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HD **CHINESE CHANGE TACK ON AQUILA BID**

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The hostile move sets the tone for future investments

CHINA'S effort to enter Australia's sought-after resources space has been a roller-coaster ride — the successes and failures have occurred against a backdrop of political uncertainty and even pockets of xenophobia.

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But as the political landscape has changed, so too has China's approach to doing business in Australia and its $1.4 billion hostile move on iron ore and coal companyAquila Resources has set the tone for its future investments.

Steel giant Baosteel was the company chosen by Beijing to gain China's first significant foothold in Australia's No 1 export — iron ore.

China has generally approached deals in Australia from a "friendly" angle and has remained silent in local media on its bids, but the game has changed.

China is on the verge of winning a hard-fought battle for Aquila and, despite an independent expert labelling Baosteel's $3.40-a-share offer as "not fair", the board of its target felt it was left with little option but to recommend investors accept the bid in the absence of a superior proposal. In its target statement, released late on Friday, Aquila said it believed its company was worth more — Grant Samuel valued it at $3.90-$5.24 — but that "on balance" the bid should be accepted.

Aquila was pushed into that decision on what was an unusually aggressive move from its Chinese suitor, one that Aquila had relied on as a board member and significant shareholder for five years.

From the outset, Baosteel blamed the move on its target's lack of progress on key iron ore and coal developments and argued it had become "frustrated" with a company it had been an investor in for five years. It then stepped up the hostility when it drew a line in the sand on value and made it clear it was not budging on its $3.40-a-share deal and would withdraw support for Aquila if its bid did not succeed. Baosteel also shot down a potential rival bid by Aquila's new 12 per cent shareholder, Mineral Resources, by firing off a letter from its top Chinese executive outlining that if its bid failed, China would not be involved in the West Pilbara iron ore project in any form, either as financier or customer.

The Chinese have learned many lessons from past failures in Australia, the most obvious being the Sino Iron project in the Pilbara, which Citic Pacific purchased from Clive Palmer. The magnetite project has been hit with extreme budget blowouts, significant delays and legal battles with Palmer.

The Asian giant learned from this disastrous project that the model of owning, developing and operating its own mine in Australia, including with mostly Chinese staff, was not a wise one.

Top Chinese executives visiting Australia over the past year soon started talking about joint ventures and working more collaboratively with local groups to seek access to Australia's high-quality ore.

A lot of the focus on this bid has been on the “new model” of bringing in a local joint venture partner. Baosteel chose Brisbane-based freight operator Aurizon for this deal. But some market chatter has questioned the “joint venture” partner being highlighted, given Aurizon isn’t an equal partner as it is only taking a 15 per cent **stake** in the target. Australia’s largest rail freight operator will also head up the infrastructure arm to develop the rail and port to support the **iron ore** project.

Another boost to **China**’s maturing approach to investment in Australia was when Tony Abbott won government last September. Joe Hockey was quick to show that the Coalition government didn’t harbour any of the past xenophobic behaviour that had been displayed towards **Chinese** investment. The Treasurer was happy to relax previous Foreign Investment Review Board conditions on **China**-backed Yanzhou’s shareholding in Yancoal Australia, a move he made on the back of changing global market conditions.

FIRB was also quick to waive through Baosteel’s bid for Aquila and some have suggested the speed of that decision soon after the offer was announced meant it was likely that the **Chinese** were already engaged with FIRB or Treasury before making the bid. This would not be a surprise given that the **Chinese** play a long game, and they have played it on Aquila. They first emerged as a 15 per cent shareholder in August 2009, at a deal valued at $6.50 a share, a long way from the $3.40 a share it has now offered to control the **company**.

Baosteel’s claim that it was left with no choice but to move on Aquila because it had not progressed its key assets fast enough has been debated by some from the target’s camp. It has been argued that that was not a fair claim and it is understood the support the **Chinese** steel giant was offering to progress the **iron ore** asset in the Pilbara might not have been on favourable conditions.

While Baosteel’s strategy on this deal is still being analysed, one thing is certain: it was not dreamt up just prior to the announcement last month, it has probably been a long time coming, possibly as far back as its first move on to the share registry. **China** came from “inside the tent” on this one, so it didn’t need to approach on a “friendly” basis because it didn’t need to do due diligence — being on the board of its target, it knows about its assets.

“I would suggest that their tactics have been heavily influenced by what they think they already know,” one observer said. “They have been in the tent for a long time.”Another school of thought on Baosteel’s hostile approach is that it probably didn’t want to deal with Aquila’s managing director and 30 per cent shareholder, Tony Poli, from the outset. Poli is known for his tough negotiating skills and had the **Chinese** tried to walk through the front door with their plans, it could have been harder to be **firm** on its price. Poli has now agreed to the deal in the absence of a superior offer.

CO aqures : Aquila Resources Ltd.

IN i211 : Metal Ore Mining | ibasicm : Basic Materials/Resources | igoldm : Gold Ore Mining | imet : Mining/Quarrying

NS ccat : Corporate/Industrial News

RE china : China | austr : Australia | apacz : Asia Pacific | asiaz : Asia | ausnz : Australia/Oceania | bric : BRIC Countries | chinaz : Greater China | devgcoz : Emerging Market Countries | dvpcoz : Developing Economies | easiaz : Eastern Asia

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