Mergers and Acquisitions – China/New Zealand

Trends and insights

March 2017

In this publication we look at New Zealand and China M&A activity in 2016 and identify likely trends for the year ahead.

2016 – strong global activity benefits New Zealand

Global uncertainty with Brexit, Trump and military tensions around China and the Middle East did not slow healthy M&A appetite, with worldwide deal value of approximately US$3.28tn. And, despite predictions of China's economy slowing, Chinese outbound direct investment in 2016 increased by a huge 44.1% to US$170.1b, according to figures from the Chinese Ministry of Commerce. It appears that these official figures may even understate the actual position, as Chinese buyers themselves announced approximately US$220.9b of overseas acquisitions globally in 2016.

New Zealand benefited from overall global activity, with inbound investment into New Zealand approved by the Overseas Investment Office (*OIO*) for the 2016 calendar year reaching $8.7b, compared to $7.6b for the same period in 2015.

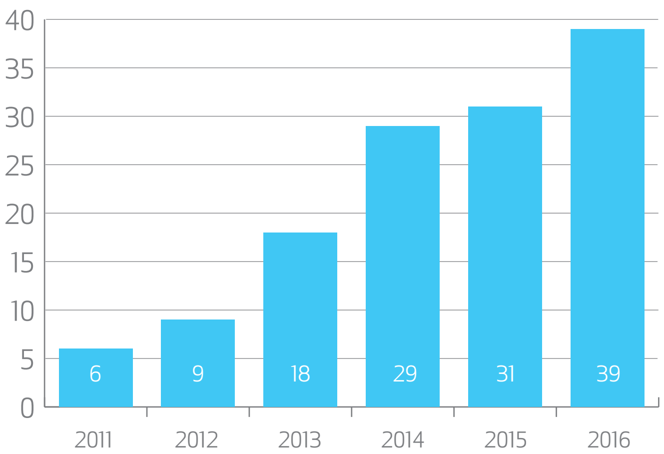
Chinese inbound investment into New Zealand has steadily increased since 2011, although it is still only a fraction of overall foreign direct investment into New Zealand. In 2016, 39 applications involving Chinese investors were approved by the OIO in respect of transactions valued at over $1.1b.

2017 expected trends at a glance

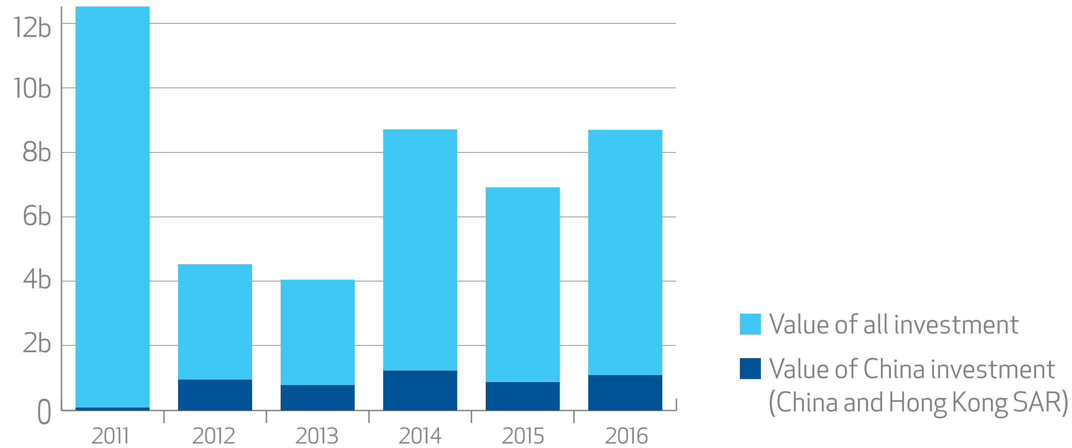
- New currency controls in China may give New Zealand a competitive edge as an investment destination as investors look to smaller markets like New Zealand.
- Chinese investment is diversifying, with increased investment expected in sectors including tourism, financial services, and value added food and nutraceuticals.
- In the absence of TPP, China may seek an increase in New Zealand's OIO consent thresholds.

