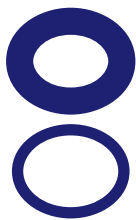


China FDI Q&A

China FDI: Will 2009 be when the dragon economy wakes?



Loo Choon Chiaw



Loo & partners LLP

俊昭法律事務所

Loo & Partners LLP
88 Amoy Street, Level Three, Singapore 069907

Tel : (65) 6322-2288 | Fax : (65) 6534-0833
Email : ccloo@loopartners.com.sg
Website: www.loopartners.com.sg

ALB: It seemed like only yesterday that when we spoke of any China direct foreign investment (FDI), we were only referring to investments into China, but this trend has been reversed over the last few years, now it has been all about Chinese outbound investment.

LCC: I certainly agree with your general observations. Since the early-80s, the PRC has been the biggest beneficiary of FDIs, which have brought advanced technology and latest know-how into the PRC. Recently, there has been a fall in FDI inflows, which ended three decades of rapid growth in FDI inflows to the PRC.

A survey of U.S. companies in the PRC published by the American Chamber of Commerce in China on 10 March 2009 found that 39% of the respondents were either postponing or had cancelled planned investments this year, while 21% indicated that they would shrink their China work force. Thus, even the PRC is not totally immune to the adverse impact of the global financial crisis (GFC).

The statistics clearly confirm that the trend will soon be reversed as the PRC enterprises begin to venture abroad. The numbers released by the PRC Ministry of Commerce (MOFCOM) (商务部) on the total amount of PRC out-bound FDIs: USD2.5 billion in 2002, and USD52.1 billion in 2008, speak for themselves.

ALB: What are the reasons behind the shift and how much more of this can we expect to see in 2009?

LCC: There is a host of reasons behind the pendulum swing. To start with, the enterprises in the PRC are relatively less exposed to the sub-prime crisis. There is an abundance of lowly-g geared, well capitalised and well managed enterprises in the PRC. The RMB has been strong. The current GFC has therefore presented a window of opportunities for these PRC enterprises to exploit the low market value of quality businesses and assets abroad as their overseas counterparts are busy deleveraging and in great need of refinancing.

It is noteworthy that the PRC Government has also shown its strong support behind the internationalisation drive of the PRC enterprises via the promulgation of new regulations. Thus, the MOFCOM has issued new regulations on 16 March 2009 ("16 March Regulations") primarily designed to encourage PRC enterprises to go international.

Under the new regulations, the MOFCOM will only review any application by a PRC enterprise for an overseas investment in excess of USD100 million or where the proposed investment relates to special purposes. When one extrapolates from the relevant statistics in 2008, it has been estimated that approximately 85% of such overseas investment applications shall be processed at the local commerce administration at the provincial level (省级商务主管部门). Furthermore, the timeline to process an overseas investment application has been greatly shortened. The review procedures have also been simplified and streamlined. On any account, the 16 March Regulations shall greatly speed up the approval process for out-bound FDIs by the PRC enterprises, thereby helping to accelerate the internationalisation drive of these enterprises.

Recently, the PRC National Development and Reform Commission (发改委) predicted a 13.2% growth in total quantum of the PRC out-bound FDIs over the 2008 number (which as mentioned earlier, stood at USD 52.1 billion) notwithstanding the negative impact of the GFC.

ALB: How did the PRC MOFCOM justify its rejection of Coke's proposed buyout of Huiyuan?

LCC: The MOFCOM has stated that its rejection of the proposed buyout by Coke (可口可乐) of Huiyuan (汇源) was based on its concerns that the proposed buyout, if to be proceeded with, would cause an adverse impact on market competition and might restrict the healthy development of the beverage industry as a whole.

It is not in dispute that at the material time, both Coke and Huiyuan held massive shares in the PRC domestic market, namely, Coke had some 50% market share of the carbonated drinks sector; and Huiyuan, on the other hand, had 46% and 39.8% market share, respectively, of the pure fruits and medium concentration beverages sectors. The MOFCOM thus concluded that the proposed buyout, if permitted, would lead to market monopolies. It was of the view that not only would the proposed buyout, if effected, create unfavorable conditions for other local beverage manufacturers, small and medium-sized ones in particular, it would also hurt the interests of both the consumers and the fruit farmers.

Furthermore, the MOFCOM held the view that if the acquisition were approved, the

ALB discusses with Loo Choon Chiaw, Loo & Partners LLP

controlling power of Coke over the juice market would be markedly increased so that other companies would be incapable of entering it.

ALB: What are your views on MOFCOM's ruling?

LCC: The MOFCOM is a market regulator and has a duty to discharge its responsibilities. Prima facie, its decision to ban the Coke's buyout of Huiyuan was in line with the PRC Anti-Monopoly Law 2007, which came into effect on 1 August 2008 (the "AML")(反垄法), which has its ultimate goal in the maintenance of fair play in the marketplace and the protection of the overall interests of all parties concerned.

