

Demystifying Chinese Investment in Australia

Update March 2013

**Australia still a priority destination,
but the world is catching up**

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About our reports



KPMG and The University of Sydney China Studies Centre have formed a strategic relationship to publish research and insights on doing business with Chinese investors. Our first report was published in September 2011, with *Demystifying Chinese Investment in Australia* representing the fifth report in our series.

Despite strong public interest, little detailed factual information has been previously available about the actual nature and distribution of China's outbound direct investment (ODI) in Australia. This update report continues our comprehensive reporting of China's ODI into Australia.

The dataset is compiled by a joint University of Sydney and KPMG team and covers investments into Australia made by entities from the People's Republic of China through M&A, joint ventures and greenfield projects. The dataset also tracks Chinese investment by subsidiaries or special purpose vehicles based in Hong Kong, Singapore and other locations. The data, however, does not include portfolio investments, such as the purchase of stocks and bonds, which does not result in foreign management, ownership, or legal control. For consistency, the geographic distribution is based on the location of the Chinese invested company and not on the physical location of the actual investment project. Completed deals which are valued below USD5 million are not included in our analysis, as such deals consistently lack detailed, reliable information. Unless otherwise indicated, the data referred to throughout this report is sourced from KPMG/University of Sydney database, and our previously published reports¹.

The University of Sydney and KPMG team obtains raw data on China's ODI from a wide variety of public information sources which are verified, analysed and presented in a consistent and summarised fashion. In line with international practice, we record deals using USD as the base currency.

We believe that the KPMG/University of Sydney dataset contains the most detailed and up-to-date information on Chinese ODI in Australia.

1. Includes Australia & China Future Partnership, September 2011; The Growing Tide: China ODI in Australia, November 2011; Demystifying Chinese Investment, August 2012; The Energy Imperative: Australia-China Opportunities, 25 September 2012.



For Australia, there is growing Chinese investment interest in agriculture, renewable energy and real estate.



Australia still a priority destination for Chinese investment...

The close of 2012 saw Australia narrowly maintain its top ranking as the most significant recipient country of Chinese outbound direct investment (ODI) accumulated since large-scale investment of this kind began in earnest in 2005.

Chinese accumulated investment flows into Australia at the end of 2012 surpassed the USD50 billion mark, further improving China's position as the ninth largest foreign direct investor in Australia in 2011 (the USA was the largest with accumulated investments of USD125 billion).

The 2012 growth rate of Chinese direct investment into Australia was nearly twice as high as the growth rate of global Chinese outbound non-financial direct investment, which grew from USD68.6 billion to USD77.2 billion in 2012².

Although below the historic peak of USD16.2 billion in 2008, Chinese direct investment inflows into Australia in 2012 increased 21 percent from 2011 levels to reach USD11.4 billion (AUD11 billion) across 27 transactions, up from USD9.4 billion in 2011 and USD3.7 billion in 2010. Notably, Canada achieved top position for the 2012 calendar year, due to the completion of one enormous transaction – the USD15.1 billion CNOOC-Nexen oil and gas company deal.

Chinese investment trends in Australia in 2012 alone show a diversification towards energy and other sectors, and away from

mining and resources, although mining still dominates. Of the total USD11.4 billion invested in 2012, 48 percent was recorded in mining, 42 percent in gas, 3 percent in agriculture and 2 percent in renewable energy (mainly wind).

The 2012 industry sector results represent a significant variance from historical data trends from September 2006 – December 2012 where mining accounted for 72.6 percent and gas 17.5 percent of total Chinese investment.

The geographic focus of investments correlates with the sectoral investment pattern, with transactions in Western Australia and Queensland together accounting for 89 percent of the value of completed transactions (56 percent recorded in Western Australia and 33 percent in Queensland).

The 2012 geographic distribution results also significantly vary from historical data trends which recorded investment in Western Australia at 31.6 percent and Queensland at 30.5 percent.

The concentration on mining and gas sector investments is also reflected in the ongoing trend of a small number of very large

value deals contributing to the annual total. Eight deals with a value over USD500 million accounted for 83.4 percent of the 2012 transaction total value.

The proportion of investments by privately owned Chinese companies rose during the year, while the share of capital invested by Chinese State-Owned Enterprises (SOEs) declined in 2012. Chinese non-state (i.e. private) investors completed 26 percent of all deals by number, and 13 percent by deal value.

These results again differ from historical trends which indicate SOEs accounted for 94 percent by value and 80 percent by number of deals between September 2006 and December 2012.

The outlook for Chinese direct investment in Australia remains positive for the Year of the Snake. The fundamentals of the Chinese economy remain positive. Global Chinese outbound direct investment is planned to grow by 15 percent in 2013³, according to Chinese Government planning records. For Australia, there is ongoing Chinese investment interest in mining and gas projects and growing interest in agriculture, renewable energy and real estate.

2. www.china.org.cn/china/NPC_CPPCC_2013/2013-03/05/content_28133377.htm

3. China's National Development and Reform Commission (NDRC) Report on the 2013 Draft Plan for National Economic and Social Development, submitted to the National People's Congress on 5 March 2013.

... but the world is catching up.

Australia is losing its dominant status relative to other countries.

While Australia's accumulated Chinese direct investment is still ahead of its main international competitors, there is no denying that the rest of the world is hot on our heels and aggressively competing for Chinese capital.

Chinese investment is geographically diversifying, and the USA and Canada in particular are catching up with Australia in attracting energy investment.

Despite Canada's huge USD15.1 billion CNOOC/Nexen deal in 2012, Australia narrowly remains the number one individual country for accumulated Chinese direct investment overseas. According to Heritage Foundation figures, Australia is the leading recipient

of Chinese non-financial investment since 2005, accounting for 13.2 percent of China's total outbound investment over the 8 year period⁴. By the end of 2012, total accumulated investment reached USD51 billion in Australia, just ahead of the USA at USD50.7 billion and USD36.7 billion in Canada. Other major recipients included Brazil and Russia. The largest investment destinations in Europe and Africa are the United Kingdom and Nigeria respectively.

These figures also show growing diversification of global Chinese ODI, particularly in resource rich countries which are potential competitors for Australia. From 2005 to 2008 Australia and the USA were the main beneficiaries, however by 2012 Chinese ODI has become far more diversified.