Overseas Investment Office transactions at a glance

Total number of Chinese investments approved by the OIO



OIO-approved investment: global and China 2011-2016



2016 – OIO-approved Chinese investment applications by sector

21% DAIRY

21% LAND DEVELOPMENT AND RESIDENTIAL

13% AGRIBUSINESS

11% FORESTRY

8% MEAT PROCESSING

5% EDUCATION

5% PHARMACEUTICALS

5% WASTE MANAGEMENT

3% OIL AND GAS

3% ACCOMMODATION

5% OTHER

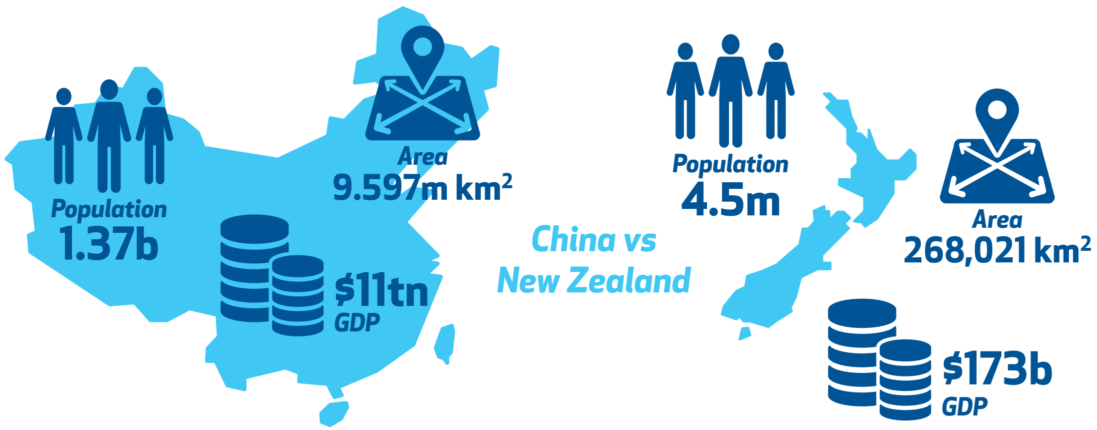
Predictions for 2017

China's new rules on yuan transfers might lead investors to look to smaller markets like New Zealand's. Meanwhile, Chinese investors are also diversifying into sectors other than dairy.

New regulatory controls in China may give New Zealand a competitive edge

As an interim measure to reduce capital outflows, regulatory restrictions have recently been put in place in China in respect of certain types of outgoing investment, including any transaction which results in a capital outflow from China of US$50m or more.

Given the average deal size here is lower than in other countries, this will have less impact on Chinese investment into New Zealand, and may see greater Chinese focus on New Zealand investment opportunities.



Source: World Bank's most recent data, 2015

Not just primary product

The stereotypical view of Chinese investment in New Zealand is that it focuses on dairy farms. However, the statistics from the OIO for 2016 show a more diverse story, with investment in land development and property projects, forestry, education, pharmaceuticals and waste management.

Examples of recent Chinese investment in New Zealand outside the primary produce sector include Waste Management, Fisher & Paykel Appliances and Hoyts.

We expect this trend to continue in 2016 with increased diversification into tourism, financial services and value added food and nutraceuticals.

In our experience, a key driver for Chinese investors is to develop or obtain brands, products or know-how, which can then be exported and sold to the significantly larger Chinese domestic market.

The Overseas Investment Act still looms large

The Overseas Investment Act remains a key concern and source of uncertainty for Chinese investors.

In 2016, Shanghai Pengxin ultimately withdrew its judicial review application in relation to the decision to decline consent for the purchase of the Lochinver sheep and beef station near Taupo. The case, had it gone ahead, would probably have resulted in some additional certainty regarding the proper application of the "counterfactual" test.

OIO counterfactual test

The counterfactual test was introduced in 2012 and it measures the scenario against which an investor's benefit claims will be measured to determine whether the investment would be of benefit to New Zealand.

There is a view among some Chinese investors that the level of scrutiny (by the Government, the media and the New Zealand public alike) of Chinese agricultural investments in New Zealand is disproportionately high. This sentiment could result in Chinese investors shifting focus further towards investments which do not involve the acquisition of "sensitive land" (particularly rural land) in 2017.

Will the OIO threshold be increased for Chinese investors?

In December 2016, the New Zealand and Chinese governments announced a commitment to upgrade and improve the FTA in order to, among other things, ensure its continued relevance.

Of interest is whether China will seek an increase in New Zealand's investment screening threshold for significant business assets. The legislated threshold in the Overseas Investment Act 2005 is $100m.

If TPP had entered into force, New Zealand would have been required, by virtue of the most-favoured-nation rule in the China FTA, to provide a higher screening threshold ($200m) to Chinese investors who are service suppliers in listed sectors (environmental, construction, engineering, computer, tourism, and those incidental to agriculture and forestry). In the absence of TPP, China may seek a higher threshold, either for these service suppliers, or potentially for investments more broadly.

> "In the absence of TPP, China may seek a higher threshold ... potentially for investments more broadly."