Critics of the ruling have raised serious concerns on the sweeping nature of Article 27(6) of the AML, which empowers the MOFCOM, when making a ruling on a matter, to take into account any important factor which may have an impact on market competition which MOFCOM deems fit (认为应当考虑的影响市场竞争的其他因素).

Be that as it may, on the surface, the prescribed procedures, in strict compliance with the AML have been fully followed in the review process. One could only make any objective and fair critique on the MOFCOM's ruling if one were furnished with the same information as those before the MOFCOM at the material time, thereby placing one in the same factual matrix as the MOFCOM was.

ALB: What about government intervention in relation to Chinese outbound investments, for example, Australia's blocking of China Minmetals' acquisition?

LCC: Australian Treasurer Wayne Swan delivered a blow to Minmetals' proposed USD1.7 billion acquisition of the world's second-largest zinc producer when he said the state-owned company would not be allowed to buy Oz Minerals' Prominent Hill mine in the Woomera Prohibited Area, a military weapons testing range.

Following the rejection, Minmetals put up a revised offer, which was approved by Swan on 23 April 2009. It is noteworthy that the approval excludes, amongst others, the Prominent Hill mine.

The approval was also made conditional upon Minmetals' undertakings to use mostly Australian managers, price products produced by OZ Assets in Australia at arms-length basis, comply with industrial relations law, honour employee entitlements, to expand production

at some sites and to support Indigenous Australian communities.

As emphasised by Swan, the undertakings were designed to protect around 2,000 Australian jobs and ensure consistency with Australia's national interest principles in accordance with the Foreign Acquisitions and Takeovers Act 1975.

ALB: What are your views on the Minmetal's acquisition?

LCC: This case is perhaps unique as the initial rejection was purportedly made on national security ground, which no sovereign country would look upon lightly.

Swan when, approving Minmetals' revised offer, had no qualms in stating expressly that the conditions imposed on Minmetals were design to protect Australian jobs and to safeguard Australia's national interest in accordance with Australian law.

I find Swan's candidness refreshing. It will be interesting to see how the Australian Regulators will deal with Chinalco's (中国铝业) proposed investment of USD19.5 billion in Rio Tinto!

ALB: Many in the industry expect FDI out of China to remain high. Would the initiative be from the private public sectors? Are we likely to see more interests in one sector of the economy than another?

LCC: The FDIs to be undertaken by the PRC enterprises would continue to be dominated by the PRC state-owned enterprises (SOEs). These are the enterprises with a deep pocket. Many of them possess a strong management team led by a dynamic and ambitious Chairman or CEO, who has an international exposure. These SOEs shall be in the pursuit of oil and gas, minerals and other natural resources abroad to ensure the steady supply of energy, raw materials and processed commodities essential to the PRC's economic independence and political stability.

ALB: Despite high levels of investment into the PRC, many still feel that elements of the regulatory regime in China are still found wanting in key areas. Can you identify some of them?

LCC: Foreign investors have been criticising the PRC for the deficiencies of its regulatory regime since the early 80s. Much water has flowed under the bridge since then. Although things have improved substantially, foreign investors

still feel that the PRC fails to provide them with an equal access to the market and a level playing field for them to carry on their businesses in the PRC. Serious concerns have regularly been raised in several areas, including: (1) inadequate protection of intellectual property rights; (2) the unfair treatment frequently received by foreign-invested firms when they bid for public procurement projects; (3) the restriction imposed on foreign investment in a wide range of sectors, eg, the petrochemical sector; (4) the lack of transparency in rule-making. Recently and since the Coke's failed buyout of Huiyuan, serious reservations have also been levied against the AML over its potential for abuse by over-zealous officials at the MOFCOM in view of the wide discretionary power vested in MOFCOM by virtue of the sweeping provisions of Article 27(6).

ALB: Are the PRC authorities aware of these deficiencies? Have measures been taken to improve things on this front?

LCC: The PRC authorities are certainly aware of the deficiencies. They also realize that in the absence of any improvement, there will be a further decline in the quantum of the in-bound FDIs, which will in turn adversely affect their long-term plan to channel more FDIs into the relatively underdeveloped areas in the western and central regions.

To improve investment conditions, the MOFCOM via its circular on "further improving examination and approval of foreign investments" (进一步改进外商投资审批工作的通知) dated 5 March 2009 (the "5 March Circular") has streamlined the approval process for in-bound FDIs. It has also empowered the local competent commercial authority (地方商务主管部门) to process an FDI application of up to USD100 million. Like the 16 March Regulations, the 5 March Circular is expected, to greatly speed up the approval process for in-bound FDIs.

ALB: As a specialist legal practitioner advising on PRC matters, how do you feel about their deficiencies?

LCC: The lack of transparency in the judicial decision making coupled with the vagueness or 'fuzziness', a term recently used by the Economist Intelligence Unit when reviewing the legal and regulatory risk of doing business in the PRC, of some of the PRC legislations have made the life of many legal practitioners who advise on such matters very difficult indeed!