

China Outbound Investments Q4 2013

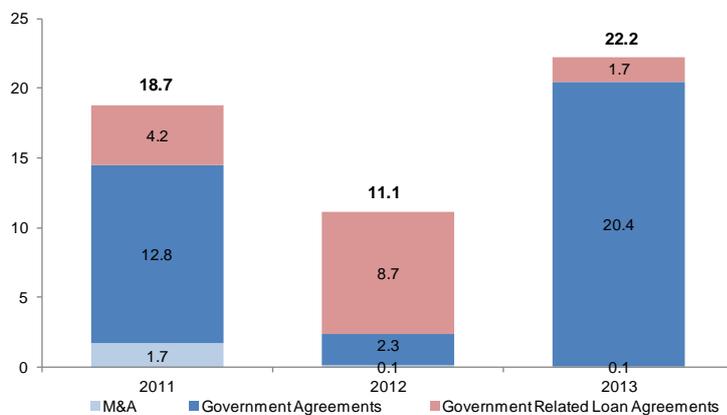
Quarterly Feature – Strategic Shift of CEE Importance

This quarter we feature what appears to be a strategic shift by China on the increased medium and long term importance of the CEE region, as well as countries within the Balkans. We think that China sees this region as possessing:

- A natural (eastern) gateway into EU countries
- Major ports in Romania and Bulgaria (and when rebuilt, Sevastopol)
- Higher GDP growth rates than in Western Europe
- Favourable labour costs, which should become even more favourable as the Yuan appreciates and/ or the cost of labour within China rises

Our conclusion is based upon recently increased investment and / or Government sponsored loans into the region. In 2013, aggregate value of Chinese investment into CEE doubled from 2012 value as shown below in Table 1.

Table 1: China Investments into CEE – Transaction Value (USD bn)



Over USD 19bn of this value was announced since November, with over 90% related to Government / loan agreements of USD 10.9bn with Romania, USD 8.0bn with Ukraine and Exim loans with Macedonia (USD 783m to provide 90% of the funding for two highways), Hungary (USD 507m both via increased credit lines plus an investment into a new CEE investment fund) and Serbia (USD 306m to fund 90% of the construction cost of a new Serbian motorway).

Premier Li's November visit to Bucharest which involved prime ministers from 16 CEE countries, which was the first by a Chinese leader to Romania in nearly a decade, was centred around Romania. During the November summit, there were a number of

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infrastructure projects announced, including the modernisation and construction of the Belgrade-Bucharest railway which will be jointly implemented by Serbia, Hungary and China. This is in addition to a number of other infrastructure projects already in progress. As readers will recall, in April 2012, Premier Wen hosted CEE leaders in Poland, which we interpreted as a signal that Poland would play a special role for China in CEE. However, since then only two small M&A transactions have been announced in Poland. Further we suspect that, the 2009 agreement between China Overseas Engineering Group (“COVEC”) and GDDKiA on Polish road construction also had something to do with this shift. In 2009, COVEC, a subsidiary of China Railway Engineering Corporation (“CREC”), was chosen as the first Chinese business to win a large European highway contract (USD 447m) to build a road from Warsaw to the German border. However, in 2011 COVEC withdrew from the project after heavy losses. In addition to the Chinese losses, the Polish subsidiary of Germany’s Bilfinger, the Austrian unit of Spanish group FCC and Budimex, the Polish unit of Spain’s Ferrovial also incurred sizeable losses on rebuilding Polish roads.

While there has been limited Chinese M&A activity in the Balkans (outside the 2011 specialty chemical deal). In 2013 selected Chinese companies have invested in a car manufacturing plant in Bulgaria and into bus manufacturing in Slovenia while Huawei and ZTE have invested in logistic centres in Hungary and Romania. Earlier this year, it was reported China’s Huanghai Auto has been in discussions on acquiring truck and special purpose vehicle factories of Serbia’s Zastava Vozila.

We expect further M&A activity in this region aligned with Chinese investments in infrastructure and industrials.

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