Annual Chinese ODI in Australia and major competitor countries (USD millions)

	2005		2006		2007		2008		2009	
	USD m	%	USD m	%	USD m	%	USD m	%	USD m	%
Australia	320	3	2,920	14.1	430	1.4	15,850	29.3	8,980	17.4
USA	1,740	18	-	-	8,600	28.6	6,770	12.5	8,160	15.8
Canada	250	3	110	0.5	-	-	-	-	3,480	6.7
Brazil	-	-	-	-	-	-	-	-	900	1.7
Russia	-	-	5,410	26.1	-	-	-	-	780	1.5
United Kingdom	-	-	800	3.9	3,040	10.1	1,990	3.7	1,700	3.3
South Africa	-	-	230	1.1	5,600	18.6	-	-	-	-

Source: Heritage Foundation (Note: percentages refer to proportion in Chinese global ODI)

4. Heritage Foundation figures differ in detail from the KPMG/University of Sydney dataset. However, they constitute the best available dataset for international comparison.

Chinese investment is geographically diversifying, and the USA and Canada in particular are catching up with Australia in attracting energy investment.

	2010		2011		2012		TOTAL	
	USD m	%	USD m	%	USD m	%	USD m	%
	3,140	4.8	8,890	11.9	10,490	13.2	51,020	13.2
	8,820	13.4	1,940	2.6	14,700	18.5	50,730	13.1
	6,590	10.0	4,880	6.6	21,350	26.8	36,660	9.5
	13,160	19.9	8,630	11.6	2,600	3.3	25,290	6.5
	3,770	5.7	1,100	1.5	1,520	1.9	12,580	3.3
	960	1.5	510	0.7	2,860	3.6	11,860	3.1
	330	0.5	1,830	2.5	-		8240	2.1



Steady investment growth in Australia since 2010

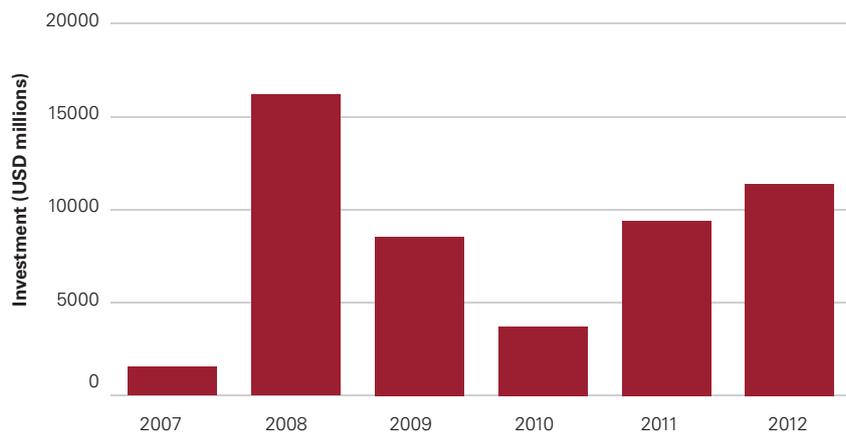
From September 2006 to December 2012 a total of 128 completed deals were recorded. During this period, an accumulated USD50.8 billion was invested by Chinese enterprises in Australia.

Chinese investment flows into Australia have maintained an incremental growth trend since 2010. Contrary to claims that flow and size of Chinese investments in Australia are falling away, total investment continued to grow over the last two years, from USD3.7 billion in 2010 to USD11.4 billion in 2012.

While inflows in 2012 are still short of the historic peak of USD16.2 billion in 2008, the two years of consecutive growth in 2011 and 2012 show that confidence in Australia as an investment destination has recovered after the remarkable slowdown in 2009-2010.

By comparison to investment from other countries, Chinese direct investment into Australia remains small, reflecting the relatively short period of time for Chinese investment in Australia. According to the latest Australian Bureau of Statistics (ABS) figures, by the end of 2011 China's direct investment stock only accounted for 2.6 percent of total foreign direct investment stock into Australia – which is approximately only 10 percent of direct investment into Australia by American companies.

Chinese investment in Australia by year



Accumulated direct investment value in Australia by the end of 2011

Country	Value (AUD millions)	Share
USA	122,379	24%
United Kingdom	69,747	14%
Japan	52,334	10%
Singapore	19,966	4%
China	13,354	3%

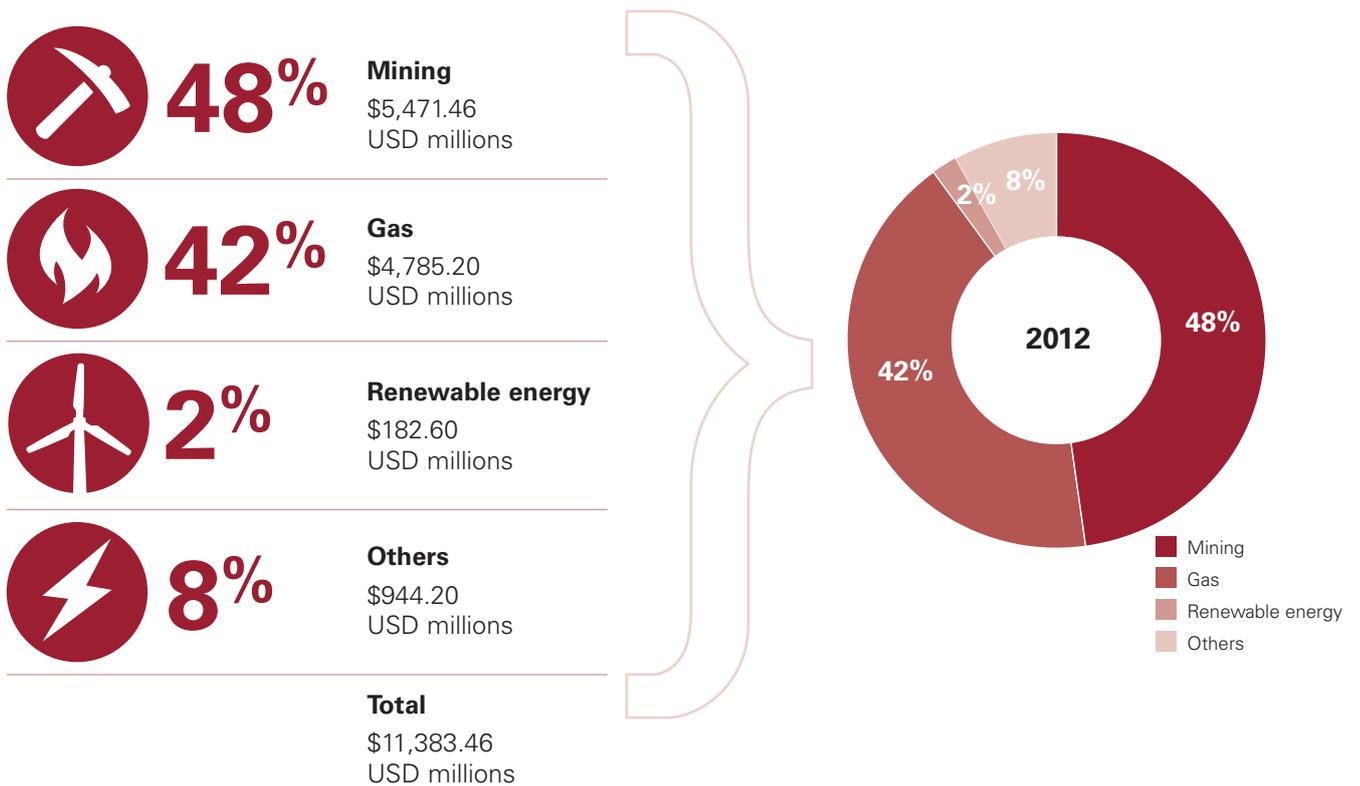
Source: Australian Bureau of Statistics, 53520 – International Investment Position, Australia

