China Outbound Investments Q2 2018

I. Overview

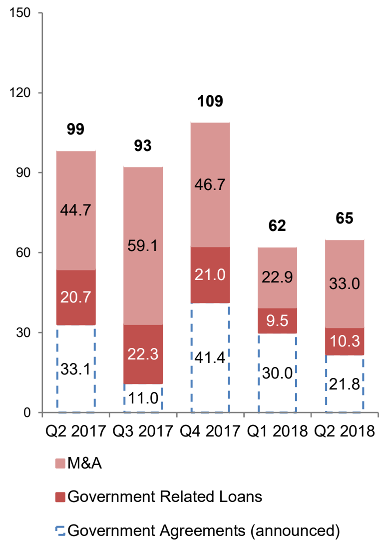
Q2 Chinese outbound investments across all 3 components we track totalled $65.1 billion, which was up 4.3% from Q1's adjusted total of $62.4 billion. M&A aggregate amounts increased from $22.9 billion to $33.0 billion, or 44.1%. This was due in part to six announced deals over $1 billion. Government Related Loan Agreements totalled $10.8 billion, up 8.4% while G2G agreements with disclosed values fell to $21.8 billion, a decline of 27.3%.

M&A/equity increased from an adjusted 155 to 194, an increase of 25.2%. The 194 number is consistent with Q4 2017 volume.

Government Related Loan Agreements saw policy bank loans increase by 33% (Q1 to Q2). When including AIIB and NDB loans, aggregate volume was up 75%.

G2G agreements with disclosed volumes were flat and only saw pledges for specific projects in Peru, Russia, Nepal, Dominican Republic and Austria.

Table 1: Aggregate Value (USD billion)



M&A Transactions / Equity Investments

↑ 44.1%

As seen above, announced M&A/equity investments volumes increased by 25.2% while aggregate values increased by 44.1%. A major contributor to this large increase was the jump in the number of larger transactions.

Unlike Q1, announced transactions over $1 billion doubled from 3 to 6 in Q2. Collectively, these 6 totalled $21.5 billion. These six transactions represented 65% of Q2 aggregate value.

The majority of increase in volume was at the smaller end of the investment spectrum. There were 63 announced transactions/investments $10 million or less representing 32% of overall announced volume.

The average transaction size for transactions with disclosed values (omitting the six transactions over $1 billion) declined to $71 million, a decline of 9.0% since Q1 2018.

Industries

Once again, Consumer led in volume with 59 announced transactions, representing 30% of total volume. The next two industries were Technology and Healthcare, which includes Life Sciences/Pharmaceuticals with 15% and 14% respectively. These two industry groups many times have overlap relative to technology in healthcare – and thus are increasingly important to China in addressing the increasing healthcare needs of it's aging population.

Industrials (14%), Financials (10%) and Communications (9%), rounded out the top six industries. Collectively, these 6 industries represented 92% of total volume.

Relative to aggregate value, the only Utilities deal this quarter accounted for 32.7% of aggregate values. The largest announced deal in Q2 was Three Gorges $10.8 offer to acquire all of the outstanding shares if EDP, a major utilities group and one of Portugal's largest organisations.

The next largest deal was Tanqi Lithium's purchase of a 23.8% stake in Sociedad Quimica y Minera de Chile (SQM), a Basic Minerals group.

The 4 Basic Materials deals represented another 14.9% of aggregate value. Thus 50% of value was in Utilities and Basic Materials.

There were two 1+ billion acquisitions in Australian healthcare and in German pharmaceuticals, one in Japanese/US automotive/consumer and one in Hong Kong real estate, comprising another 15% of aggregate announced values.

Geographies

Q2 M&A/equity investments were spread rather equally across the three major continents. North America led with 34% of total volume, followed closely by Asia with 31% and then Asia with 26%. Collectively, these 3 continents represented over 90% of aggregate volume.

The European activity was focused on UK, Germany and Scandinavia. There were a handful of acquisitions across Scandinavia, in advance of the official launch of the Polar Silk Road. Other countries of focus included the UK and Germany, two of China's top European markets. The UK activity saw mostly smaller investments across sectors while German activity remained focussed on mid-sized industrial deals, with only one over $1 billion.

There were 7 transactions in Australia. While half of these were in energy and infrastructure, the remainder were in consumer and healthcare, including the only one over $1 billion this quarter as large scale acquisitions by Chinese acquirers into Australia remain sensitive.

In the middle east/Africa there were 6 announced transactions, two each in Israel (technology), the UAE (communications) and one in South Africa) (also in communications).

Government Related Loan Agreements

↑ 8.4%

In Q2, Government related policy bank loans, AIIB loans and NDB loans all saw increases. There were 12 committed policy bank loans, up 33.3% from Q1, 3 AIIB commitments, up from 2 in Q1 and 6 NBD commitments, up from 1 in Q1. In aggregate, Q2 volume increased from 12 to 21 or 75%.

Relative to aggregate amounts, the 3 components totalled $10.3 billion, up 8.4% from $9.5 billion in Q1.

The largest recipients of policy bank loans in Q2 were Bangladesh followed by Sri Lanka. One of the Sri Lanka loans had an effective interest rate of 5.3%. Pakistan and Uzbekistan were also significant recipients.

