

China Funds Management: Quarterly Update 1Q09 *All Change!*

Z-Ben Advisors is pleased to reintroduce our *China Funds Management: Quarterly Update*, which has been thoroughly redesigned to meet clients' requests, assessing the impact of the quarter's most important developments with a better mix of quantitative and qualitative research and putting more focus on firms that showed the greatest success or failure.

That Chinese investors are now engaged in wholesale portfolio restructuring is undeniable: a glance at this report's review of fixed-income and money market funds will prove that point. Overall industry assets, however, have not yet climbed as a result of investor re-risking. Nonetheless, the feeling that new inflows are imminent is widespread among FMCs and much of their current activity – whether in fund launches, asset gathering or the ramping up of development plans – can be explained by that sentiment. In this report, we detail the effects of investors' new mindset on existing funds (and fund ranges) in Q1 and assess how well – and how quickly – China's 60 FMCs can react to a new market mood.

Massive shift away from fixed income funds

After gorging on bond and money market funds throughout 2008, and especially towards the end of the year, investors reassessed their desire for risk and decided to par back on their positions. By end-Q1, fixed income exposure

For the current quarter, Z-Ben Advisors expects continued selling pressure on all fixed income product classes. Those managers with the greatest exposure are expected to see AUM and market share decline over the period.

Industry AUM up fractionally

The shift away from fixed income exposure was so widespread that it ultimately depressed the rate of industry AUM growth (3.5% Q-Q). Sharply negative relative performance by equity funds certainly didn't help matters much either.

Z-Ben Advisors expects Q2 to close with a rebound in AUM and a more robust rate of growth. As noted above, we are expecting a further scaling back on fixed income positions. This time, the proceeds should be redeployed (in an asymmetric fashion) into equity mutual funds.

Rmb1.00 threat assessment

Million of retail investors continue to sit on unrealized losses after buying in at or near the market's 2007 peak. With the equities market edging higher means the potential for greater redemption pressure on FMCs

For the industry, the threat remains muted. The CSI 300 index would need to move 40% higher before widespread redemptions were to take effect. Still, the threat remains and will need to be addressed by all managers.

Demand is good, just not Rmb15bn good

Several weeks ago, Changsheng FMC announced, quite unexpectedly, massive demand (Rmb15bn, USD2.2bn) for its latest equity mutual fund. Demand, however, was supported by certain product specific qualities.

The probabilities of generic equity mutual funds raising similar levels of AUM are low. It is widely expected, however, that other FMCs will apply for their own levered product if history is any indication

QUARTERLY HIGHLIGHTS

Top FMC Market Share Gainers

| | Q1 AUM (Rmb bn) | Qrt Δ in Share (Basis Points) |
|----------------------|--------------------|----------------------------------|
| E-Fund | 100.8 | 50 |
| China Post & Capital | 36.3 | 48 |
| Guangfa | 78.0 | 43 |
| Rongtong | 45.9 | 39 |
| AEGON-Industrial | 32.4 | 32 |

Bottom FMCs Market Share Gainers

| | Q1 AUM (Rmb bn) | Qrt Δ in Share (Basis Points) |
|--------------------|--------------------|----------------------------------|
| Harvest | 115.2 | -135 |
| ICBC Credit Suisse | 56.0 | -109 |
| CCB Principal | 31.8 | -37 |
| China Merchants | 34.4 | -33 |
| Bosera | 124.4 | -29 |

Top Performing Mutual Funds

| Product | Q1 AUM (Rmb bn) | Q1 Return |
|---|--------------------|--------------|
| China Post & Capital Core Enhanced Fund | 13.4 | 45.5% |
| New Century Growth Equity Fund | 0.2 | 39.6% |
| Golden Eagle Small/Mid Cap Fund | 0.8 | 39.5% |
| China AMC Large Cap Enhanced Fund | 4.1 | 37.8% |
| China Post & Capital Core Growth Fund | 22.8 | 37.2% |
| GTJA Allianz Enhanced Equity Fund | 1.9 | 36.7% |
| AEGON-Industrial SRI Equity Fund | 2.6 | 36.4% |
| Full Goal Tianrui Regional Wealth Fund | 6.3 | 36.0% |
| Harvest Thematically Enhanced Fund | 7.8 | 35.3% |
| Guangfa Small Cap Growth Fund | 9.5 | 34.8% |
| BENCHMARK: CSI 300 Index | | 38.0% |

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Table of Contents

| | | |
|------------------------------|-------|----|
| Executive Summary | | 5 |
| 1. Market Sizing & Analysis | | |
| 1.11 Thematic Overview | | 7 |
| 1.13 Industry AUM | ..... | 8 |
| 1.15 Industry Fund Flows | ..... | 9 |
| 1.17 Organic Growth | ..... | 10 |
| 1.19 New Products | ..... | 11 |
| 1.21 Demand Trends | ..... | 12 |
| 1.23 Demand Assessment | ..... | 13 |
| 1.24 Product Innovation | ..... | 14 |
| 1.26 Money Market Flows | ..... | 15 |
| 1.28 Bond Flows | ..... | 16 |
| 1.30 The Rmb1.00 Dilemma | ..... | 17 |
| 2. Performance | | |
| 2.11 Asset Class Performance | ..... | 18 |
| 2.12 Allocation Trends | ..... | 19 |
| 2.14 Top Performers | ..... | 20 |
| 2.16 Bottom Performers | ..... | 21 |
| 2.17 Lessons Learnt | ..... | 22 |
| 3. The Impact | | |
| 3.11 QDII Funds | ..... | 23 |
| 3.13 ETFs | ..... | 24 |
| 3.15 Dividends | ..... | 25 |
| 3.17 Proprietary Trading | ..... | 26 |
| 3.19 PM Moves | ..... | 27 |
| 3.21 Distribution | ..... | 28 |
| 3.22 Fee Extraction | ..... | 29 |

Table of Contents

| | | |
|--------------------------|-------|-------|
| 4. Competitive Fallout | | |
| 4.11 Market Share | ..... | 30 |
| 4.12 Market Share Trends | ..... | 31 |
| 4.14 FMC Evaluation | ..... | 32-35 |
| Appendix | | |
| Domestic FMC Matrix | ..... | 36 |
| Sino-foreign FMC Matrix | ..... | 37 |

Executive Summary

It was a quarter of dramatic shifts in every area of Chinese fund management life: fund flows, asset allocation, buyer behavior, and fund performance all changed dramatically, fulfilling at least some of the promise that was delivered in Q4. Operationally, gamblers on growth were rewarded to an outsize degree, while those who had bet – either in range construction or asset allocation – against growth were punished. Growth risks are perhaps now in better equipoise, which will only make decisions more difficult for firms which have yet to commit themselves to a post-meltdown strategy.

- Industry AUM growth isn't matching performance gains and won't until outflows from money market (and, to a lesser extent, bond) funds stabilize – with luck, as early as Q2. FMCs with low FI/MM exposure are gaining market share while others stagnate.
- Shares in issue are declining dramatically for the same reason with only a handful of high-equity FMCs picking up sharply.
- Huge drops in market share at a number of bank-backed JVs suggest that 2008's favorite business model is due for reconsideration. Those worst punished last year – domestics with all-equity fund ranges – are currently eating their lunch. Both models now appear to produce highly volatile AUM.
- Industry fee extraction ability rose for the first time in three quarters, but this perhaps better reflects the AUM growth success of a small number of FMCs with high equity concentrations than the broader mass. Expect firms which rely heavily on MM/FI funds for fee income to be forced to launch into the equity space.
- Funds launched recently with heavy institutional support are drowning in redemptions: 2008's preferred method of guaranteeing high launch AUM is now breaking down badly.
- The Rmb1.00 threat is materializing, driving redemptions higher for a handful of funds. Expect this trend to gain some momentum as the domestic equity market continues to rise and, potentially, place an artificial ceiling on industry AUM.
- Top-performing equity funds, without exception, are taking more risk and allocating higher proportions of their AUM to equities, reversing 2008's key trend. Expect the broad mass of equity funds to be forced to follow suit, regardless of market conditions.
- QDII funds remain mired, for the most part, in mediocrity. Signs that the quota approval tap is being turned back on could revive interest in the sector, albeit at the expense of some existing QDII funds' prospects for growth. Performance relative to domestic funds remains an issue.

Executive Summary

- Proprietary trading, an occasionally reliable indicator of market sentiment, suggests that many FMCs are putting their own money back to work in the equity markets. Other FMCs, however, are using the market rally to exit from trades put in place over the past several years.
- The volume of PM moves is set to stabilize as the impact of new registration requirements is felt. Good news for those FMCs with strong teams in place, bad news for those hoping to hire from a shrinking pool.
- The recent Rmb15bn (USD2.2bn) product launch from Changsheng was an anomaly. Demand for new equity funds is on the rise, but should hold at a launch average between Rmb2.5bn and Rmb3.5bn.

Z-Ben Advisors expects the very same trends in evidence in Q1, and highlighted throughout this report, to hold firm during the current quarter. While there may not be as significant an outflow from money market and bond funds, redemptions are still expected to run at high levels. At the same time, demand for equity funds is steadily rising. All that stands in the way of industry AUM growing at a faster clip is equity market sentiment. Currently, the CSI 300 index is up in excess of 70% from the low reached last year. There are those who strongly believe that valuations are stretched and are looking for a correction in the coming months. Then there are those which see continued upside given the success of Chinese policy in reaction to the global financial crisis. Investor opinion, not FMC opinion, is likely to drive flows in the near term.

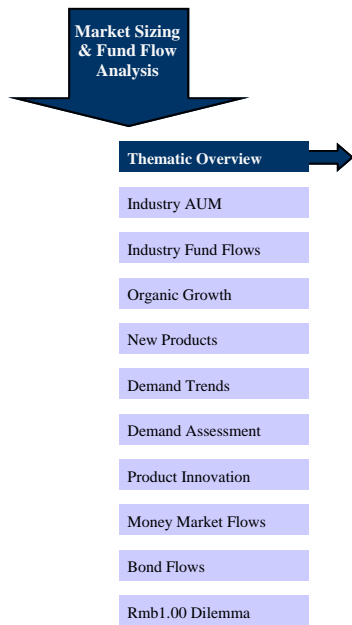


Exhibit 1.11: Thematic overview

| | 4Q08 | 1Q09 | 2Q09 |
|-------------------------------|--|--|--|
| Ample Liquidity | Accommodative monetary policy has remained in place for the past six months and is expected to hold firm until there are clear signs of economic improvement within the local economy. | | |
| Equities Market Rally | The CSI 300 bottomed out as newly launched equity mutual funds started to post positive results. | One of the stronger quarters on record with the CSI 300 gain nearly 40%. | Conditions remain strong, but concerns abound of an impending market correction |
| Sales of Mutual Funds Improve | Complete attention remained on the issuance of fixed income product alternatives. | Fundraising results improved materially but still fixed-income products dominated. | Fundraising to improve, but marginal industry net inflows. FMCs to press innovation. |

There are numerous opinions as to what direction the CSI 300 will track in the coming months, although a growing number of market participants are projecting a sharp pullback heading into the summer months. For FMCs, the outcome for the industry will be dependent on which scenario plays out in the end. If share prices do move higher then industry AUM will find support and benefit those firms coming to market with a new equity product. Any correction, which Z-Ben Advisors deems as unlikely, would lead to subpar growth and a lessening in investor demand.

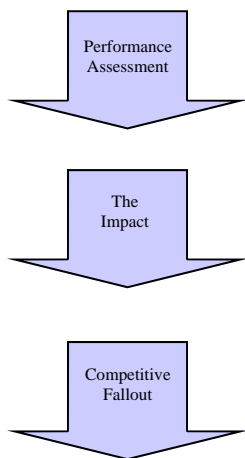


Exhibit 1.12: Equities market scenario test

| | Most Likely | What Products Benefit? | What Firms Benefit? |
|--|--|--|--|
| | Equities market runs between 2200 and 3000 | Flexible products Equity products aiming to catch | China AMC, AEGON Industrial |
| | CSI 300 further rallies to above 3200 | ETF and index funds, New products & Top performers | China Post & Capital, Everbright Pramerica, Invesco Great Wall |
| | Market corrects and remains sluggish over year | Newly launched products including QDII | ABN Amro TEDA |
| | Least Likely | | |

Industry AUM: Growth well below expectations

Market Sizing & Fund Flow Analysis

Thematic Overview

Industry AUM

Industry Fund Flows

Organic Growth

New Products

Demand Trends

Demand Assessment

Product Innovation

Money Market Flows

Bond Flows

Rmb1.00 Dilemma

Performance Assessment

The Impact

Competitive Fallout

After finally bottoming out towards the end of 2008, China's equities market rallied at a pace few within the funds industry had projected, with the benchmark CSI 300 index closing Q1 up by 38%. Still, and even though the industry remains heavily concentrated towards equity mutual funds, total AUM for the period grew by a less than expected 3.5%. There were several factors behind this depressed rate of growth and some may remain in place, capping growth in Q2 as well.

Poor relative performance by nearly all equity mutual funds (averaging 23.6% for the period) meant less support for AUM growth from capital appreciation. For the most part, portfolio managers were skeptical of the sustainability of the market's rally and didn't increase their exposure to stocks until quarter's end.

Sharp and highly unexpected outflows from fixed income products also led to the lower growth rate. Neither money market nor bond funds offered investors attractive yields over straight time deposits. At the same time, positive momentum in the equities market exacerbated the selloff in fixed income products.

The two abovementioned variables, equity underperformance and outflows from fixed income funds, are expected to continue to cap AUM growth in Q2. Still, Z-Ben Advisors does expect AUM to breach the Rmb2.1tr mark. The one variable which may keep growth at lower than expected levels is higher rates of redemptions from those equity funds whose NAV is now nearing par. After two years of unrealized losses, investors will increasingly have opportunities to exit at cost.

Exhibit 1.13 : AUM growth has stabilized...

Quarter-on-quarter change in AUM

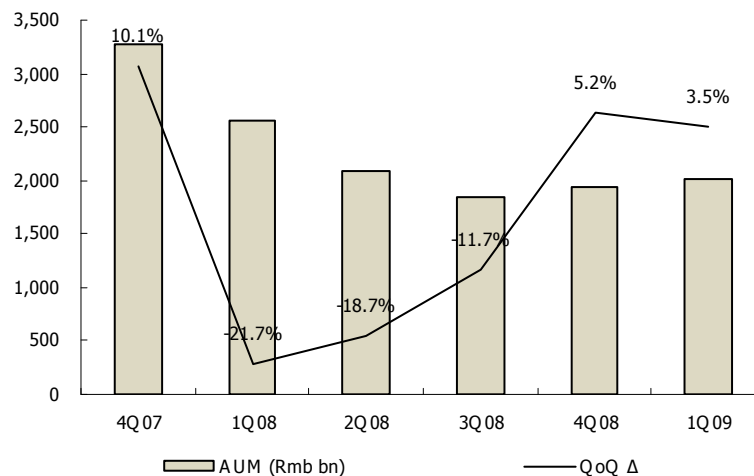
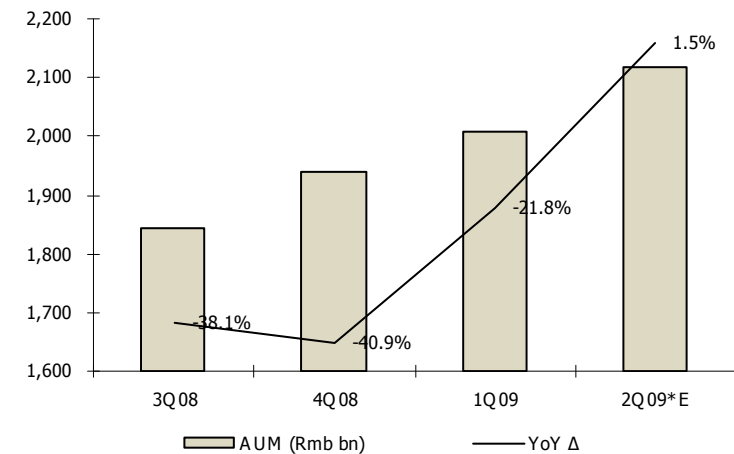
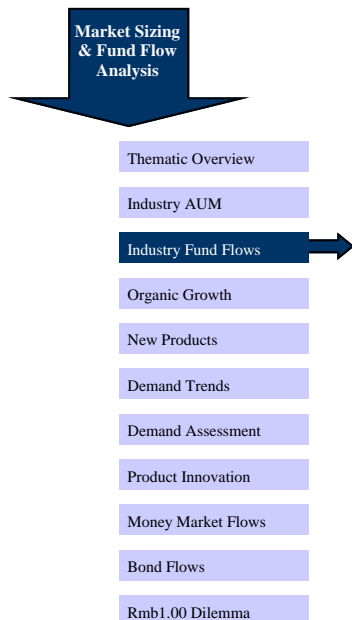


Exhibit 1.14: ... and should turn positive by end-Q2

Year-on-year change in AUM



Industry Fund Flows: Massive outflows as investors shed fixed income exposure



The decision by investors to exit from money market and bond funds was so widespread that it led to a 8.7% decline in total industry units/shares in issuance. The quarterly decline also represented a near total reversal of the net fund inflows that occurred at the end of last year. Somewhat confounding is determining where, exactly, all of the proceeds were deployed. Certain FMCs did attract net new flows, but there was a small contingent of investors which, it appears, simply decided to exit the funds industry altogether.