Chinese investment in Australia by industry

Chinese ODI by industry in 2012

In 2012, Chinese investment into Australia remained heavily concentrated on mining resources and energy in response to continued Chinese demand for construction and energy-related commodities. However, we witnessed a gradual shift of investment from resources to energy, particularly to the LNG sector.

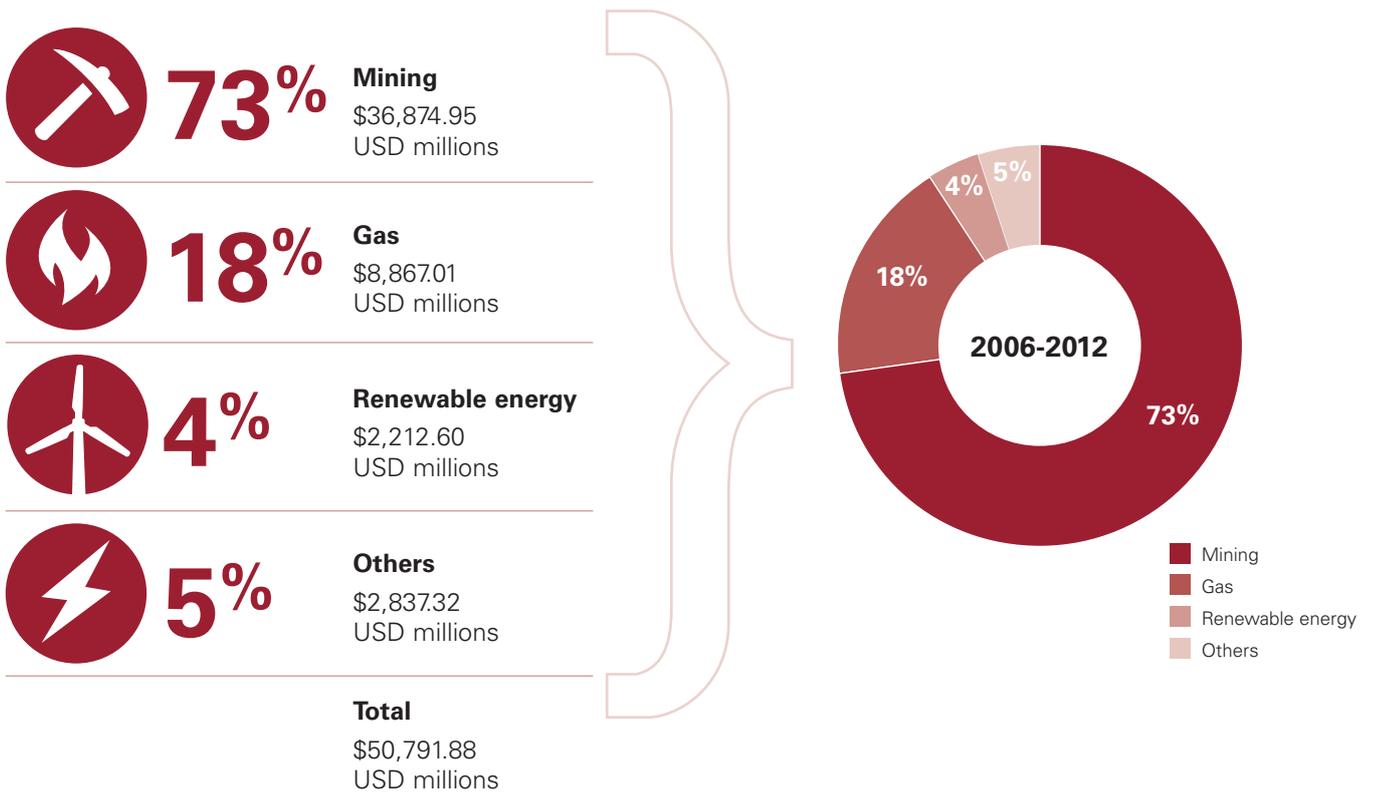
Eight percent of Chinese investment went into a variety of other sectors. Despite public commentary that Chinese investors are 'buying up Australian farms and land', our analysis shows that Chinese investment of USD296 million into Australian agriculture accounted for only 2.6 percent of total Chinese investment inflows in 2012.



Over the last six years, the mining sector received the largest share of Chinese investment in Australia.

Accumulated Chinese ODI by industry 2006-2012

Over the last six years, the mining sector received the largest share of Chinese investment in Australia, accounting for 73 percent of the total investment flows, followed by gas (18 percent) and renewable energy (4 percent).

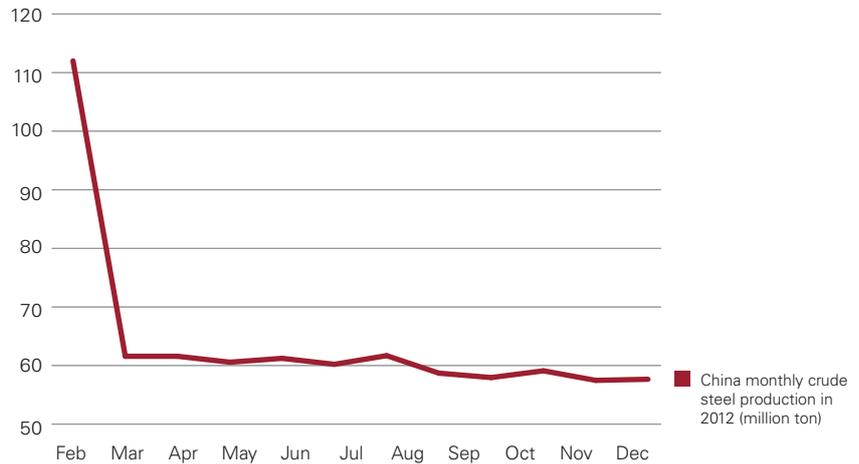




China's plan to diversify its energy consumption structure and reduce reliance on coal for power generation explains the growing interest of Chinese companies to bid for Australian LNG projects.

