China Outbound Investments Q3 2019

Overview

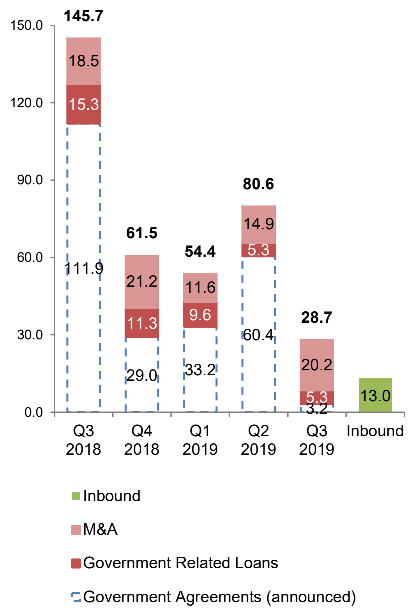
Chinese outbound M&A /Equity investments rebounded strongly in Q3; Policy Bank loans continued to decline as the infrastructure component of the BRI programme reaches maturation in key BRI markets and as the focus switches to the Digital Silk Road and the growing number of SEZs (as set out in our recently released study on Oman with SIIS).

The signification reduction in outbound pledges with disclosed amounts and committed loans continues the trend we have seen over the past five quarters. We have begun to focus on inbound China FDI growth, led by Q3 pledges from major European, Gulf and Asian countries and capital being attracted by improving Asian equity markets.

Key Findings

- M&A/Equity investments aggregate amounts increased by 42.3% while volumes increased by 31.3% – continuing the double digit increases by each during Q2.
- The Consumer sector saw the largest volume and aggregate amounts. It was followed by Technology (mostly smaller minority investments) and Healthcare – no investment over $100 million. Logistics and ports also saw increased activity.
- Relative to geographies, Asia (increasing activity in India, Japan and Indonesia) and Europe (including increased activity in Scandinavia and 17+1) represented circa 70% of volume. The declines in the USA were offset by increased activity across LAC and Africa (7 countries this quarter).
- We highlight inbound Q3 FDI pledges by Japan, Netherlands, France, UAE, the Netherlands and USA totalling $13 billion. Even before these pledges/investments, Chinese inbound FDI had already increased from $135 billion at y/e 2018 to circa $155+ billion by end Q3.
- Government related loans represented only $5.3 billion in aggregate amounts, 4900% below the rolling four quarter average of $10.4 billion. All Q3 policy bank loans were to BRI countries (save Colombia). Interestingly, three of the AIIB commitments were related to investments in various funds.
- As seen in BRF II, China and BRI countries have moved away G2G agreements to B2B agreements. While major B2B agreements this quarter were signed with UAE and Germany, activity this quarter with disclosed amounts showed only $5.4 billion. Once removing the G2G loans, the adjusted disclosed total was only $3.2 billion. However, when averaging the large B2B in Q2 with Q3, produces a two quarter average of $33.4 million, only slightly below the rolling four quarter average of $36.1 billion.

Table 1: Aggregate Value (USD billion)



Chinese Outbound M&A Transactions/Equity Investments

42.3%

$20.2 bn

Q3 aggregate amounts of M&A/Equity investments increased from $14.2 billion in Q2 to $20.2 billion, an increase of 42.3%. This marks the 2nd consecutive quarter of double digit growth (increase of 21.6% from Q1 to Q2). Q3 transaction volume was 189, a 31.3% increase from Q2 volumes. Q3 volume marked a sharp reversal from Q2's decline of 15.3% which followed Q1's decline of 9.6%.

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Q3 also saw the return of an increasing number of transactions/investments of $1 billion or larger, across a number of industries:

- China Yangtze Power acquisition of Sempra Americas (Peru) for $3.6 billion
- Beijing Automotive (BAIC) acquisition of 5% stake in Daimler (Germany) for $2.8 billion
- Joseph Tsai acquisition of remaining 51% stake in Brooklyn Nets (USA) for $2.35 billion
- Jiangsu Shagang Group acquisition of 24% stake in Global Switch (UK) for $2.2 billion
- Giant Network Group acquisition of 42% stake in Playtika (Israel) for $1.6 billion

Just below the $1 billion threshold was China Mengniu Dairy's $0.9 billion announced acquisition of Bellamy's (Australia).

Collectively, these 6 transactions/investments represented $13.5 billion or 66% of Q3 aggregate amounts, and were spread almost evenly across regions.

Average transaction/investment size for the 156 transactions/investments with disclosed values produces an average of $129.6 million. After removing the 6 largest transactions/investments reduces the average size to $44.7 million.

It is also worth noting that 46.8% of all transactions/investment volume with disclosed values involved amounts of $10 million or less.