The move out of fixed income product alternatives closely matched, and came in at nearly the same level, the exodus from the product category in 2006. Market conditions then were the same as today: equities rising off a low reached in the previous year, leading investors to reassess their tolerance for risk.

Using the past as a guide indicates that net inflows should rebound, and potentially at a sharp rate, during the current quarter. For the current quarter, however, it is expected that any reduction in fixed income product exposure will see the proceeds redirected and used to purchase equity funds.

Z-Ben Advisors expects there to be an asymmetrical flow of funds in Q2 and much like the one which took place in 2006. Investors redeeming shares in a fixed income products (with those at risk including **Harvest, Fortis Haitong** and **ICBC Credit Suisse**) will redeploy the proceeds into equity products from a rival FMC including **China Post & Capital, Guangfa** and **Everbright Pramerica**.

Exhibit 1.15 : Redemptions at a multi-year high
Quarter-on-quarter change in units/shares in issuance

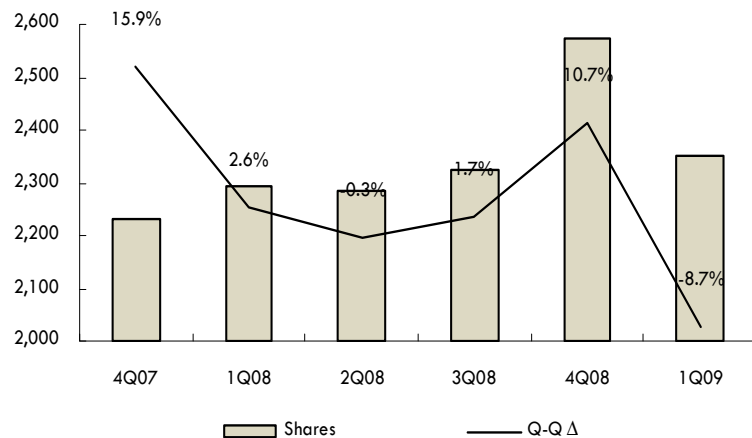
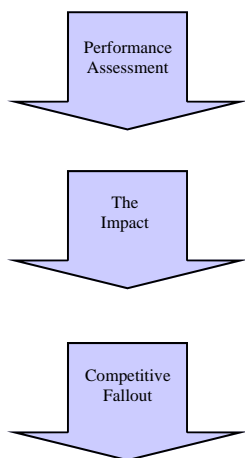
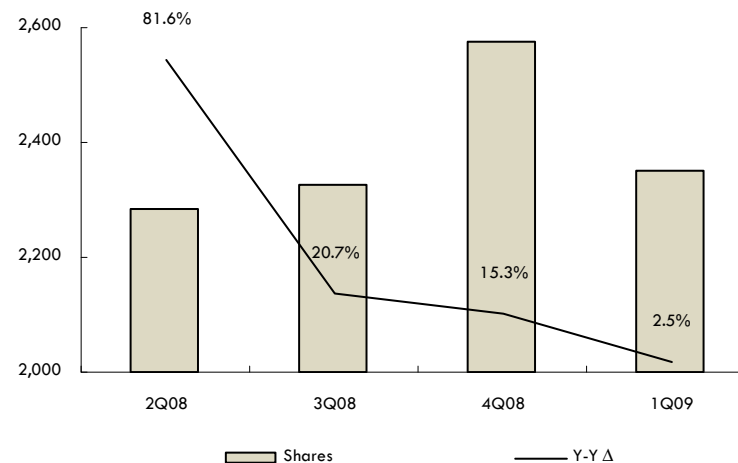


Exhibit 1.16: Outflows appear to have bottomed out
Year-on-year change in units/shares in issuance



Organic Growth: Negative and Weakening

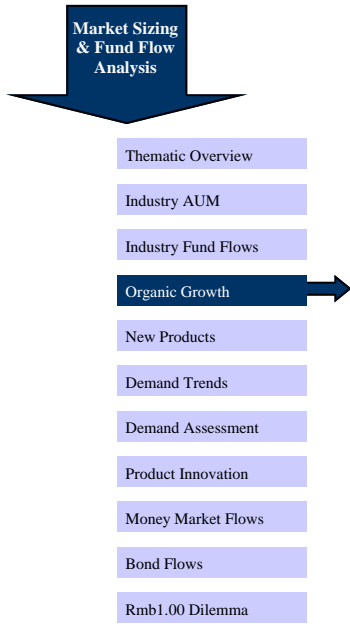


Exhibit 1.17 : Organic growth dropped sharply
Change in units/shares from seasoned funds (excluding MMFs)

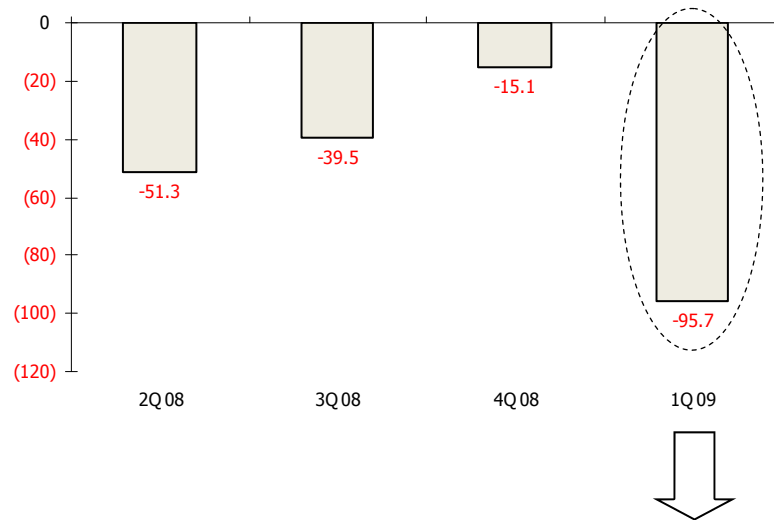
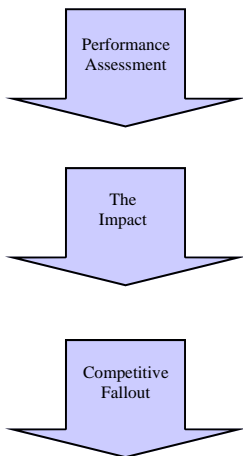
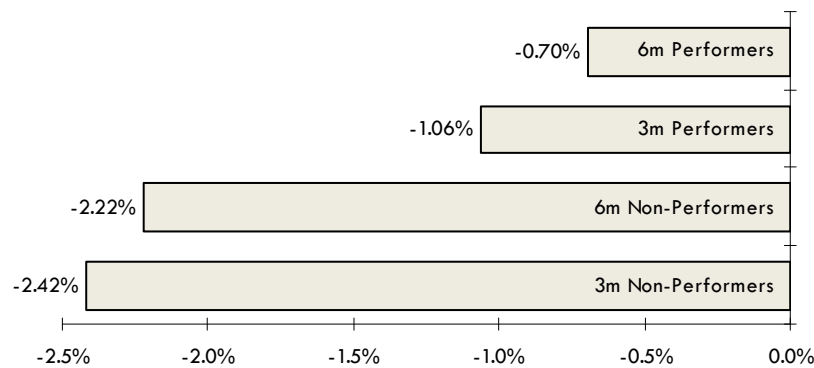


Exhibit 1.18 : To retain assets, performance mattered
Performance against change in units/share in issuance



While outflows from fixed income were the primary driver behind the sharp reduction in total industry units/shares in issuance, the decline was also the result of outflows from other products.

Z-Ben Advisors' measurement of organic unit/share growth, full quarter flows excluding those from money market funds, shows a 95.7bn reduction in total industry units/shares.

Declining organic growth would have been primarily affected by investors redeeming from bond funds. At the same time, evidence of investors exiting from some equity funds was present, as discussed below.

For Q2, the rate of organic growth will be influenced by two factors: FMCs ability to retain assets among their most recent product launches and the speed at which investors exit from "in the money" positions established at or near the market's 2007 peak.

Without question, performance still matters when it comes to a FMCs' ability to succeed in retaining assets. Stronger relative-to-peer performance doesn't yet support the ability to attract new fund flows. Weaker performance, however, does lead to a risk of two to three times the outflows.

Current market conditions and recent performance (especially in the equity fund space) would indicate positive fund flows during the current quarter for **China Post & Capital** - having two of the top ten performing funds in Q1 - with gains also expected at **AEGON Industrial** and industry heavyweight **China AMC**.

New Products: The struggle to raise and retain assets

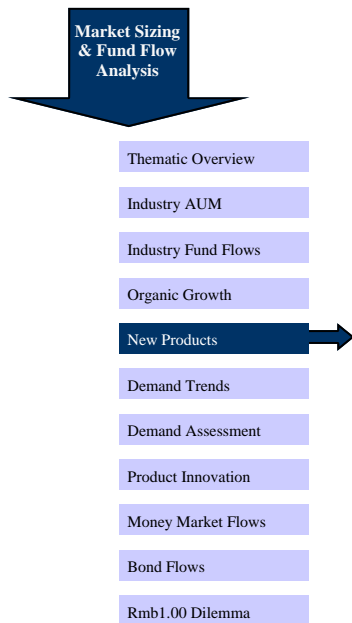


Exhibit 1.19 : New product fund raising stalled out
Total AUM raised in new products (Rmb bn)

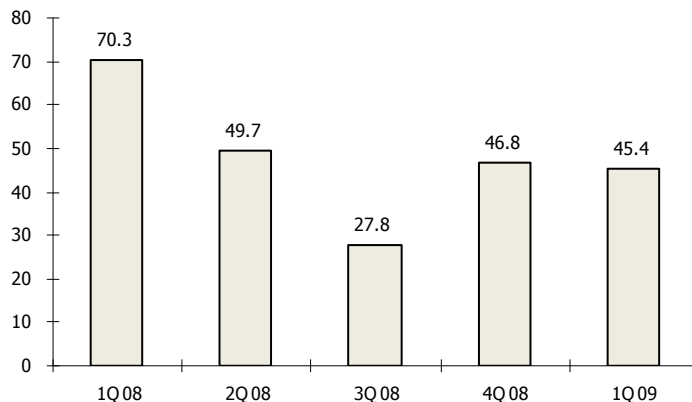
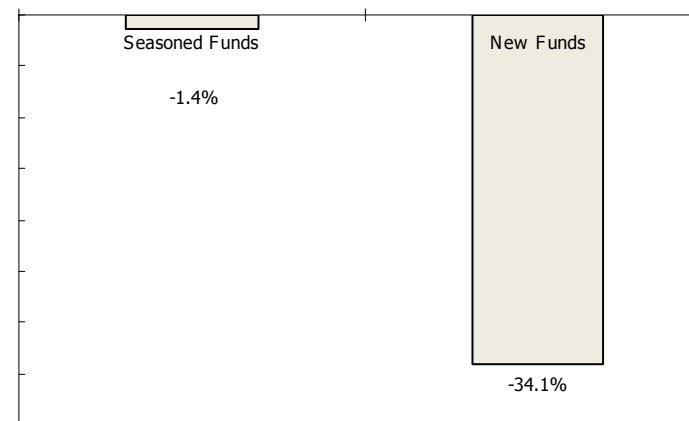


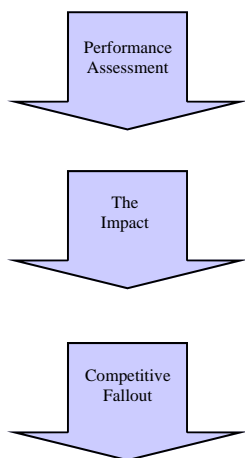
Exhibit 1.20 : New products also came under stiff selling pressure
Comparable redemption rates; seasoned vs. new funds



Fundraising activities are still well above last year’s lows. For Q1, however, demand stalled with total AUM raised coming in around the same level as 4Q08. Even adjusting for the cyclicity of Chinese New Year shows a marked slowdown in demand compared to the same period in 2008.

The focus here is not specifically on fundraising, rather the ability for FMCs to retain assets six months post launch. Pressure is clearly being applied with a sharp selloff typical once a recently launched product opens for redemptions. The greater than one-third reduction had been expected given that the majority of mutual funds launched in the recent past were, for the most part, bond funds.

Both the rate of AUM and unit/shares in issuance growth is expected to be supported during the current quarter by a marked increase in demand for new equity product offerings. At the same time, the number of FMCs going to market with a new product is rising with, on average, 12 new funds launched per month. Having said that, success during the subscription process will need to be matched with success in retaining AUM.



Demand Trends: Stronger (retail) demand for equity funds resurfaces

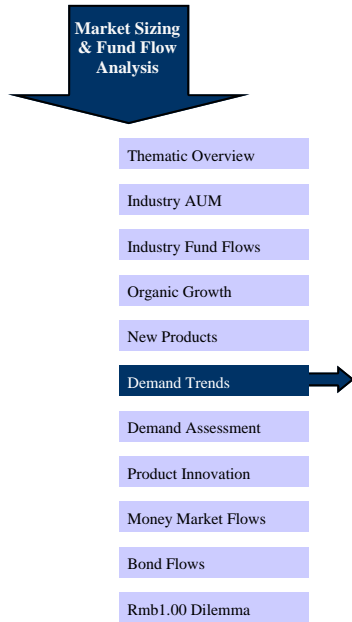


Exhibit 1.21: Total AUM raised failed to climb

Total AUM raised (Rmb bn)

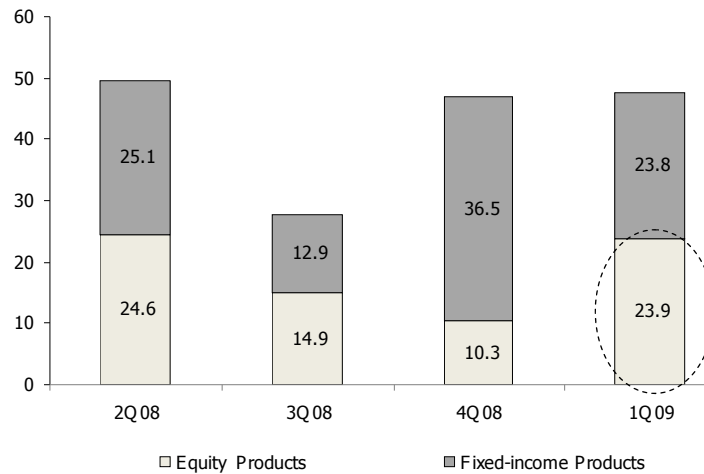
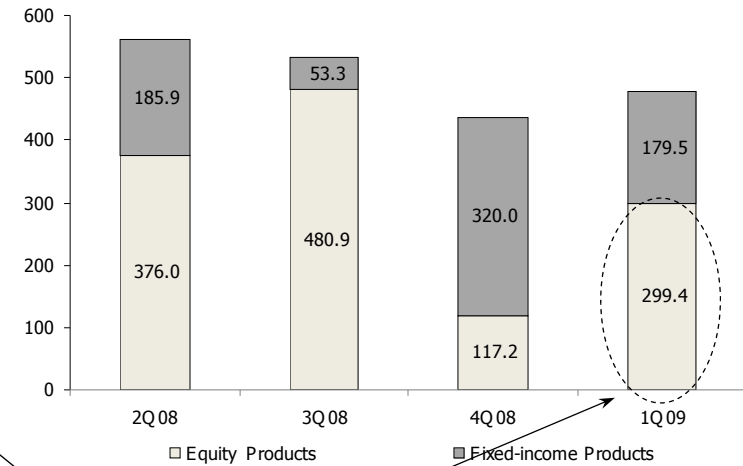


Exhibit 1.22: Retail demand moving back in favor of equity funds

Total accounts opened (,000)

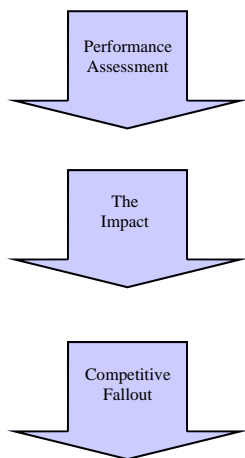


Demand for equity products rose significantly in Q1

Of all of the changes which occurred in Q1 it was the pick up in demand for newly launched equity mutual funds that came as the second most surprising trend. The most surprising trend? A clear and undeniable shift in demand for equity funds by retail investors. Granted, demand remained at lower levels than in the past. Still, the data shows even more evidence of a bottoming of appetite for equity exposure in 4Q08.