The shift in Chinese investment away from mining indicates a lagged response to changes in domestic conditions in China and global markets. The Chinese steel and iron industry experienced a slowdown in 2012 as property sector and new infrastructure spending was deliberately slowed down to address inflation. Crude steel output halved in March 2012 and remained low for the rest of 2012. Until mid-September 2012, steel prices were on the decline with the steel price composite index for steel products falling from 105 points to a low of 87 points.

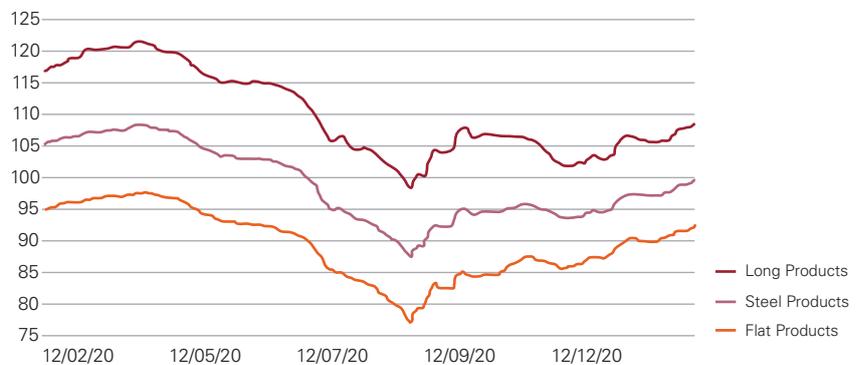
China’s monthly crude steel production



Source: National Bureau of Statistics of China

China’s Steel Price Index

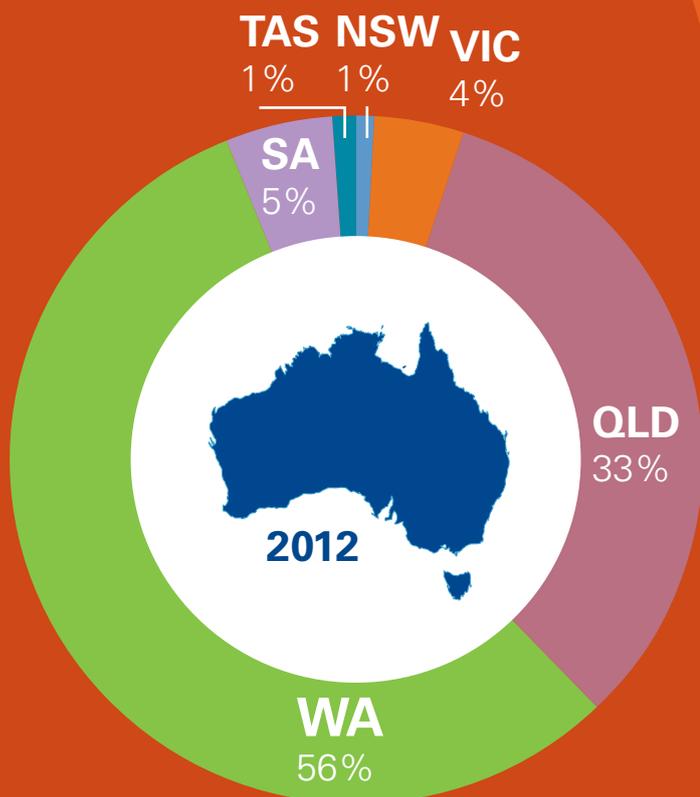
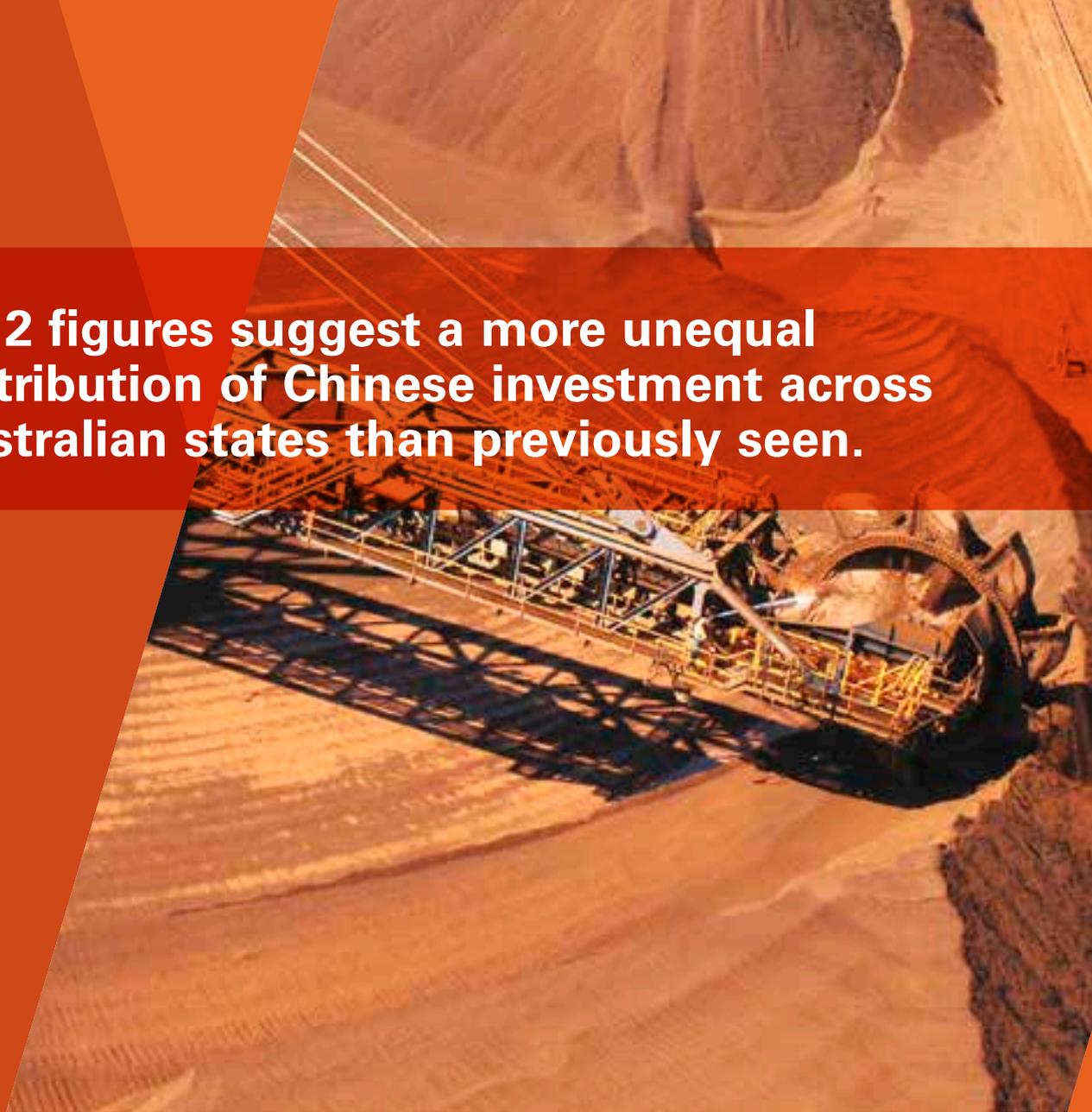
SteelHome China Steel Price Index (SHCNSI)(2012-02-19-2013-02-19)
 Benchmark date: Sept.28, 2004 Source: SteelHome website (www.steelhome.cn)