Two of the NBD loans were to Russia, one to Brazil and one to India. Two of the AIIB loans were also to India, including one investment into an Indian fund of funds.

The backlog remains strong although Iran has begun to draw down on the $25 billion of pledges made during 2017.

Government Agreements

↓ 27.3%

G2G Agreements

Q2 saw President Xi and Premier Li meeting with leaders of 18 countries, several of which were related to the SCO Summit. When including Wang Yi's visits, the number increases to 29 countries.

There were specific G2G agreements signed with 6 countries, which is consistent with Q1. Disclosed aggregate amounts totalled $21.8 billion, down from $30 billion in Q1, representing a decline of 27.3%.

Leading Q2 was Peru for $10 billion, representing investments in ports, railway/infrastructure and copper mining. Another important G2G set of agreements this quarter was the agreement for China and Russia to cooperate on both nuclear projects as well as in the financials sector. There were also meaningful agreements in Nepal, Dominican Republic and Austria, which expects to play a positive role in EU-China cooperation going forward. Bolivia also saw a small pledge.

There were also leadership meetings with India, Japan, Kuwait, Oman, France, Algeria and Portugal, where no amounts were disclosed.

II. Quarterly Feature – Increasing Connectivity with India

During Q2, President Xi invited Prime Minister Modi to China for a couple of days for private talks. The goal of the exercise was to build a framework for additional cooperation, in advance of the upcoming SCO and BRICS summits.

Separate from the private meetings, AIIB, owned 30% by China, had already shown an increased willingness to collaborate with India as shown in the Q2 deals listed below:

- In April, AIIB's Board approved lending $140 million of a $502 million credit facility to Madya Pradesh Rural Development to fund the Rural Connectivity project – focussed on rural roads in India's 2nd largest state. The World Bank led this financing with $210 million.
- In late June, AIIB's Board approved investing $100 million into Phase 1 of The National Investment and Infrastructure Fund (NIIF) – a $600 million India based fund of funds, in which India will invest $500 million. The Fund will exclusively invest in India and intends to operate mostly through scalable platform companies that will target infrastructure assets primarily in the following sectors: roads, ports, airports, power (generation, transmission, distribution), urban infrastructure and logistics. AIIB is also considering investing an additional $100 million in Fund 2.

The two Q2 loans represent the 6th and 7th loans made by AIIB to India since Q1 2017. The seven loans represent 25% of the aggregate volume of AIIB outstanding loans since inception.

It is important to also remember that Modi has invited President Xi to India in 2019, an invitation which he has already accepted. In the interim, the two countries have also agreed visits by Ministers from both countries to each other during the remainder of 2018.

Overview of Grisons Peak

Grisons Peak LLP is a London based merchant banking firm specializing in a number of sectors including financial services (including real estate), infrastructure, healthcare and consumer. We provide independent advice on cross border M&A, ECM and high yield issues, both public and private. We also selectively co-invest in equity stakes alongside our clients.

We operate via joint ventures and partnerships throughout Europe, the Middle East, Africa and in North Asia. Since its founding in 2003, the firm has advised on over €25 billion transactions across three continents. In the Advisory area, over the past 58 months, the firm has advised on 24 completed transactions and on 32 binding offers, mostly in emerging markets. In the Advisory area, we focus on transaction execution since virtually all of the firm's clients have done business with Grisons Peak or representatives of the firm previously. We also do not advertise as we are very discreet regarding our Advisory clients (hence only a 1 page website for this business).

In 2008, Grisons Peak founded *China Outbound Investments*, which tracks and analyses Chinese G2G agreements, Chinese Government related loans and M&A/equity investments in a single quarterly report, all of which have been reconciled with original source documents whenever possible. This database also includes bespoke capabilities which measure Chinese Government related loans linked to individual infrastructure/renewable energy projects since 2013. Our research has been cited by many major press including *The Financial Times, FT Confidential, EM Squared, The Wall Street Journal, Bloomberg, China Daily, Xinhua, The South China Morning Post, Australian Financial Review, Euromoney, Thompson Reuters, Global Trade, IFR Asia* and several others. Two of the Financial Times articles have been cover page stories; two on Chinese ports and logistics generated over 100,000 paid downloads.

This database has also been used by major universities for academic research regarding Chinese outbound investment in the UK (Cass Business School), the US (New York University) and presented in the UK House of Commons.

In Q1 2018, we published, via GOSS Research, a longitudinal study on Chinese investment into Cambodia – the first such BRI/China country study. Article entitled "Exporting the Chinese Model to BRI Countries".

Our unique research on BRI has been presented to over 10 Asian universities and used in Executive Seminars at Cambridge University, the University of Edinburgh, as well as in major conferences such as GOSS Research Forum (Hong Kong) and industry conferences such as ILSS Intermodal (Shanghai and Amsterdam) and Clarksons, in the UK.

During Q2 we have created various presentations for the United Nations; "Belt and Road" China UK Investment London Forum; KPMG; SIIS – Shanghai Institutes for International Studies; 48 Group; Thomson Reuters and EBRD including:

- UNECE International PPP Forum
- Selected BRI Case Studies: Shareholder Returns – Additional Upside
- CPEC Operational Energy Projects
- Polar Silk Road to 48 Group
- Halo Effects of Successful Chinese Investment into Sri Lanka

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