Arriving at the above conclusion could very well be in error or, at the very least, the connecting of two few dots. A closer examination of the product-by-product results (provided on the following page) shows that they were skewed towards the **E-Fund Leading Enterprise Equity Fund** (Rmb4.1bn, 42k accounts) and the **ICBC Credit Suisse CSI 300 Index Fund** (Rmb3.6bn, 77k accounts). The majority of other generic equity fund which were launched in Q1 pulled in AUM averaging Rmb1.5bn.

Z-Ben Advisors feels quite confident in projecting rising demand for equity funds in Q2 and possibly beyond. Data collected during the current quarter finds FMCs raising AUM well above the Q1 average with more recently launched equity funds attracting Rmb2.5bn in AUM. What has yet to become clear is how robust retail demand is for funds.



Demand Assessment: A final drive into the fixed income marketplace

Market Sizing & Fund Flow Analysis

Thematic Overview

Industry AUM

Industry Fund Flows

Organic Growth

New Products

Demand Trends

Demand Assessment

Product Innovation

Money Market Flows

Bond Flows

Rmb1.00 Dilemma

Performance Assessment

The Impact

Competitive Fallout

Exhibit 1.23: A wide disparity in fundraising results

New products launched in Q1 ranked by AUM raised (Rmb m)

| PRODUCT | DATE LAUNCHED | AUM RAISED | ACCOUNTS OPENED | AVERAGE ACCT. SIZE |
|---|---------------|---------------|-----------------|--------------------|
| Bank of Communications Schroders Guaranteed Fund | 21/Jan/09 | 4,956.38 | 46,900 | 105,680 |
| E-Fund Leading Enterprises Equity Fund | 26/Mar/09 | 4,091.75 | 42,338 | 96,645 |
| UBS SDIC Money Market Fund | 19/Jan/09 | 3,832.96 | 8,336 | 459,808 |
| ICBC Credit Suisse CSI 300 Index Fund | 5/Mar/09 | 3,606.42 | 77,085 | 46,785 |
| GTJA Allianz Enhanced Bond Fund | 11/Mar/09 | 3,072.18 | 11,086 | 277,123 |
| Harvest Quantitative Alpha Equity Fund | 20/Mar/09 | 2,961.22 | 28,331 | 104,522 |
| Minsheng Royal Blue Chips Balanced Fund | 27/Mar/09 | 2,718.58 | 25,174 | 107,991 |
| Fortune SGAM Enhanced Bond Fund | 17/Feb/09 | 2,258.21 | 18,453 | 122,376 |
| AEGON-Industrial Organic Growth Balanced Fund | 25/Mar/09 | 1,980.25 | 21,993 | 90,040 |
| Guotai Dual-income Bond Fund | 11/Mar/09 | 1,980.21 | 11,595 | 170,782 |
| Southern CSI 300 Index Fund | 25/Mar/09 | 1,580.75 | 26,302 | 60,100 |
| CITIC-Prudential Classic Bond Fund | 11/Mar/09 | 1,563.95 | 8,897 | 175,784 |
| China Universal Enhanced Value Equity Fund | 23/Jan/09 | 1,512.52 | 11,964 | 126,423 |
| KBC-Goldstate Fengli Bond Index | 23/Mar/09 | 1,474.81 | 34,707 | 42,493 |
| Huashang Enhanced Bond Fund | 23/Jan/09 | 1,245.29 | 12,160 | 102,408 |
| Lord Abbett China Bond Fund | 4/Mar/09 | 1,184.23 | 8,915 | 132,836 |
| Lion Growth Equity Fund | 10/Mar/09 | 1,167.84 | 14,435 | 80,903 |
| Franklin Templeton Sealand Dynamic Growth Equity Fund | 25/Mar/09 | 1,109.60 | 11,104 | 99,928 |
| Everbright Pramerica Enhanced Equity Fund | 4/Mar/09 | 1,040.50 | 14,757 | 70,509 |
| China International Mid/Small Cap Equity Fund | 21/Jan/09 | 826.06 | 13,167 | 62,737 |
| Baoying Core Advantage Balanced Fund | 17/Mar/09 | 776.69 | 10,410 | 74,610 |
| Great Wall Dual-engine Equity Fund | 15/Jan/09 | 485.75 | 2,298 | 211,380 |
| TOTALS | | 45,426 | 460,407 | - |
| AVERAGE | | 2,065 | 20,928 | 128,267 |

No matter what the data on the previous page may indicate, the exhibit above would suggest a continued push among FMCs to introduce new fixed income products. This certainly assisted **Bank of Communications Schroders** in retaining market share (more on that later). The data also shows the continuing strength of such brands as **E-Fund** and **Harvest** in attracting those investors seeking equity exposure.

FMCs which attempted a fixed income offering in Q1, recognizing the time lag between application, approval and launch, could find themselves under asset-raising pressure this quarter if investors continue to exit the class. This would be doubly true for already-launched funds such as **UBS SDIC Money Market Fund** and the **GTJA Allianz Enhanced Bond Fund**.

Product Innovation: Two classes are better than one?

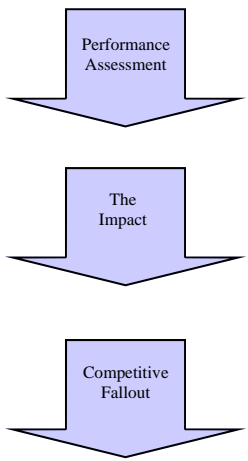
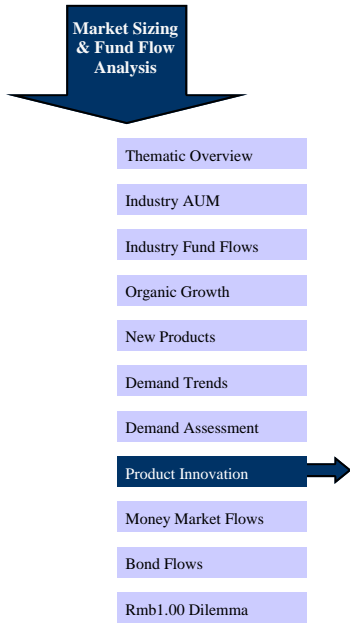
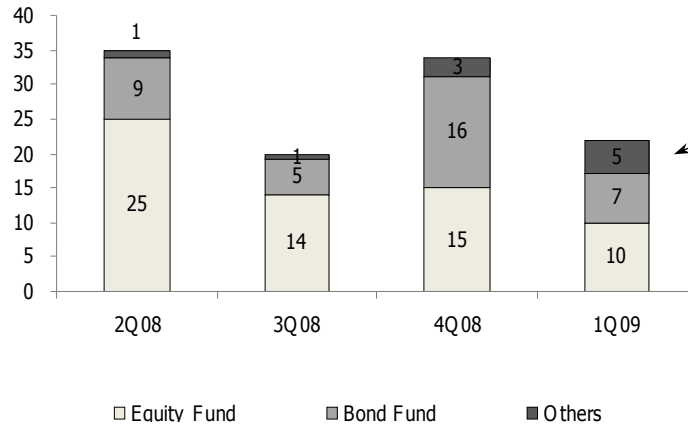


Exhibit 1.24: A mix and mash of new product types

Number of new product brought to market



For Q1 there was a moderate degree of diversity with five “other” products launched. These consisted of index funds, a guaranteed fund and, counter-intuitively, a new money market fund from **UBS SDIC**.

For the current quarter, diversity will still be the focus among FMCs, but with a considerable slant towards products deemed as innovative in nature (see exhibit below).

For the current quarter, the name of the game is innovation. And by that we mean dual-class products offering investors both a guaranteed return (normally around 5%) and embedded leverage which can act as jet fuel, or cold water, to boost/impair performance.

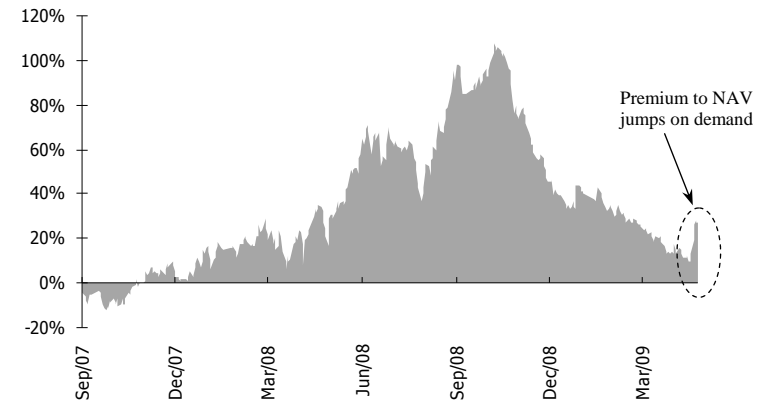
There had only been one such product available; **UBS SDIC Ruifu Classified Fund**. Recognizing that a market need may not be fully met, **Changsheng** decided that the time was right and recently introduced its own alternative. Correctly timed indeed! The product went on to raise nearly Rmb15bn in a single day.

Whether this is true innovation remains to be seen. What shouldn't be expected is similarly-sized fund raising results from newly-launched generic equity funds. End demand should remain between Rmb2.5bn and Rmb3.0bn (depending on market conditions).

Still, expected is a mad dash by dozens of FMCs to be the next to market with a guaranteed/leveraged product.

Exhibit 1.25: Investors bet on easy money from dual-class funds

UBS-SDIC Ruifu Fund discount/premium to NAV



Money Market Flows: Weaker interest rates are behind the sell-off

Market Sizing & Fund Flow Analysis

- Thematic Overview
- Industry AUM
- Industry Fund Flows
- Organic Growth
- New Products
- Demand Trends
- Demand Assessment
- Product Innovation
- Money Market Flows**
- Bond Flows
- Rmb1.00 Dilemma

Exhibit 1.26: Equities made a compelling buying argument

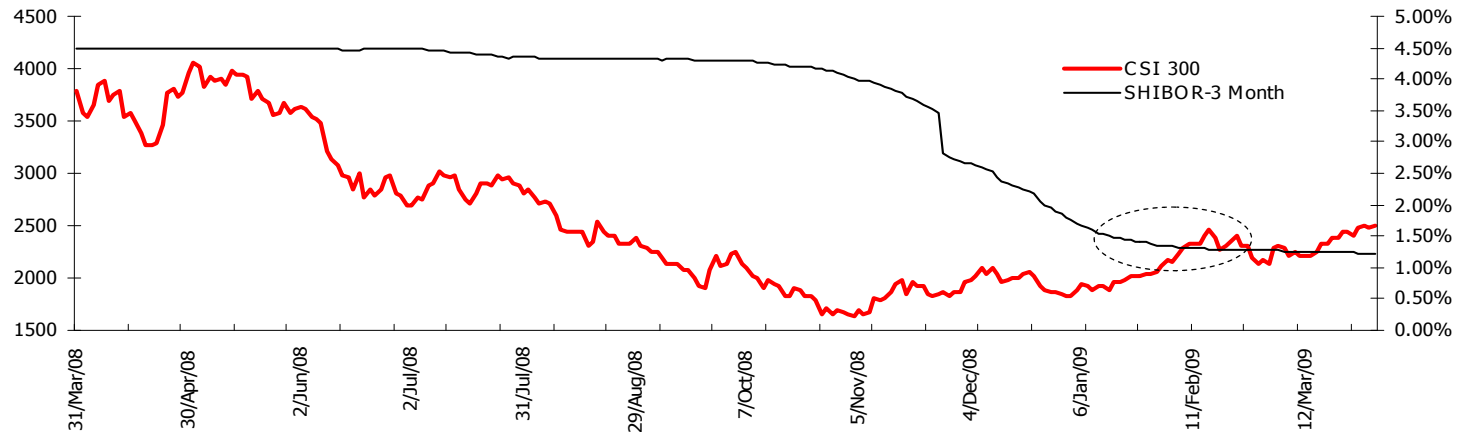
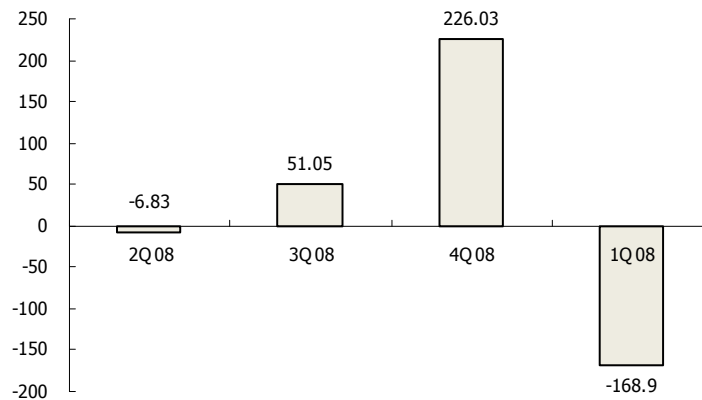


Exhibit 1.27: Investors reacted by dumping MMFs in droves

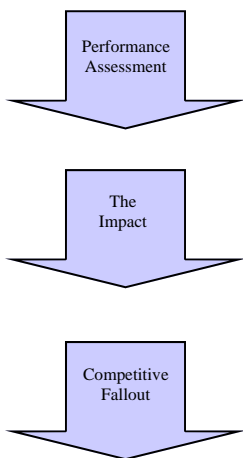
Quarter-on-quarter Δ in total MMF units/shares in issuance (bn)



Not only were investors attracted to a better-performing equities market, they were also put off by further declines in interest rates with the Shanghai Inter-Bank Offer Rate (SHIBOR) which fell to less than 125bps versus 180bps at end-08.

These lower market rates were behind extremely weak performance among money market and bond funds in Q1. This, along with a better outlook for the equities market, was behind the massive - not to mention sudden - sell off from fixed income product exposure.

Downward pressure on fixed income funds hasn't yet subsided. FMCs which remain overly dependent on the product category can expect redemptions to take place. Unless properly addressed, the likes of **Harvest** and **Fortis Haitong** could see a further deterioration in market share this quarter.



Bond Flows: So long and farewell, at least for now

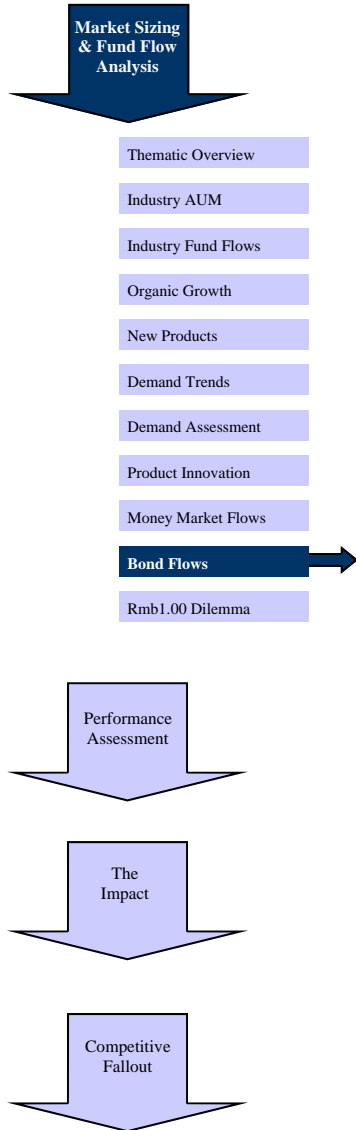
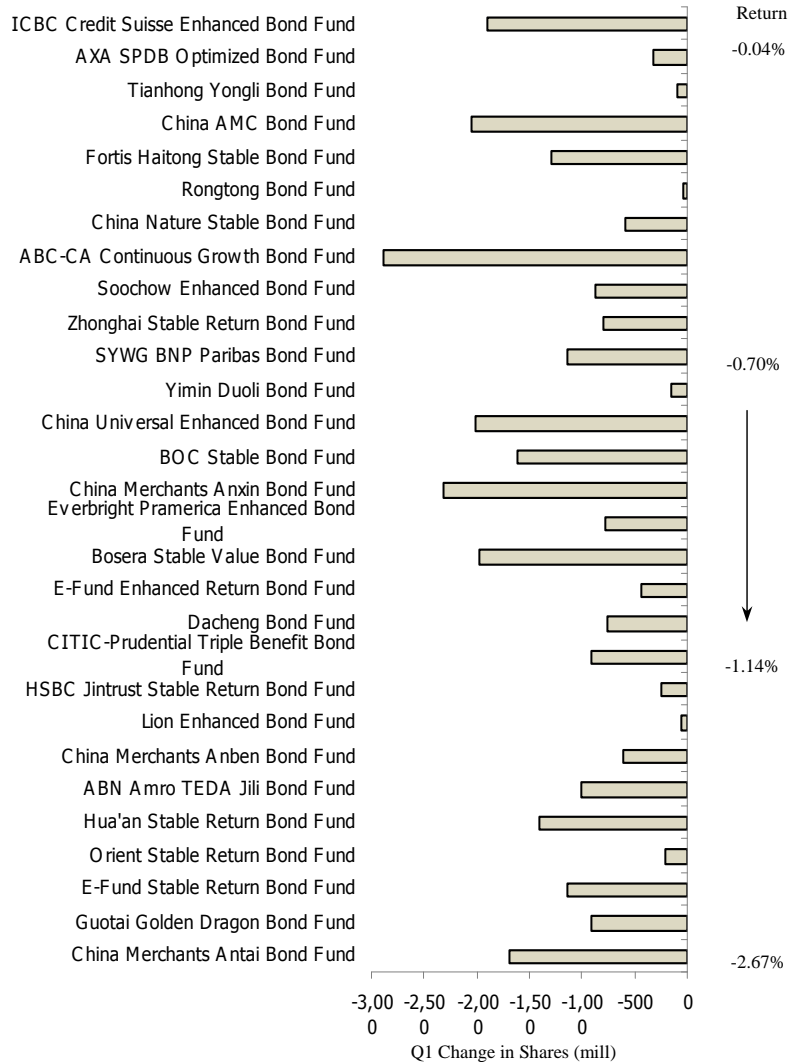


Exhibit 1.28: Half of all bond funds delivered a negative return in Q1

Periodic change in units/shares vs. return



Money market funds weren't the only asset class affected by changing market conditions. The same pressure on performance, along with appetite for equity exposure, led investors to exit from bond funds.