Similar to Q2, three of these six major transactions/investments were for minority stakes, down from all 4 above $1 billion in Q2 which were minority stakes, but still consistent with the message that Chinese investors no longer insist on control or even route to control in many cases. (An example was CNOOC's acquisition of 10% stake in Arctic2 LNG (Russia) for $2.5 billion).

Industries

The Consumer sector returned to the most active after two quarters of decline. There were 45 transactions/investments in the sector, representing 23.8% of total volume, a significant increase from Q2's 16.1% (we classify e-commerce as retail). It terms of aggregate values, 4 of the 6 large transactions in the quarter took place in the Consumer sector. There were also a number of mid-sized education acquisitions in the UK and Australia.

Technology saw 22.2% of quarterly volume – recovering to Q1 2019 and Q4 2018 levels from its Q2 lows. There was one major transaction in this sector, which also saw a number of other investments, mostly into BRI countries and India, in the $200- $500 million range.

Healthcare, which includes pharma/biopharma and biotech, ranked 3rd in volume with 14.8%. While this percentage has decreased from 17.5% in Q2, it is higher than the 13% in both Q1 2019 and Q4 2018. Once again, virtually all of investment sizes were substantially below $100 million, with targets based mostly in the UK/EU.

Financials continued the quarterly decline, falling from 13% in Q1 to 11.9% in Q2 and now at 10.6% in Q3. With virtually no real estate activity, we have seen activity in crypto as well as investments into digital banking in the UK, Germany and LAC.

These were followed by Industrials, Energy and Communications/Telecoms/Media. In Industrials, there were investments in German robotics, engineering and 3D printing in Israel.

A new entry is logistics with 5.8%. This is not really a surprise as we have seen increased investment flows into logistics as it is such an important link to e-commerce throughout the BRI. There were logistics transactions in Hong Kong and Russia, with a $400+ million deal across Europe but based in the Netherlands. There was also a deal involving a port in Singapore.

Geographies

Asia continues to lead – for the 2nd consecutive quarter it represented 43% of total volume. Leading in activity, in descending order, were Hong Kong (despite all of the unrest), Singapore, India, Indonesia, Japan and Malaysia. The Japanese and Indonesian volumes marked a meaningful increase from prior quarters. Also seeing activity were Thailand, Myanmar, South Korea, Taiwan (crypto) and Pakistan, a new entrant in 2019.

Europe fell slightly from 25.7% in Q2 to 23.3% in Q3. The UK and Germany remain the leading countries both in volume and amount as they each had one investment above $2 billion value. They were followed by Switzerland, Netherlands and France. Italy, Belgium and Luxembourg each attracted one investment this quarter. Volumes increased across Scandinavia with transactions/investments across Finland, Sweden and Norway. In the 17+1 Region, there were transactions announced in both Estonia and Romania.

North America continued its quarterly declines producing only 18.5%% of Q3 volume, down from 25% of Q1 volume and 21.6% of Q2 volume. The 18.5% figure includes Canadian transactions as well as small stakes in domestic led investor syndicates. The main exception to this was the $2.35 billion acquisition of the controlling stake in the Brooklyn Nets NBA franchise by one of the former senior executives within Alibaba.

Latin America Caribbean (LAC) saw 8 Q3 investments. Brazil led in volume but Peru in size as it saw the largest Q3 transaction. Also receiving Chinese investments were Antiqua, Trinidad, Argentina and Cayman. We anticipate increased Chinese inbound investment as circa 19 LAC countries (out of 33) had already signed the BRI MoU.

The Middle East saw 7 investments. All but one of these were in Israel and in technology. One of the five transactions over $1 billion in Q3 was also in Israel. The investment outside of Israel was in Dubai. While it was a small tech investment, we believe it to be a precursor of increased future activity as per the B2B agreements during BRF II between the UAE and China.

Africa is a new geographic entrant – also seeing 7 investments this quarter. Ethiopia, Kenya, Ghana, Nigeria, Zambia, Mozambique and Seychelles each saw one investment this quarter. While these were all relatively small, the size of the 2 African based IPOs done to date in 2019 is increasing- which we expect to see in the next level round of investing.

Finally, Australia also saw 7 transactions/investments this quarter. Several of these were Consumer sector transactions including the nearly $1 billion deal for Bellamy's, a major Australian food and beverage company, and parent company of Bellamy's Organic, Australia's largest organic infant formula producer. There were also deals in education, logistics and fintech, as well as a basic materials deal.

Chinese Inbound M&A Transactions/Equity Investments $13.0 bn

This is a relatively new component of our quarterly analyses, but one which we feel will become increasingly important over time. This quarter we highlight inbound FDI investments by Japan, Netherlands, France, UAE and the Netherlands. Aggregate inbound pledges in Q3 totalled $13 billion. Even before these pledges/investments, Chinese inbound FDI had already increased from $135 billion at year end 2018 to a run rate of circa $155 billion by end of Q2 (we estimate of $160 billion by end of Q3).