Source: Shanghai SteelHome Information and Technology Co.,Ltd

Global demand for LNG has increased significantly in the last two years primarily due to the sharp increase in demand from Japan and the emergence of new LNG importing markets. Currently, global LNG trade is constrained by supply shortfall due to lower overall gas output. This gap in global supply and demand, together with China’s plan to diversify its energy consumption structure and reduce reliance on coal for power generation explains the growing interest of Chinese companies to bid for Australian LNG projects. However, China is also actively looking at other gas supply options, for example Russia and its neighbouring states.

2012 figures suggest a more unequal distribution of Chinese investment across Australian states than previously seen.



Geographic distribution in 2012

Total completed deals by state in 2012 (value, USD million)

WA	\$6,383.60 million
QLD	\$3,732.04 million
SA	\$523.00 million
VIC	\$444.52 million
TAS	\$182.60 million
NSW	\$117.70 million

Chinese investment in Australia by geography

The continuing focus on mining and gas is reflected in the geographic distribution of Chinese investment.

2012 figures suggest a more unequal distribution of Chinese investment across Australian states than previously seen. In 2012, Western Australia attracted 56 percent and Queensland 33 percent of Chinese investment flows. Companies officially incorporated in these two states together accounted for nearly 90 percent of the 2012 Chinese investment capital.

The concentration of 2012 investment in Western Australia and Queensland differs from historical trends. New South Wales (NSW) and Victoria have captured relatively less Chinese capital in 2012 (USD118 million or 1 percent and USD444 million or 4 percent respectively), compared to their historic share.

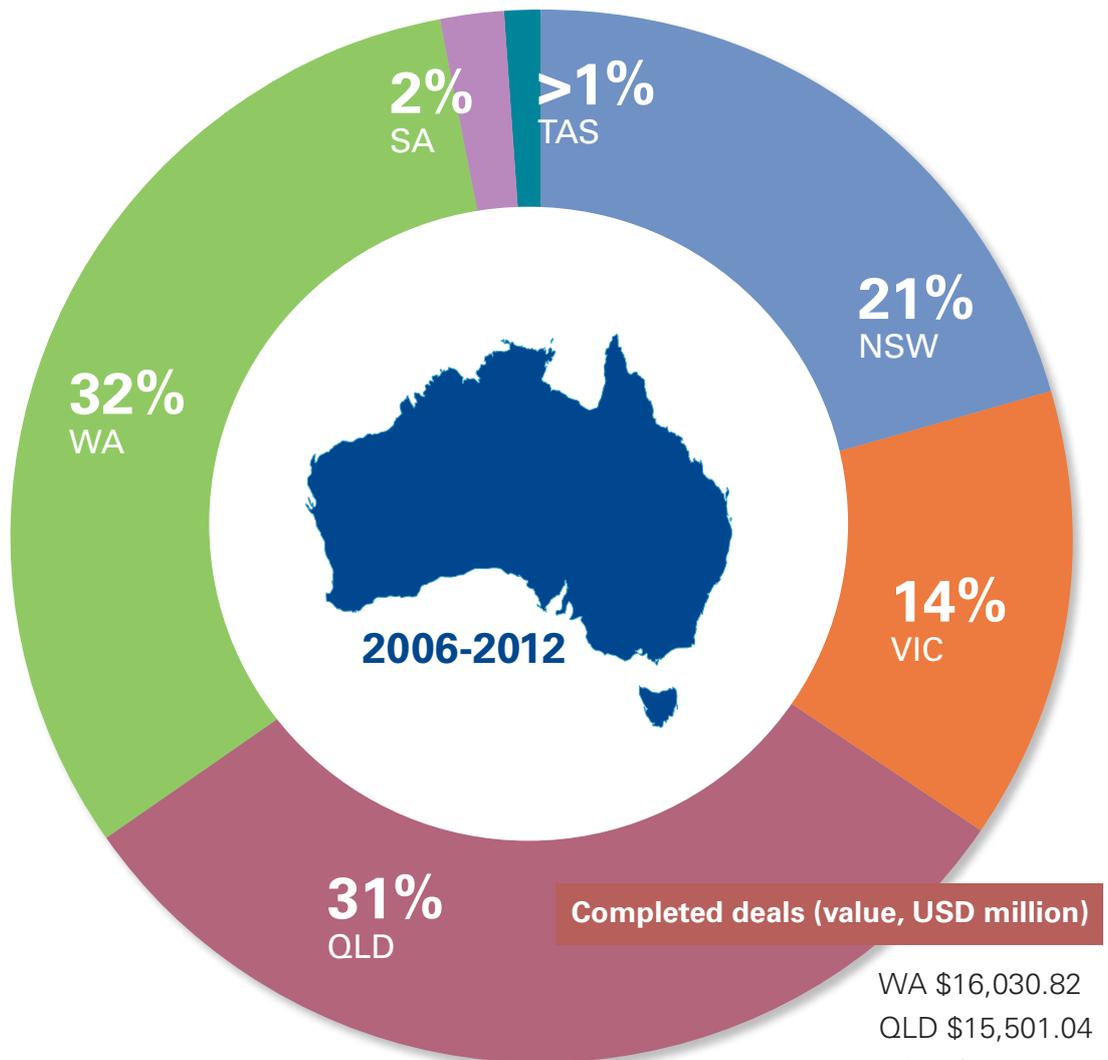
Meanwhile, 2012 results for South Australia (5 percent) and Tasmania (1 percent) exceed their historical levels. While there is certainly project level investment by Chinese companies in the Northern Territory, our data did not identify completed investments by Chinese investors in Northern Territory-headquartered companies above USD5 million.