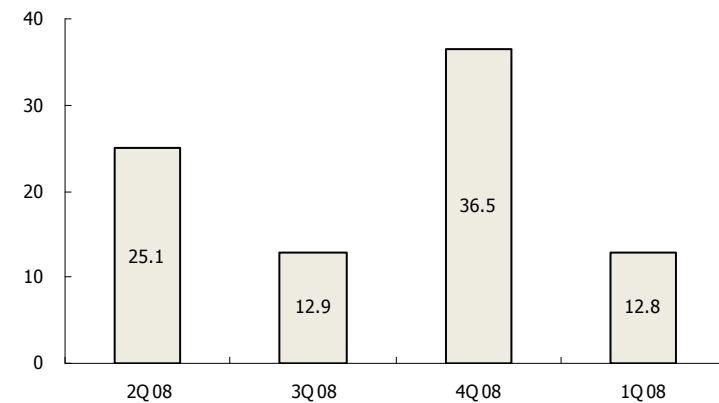
Overall, bond funds finished the period with a 31% outright decline in total units/shares in issuance (53bn). At the same time, end demand for newly launched bond funds fell by nearly two thirds in Q1.

The outlook for bond funds is darkening. Investors now view the product category as a less than attractive option given that half of the 59 funds on offer delivered negative absolute returns in Q1.

Much like their money market counterparts, there is a heightened risk of further redemptions among all bond funds in Q2. Here again, FMCs with AUM reliant on the product category will see market share negatively impacted.

Exhibit 1.29: Demand for new bonds funds is falling fast

Total AUM from new bond funds (Rmb bn)



Rmb1.00 Dilemma: The legacy and threat of redemptions

Market Sizing & Fund Flow Analysis

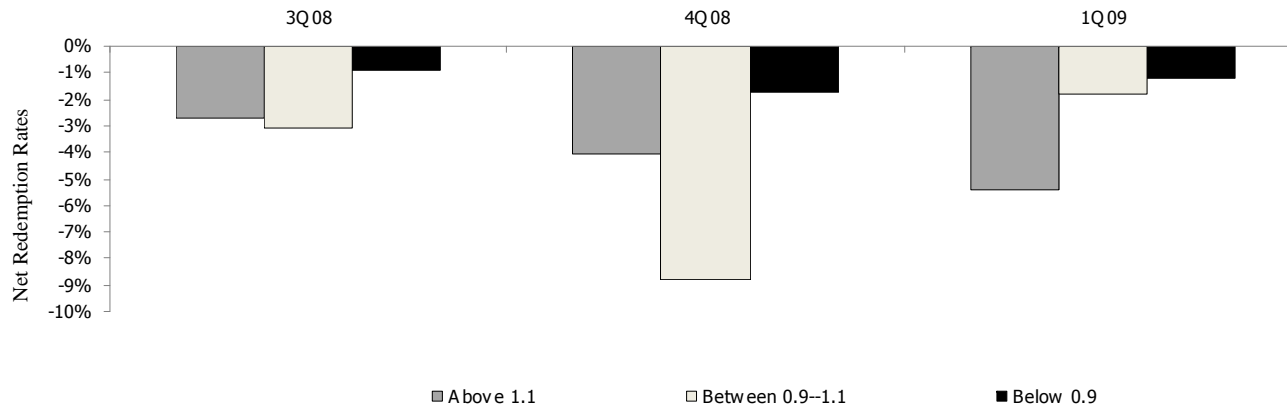
- Thematic Overview
- Industry AUM
- Industry Fund Flows
- Organic Growth
- New Products
- Demand Trends
- Demand Assessment
- Product Innovation
- Money Market Flows
- Bond Flows
- Rmb1.00 Dilemma**

Performance Assessment

The Impact

Competitive Fallout

Exhibit 1.30: Investors decide to lock in gains
Redemption rates for different NAV values



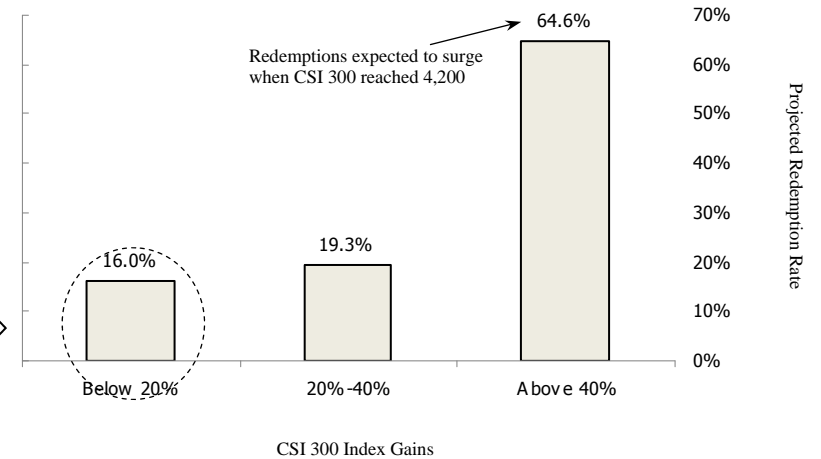
FMCs need to recognize the threat of added redemption pressure resulting from any additional gains in the CSI 300. A large swath of investors are looking for a point at which to recoup losses incurred from positions established at or near the market's 2007 peak.

The threat of redemptions will not turn acute until the CSI 300 moves up an additional 40%. Still, there are FMCs now at risk, three of which are highlighted below. To best address the potential for higher rates of redemptions, fund managers should start to reallocating resources towards attracting new demand for their "at risk" products.

Three Most Endangered Managers in the Short Term

| FMC | Units/Shares At Risk (Bn) | AUM at Risk |
|--------------------|----------------------------|-------------|
| Soochow | 4.09 | 45.27% |
| Yinhua | 16.96 | 31.25% |
| INVESCO Great Wall | 17.99 | 29.92% |

Exhibit 1.31: Redemptions projected to rise in tandem with the CSI 300 index
Redemption rates under different scenarios



Asset Class Performance: Absolute gains, but a relative disaster

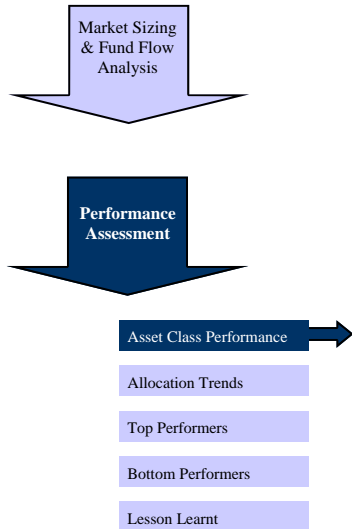
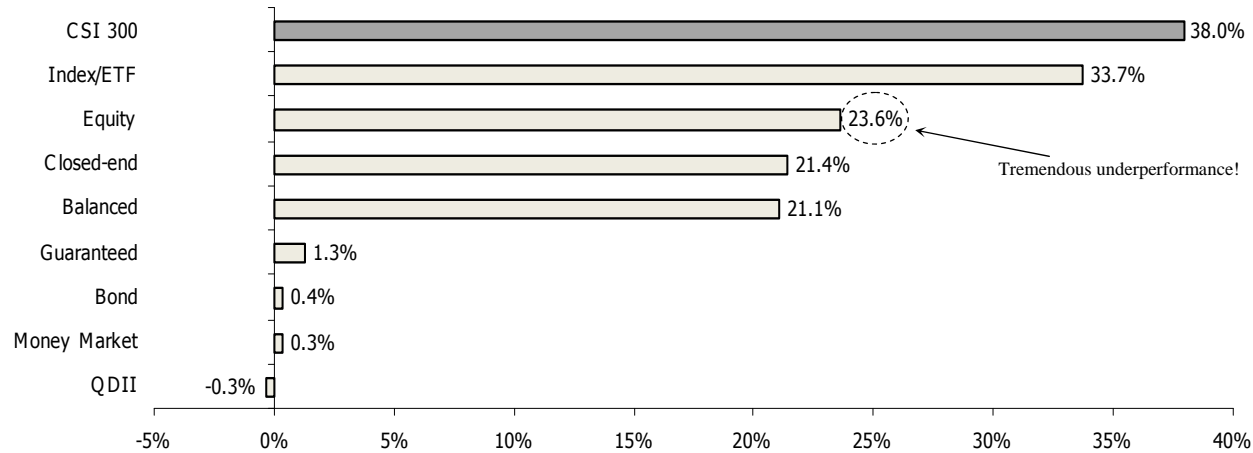


Exhibit 2.11: FMCs closed the quarter well below the benchmark

Q1 weighted average performance by product category

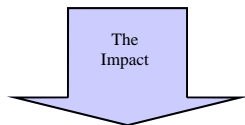


The benchmark CSI 300 index closed Q1 up 38%, making for one of the best quarterly periods on record. Nevertheless, FMCs failed to match this performance with the average equity mutual fund reporting gains well below the index. For the most part, this underperformance was the result of portfolio managers (with several fingers burned from last year) moving too slowly to increase their equity exposure.

Rapidly deteriorating conditions for interest rates had the expected impact on both money market and bond funds: periodic performance was well below the historic average. Those FMCs which had been anticipating additional cuts in rates by the PBoC were sorely punished by the bad call.

It will be necessary to monitor QDII mutual funds. While the offshore product category posted the worst-ever relative-to-onshore performance in Q1, more recent developments show gains which are stronger than those being reported by domestic mutual funds. Even fresh demand - scant as it is - can be found.

For the current quarter, portfolio managers will be forced to take a stand. Will equity prices move higher or will they correct (or simply stay range-bound)? Z-Ben Advisors believes that many portfolio managers' moves to increase equity exposure occurred at or near end-Q1 (Window dressing? See next page). For Q2, those FMCs best able to read the signs ahead of their competitors, whatever the direction but currently looking positive, should end the period far better positioned.



Allocation Trends: Getting aggressive or simply window dressing?

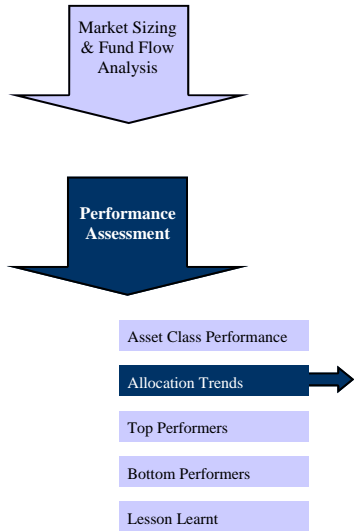
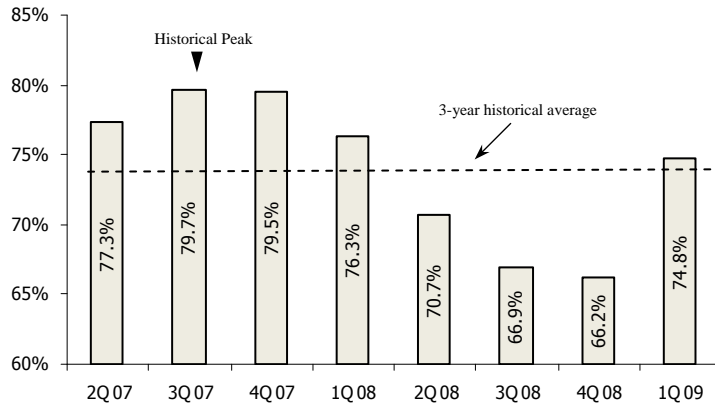


Exhibit2.12: Equity allocation moving back to trend line

Average equity fund stock allocation



Not wanting to let a good market rally go to waste, lest they be left behind, portfolio managers put more of their funds' idle assets to work. The moves were probably made at quarter's end based upon the earlier commentary on negative relative performance versus the CSI 300 index.

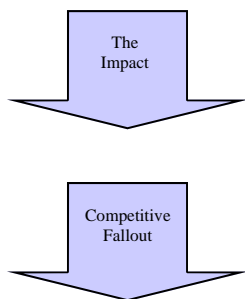
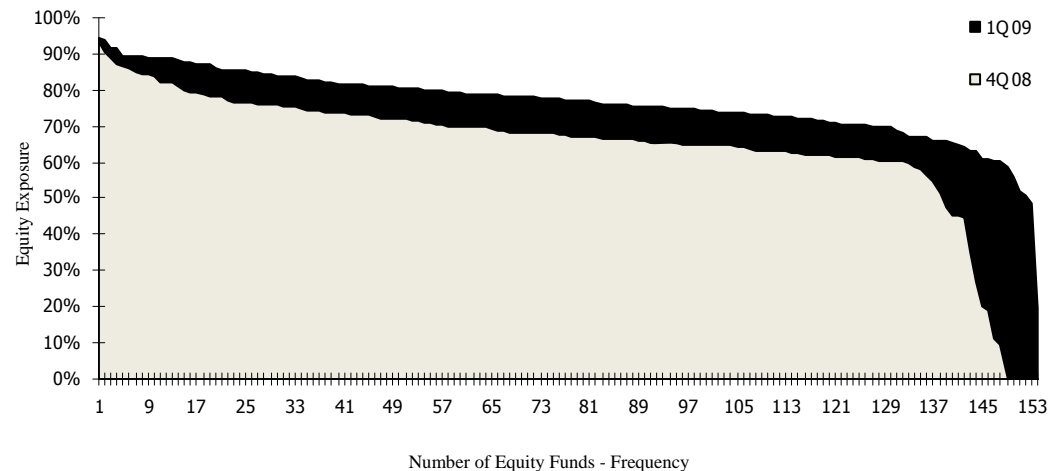
Window dressing or not, the move into equities was found throughout the entire product universe. Compared to 4Q08, the distribution of equity exposure moved in a positive direction.

Among those equity funds recently launched, the decision was made to quickly put cash to work. For the likes of the **Dacheng Strategic Return Fund** and the **CCB Principal Core Enhanced Fund** this then meant the start of a solid performance track record.

For Q2, and as the CSI 300 index moves steadily higher, FMCs are expected, at a minimum, to retain their collective exposure to equities. What remains to be seen is whether or not this will be expanded.

