

**HD** Boost in **Chinese** buyers is good news for Australian companies, but understanding the drivers for this is key

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"IF THERE IS A WAVE, THERE MUST BE **WIND**"

(**Chinese** proverb)

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The last three months have seen more **Chinese** bidders in the public **M&A** market than for the whole of 2013. While some commentators have attributed this uptick in **Chinese** buyers to the relaxation of the NDRC approvals, in reality it's more likely a result of **Chinese** bidders picking what they see as the bottom of the resource cycle and looking to average down their cost of **acquisition**.

In addition to the formal changes to NDRC's approval process, there seems to be a new willingness to relax the "one-bidder policy". Until this policy is clarified, there is considerable advantage to targets and bidders in designing deal protection mechanisms that address this issue.

The changes to the NDRC approval process, which in summary lift the threshold for approval from NDRC to USD1 **billion**, were announced in December 2013 and the implementing regulations followed on 24 April 2014 (see our article POE investors travelling a thousand miles in one day). Despite the changes in the approvals policy, two of the four deals recently announced, namely the takeover by Landbridge **Energy** of Westside and the takeover by Guangdong Assets Management Limited (GRAM) of PanAust are conditional on PRC regulatory approvals. The deals so far announced by **Chinese** bidders in 2014 indicate some changes in the nature of **Chinese** bids as compared to 2012 and 2013 but also a consolidation of other trends previously identified (see **M&A Review 2012** and **M&A Review 2013**). Most notable are:

an apparent shift back from Privately Owned Enterprises (POEs) to State Owned Enterprises (SOEs) from provincial areas;

an ongoing shift from obtaining target recommendation to making offers directly to shareholders without target recommendation and in some cases a recommendation to reject; and

a continuing reliance on pre-bid stakes.

In our 2013 review of **M&A** deals, 100% of the public deals in our deal sample involving **Chinese** bidders were undertaken by POEs. In contrast, three of the four deals announced during the last three months have been SOEs - Norton **Gold** Fields (whose majority shareholder is Zijin **Mining**), Baosteel and GRAM - and in particular SOEs from the provinces rather than central SOEs in Beijing.

Two of three SOE bidders (Baosteel and GRAM) already have significant pre-bid stakes in their targets. These existing stakes were acquired closer to the top than the bottom of the resource cycle. In a continuation of this trend, Cuesta **Coal** on 21 May announced its major shareholder, state-owned Beijing Guoli **Energy** Investment **Company**, would inject \$15 **million** into the **company** via two separate share placements to increase its **stake** from 36% to 54%.

Recent allegations of corruption plaguing senior executives in **Chinese** SOEs has damaged the reputation of these companies and the questions of accountability may also be responsible for driving SOEs to seek to lower their cost base and book a profit from their overseas investments. This focus on profitability and ultimately accountability is evidenced by this month's report from the State AgencyXinhua

that the pace of SOE profit growth increased by 6.5% in January to April 2014 as compared to the same period last year. The profits of SOEs administered by provincial governments increased by 5.1% year on year, a marked turnaround on the 14.7% year on year decline for the same period in 2013.

Irrespective of the causes of the recent spike in PRC investment in Australia, the amendments to the PRC regulatory approvals process are certainly a welcome sign for PRC investment in Australia. That said, questions remain about the impact of the change to the so called "one-bidder" policy.

The recent **acquisition** battle between two **Chinese** companies over a Cayman registered semiconductor **firm** may shed light on **China's** changing overseas investment approval process. In this case two SOEs - Tsinghua Unigroup of Beijing (Unigroup) and the Shanghai Pudong Science and Technology Investment **Company** (PSTI) - were bidding separately for Nasdaq listed RDA Microelectronics.

In September 2013, PSTI bid USD15.50 for each of RDA's American depository shares and in October 2013 Unigroup offered USD18.50 per share. PSTI received a confirmation letter from NDRC (which would previously have granted it exclusivity in relation to a deal) in November 2013. However RDA unsurprisingly selected the higher bidder for its shares and executed an agreement with Unigroup. Many media outlets reported at the end of November that Unigroup had received a letter from NDRC advising them that without a confirmation letter, their move to acquire RDA was illegal.

However, in a new twist the **Chinese** press is now reporting that NDRC has indicated that a confirmation letter is not an exclusive document and that when PSTI obtained its exclusivity letter it had not entered into any binding agreement with RDA and that "such a move to jump the gun in submitting an application before even the most basic conditions of the deal had been agreed might mislead the regulatory departments".

On 20 December 2013, RDA and Unigroup announced the amendment to their merger agreement to reflect the changes to the NDRC approvals process. It now seems the merger agreement is no longer conditional on receipt of NDRC approval with an **acquisition** price of USD910 **million**. On 5 May 2014, the parties announced their ongoing commitment to close the transaction and reiterated the long stop date of 8 August 2014 for completion.

Two days later, on 7 May, PSTI issued a press release noting that six months had passed since RDA and Unigroup entered into their merger agreement and stating that PSTI had obtained an extension of its NDRC confirmation letter for an **acquisition** of RDA through to November 2014.

Understanding the shifting NDRC approvals process is vital for Australian companies keen to realise the opportunities offered by **Chinese** investment. For PRC bidders, ensuring a target understands the status of confirmation letters and "pre-clearance" will remain important. Target boards will continue to rely on these to assess the certainty of a PRC bid until there is further clarity on this issue. Until the one bidder policy is clarified, there is considerable advantage to both sides in designing deal protection mechanisms that address this issue.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

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