Japan

- In July 2019, Toyota announced a new investment totalling $600 million in Didi. As part of the deal, the two companies will also set up a JV with GAC Toyota Motor to provide vehicle-related services to drivers on Didi's ridesharing platform
- Also in July 2019, Toyota and BYD announced that they will jointly develop battery electric vehicles (BEVs), including sedans and low-floor SUVs, as well as onboard batteries for the BEVs and other vehicles
- Toyota announced that it has reached a deal with China's Contemporary Amperex Technology Co., Limited (CATL) to develop batteries for electric cars
- Japanese investment bank Nomura Holdings Inc.'s first securities joint venture in China has its top management team in place and expects to open for business by the end of this year
- The Shanghai bureau of China's securities regulator approved the qualification of seven Chinese and Japanese executives for Nomura Orient International Securities, a joint venture between Nomura and Shanghai-based Orient International Co. Ltd
- Nomura plans to open its office for Nomura Orient (51%) by year end 2019, hiring as many as 100 staff in brokerage, trading, asset management. Chair is ex China Re. Deal size RmB 1.01bn ($141m)

Netherlands

- In September, IKEA committed to invest an incremental $1.4 billion into China, increasing Chinese staff numbers from 14,000 to 17,000.

France

- In July, Renault said it was embarking on a second electric vehicle JV in China with a $145 million investment to form a JV with JMEV, an electric car unit of China's Jiangling Motors Corporation Group (JMCG).

UAE

- Dubai's largest listed developer Emaar Properties signed an agreement to help deliver an $11 billion project at the site of Beijing's new mega airport. The project, which is expected to take 10 years, includes residential and leisure facilities. The value of the project includes the 5 km2 of land at the airport. Beijing Daxing International Airport opened in October (it is extraordinary).

USA

- In August, Goldman Sachs announced plans to increase its stake in Goldman Sachs Gao Hua Securities Co from 33% to 51%. Goldman, which will become the latest foreign bank to gain control of its investment banking business in China, apparently plans to eventually move employees and businesses from Beijing Gao Hua into Goldman.
- In May 2019, cloud-computing infrastructure Beijing Qinhuai Technology has obtained $570 million in funding from Bain Capital This deal is the single biggest investment ever made in a Chinese data centre (excluded from totals but worth noting).

Government Related Loan Agreements 0%

Volume of Government related loan commitments doubled from 10 in Q2 to 20 in Q3, while aggregate amounts were flat at $5.3 billion. However, there were substantial shifts within each of the various components.

There were 9 policy bank loans, an increase of 50% in volume over Q2 volume, but only $2.2 billion in aggregate amounts (% change). This continues the trend of decreasing amounts which we have seen the past several quarters.

New committed policy bank loans this quarter were extended to Turkey, Philippines, Uzbekistan, Bangladesh (all BRI countries) and Colombia (not yet signed the BRI). One of the Uzbekistan loans agreements was denominated in RMB – a first for Uzbekistan.

There were 9 AIIB committed facilities, an increase of 125% from Q2. These consisted of 6 senior bank facilities and 3 fund commitments of $1.05 billion. The senior debt commitments were to India, Turkey, Pakistan, Cambodia and Bangladesh. When disclosed, the maturities of these were all 30 years and mostly with a 5.0-5.5 years grace period. Virtually all of these loans were multilateral.

The fund commitments were to Hong Kong and India. Maturities for the funds ranged from 5-7 years.

After approving no new loans in Q2, NDB approved 4 loans totalling $1.7 billion. Recipient countries were led by India, followed by South Africa and Russia. Unlike the multilateral structure of the AIIB loans, all the NDB loans appear to be bilateral.

Government/B2B Agreements -96.6%

G2G to now embrace B2B Agreements

Q2 was dominated by the $64 billion of announced (primarily B2B) agreements announced at BRF II. G2G/B2B announcements this quarter with disclosed amounts was much more subdued, with aggregate amounts of only $5.4 billion. Once removing the G2G loan embedded within the G2G deals, the adjusted total was only $2.3 billion.

In Q3 there were only a few countries involved in agreements with disclosed values this quarter, which we excerpt below.

Bangladesh ($4.0bn) – in July, the two countries signed nine agreements across a number of sectors including power, finance, culture, tourism, and technology, totalling circa $4 billion. The largest amounts were loans to the power sector (discussed in a previous section).China also agreed to provide Bangladesh with 2,500 metric tons of rice as aid for Rohingya refugees.