Exhibit2.13: Increased exposure held throughout the industry

Periodic equity exposure distribution



Top Performers: The mice that roared

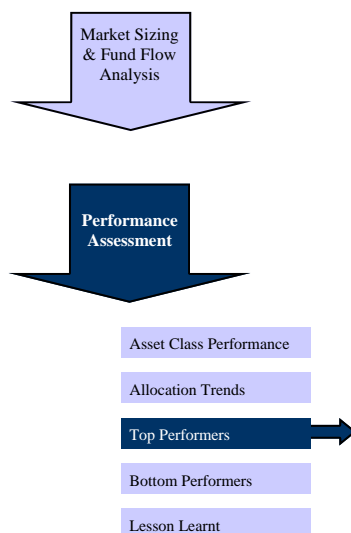


Exhibit 2.14: Small and mid-sized FMCs triumphed

Top Q1 performing equity mutual funds

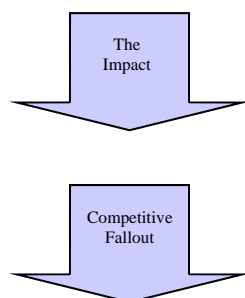
| Fund | Q1 AUM | Q1 RTN% | 1-YR RTN% | 2-YR RTN% | Δ SHARE | SHARPE | EQUITY% |
|--|---------|--------------|---------------|---------------|---------------|--------------|--------------|
| China Post & Capital Core Enhanced Fund | 13,426 | 45.5 | -22.53 | 14.74 | 2.8% | 19.40 | 88.83% |
| New Century Growth Equity Fund | 199 | 39.6 | | | 68.8% | 23.95 | 83.95% |
| Golden Eagle Small/Mid Cap Enhanced Fund | 754 | 39.5 | 1.42 | 13.75 | 235.8% | 21.41 | 54.48% |
| China AMC Enhanced Large Cap Fund | 4,135 | 37.8 | -1.48 | 81.95 | -1.2% | 20.24 | 55.63% |
| China Post & Capital Core Growth Fund | 22,8467 | 37.2 | -24.35 | | -1.0% | 17.78 | 78.44% |
| GTJA Allianz Enhanced Equity Fund | 1,888 | 36.7 | -27.32 | -0.29 | -0.4% | 15.64 | 85.41% |
| AEGON-Industrial SRI Equity Fund | 2,566 | 36.4 | | | 112.5% | 21.09 | 84.99% |
| Full Goal Tianrui Regional Wealth Fund | 6,333 | 36.0 | -15.63 | 12.74 | 24.1% | 17.66 | 84.79% |
| Harvest Thematically Enhanced Fund | 7,805 | 35.3 | -16.70 | 15.25 | 15.9% | 14.93 | 91.55% |
| Guangfa Small Cap Growth Fund | 9,502 | 34.8 | -28.78 | 0.08 | 1.0% | 16.10 | 80.77% |
| Equity Fund Average | | 22.2% | -22.1% | 11.52% | -0.41% | 12.94 | 73.5% |

While the top ranking equity funds in Q1 include a few recognizable names, such as **Harvest** and **Full Goal**, the period was dominated by many of the industry's small- and mid-tier FMCs. It was also a period which ushered in the return of **China Post & Capital**.

At the same time, **Golden Eagle** proved how even the smallest of firms can attract new demand so long as they can point to consistently strong relative-to-peer performance. The portfolio manager should also be commended for achieving the results (stock picking prowess) with actual equity exposure of just slightly more than half.

There is also **AEGON Industrial** which continues to deliver strong relative-to-peer performance. The firm ended up with net new inflows which proved to be so robust that total units/shares in issuance more than doubled in Q1

Not to be overlooked is the **China AMC Enhanced Large Cap Fund**. While consistently ranked among the best performing mutual fund, the portfolio manager recently questioned the sustainability of the current rally in equities. This concern is made evident in the fund's lower than average - and by a wide margin - exposure to equities (55.6%).



OUTLOOK: The composition of the top performing funds in Q2 will be dependent on where the equities market trends. Currently, those FMCs positioned for additional gains are best placed. A sell off would, however, benefit those firms readily seen as being the best defensive players.



Exhibit 2.15: Which FMCs are best positioned?

| Strategy | Fund Houses |
|--|---|
| Aggressive Equity Allocation | China Post & Capital, Everbright Pramerica, Guangfa |
| High beta (financial services, real estate and small/mid cap stocks) | Golden Eagle, China AMC, AEGON-Industrial |
| Defensive | ABN Amro TEDA, Galaxy |

Bottom Performers: Hare beats tortoises

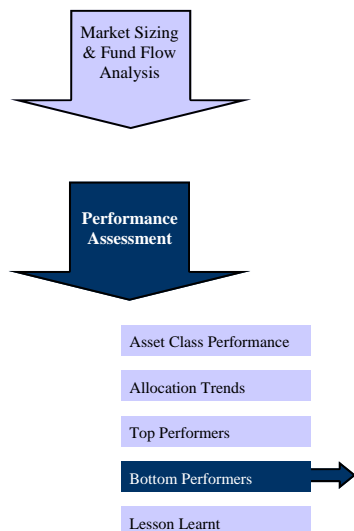


Exhibit2.16: Weak returns from a broad range of mistakes

Bottom Q1 performing equity mutual funds

| Fund | 1Q09 AUM | Q1 RTN% | 1-YR RTN% | 2-YR RTN% | Δ SHARES | SHARPE | EQUITY% |
|---|----------|--------------|---------------|---------------|---------------|--------------|--------------|
| HSBC Jintrust 2016 Lifecycle Fund | 820 | 6.69 | -8.10 | 17.76 | -1.0% | 7.70 | 41.97% |
| China Universal Blue Chip Balanced Fund | 560 | 7.57 | | | -22.5% | 5.59 | 77.03% |
| Soochow Value & Growth Fund | 1,693 | 7.76 | -34.51 | 17.87 | -7.5% | 4.18 | 85.56% |
| Full Goal Tianyi Value Fund | 11,082 | 8.44 | -24.92 | 9.41 | -5.7% | 5.50 | 78.30% |
| INVESCO Great Wall Dynamic Balancing Fund | 6,108 | 9.29 | -25.26 | 3.75 | -2.1% | 9.32 | 47.46% |
| China Universal Focused Growth Fund | 10,336 | 9.89 | -31.48 | -6.01 | -2.1% | 6.50 | 89.44% |
| GTJA Allianz Anxin Growth Fund | 455 | 9.97 | -12.25 | 15.30 | 227.2% | 8.14 | 51.55% |
| China Merchants Antai Balanced Fund | 173 | 10.36 | -8.00 | 16.70 | -0.5% | 10.57 | 48.58% |
| China Universal Balanced Growth Fund | 19,097 | 10.47 | -25.00 | 5.91 | -2.1% | 6.86 | 87.67% |
| E-Fund Stable Growth Fund | 4,089 | 10.53 | -16.75 | 15.72 | -9.7% | 8.78 | 53.40% |
| Equity Fund Average | | 22.2% | -22.1% | 11.52% | -0.41% | 12.94 | 73.5% |

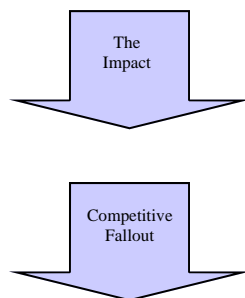
Risk aversion by FMCs crippled performance in Q1. Those products having a lower equity allocation and lower Sharpe ratio all but guaranteed sharp underperformance. Still, many of the FMCs included in the sample are typically slow asset allocators. Expect the group to revise their exposure to stocks upwards regardless of market conditions.

A qualitative assessment of why some funds underperform shows equity exposure to be only one of four possible variables. Stockpicking affected two FMCs (**Full Goal** and **INVESCO Great Wall**) which normally tend to outperform in times when equities are rising. But it is **China Universal** which may be testing investors' patience most having three of the worst performing funds in Q1 even with equity exposure at +85%.

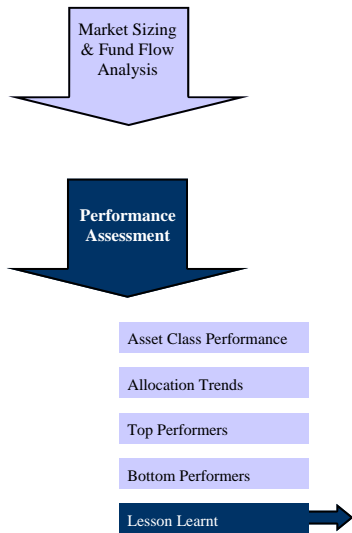
Exhibit2.17: How not to succeed in volatile times

Qualitative matrix of bottom performing funds

| Fund | Market Timing | Equity Exposure | Industry Allocation | Stockpicking |
|---|---------------|-----------------|---------------------|--------------|
| HSBC Jintrust Lifecycle Fund | √ | √ | | |
| Soochow Value & Growth Fund | √ | | | |
| Full Goal Tianyi Value Fund | √ | | √ | √ |
| INVESCO Great Wall Dynamic Balance Fund | | √ | | √ |
| China Universal Balanced Growth Fund | √ | | √ | √ |
| GTJA Allianz Anxin Growth Fund | √ | √ | | |
| China Merchants Antai Balanced Fund | | √ | | |
| E-Fund Stable Growth Fund | | √ | | |



Lessons Learnt: Insight from those in the know



What it takes to win.....

In both 2007 and 2008, the defining variable separating the top performing funds from the rest of the pack was speed at shifting asset allocation. Those FMCs quick to ramp up equity exposure early in 2007 delivered better relative-to-peer performance. The data included within this report shows a clear increase in the average exposure to stocks among equity funds. What Z-Ben Advisors has been unable to ascertain with certainty is whether these increases signal a true commitment on the part of the portfolio managers or if they were nothing more than window dressing.

Small would appear to be beautiful of late as all but two of the top ten best-returning funds managed AUM of less than Rmb10bn (and as low as Rmb0.2bn.) When evaluating the underlying portfolio of many top-performing funds we find that stockpicking proved to be invaluable. Getting in an out of small and midcap shares is simply an easier job for fund managers who leave a smaller footprint.

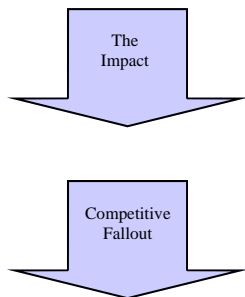
Conditions, on multiple levels, change rapidly in China. A strategy which worked in one quarter can prove devastating in the next. From Z-Ben Advisors' perspective, growth risks are now better balanced, which should prompt larger equity allocations. Whether or not being far ahead of the pack will be rewarding is the current quarter's key question.

..... and what should be avoided

Unless you must, never commit to a specific strategy. Z-Ben Advisors is an ardent proponent that FMCs should create a portfolio of products having clearly defined investment objectives. For all, however, there should be at least one product which allows for the upmost flexibility in setting equity allocation.

Experience counts no matter market conditions. This proved to be truer than not in Q1, and we would argue in the current quarter, will count again when it comes to identifying sector rotation and, in the best possible scenario, those stocks well placed in the industry.

Brushing themselves off, many of the worst performing funds in Q1 have taken action. Having said that, and even though Z-Ben Advisors' outlook for the equities market is positive, FMCs will also need to communicate to investors that capturing more of the market's gains increases the potential for volatility. Equity-avoiding allocation strategies gave many investors a smooth, if downhill, ride in 2008. To obtain stronger absolute and relative performance in 2009, these same investors will have to be reminded that they will be required to accept a choppier ride.



QDII Funds: The good and bad news



QDII Funds

ETF Churn

Dividends

Proprietary Trading

Manager Moves

Distribution

Fee Ratios



For the first time ever, QDII mutual funds posted quarter-on-quarter organic growth in total units/shares in issuance albeit slight at just 0.31bn shares. Notwithstanding this possible silver lining, although it is getting a lot of play locally, China's small contingent of offshore products ended the period with a massive gap in performance (-0.31%) compared to the returns delivered by onshore equity mutual funds (23.6%).

In possible response to this very weak relative-to-onshore performance, FMCs with a QDII mutual fund having a NAV greater than Rmb1.00 are now declaring dividends. The first to do so was **Fortis Haitong** which is expected to be quickly followed by **Bank of Communications Schroders**. Performance, however, will remain at the mercy of near term global market trends.

Irrespective of the challenges which exist, the outlook for QDII remains firmly intact. Recently, CSRC approved the 29th manager to participate (**ABN Amro TEDA**) and there is growing speculation within the market that the State Administration of Foreign Exchange (SAFE) is set to make USD5.0bn of new quota available. Furthermore, CSRC announced a broadening in the scheme by permitting FMCs to begin marketing QDII segregated accounts. For more on the topic see Z-Ben Advisors' latest *QDII Quarterly Review: "Start Your Engines (Really!)"*

While there is a distinct possibility of new QDII mutual funds coming to market sometime in the coming months (although most likely capped at USD1.0bn each), demand will more than likely be soft. Nevertheless, with only nine QDII mutual funds currently on offer, there is ample room for competition and all FMCs would be well advised to have a "bucket" in place for when demand does - and it will - resurface.

Exhibit 3.11: A First! Net increase in subscriptions for QDII

Quarter-on-quarter Δ in total QDII units/shares in issuance (bn)

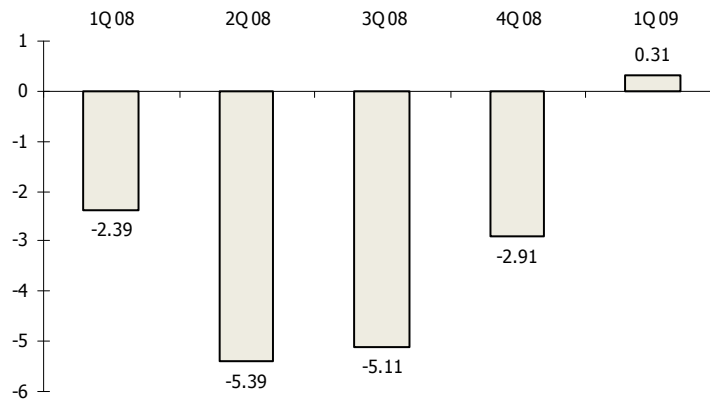
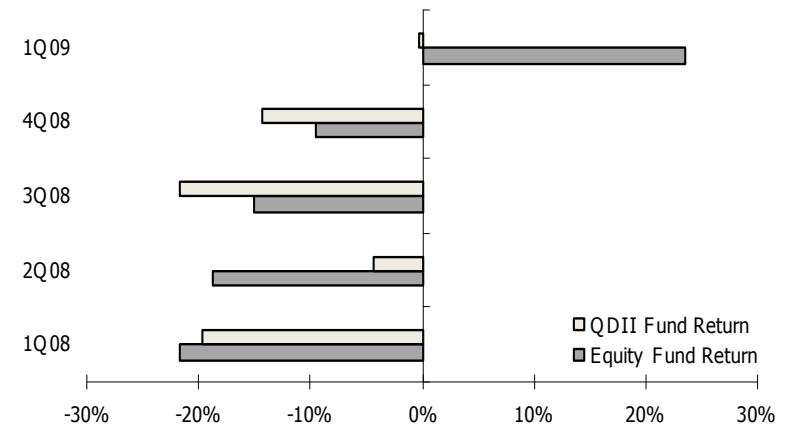


Exhibit 3.12: Massive disconnect in onshore vs. offshore returns

Periodic return comparables

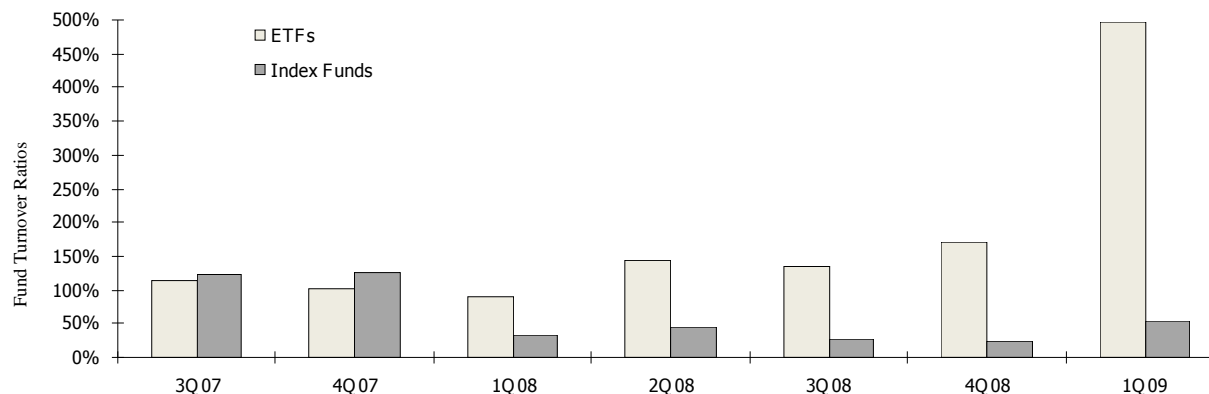


ETF Churn: Arbitrage opportunities aplenty



- QDII Funds
- ETF Churn** →
- Dividends
- Proprietary Trading
- Manager Moves
- Distribution
- Fee Ratios

Exhibit 3.13 : Trading volumes among ETFs surged in Q1
Gross redemption and subscription



Even though actual net redemptions for ETFs registered in the single digits (5.2%) for all of Q1, gross redemptions and subscriptions totaled nearly 5x the outstanding units/shares in issuance. Behind this odd phenomenon are a growing number of investors using ETFs as a tool for arbitraging price discrepancies.