While investment in Western Australia and Queensland is highly concentrated in mining and resource industries, NSW and Victoria's engagement with Chinese companies was more diversified across various sectors – which is an encouraging trend for the future.

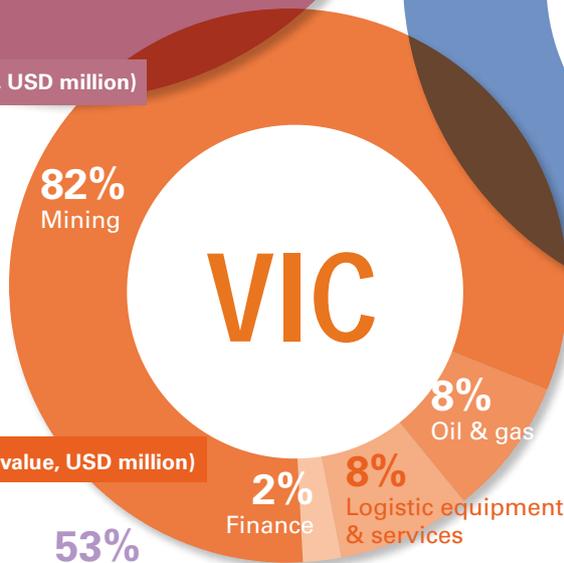
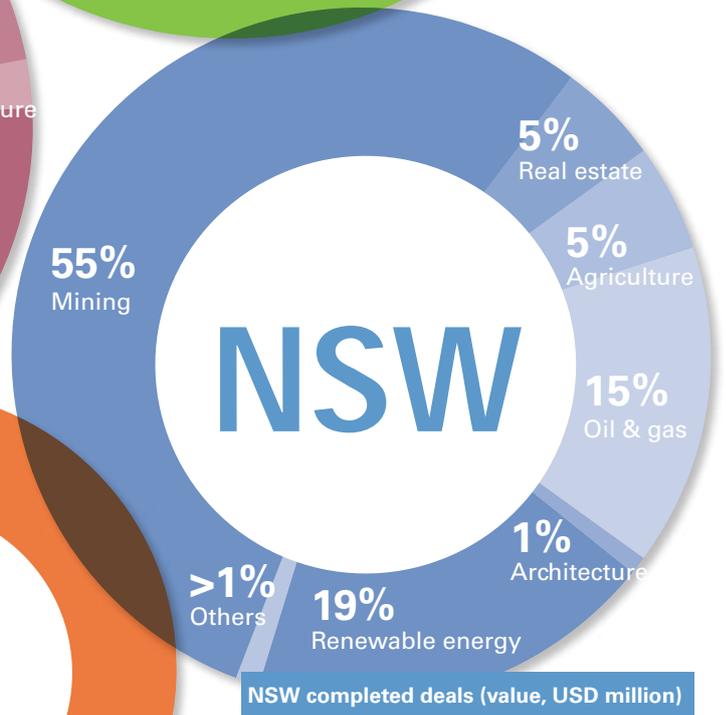
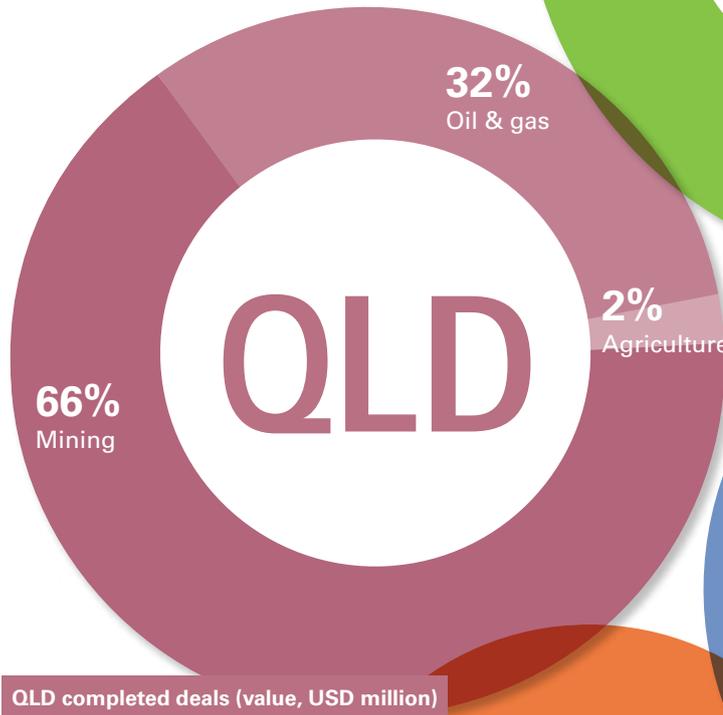
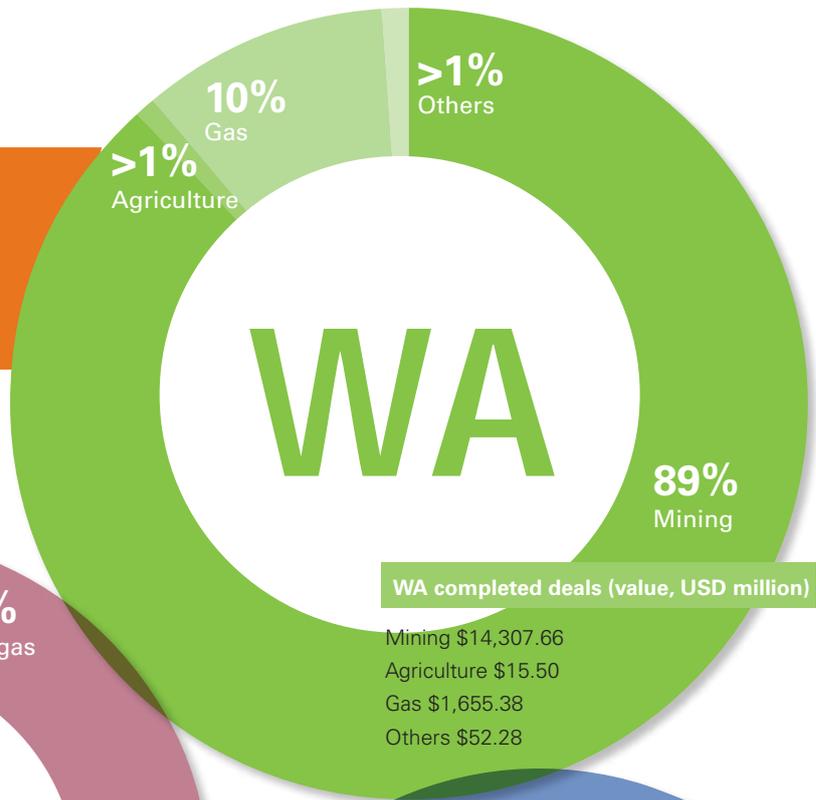
Chinese accumulated ODI 2006–2012 by geographic and industry distribution

