Bin Yuan Capital China Equity Strategy – Second Quarter 2014

Performance Attribution (H share only, A share is available upon request)

During the quarter, the top performer in our portfolio was Sunny Optical, an optical device player; the market had a concern on rising competition in camera module sector. However we like its strong R&D capability in lens, wider application of optical device and we are positive on its trend of being accepted by large customers.

Sinotrans continued to be a major performance contributor during the period; it was under covered and misunderstood by the market and was traded at 40-50% discount of its book value when we first bought it and started to be known by the street gradually.

China Market Review and Portfolio Positioning

At the time Bin Yuan Capital launched its China fund in early 2013, we had the view that China off shore listed stocks should outperform China on shore listed A share stocks due to cheap valuation. At that time, the PE ratio for H shares of those sectors was 10 times versus 31.3 times and 41.1 times respectively of those sectors in A Share market small and GEM board. The H share market has outperformed A share market by 12% during the period.

The off shore listed stocks will continue to outperform A share market in the next 12 months. The A share market will continue to be traded in a range without a trend, unless the A share GEM board may stay on the path of reaching new height and making the bubble bigger.

Today the market has reached a consensus that China GDP growth will slow down. The over-reliance on investment to drive economic growth has caused overcapacity in many traditional industries. Cost based manufacturing is much less competitive today due to slower growth in productivity. It will continue to be a challenge for these corporates to maintain strong balance sheet and earnings in the next few quarters.

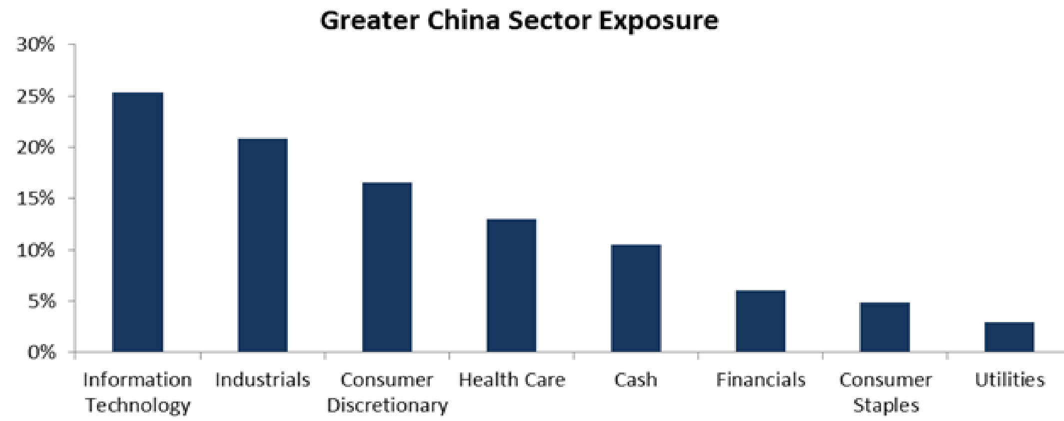
Those non-traditional sectors, domestic service sectors in particular, will enjoy better margin and earnings growth. However, in the A share market, fast growth companies are chased by domestic investors. Due to limited supply and smaller market capitalization, those stocks are easily squeezed and the prices were pushed up to a very high level. The GEM board has a price earnings ratio of 60 times with a 5 times price to book value. We can find similar companies that traded only at low teen on PE and close to one time book value. When the HK-SH through train starts in future, those low valuation growth stocks shall attract many domestic investors.

We continue to have a very low exposure in banks and no exposure in properties. We do not expect the property prices to collapse, but we strongly believe that the oversupply situation exist, at current market price, in property market in second and lower tier cities. Property developers are postponing new projects which will lead to slower growth for other related sectors such as capital goods, household compliance, etc. The best time for property developers is over.

Due to higher household saving rate, lower household net financial leverage, and the bank interest margin protection, it is less likely that banks will go bankrupt. The challenge for the banks is the loan growth. The industrials face overcapacity and very weak demand problems. Banks are very cautious to offer loans to industrial and capital goods sectors. The Chinese banks have a tradition of not willing to lend to services sector which is currently the growth engine for today economy. Thus the loan growth is difficult. We expect that banks are having issues in their balance sheet that the non-performing loan ratio should be more than doubled compared to their current level. Deregulation becomes the order of day to improve banking sector's operation efficiency.

We still like the services sector including internet and internet of things. It is notable to see that lots of innovation and technology are having great impact on people's daily life. However, as most of these companies are treasured by venture and private equity investors who have started to compete fiercely on deals, it starts to raise market concern on overvaluation. The word "Online" has heat up and drawn attention of investors all over the world. Investment price is based on counting number of users. Billions of dollars are chasing those stocks that may not generate earnings for the next three to five years.

Our portfolio exposure is as below (H share only, A share is available upon request)



China Economy Outlook

At macro level, the economy is still in a consolidation stage after a high growth period that ended in 2009. To maintain above 7.5% GDP growth in the future is very difficult. Releasing some liquidity through RRR reduction and bank capital ratio rebalance can only help mitigating a bit the slowdown. Nevertheless, we view the slower economic growth positively for China in the long run. Temper economic growth will force the country to undertake economic reform and industry consolidation, which will further generate great investment opportunities. We hold positive as we are witnessing the economic transition.

The economic reform trend is positive under the new leadership. We have already seen capacity consolidation in some industries. Reducing the burden of companies dealing with government is another very positive sign. The next big project for the government is to breakdown the interest groups who control those large regulated industries. The misallocation of the financial resources and unfair wealth distribution (through corruption) will be corrected in due course. It will largely benefit the overall economy and the private sector.

For the portfolio investment, we continue to be bullish on the themes we liked in the past three years. The A share market will still be in a trading range for the near future and H shares will continue to perform better than A shares. Our focus will still be on identifying long term themes and stock selection.

Sincerely,

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