The opportunity to earn profits with little risk has been in place for some time. But with equity prices moving higher, far better liquidity (Rmb4.56tr worth of new bank loans) along with the active promotion of ETFs, made it arguably easier to gain by trading in and out of these passive products.

Investor churn can positively augment a FMC's top and bottom line as front and back end fees accrue to the manager. This, along with a limited number of available ETFs currently available, has led to an increasing number of applications for new product substitutes (see table below). Still, the sudden jump in Q1 turnover may attract regulatory attention and restrict the approval of new ETFs

Exhibit 3.14 : FMCs continue to press for new ETFs

Proposed ETFs awaiting product approval

| ETF | FMC | Exchange |
|-------------------------|--------------------|----------------|
| CSI300 | AIG-Huatai | Shanghai |
| CSI300 | Southern | Shenzhen |
| Shanghai Mega Cap | Bosera | Shanghai |
| SOE Index | ICBC-Credit Suisse | Shanghai |
| Growth Enterprise Board | TBD | GEM - Shenzhen |



Dividends: Meeting investors' demands for income



- QDII Funds
- ETF Churn
- Dividends** →
- Proprietary Trading
- Manager Moves
- Distribution
- Fee Ratios



Even though the CSI 300 index gained considerable ground in Q1, FMCs were reluctant to declare a dividend in their equity funds. With many such funds trading at NAVs under Rmb1.00, the issuance of a dividend might have been all but impossible. Such was not the case for recently launched funds, as the vast majority (22 out of 25) of those funds declaring a dividend were brought to market over the past year. Still, most of these were bond funds which are supposed to pay income.

Not only has the number of dividend declarations subsided, so too has the average dividend payment itself dropped with just Rmb0.373 per ten shares paid throughout Q1. This is the result of fixed income dominance and the product category's weak performance, which limited the size of dividends which could be distributed back to investors.

Investors have been clamoring (with increasing volume) for income and FMCs should closely monitor this situation in Q2. Doing so would also be advantageous to a manager. Research clearly shows greater success in retaining assets among those funds which declare a dividend versus those which do not. Having said that, investors have a rather short memory. If the equities market moves steadily higher it would be expected that investors would want less income in favor of greater capital appreciation.

Irrespective of, or even in spite of, the just-noted points, there are a number of FMCs in a position for one or more of their products to pay a dividend. There is the **Fortis Haitong Stylized Advantage Fund** and the **AIG Huatai Value & Growth Fund** both of which are prime candidates to declare a dividend.

Exhibit 3.15: Dividend paid by open-ended funds decreased
Quarter-on-quarter change in dividend payment

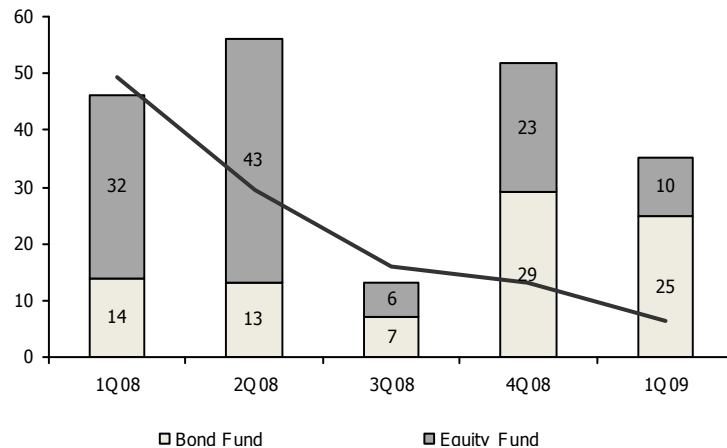
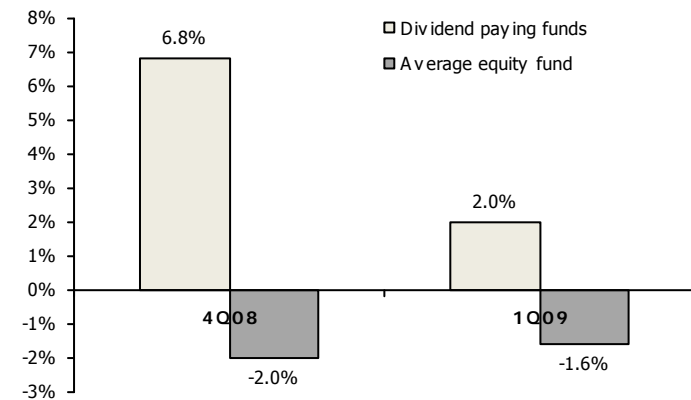


Exhibit 3.16: Dividend payers continue to retain more assets?
Quarterly change in shares of equity funds



Proprietary Trading: Market uncertainty prompts strategic change



- QDII Funds
- ETF Churn
- Dividends
- Proprietary Trading
- Manager Moves
- Distribution
- Fee Ratios



Overall, the total level of FMC proprietary investment activity declined in Q1 (Rmb423m vs. Rmb376m), but it was the destination to where the in-house capital went which needs to be noted. The final quarter of 2008 saw a full three-quarters of investment directed into fixed income funds. For Q1, the opposite was the case - and more so - with FMCs allocating nearly 90% of their collective investment into equity funds.

Prop trades have reverted back to their original objective: acting as an internal cash management tool and, fingers crossed, an auxiliary source of income for FMCs. No longer, or at least to a lesser extent, are FMCs using their own capital base to support a new product launch.

But for every FMC deploying capital into a product, another is using the current market rally to lock in gains. While highly inconsistent quarter-to-quarter, combined prop redemptions in Q1 totaled Rmb281m, well above the Rmb41m sold at the end of last year. FMCs continue to sit on large prop trades made over the past several years and may look to use the current market rally to sell out of their positions. Such an outcome isn't, however, guaranteed. FMCs were highly profitable throughout 2008 and have ample cash to invest without tapping long-term reserves.

There is also the issue of whether the prop trades actually made any money. The answer is yes for the **CITIC Prudential Dual Income Bond Fund** with a 30% estimated gain. Elsewhere, **CCB Principal** announced the unwinding of three positions none of which earned the FMC a profit. The losses were also rather steep ranging between -23% and -34%.

Exhibit 3.17: Equity prop investing is rising ...

Proprietary investing by fund managers (Rmb m)

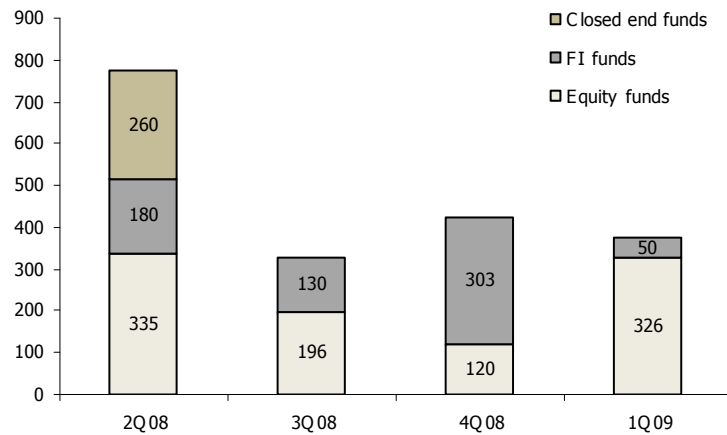
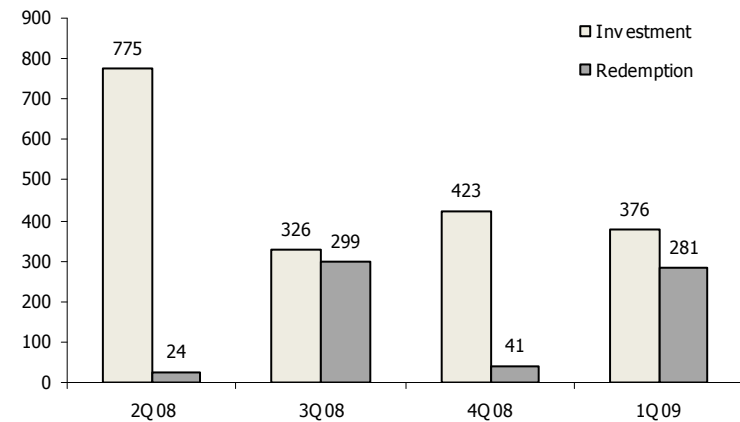


Exhibit 3.18: ... but so are overall redemptions

Proprietary redemptions by fund managers (Rmb m)



Manager Moves: Addressing turnover is now about quality, not quantity

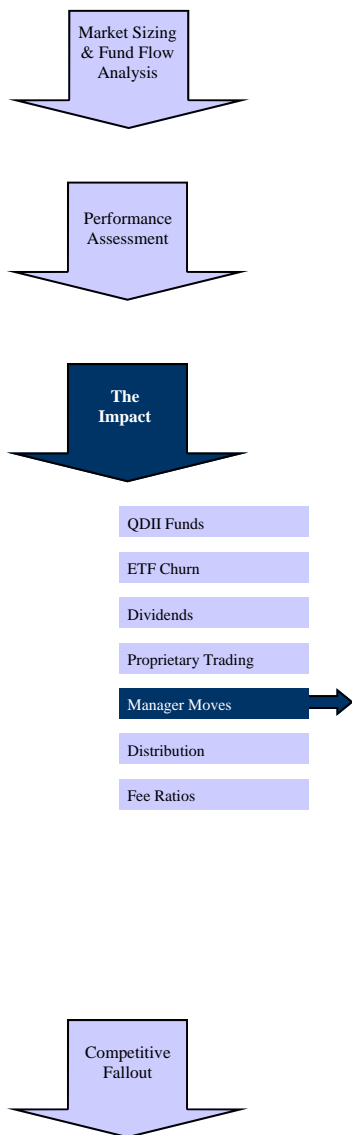
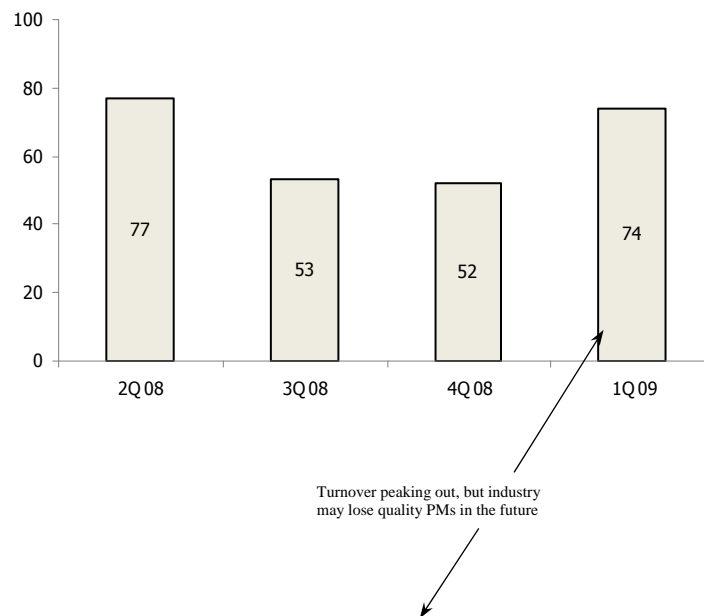


Exhibit 3.19: PM turnover was artificially high in Q1

Quarter-on-quarter change in PM move



Even though the turnover rate among the industry’s portfolio managers (PMs) rose in Q1, it is widely expected to trend downward in coming months. Recently introduced rules - going into effect on April 1st and supported by the Securities Association of China - will now make it far more challenging for PMs to job hop.

While the expectation of lower turnover is readily agreed, FMCs may need to shift their attention away from “quantity” and consider whether “quality” departures will become an issue. Several individuals left the industry altogether, including a few highly experienced PMs.

Given the new rules, PMs may begin to push internally for a reassignment. A more liberalized segregated accounts business (minimum account requirements were recently reduced from Rmb 50m to Rmb1m) could result in seasoned PMs exiting from managing mutual funds in favor of private in-house clients.

All PMs will be forced to take a long, hard look if opportunity comes knocking. More moves can be expected, but only when the time is right. This is a vitally important concept for all FMCs to keep in mind, but especially those firms with individuals running a top performing fund, such as **AEGON Industrial** and **Golden Eagle**.

Exhibit 3.20: More experienced managers bid adieu

Recent high profile departures

| Name | Funds managed | Return | CSI 300 | Remark |
|---------------------------|--|--------|---------|--------|
| Mr. Yan Zhenghua | 2007.07-2009.03: China AMC Return Fund/Return #2 Fund | -6% | -48% | - |
| Mr. Zhang Guoqiang | 2006.07-2009.02: CITIC Stable Dual Income Bond Fund | 44% | 72% | - |
| Mr. Zeng Zhaoxiong | 2007.03-2009.01: First State Cinda Leading Growth Fund | -17% | -23% | CIO |
| Ms. Wang Xinyan | 2007.06-2009.03: Enhanced Blue Chip Fund | -29% | -45% | CIO |

Distribution: Rabid demand for a single channel

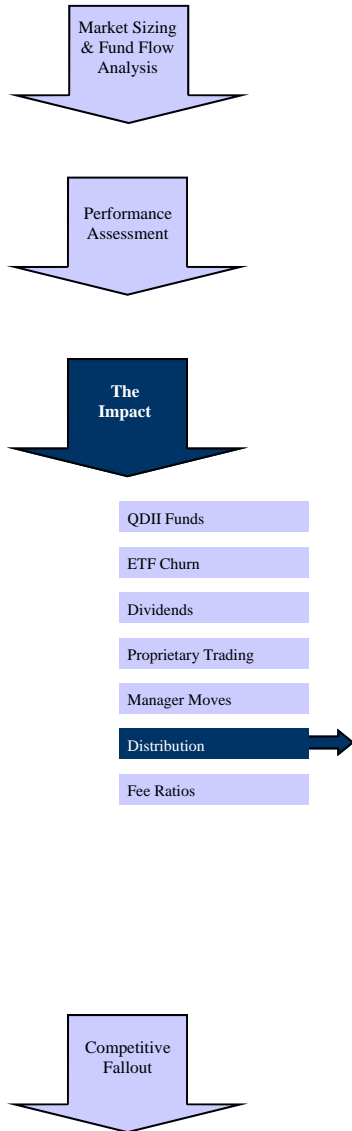
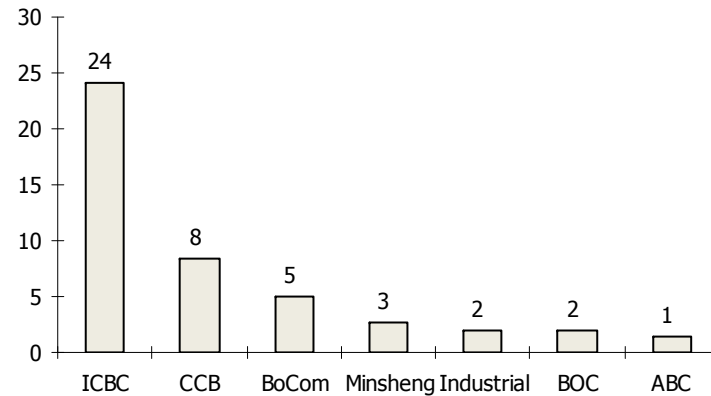


Exhibit 3.21: ICBC is the king of distributors

Number of new products brought to market



Historically, FMCs chased after those commercial banks having the widest branch network. For a number of reasons, demand for access in Q1 centered on just two of the channels, CCB and ICBC, with FMCs strongly preferring ICBC.

One distributing practice which will need to be revised is last year's use of institutional support at the time a new product went to market. With demand at depressed levels, FMCs required the assistance of institutional customers, which was evident from starkly higher average accounts sizes. It is now clear that the support was temporary and redemptions are playing merry hob with the size and performance of many of 2008's most notable new funds.

There is considerable room for alternative distribution channels and China International has proven that a quasi-direct sales force can greatly assist in both assets gathering and retention. Other new models are also being introduced, albeit still via the bank channel. Savings plans such as DEDT have immense promise but will be slow to change the dominant distribution tactic: call ICBC and plead.