During the meetings, both countries discussed joint projects including the 8th China-Bangladesh Friendship Bridge, China-Bangladesh Friendship Exhibition Center, Padma Bridge Rail Link Project, Multi-lane road tunnel under the river Karnaphuli, Installation of Single Point Mooring (SPM) with Double Pipe Line Project in Chattogram area. Future projects include establishing the China Economic and Industrial Zone in Chattogram as well as cooperation in agriculture, marine, science, technology, Climate Change and establishing Climate Adaptation Center in Bangladesh. The two sides agreed to continue joint feasibility study on China-Bangladesh Free Trade Agreement (FTA).

Uzbekistan ($0.8) – In late August, President Xi met with visiting Uzbek Prime Minister Aripov in Beijing, which was proceeded by the 5th meeting by the Uzbekistan-China Intergovernmental Cooperation Committee. Virtually all of the disclosed amounts were related to Government backed loans (discussed previously) across tourism (upgrading the domestic airline carrier) telecommunications (significant upgrade to move to 5G ultimately) and renewable energy (hydropower). Trade is also important; in H1 China became Uzbekistan's largest trade partner, with a goal of further increasing agricultural imports.

Colombia ($0.4bn) – In late July, Colombia and China signed 12 bilateral agreements in areas including judicial cooperation, agricultural investment and trade, transportation, e-commerce, imports of avocados, 5G and finance. The only agreement with a disclosed amount was the Mar 2 road project, which will connect second city Medellín with the Gulf of Urabá on the Caribbean coast (discussed in a prior section).

Philippines ($0.22bn) – in late August, Philippines and China signed six agreements in infrastructure construction, industrial parks, telecommunications, energy and other fields. The only one with stated values was loan agreement of project management consultancy of the Philippine National Railways South Long Haul Project (set out previously).

Bilateral – no disclosed values.

Over the past 5 quarters, it has become clear that China has increasingly welcomed inbound FDI. Two of the leading countries to date were actively negotiating new bilateral investments with China during Q3. We set these out below.

UAE (ND) – in mid-July, President Xi held talks with Crown Prince of Abu Dhabi Mohamed bin Zayed Al Nahyan. The two sides agreed to accelerate the joint construction of the BRI with high quality, strengthen the alignment of each other's development strategies, strive to achieve the goal of $200 billion of bilateral trade in 2030, finish the Khalifa Port Container Terminal II and the China-UAE Industrial Capacity Cooperation Demonstration Zone. The UAE-China Economic Forum, which began in Beijing, witnessed the signing of 16 MoUs, related to various sectors between the UAE and China.

Germany (ND) – in early September both President Xi and Premier Li met with Chancellor Merkel during her 12th visit to China, during which both countries signed 11 cooperation agreements, many of which are FDI inbound. The agreements range from aeronautical engineering, shipping, energy, electromobility, finance, insurance to networked driving and the prevention and recycling of waste. President Xi noted that China is accelerating the opening of financial and service industries and welcomes German enterprises' investment in these sectors and that German enterprises are welcome to participate in the construction of the Yangtze River Economic Belt.

Other countries where agreements were signed, but with no amounts disclosed, included Kazakhstan and Bulgaria.

Also in Q3, both Solomon Islands and Kirabati voted to switch their relationship with Taiwan and take up diplomatic relations with Beijing.

Overview of Grisons Peak

Grisons Peak is a UK based merchant bank focused on Asia which owns and operates an advisory business, a consultancy business and a China macro research business.

The advisory business was launched in 2003. During the period 2003-2018, Grisons Peak advised on over $25 billion of completed transactions. Initially, these were focused in the Financial sector. However, as Technology developed into a larger component of Financials, especially in emerging markets, the advisory business focus moved into Technology, which we consider to be an enabler across industries. As OBOR and the BRI developed, the advisory business was adjusted to follow the BRI geographically.

The Chinese macro research business is based upon a proprietary base, launched during 2008, which tracks all Chinese outbound investment across G2G/B2B, Government related loans and public and private outbound equity investments (www.chinainvestmentresearch.org). Beginning in 2018, as China began to focus on inbound FDI, we began also monitoring China inbound. We bring a forensic discipline to analysing data, with the goal to either reconcile and/or footnote each number back to original sources, which we believe is unique to other data providers. We also track Chinese outbound investments below $10 million, as they have represented circa 35% of Chinese outbound volume since 2017. We believe that this is also unique to other financial data providers. This degree of discipline is loss making – as we also choose to release quarterly data publically, without cost as a way of educating those interested in clean data/facts about the BRI. Our data/research has been quoted by financial press globally and utilized by a number of major universities and think tanks as a basis for academic studies.

Based on over one decade of this data, in 2016 Grisons Peak launched a Consultancy business, which utilizes this data for bespoke studies prepared for selected major corporate and services organizations, academic institutions and governments. We also present this information at major BRI conferences globally. Over the past three years, bespoke Consultancy has become an increasing focus of Grisons Peak.

Grisons Peak LLP is Authorised and Regulated by the Financial Conduct Authority.

For further information on this, please visit: www.chinainvestmentresearch.org.