From September 2006 to December 2012, nearly two thirds of the total Chinese investment was absorbed by Western Australia and Queensland, followed by NSW with USD10.8 billion and Victoria with USD7.1 billion.

While investment in Western Australia and Queensland is highly concentrated in mining and resource industries, NSW and Victoria’s engagement with Chinese companies was more diverse. In particular, investment diversity remains greatest in NSW.

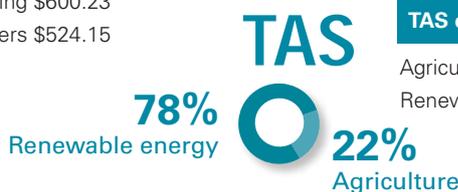


Total completed deals by state and industry 2006-2012



SA completed deals (value, USD million)

Mining \$600.23
Others \$524.15



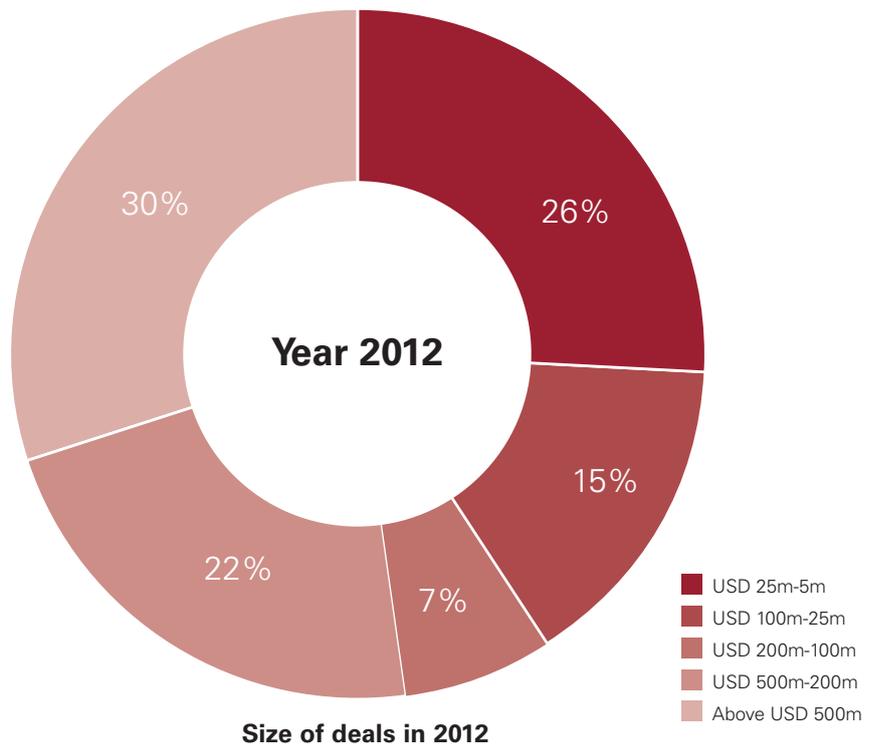
TAS completed deals (value, USD million)

Agriculture \$50.66
Renewable energy \$182.60

Chinese investment in Australia by deal size

Chinese investment in Australia by deal size

In 2012, the average size of the completed deals in Australia remained large compared with those of other countries. Over 50 percent of the number of all completed deals had a transaction value over USD200 million. The 30 percent ratio of mega investments (over USD500 million) was relatively higher in 2012 than historical averages between 2006-2012 (19 percent), while the mid-size deals (USD25-100 million) were relatively far fewer (15 percent) than normal (27 percent).



Chinese deals in Australia by ownership

Perhaps most interestingly, we noticed a relatively larger volume of investments by privately owned Chinese companies in 2012 (26 percent of total), with State-Owned Enterprise (SOE) investment reduced to 74 percent by number of deals, and 87 percent by value.

As predicted in our earlier reports, we are starting to see the next wave of Chinese investment in Australia is being made by privately owned companies.

In view of the large size of deals in Australia, the dominance of SOEs is likely to continue as these companies dominate the energy, mining and infrastructure sectors at home in China and have strong central government support to invest abroad.

2012 deals by ownership

Ownership	Investment Value (USD million)	%	no. deals	%
SOE	9,927.04	87%	20	74%
Private	1,456.42	13%	7	26%
Total	11,383.46	100%	27	100%

We are starting to see the next wave of Chinese investment in Australia is being made by privately owned companies.



China domestic outlook

Fundamentals remain strong in China's economic outlook which should underwrite ongoing demand for Australian natural resources.

We believe that China's economy bottomed out in the third quarter of 2012, has now stabilised, and is showing a positive trend and on target to meet 8 percent GDP growth in 2013. Considering the growth in the scale of China's economy in the past decade, achieving this growth rate is impressive.

The fundamental macros for the Chinese economy are encouraging – its urbanisation rate at 52 percent still significantly lags developed economies, net trade figures are steadily improving, the PMI index is stable and inflation appears under control. The structural shift towards a domestic consumption driven

growth is underway and spending patterns by the large and rapidly growing wealthy and middle class population underwrite the long term repositioning away from fixed asset investment driven growth. Industrial manufacturing remains a key GDP driver.