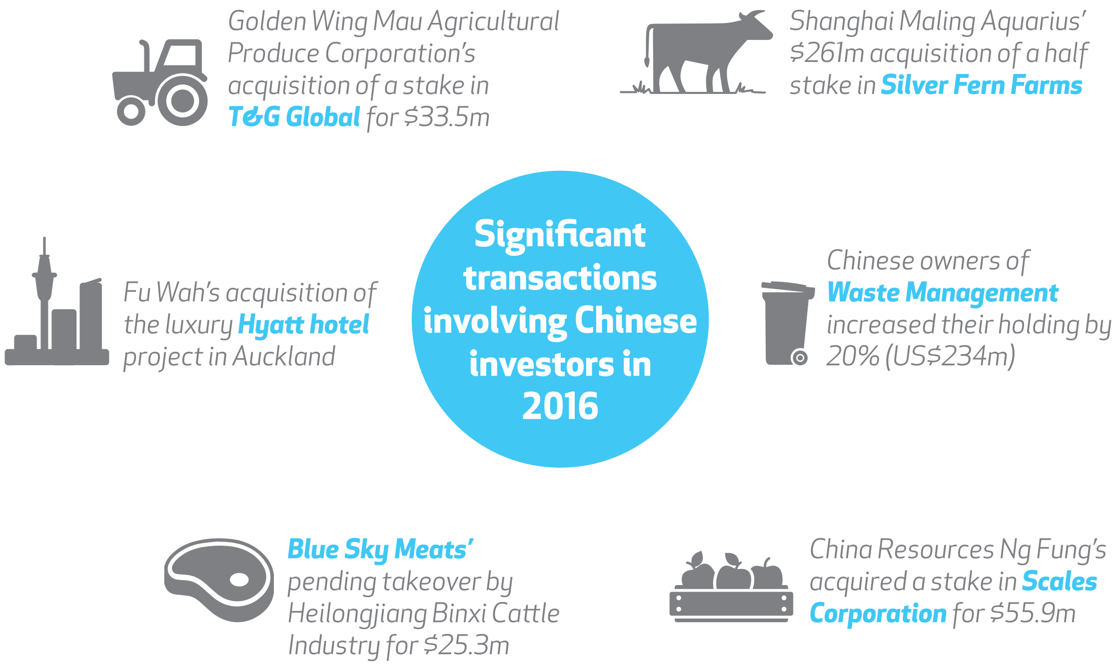
Benefits of Chinese investment for New Zealand

Foreign direct investment has a number of benefits

Foreign direct investment is important for a small and open economy like New Zealand's and, according to the New Zealand Treasury, closer economic ties with China have already "increased the income and purchasing power of New Zealanders, contributing to higher living standards."

One of the Overseas Investment Act's criteria for certain deals is that the investment will result in benefits to New Zealand – for example, creating new job opportunities, increasing export receipts, marketing competition and efficiency. In Shanghai Maling's application to invest in Silver Fern Farms, the OIO considered that the investment would allow Silver Fern Farms to increase its exports.

Recently, the OIO-approved Chinese company Cuilam Industry's purchase of Southland's Prime Range Meats on the basis that the investment would provide jobs, increase efficiency/productivity and increase export receipts, as well as provide additional investment for development purposes.



Chapman Tripp's China Desk

Connecting New Zealand businesses and foreign investors

Our dedicated China Desk advises both New Zealand businesses and their Chinese counterparties entering or active in the New Zealand market through a focused, multi-disciplinary team of M&A, property, finance, commercial and litigation specialists. Our senior partners and Mandarin-speaking lawyers work together to obtain the best possible outcomes for clients.

We have close relationships with international and local law firms in China and business partners on the ground in Shanghai and Beijing, ensuring our clients have the connections and support they need.

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Band 1, Corporate and Commercial, Chambers Asia Pacific 2017

"The property team is excellent. They are commercially aware and provide accurate advice."

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China desk recent M&A highlights

We have advised:

- Fu Wah International Group on its acquisitions and development of residential and hotel projects in New Zealand including the construction of its luxury Hyatt hotel project in Auckland
- Beijing General Aviation on its 50% equity investment in Pacific Aerospace, and on the establishment of a joint venture with Pacific Aerospace called Beijing Pan Pacific Aerospace Technology
- Shanghai Pengxin on its successful OIO application to purchase over 7800ha of substantial dairy farming assets (the Crafar Farms)
- Shanghai CRED Real Estate on the acquisition and OIO application to purchase the Peppers Carrington Resort and Karikari Winery Estate
- Sinochem Corporation on its proposed acquisition of Australian listed crop protection and seed company, Nufarm, by way of a scheme of arrangement effected under the Australian Corporations Law
- China Minmetals on the acquisition and disposition of an industrial property portfolio and the development of residential apartment complexes
- Sino-Forest Corporation on all aspects of its $100m acquisition of the Mangakahia Forest Estate
- CNBM Forest Products New Zealand, a subsidiary of China National Building Materials Group Corporation, on its acquisition of forestry assets
- Nimble Group on its acquisition and development of several pieces of land in Auckland and the restructuring of its New Zealand platform Avanda
- Beijing Allied Faxi Food on its successful retrospective OIO application for its purchase of sensitive land in New Zealand in 2014
- Beijing Sanyuan Food on its successful OIO application in relation to its restructure of assets involving sensitive land in New Zealand, and
- ID Leisure Ventures, founded by Chinese billionaire Sun Xishuang, on the New Zealand elements of their AU$900m acquisition of Hoyts Group.

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Chapman Tripp is New Zealand's leading full-service commercial law firm, with offices in Auckland, Wellington and Christchurch. Our lawyers are recognised leaders in corporate and commercial, mergers and acquisitions, capital markets, banking and finance, restructuring and insolvency, litigation and dispute resolution, employment, government and public law, intellectual property, telecommunications, real estate and construction, energy and natural resources, and tax law.

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