and solutions have been widely used in UK, France, Germany, Spain, and Netherlands60.

In South East Asia and the Middle East, Huawei has been doing well, too. Its recent achievements include implementing 4G mobile ultra-broadband network and establishing GNOC (Global Network Operation Center) in India, helping the carrier LG Uplus construct an LTE-A network and working with SK Telecom to construct the industry’s first microwave-borne CPRI network in South Korea, helping Thailand’s PEA ( Provincial Electricity Authority) build a secure high-speed production network, and cooperation with Etisalat and STC (Saudi Telecom Company).

In recent years, Huawei has been closely partnering with Telefonica. In the fixed network domain, the two companies jointly drive the application of SDN (Software Defined Network) in multiple scenarios such as mobile bearer networks, data centers, and smart pipes for MANs, and translate SDN technologies into commercial applications. In 2014, in the IT domain, Huawei and Telefonica jointly initiated the most innovative next-generation architecture for ICT transformation in the telecom industry. Huawei helped Telefonica’s UK subsidiary successfully deepen ICT transformation through the VAS Cloud project, and commercially deployed the industry’s first cloud-based value-added service in the UK. Spanning six Latin American countries (Spain, Chile, Peru, Colombia, Argentina, and Ecuador), Telefonica’s IT transformation project migrated services over a distance of more than 8,000 km for the first time and moved 80% of the telecom services to the cloud.

In late 2014, Huawei worked with industry partners to build the world’s first 5G testbed in the UK, which will greatly accelerate 5G research. On December 3, 2014, Huawei released the third annual white paper on December 3, 2014, Huawei released the third annual white paper on cybersecurity in Berlin: Cyber Security Perspectives: 100 requirements when considering end-to-end cyber security with your technology vendors. This paper is one of the positive steps Huawei is taking to establish cyber security policies and standards. In the internet domain, Huawei has constructed an efficient and secure cloud platform for Qwant, France’s top search engine company, and built a cost-effective hosting platform for LeaseWeb in the Netherlands. In the media and entertainment domain, Huawei’s Omnimedia Solution has been deployed broadly in many countries including France and Italy. As part of its efforts to globalize, Huawei has established strategic alliances, global partnerships, or collaborations in certain domains, with world-leading vendors and telecom carriers such as SAP, Accenture, Intel, Vodafone, Deutsche Telekom, Telefonica, etc; these alliances are designed to integrate high-grade resources and capabilities and help build a favorable industry environment.

**Inspiration from Huawei’s Successful Globalization Strategy**

As Huawei’s rotating and acting CEO, Mr. Hu Houkun said, “Globalization and localization are two sides of the same coin”61. Huawei, a company now operating in over 170 countries and regions, has globalized its operations and investment, and is building a fully integrated global value chain using the best resources in the world. And this value chain can be shared with customers around the world. Through its localized operations, Huawei collaborates with the best local companies and organizations, creating value for local industries and enterprises on one hand, and creating jobs and paying taxes on the other. Furthermore, the value created locally contributes to Huawei’s global value chain. Huawei is paying a lot of attention to its partnership with local governments, media, and other stakeholders and trying to achieve win-win collaboration.

On the road to globalization, Huawei is using the “Glocalization” strategy. When Huawei enters a new international market, it tries to build partnerships with local stakeholders, including telecom companies, distributors, business software companies, IT advisors, government, media, and even universities, instead of a direct merger or acquisition. This kind of strategy has not only helped Huawei grow fast in the local market, but also build a good image locally, which is the foundation of Huawei’s long-term global development. In addition, Huawei keeps on raising salaries and incentives for field units and high-performers by implementing its unique bonus mechanism. In terms of the long-term incentives, Huawei pays a lot of attention to outstanding junior and mid-level employees via the Time Unit Plan (TUP), through which Huawei’s long-term success and benefits can be shared globally.

**Huawei’s successfully globalization strategies include the followings:**

- Changing the operational model from “issuing orders” to “delegating authority”
- Shifting the management mode from “function-centered” to “project-centered”
- Continuing process transformations to increase operational efficiency
- Placing cyber security and user privacy protection above Huawei’s business interests
- Promoting “Glocalized” operations
- Developing Huawei into an attractive career platform for outstanding talents to create and share value

**Embracing the future and building a Better Connected World**

Adopting a similar vision to ET: Huawei is striving for a “Better Connected World”. A more connected world will impact every individual, organization, and industry and Huawei’s strategies will continue to develop this megatrend to maximize its potential in the global market.

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61 Source: Huawei Annual Report 2014
Conclusion: China’s overseas investment offers a promising future

The world is witnessing the boom of Chinese outbound investment. In 2015, the gradual implementation of the “One Belt, One Road” initiative and other national strategies and the benefits from the financial reform and the acceleration of the Renminbi’s internationalization are encouraging Chinese enterprises to accelerate their overseas expansion so as to be more active in the world’s capital market.

In the last decade, the footprints of Chinese enterprises have spread from neighboring developing countries to the whole globe, achieving a qualitative leap in both scale and structure. And with the growth of fertile conditions for China’s outbound investment, more Chinese enterprises are expected to realize more healthier and sustainable strategic growth. There are a large number of opportunities and risks in the ever-changing world market and we expect Chinese enterprises to not only grasp the opportunities but also to think calmly and prepared before expansion overseas so as to make solid and great steps in their internationalization.

Starting from 2015, China is expected to be a net capital exporting country. With the gradual implementation of favorable policies and the development of Chinese enterprises, China’s capital is able to take advantage of the unprecedented opportunities for “going out”. The stars certainly seem to be aligned for Chinese outbound investment: the conditions are right, the opportunities are there and the world is waiting.
Navigating the Belt and Road – Financial sector paves the way for infrastructure – August 2015
China Overseas Investment Network helps Chinese businesses navigate through global markets

The China Overseas Investment Network (COIN) links EY professionals around the globe, facilitates collaboration, and provides consistent and coordinated services to our clients with overseas investment from China. Building on the existing China Business Group in the Americas, EMEIA, Asia-Pacific and Japan areas, COIN has expanded our network in nearly 65 countries and territories around the world.

Our globally integrated structure enables us to deploy dedicated teams with strong local experience, and profound industry knowledge to provide our clients with one-stop professional service from planning stage to execution stage to integration stage, helping our clients navigate through global markets.
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Our global COIN network

For more information on our China Overseas Investment Network, please visit our website at www.ey.com/cn/coin or contact:

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