Fee Ratios: On the rebound

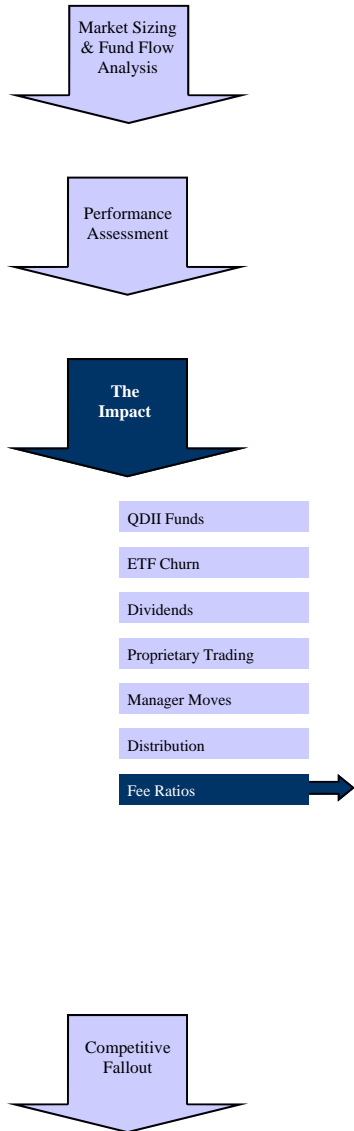
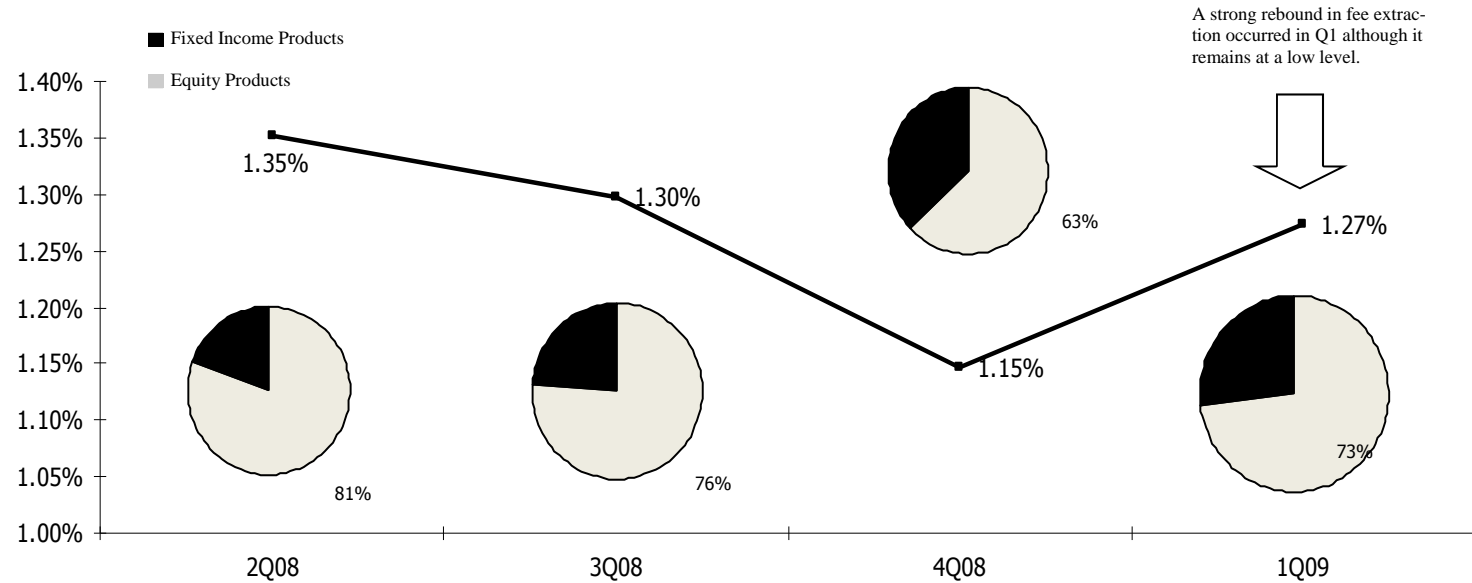


Exhibit 3.22: Fee extraction up, but unsettled
Average fee extraction vs. industry AUM segmentation



After declining throughout all of 2008, the industry’s weighted average fee extraction rate rose by 12bps in Q1 as the result of investors’ exodus from fixed income products towards higher fee-generating equity funds. A further expansion in the fee extraction rate is expected in Q2 as the same conditions which existed last quarter impact fund flows. Just how far the industry’s fee extraction rate can climb, however, is uncertain and a return to +140bps may not be a high probability.

The impact of an improving potential fee extraction rate will affect all FMCs differently. To best protect against any material erosion in revenue and profitability, those firms with a higher concentration in fixed income products can be expected, if not forced, to launch a new equity fund. Those seeing large jumps in fees, however, may not necessarily be able to exploit their gains quickly: highly equity-focused FMCs were some of 2008’s worst performers and may prefer to run cash reserves back up to healthier levels before moving forward with new funds.

Market Share: A tale of two outcomes

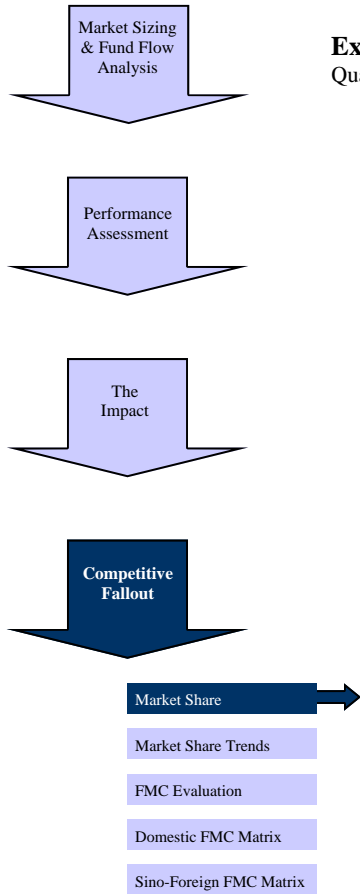
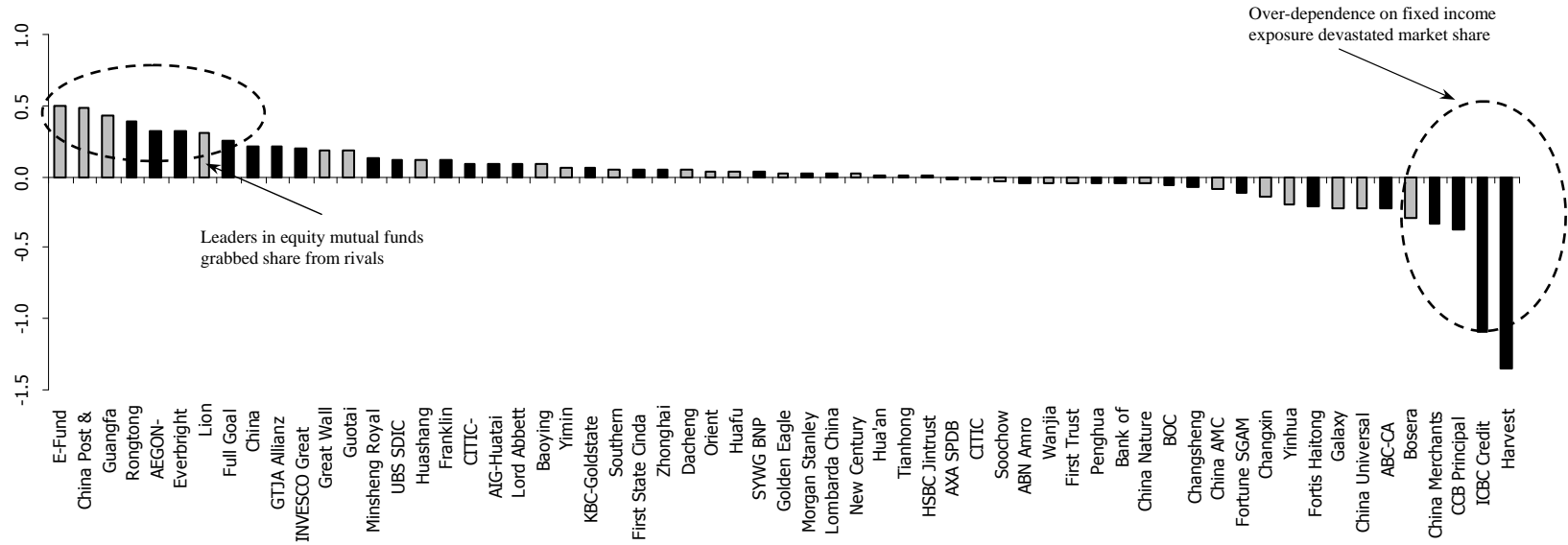


Exhibit 4.11: The good, the bad and the truly ugly
Quarterly change in market share (bps)

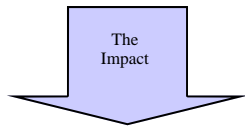


It proved to be a rather easy task when the time came to assess the change in market share for Q1. For those FMCs which are widely recognized as leaders in the equity fund space, gains in share were typical, including a 50bps pick up for **E-Fund**. At the opposite end of the spectrum were FMCs overly exposed to fixed income, with **Harvest** shedding 135bps of share and **ICBC Credit Suisse** losing 109bps.

The muddled masses were left, for the most part, neither gaining or losing ground. For Q2, however, there is the expectation of heightened turnover in the market share leadership rankings. A number of FMCs were still at risk of fixed income redemptions - including **Fortis Haitong** - while managers such as **China Post & Capital** look to be moving from strength to strength.

To break out and rise above the noise, FMCs ranked in the middle will need to take action. Ramping up relative performance in equity funds, along with a bit of luck when launching a new product (such as with **Changsheng**), could make all the difference.

Market Share Trends: A slightly more competitive landscape



- Market Share
- Market Share Trends
- FMC Evaluation
- Domestic FMC Matrix
- Sino-Foreign FMC Matrix

Small-and-mid-tier companies trumped their larger rivals in Q1 and, in doing so, led to further declines in the collective share of the top five FMCs which, at end-Q1, stood at just above 32% (down nearly two full percentage points). This lessening in competitive concentration is expected to continue over the current quarter. Having said that, a cyclical bottom may have been reached and the industry's largest FMCs never lie down when times are good. AUM growth and asset gathering from the likes of **China AMC** and **Southern** in the second half of the year should be above the industry average.

The FMCs suffering the brunt of investors' exodus from fixed income products were those backed by a commercial bank. Granted, these managers, including **ICBC Credit Suisse** and **CCB Principal**, benefited from considerable demand for cash-equivalent exposure in 4Q08. Then again, that demand proved to be short lived. As a group, also including **Bank of Communications Schroders**, which ended the period slightly up, their 18.3% combined share of Sino-foreign AUM declined to 15.4%.

Market share for Q2 will be impacted by two variables, each of which has been stressed throughout this report. They are also the very same factors impacting market share in Q1: fixed income redemptions and the combination of inflows and capital appreciation among equity mutual funds. FMCs whose product profile is biased towards fixed income (including those bank-backed managers noted above) are at risk of losing share. Managers recognized in the market as leaders in equity fund management, including **Guangfa** and **China International** to name just two, are well placed to grab share from their rivals.

Exhibit 4.12: The largest manager are losing their mojo
Top five FMCs' market share and AUM (Rmb bn)

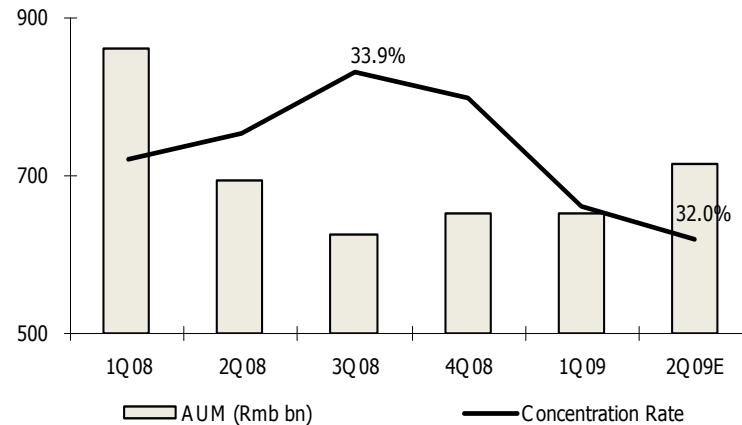
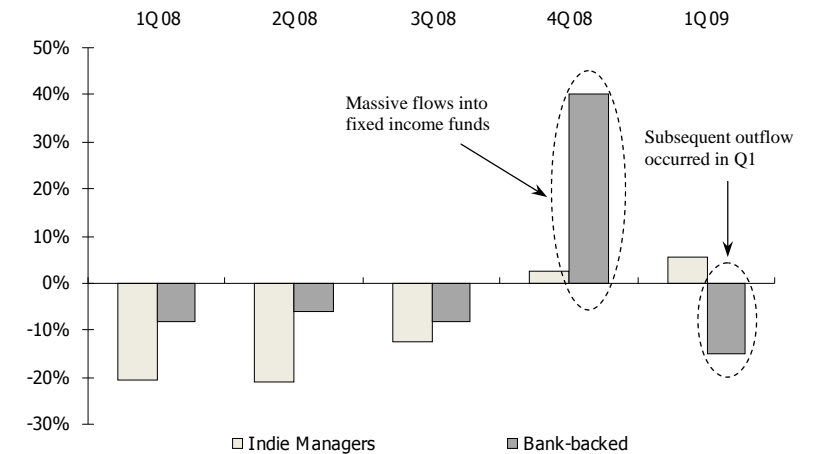
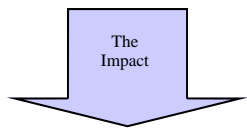


Exhibit 4.13: Bank-backed FMCs were hardest hit by FI fund flows
Quarterly AUM growth rates

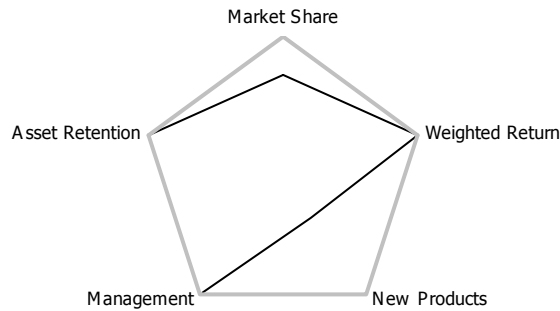


FMC Evaluation: The leaders



- Market Share
- Market Share Trends
- FMC Evaluation** →
- Domestic FMC Matrix
- Sino-Foreign FMC Matrix

China Post & Capital



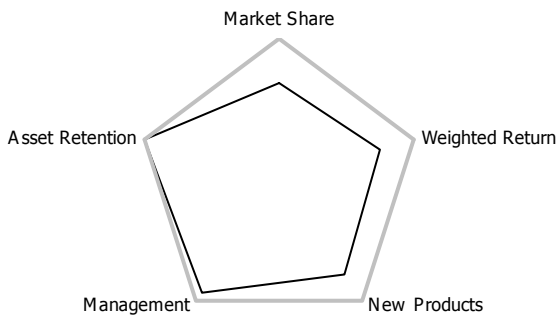
The delivery of superb returns was the most prominent achievement by China Post & Capital in the quarter: the firm’s flagship Core Enhanced Fund outperformed the CSI 300 index by 7.5 percentage points while its sibling Core Growth Fund finished only a fraction behind the market.

Behind the performance was stellar stockpicking. Higher than industry average equity exposure (a decision which was maintained through last year’s market downturn) also gave returns a strong beta boost.

China Post & Capital had closed its funds to new subscriptions for more than a year. However, management announced the reopening of the Core Enhanced Fund three days prior to the quarter’s end with new subscriptions totaling 548m shares over that short period of time.

The primary weakness which needs to be addressed is the firms’ limited product range, which constitutes only two highly-similar equity funds.

GTJA Allianz

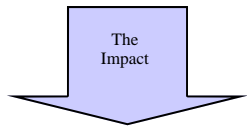


Change can be good and things will certainly look that way for GTJA Allianz. A realignment within the C-suite, including the appointment of a seasoned local executive into the role of General Manager as well as new investment professionals, appears to have had a healthy impact on both asset retention and sales

The firm finally launched its first fixed income product, a much-needed and diversifying extension to its range, which raised the largest amount of AUM of any new bond fund in Q1.

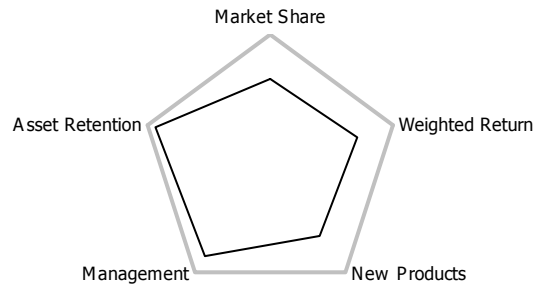
Although that success, coupled with good sales elsewhere, almost doubled GTJA Allianz’ market share, the firm remains small at 47 basis points in total industry share, a low total that suffers for being spread across a seven product range. Creating scale remains a challenge.

FMC Evaluation: The leaders



- Market Share
- Market Share Trends
- FMC Evaluation** →
- Domestic FMC Matrix
- Sino-Foreign FMC Matrix

AEGON Industrial

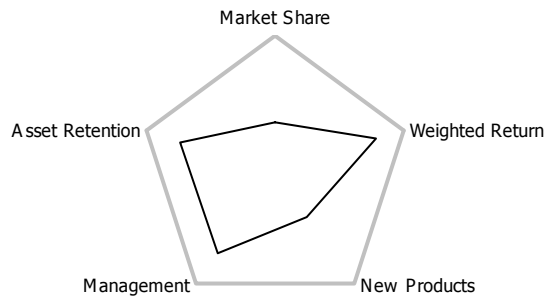


The firm was one of the more successful fund houses in all of 2008. That success has been carried over into the current year with fund redemption levels in Q1 lower than any of its competitors.

Overall, management appears to be running a stable and conservative business, which makes its decision to upweight equities by 2000 basis points in Q1 (to 68%) all the more surprising. In hindsight, of course, this proved to be a very shrewd move.

Investment success hasn't yet translated into substantial sales or product launch growth for AEGON Industrial. Inflows and launch sizes remain below the industry average. Attention should be refocused on launching a new equity fund which is where its recent performance track record could best be leveraged.

Golden Eagle

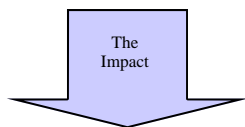


Small companies and small funds - the ones capable of reacting quickly - had the table set for them in Q1. And it was Golden Eagle which made the most of the market's high returns and high cross-sectional volatility.

The Golden Eagle Small/Mid Cap Fund was the best performing balanced fund for the period. Performance, directly supported by investor demand, led to a tripling of the product's shares in issue by quarter's end.

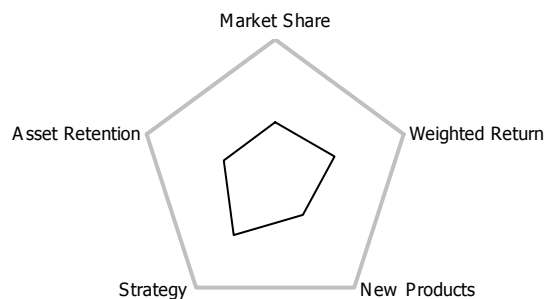
The quarterly retention rate for the firm's sibling balanced fund, launched last year, was much less attractive. In fact, with a loss of a third of its shares in issue it appears that investors used the 33.9% gain in Q1 as a point in which to exit. Stability remains elusive for Golden Eagle (and for many smaller firms) but any continuation of its current performance streak can only help.

FMC Evaluation: The laggards



- Market Share
- Market Share Trends
- FMC Evaluation** →
- Domestic FMC Matrix
- Sino-Foreign FMC Matrix

ABC-CA



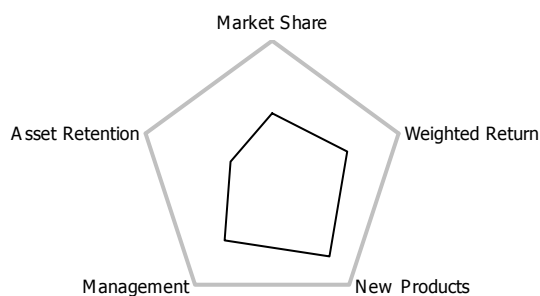
Huge redemptions in the second product launched by ABC-CA caused it to suffer the worst pains of the quarter. However, the pain was predictable: Q1 saw an exact repeat of the company’s experiences with its debut fund, which also lost more than 50% after opening to redemptions post-launch.

Unfortunately, that first fund lost an additional 50% of its shares in issuance in Q1 as well. So, even though the firm raised the single largest equity mutual fund in 2008, that fund is now a quarter of its original size.

In the end, ABC-CA shed considerable market share in Q1. A firm which had, in its first year, taken 5.0% of share found nearly half of that given back in Q1.

Market share, currently 2.7%, should expand in the current quarter with the recent successful launch of a third fund, raising Rmb6.5bn. Attention, however, must be directed at asset retention.

Harvest



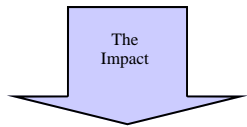
Harvest had steadily climbed the market share rankings, peaking out in the number two spot. Massive redemptions from its various fixed income products, however, led to the sharpest Q1 decline in market share among all fund managers. In the end, the firm dropped to the third spot.

Mediocre performance among the firm’s mainstream funds was widespread although may have been the result of heightened redemption pressure elsewhere.

One quarter does not make a trend, and Harvest was not alone in suffering from fixed income outflows. Furthermore, the firm delivered considerable success in a recently launched equity fund.

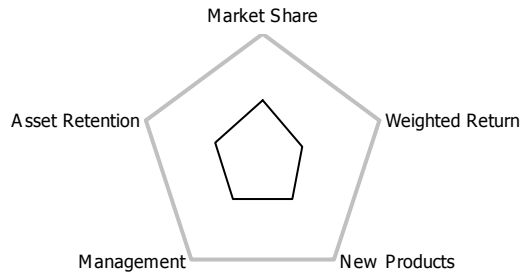
Notwithstanding the above comment, management will need to closely monitor its fixed income product exposure. Redemption pressure remains intact and, pending the severity in Q2, may keep market share growth subdued.

FMC Evaluation: The laggards



- Market Share
- Market Share Trends
- FMC Evaluation** →
- Domestic FMC Matrix
- Sino-Foreign FMC Matrix

China Universal

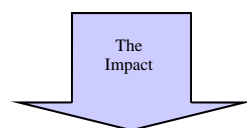


At one of the more seasoned FMCs, it looks as though management took their eye off the stockpicking ball. Even though its various funds had well above average equity exposure, performance was poor, including two of the bottom ten performing products in Q1

The firm's latest product launch had moderate success with Rmb1.5bn in assets raised. Still, the product opened for redemptions 10 days prior to the quarter's end and saw a third of those assets head for the door.

The firm might be well served to look outside for fresh blood much like GTJA Allianz did late last year. By no means is a wholesale turn-over in management required, but more attention paid to the investment department might be necessary.

Appendix I: Domestic FMCs



Market Share

Market Share Trends

FMC Evaluation

Domestic FMC Matrix

Sino-Foreign FMC Matrix

Exhibit 2.22b: A concentrated lot
Domestic FMCs sample Q1 data

| | 1Q09 AUM | QRTL AUM Δ | QRTL AUM % Δ | WEIGHTED RETURN % | NO. OF PRODUCTS | EQT % | BND % | CAS % | OTH % |
|----------------------|-------------|---------------|-----------------|----------------------|--------------------|----------|----------|----------|----------|
| Baoying | 11.3 | 2.0 | 22.0% | 21.9% | 7 | 50% | 20% | 29% | 1% |
| Bosera | 124.4 | -1.3 | -1.0% | 19.3% | 14 | 66% | 15% | 14% | 5% |
| Changxin | 21.3 | -2.0 | -8.7% | 15.1% | 6 | 53% | 22% | 21% | 3% |
| China AMC | 202.8 | 4.7 | 2.4% | 15.8% | 23 | 53% | 31% | 14% | 1% |
| China Nature | 5.4 | -0.8 | -13.4% | 10.2% | 6 | 44% | 27% | 27% | 1% |
| China Post & Capital | 36.3 | 10.5 | 40.6% | 40.3% | 2 | 82% | 0% | 17% | 1% |
| China Universal | 44.3 | -2.9 | -6.1% | 8.1% | 7 | 70% | 21% | 8% | 1% |
| Dacheng | 74.1 | 3.3 | 4.7% | 23.0% | 15 | 74% | 18% | 7% | 1% |
| E-Fund | 100.8 | 13.2 | 15.0% | 22.0% | 17 | 68% | 17% | 11% | 4% |
| First Trust | 12.2 | -0.4 | -3.1% | 18.0% | 5 | 61% | 29% | 5% | 4% |
| Galaxy | 12.1 | -3.8 | -24.1% | 12.6% | 7 | 42% | 26% | 24% | 7% |
| Golden Eagle | 2.5 | 0.6 | 32.6% | 27.5% | 3 | 64% | 21% | 9% | 6% |
| Great Wall | 33.7 | 4.7 | 16.2% | 23.9% | 10 | 74% | 6% | 18% | 1% |
| Guangfa | 78.0 | 11.0 | 16.5% | 23.5% | 10 | 67% | 20% | 12% | 1% |
| Guotai | 36.4 | 4.7 | 15.0% | 24.0% | 14 | 64% | 18% | 16% | 2% |
| Hua'an | 72.1 | 2.7 | 3.8% | 20.1% | 12 | 55% | 31% | 12% | 2% |
| Huafu | 5.7 | 0.9 | 18.5% | 14.4% | 5 | 45% | 46% | 6% | 3% |
| Huashang | 7.3 | 2.5 | 53.2% | 28.5% | 3 | 76% | 10% | 12% | 1% |
| Lion | 40.4 | 7.2 | 21.7% | 21.1% | 7 | 68% | 12% | 19% | 1% |
| New Century | 1.4 | 0.4 | 34.5% | 30.5% | 2 | 88% | 4% | 6% | 1% |
| Orient | 8.4 | 1.0 | 13.7% | 24.6% | 5 | 74% | 14% | 10% | 1% |
| Soochow | 7.2 | -0.3 | -4.2% | 13.3% | 4 | 72% | 11% | 15% | 2% |
| Southern | 107.6 | 4.7 | 4.6% | 11.0% | 18 | 56% | 33% | 10% | 1% |
| Tianhong | 3.7 | 0.3 | 8.7% | 15.3% | 3 | 69% | 20% | 10% | 1% |
| Wanjia | 12.5 | -0.4 | -2.9% | 17.1% | 6 | 48% | 31% | 20% | 2% |
| Yimin | 7.1 | 1.4 | 24.6% | 23.6% | 4 | 72% | 12% | 13% | 3% |
| Yinhua | 50.4 | -2.0 | -3.8% | 22.0% | 11 | 72% | 12% | 15% | 1% |

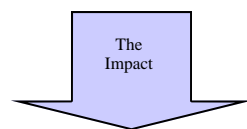
The number of domestic managers declined by one last quarter as **China AMC** assumed control of the public mutual funds run by **CITIC FMC**.

Three of the five highest-ranked weighted fund returns can be found among domestic FMC, where commitment to an all-equities, high-exposure product range is often higher than at Sino-foreign JVs.

Galaxy's AUM losses show the volatility that can strike firms with a largely defensive approach to range construction when investor risk appetite picks up.

A handful of very small domestics, such as **Yimin**, **Huashang** and **Golden Eagle**, grew AUM sharply thanks to a well-timed product launch in late '08.

Appendix II: Sino-foreign FMCs



Market Share

Market Share Trends

FMC Evaluation

Domestic FMC Matrix

FMC Evaluation

Exhibit 2.22b: A crowded and very diverse field

Sino-foreign FMCs sample Q1 data

| | 1Q09 AUM | QRTL AUM Δ | QRTL AUM % Δ | WEIGHTED RETURN % | NO. OF PRODUCTS | EQT % | BND % | CAS % | OTH % |
|----------------------------------|-------------|---------------|-----------------|----------------------|--------------------|----------|----------|----------|----------|
| ABC-CA | 5.5 | -4.3 | -43.8% | 9.94% | 2 | 33% | 42% | 21% | 4% |
| ABN Amro TEDA | 20.7 | -0.1 | -0.3% | 20.5% | 10 | 72% | 17% | 9% | 1% |
| AEGON-Industrial | 32.4 | 7.3 | 28.9% | 21.8% | 6 | 69% | 20% | 9% | 2% |
| AIG-Huatai | 15.0 | 2.3 | 17.8% | 23.5% | 5 | 64% | 10% | 24% | 1% |
| AXA SPDB | 1.5 | -0.2 | -11.5% | 13.9% | 2 | 52% | 27% | 16% | 5% |
| Bank of Communications Schroders | 49.0 | 0.7 | 1.4% | 11.2% | 8 | 48% | 37% | 11% | 4% |
| BOC | 21.9 | -0.4 | -1.7% | 19.2% | 6 | 75% | 16% | 7% | 2% |
| CCB Principal | 31.8 | -6.0 | -16.0% | 15.4% | 7 | 46% | 29% | 15% | 10% |
| Changsheng | 26.8 | -0.5 | -1.9% | 18.2% | 11 | 59% | 27% | 13% | 1% |
| China International | 54.9 | 5.9 | 12.0% | 13.2% | 9 | 71% | 13% | 10% | 6% |
| China Merchants | 34.4 | -5.3 | -13.3% | 11.0% | 10 | 50% | 42% | 6% | 2% |
| CITIC-Prudential | 11.6 | 2.2 | 23.7% | 18.5% | 5 | 59% | 18% | 21% | 2% |
| Everbright Pramerica | 30.5 | 7.2 | 30.8% | 29.4% | 7 | 79% | 6% | 11% | 3% |
| First State Cinda | 7.0 | 1.1 | 19.0% | 22.7% | 2 | 79% | 0% | 19% | 1% |
| Fortis Haitong | 35.6 | -2.9 | -7.5% | 16.7% | 9 | 49% | 32% | 18% | 1% |
| Fortune SGAM | 47.4 | -0.7 | -1.5% | 23.8% | 12 | 63% | 17% | 19% | 2% |
| Franklin Templeton Sealand | 16.3 | 2.7 | 20.1% | 19.3% | 6 | 69% | 17% | 13% | 1% |
| Full Goal | 46.8 | 6.5 | 16.1% | 14.7% | 13 | 65% | 24% | 10% | 1% |
| GTJA Allianz | 9.5 | 4.3 | 82.6% | 24.5% | 7 | 74% | 13% | 9% | 3% |
| Harvest | 115.2 | -22.3 | -16.2% | 17.1% | 17 | 64% | 24% | 9% | 3% |
| HSBC Jintrust | 6.6 | 0.3 | 4.4% | 13.3% | 5 | 57% | 29% | 13% | 1% |
| ICBC Credit Suisse | 56.0 | -19.2 | -25.5% | 10.2% | 10 | 38% | 55% | 5% | 2% |
| INVESCO Great Wall | 47.2 | 5.4 | 13.0% | 19.7% | 10 | 73% | 15% | 11% | 1% |
| KBC-Goldstate | 5.2 | 1.3 | 32.7% | 1.5% | 3 | 11% | 78% | 9% | 2% |
| Lombarda China | 2.6 | 0.5 | 21.9% | 27.9% | 2 | 83% | 1% | 15% | 1% |
| Lord Abbett China | 5.2 | 1.8 | 54.7% | 21.8% | 3 | 76% | 0% | 12% | 12% |
| Minsheng Royal | 2.7 | 2.7 | - | - | 1 | - | - | - | - |
| Morgan Stanley Huaxin | 2.1 | 0.5 | 27.5% | 21.5% | 3 | 57% | 11% | 29% | 2% |
| Penghua | 48.4 | 0.7 | 1.5% | 19.6% | 12 | 57% | 20% | 22% | 1% |
| Rongtong | 45.9 | 9.1 | 24.8% | 24.8% | 10 | 77% | 13% | 9% | 1% |
| SYWG BNP Paribas | 11.5 | 1.0 | 10.0% | 22.0% | 7 | 67% | 17% | 16% | 0% |
| UBS SDIC | 23.6 | 3.1 | 15.3% | 19.3% | 9 | 67% | 25% | 7% | 1% |
| Zhonghai | 16.9 | 1.4 | 9.3% | 19.0% | 5 | 61% | 13% | 25% | 1% |

The asset retention challenges faced by bank-backed JVs are evident in the quarterly AUM change column and are likely also affecting these FMC's fund returns.

Harvest's startling loss of AUM, like Galaxy's, shows that assets raised in low-volatility fund classes may themselves be the most volatile components of AUM.

Equity exposure has typically been slightly lower at JVs than domestics and this, more than any other factor, probably contributed to the relatively tight bunching of JV weighted returns.

Smaller JVs failed to match the AUM growth of many of their domestic peers.