The prospect for further growth in China's service sector and the expanding private sector are promising. Meanwhile, accumulated foreign reserves and macroeconomic policies provide strong safeguards against major economic risks.

Political transition to the new leadership team takes effect this month. The incoming President,

Premier and members of the Politburo Standing Committee are widely regarded as highly experienced, pro-economic growth advocates, yet they are highly focused on China's domestic social agenda. The majority of these senior leaders are well known in Australian political and business circles.

Recent comments by outgoing Premier Wen Jiabao indicate China's economy still faces a number of challenges, including balancing environmental and social stability with economic growth and global economic integration.

Australia-China trade outlook

Our annual trade volume with China now exceeds AUD120 billion.

China is our number one trade partner, but China is also the number one trade partner of over 100 other countries.

Australia remains a stable and reliable supplier of high quality, high volume natural resources: iron ore, copper, coal, gas which are needed as China's urbanisation trend continues and the slow transition to cleaner energy takes place.

The opportunities for Australia to supply safe, high quality food and agricultural products (dairy, meat, grains, wine, cotton, wool etc) are plentiful. Australia utilises only 40-50 percent of domestic food production capacity and we should make every effort to ensure that we are the preferred supplier for China for the long term.

The Australian tourism market is now benefitting hugely from the 600,000+ Chinese tourists coming

to our country every year, representing AUD4.2 billion in revenue

The new Significant Investor Visa announced in late 2012 has already attracted over 200 applications for the AUD5 million investment class visas and this should benefit Australia's funds management, real estate, education sectors and broader economy. Chinese migrant applicants represent a large proportion of this group.

Australia-China investment outlook

Chinese investment in Australia is not simply one-dimensional resource-seeking and off-take oriented. It includes technology seeking and technology deploying strategies and access to domestic Australian markets.

Australia needs to create commercial frameworks that helps diversify co-operation between Australian and Chinese partners and expand their joint ventures into other global markets, including China.

Australia's traditional advantages in natural resource endowments, stable and reliable institutional systems and low sovereign risk are strong in competition with developing countries as suppliers of resources and energy, but count for less when competing with the USA and Canada.

We expect continued strong Chinese investment in LNG, minerals and renewable energy. We are encouraged by Chinese investment diversification trends in Australia and in particular expect significantly more investment in the food and real estate sectors in 2013.

Food security has emerged as a key theme for China in the past twelve months, but it extends well

beyond importing raw commodities and acquiring Australian farming land. To ensure high quality and safety standards are maintained for premium product branding back in China, more Chinese investors are interested in acquiring or developing food processing facilities in Australia which could help increase the onshore value add, creating employment opportunities for Australians and Chinese together.

Chinese have long believed in real estate as a core investment category and we are seeing more activity in the commercial, residential, retail and hospitality sectors in key Australian cities and tourism destinations. This creates vast opportunities for Australian financial services, construction, and design and architecture companies to jointly deliver new landmark real estate projects.

Australian energy-related infrastructure and civil infrastructure present large scale portfolio investment opportunities for Chinese corporate and financial investors. However, this requires joint Australian/Chinese co-operation to win and successfully deliver major infrastructure projects. For example, we need to see Chinese engineering, procurement, construction and management (EPCM) operations and financial services companies teaming up with reputable, trusted and experienced Australian partners.



 **Australia urgently needs to build a
China-capable workforce from board
level through to university graduates...**



Our competitive future

Australia needs to develop new and creative competitive strategies to maintain its position as a preferred investment partner for China.

Perhaps more importantly, we need specific commitment to action and follow through by government and corporate Australia.

This requires the joint, long term commitment of Australian and Chinese governments, educational institutions, the corporate sector and general public.

All stakeholders must work together to address the broader challenges around Australia's operating cost environment, workplace productivity and perception and policy issues such as public attitudes towards Chinese investors in Australia.

Australia urgently needs to build an China-capable workforce from board level through to university graduates and should look to promote educational exchange programs, cultural diversity employment programs, leverage off the large pool of existing Australian educated Chinese talent and better utilise experienced expatriate Australians currently working throughout Greater China.

We believe Australian and Chinese companies should work together to jointly compete for, win and successfully deliver desired financial objectives. Under this model Chinese companies will bring investment capital, secured off-take, technology and lower cost delivery models; while Australian partners bring local commercial and industry experience and business networks, strong local management and staff, regulatory understanding and local Australian investment capital.

Through aspirational frameworks such as the Federal Government's Australia in the Asian Century white paper and more balanced media coverage, we believe 2012 marked an important turning point in how Australia sees China. We remain confident that both countries are committed to pragmatic decision making and positive relationship building.

Appendix

A sample of completed deals – summary 2012

Chinese investor company	Australian company	State	Industry
Taurus Mineral Ltd – Guangdong Nuclear Power Group Co.	Extract Resources Ltd.	WA	Mining
PetroChina	Browse LNG project – Woodside Petroleum Ltd.	WA	LNG
Shandong Jining Ruyi Woolen Textile Co., Ltd	Cubbie Group Ltd.	QLD	Agriculture
State Grid Corporation	ElectraNet	SA	Grid
HNA Group	Office building	NSW	Real estate
Consortium of Chinese and South African entities	Rio Tinto	VIC	Mining
Guo Hua Energy Investment Co.	Musselroe wind farm – Hydro Tasmania	TAS	Renewable energy

A sample of deals – summary accumulated 2006-2012

Company name
Chinalco (Shinning Prospect Pte. Ltd)
Yanzhou Coal Mining Company (Yancoal Australia)
Yanzhou Coal Mining Company
Taurus
China National Offshore Oil Corporation Ltd
PetroChina Company Ltd
PetroChina Company Ltd
Sinopec Corp.
Minmetals Resource Ltd



Level of state ownership	Other owners	Managing owners	Listed	Australian company	Year	Equity	Comments
100%	0%	Chinalco (100% SASAC)	n.a.	Rio Tinto	2008 2009	9.3% 9.8%	
52.86%	47.14%	Yankuang Group (Shandong SASAC 100%)	HK, NY, Shanghai	Felix Resources	2009	100%	
52.86%	47.14%	Yankuang Group (Shandong SASAC 100%)	HK, NY, Shanghai	Gloucester Coal	2011	merger	Yancoal 78% stake, Gloucester 22% stake
100%	0%	Guangdong Nuclear Power Group (100% SASAC)	n.a.	Extract Resources Ltd. (EXT)	2012 2012	91.34% 100%	
64.43%	35.57%	China National Offshore Oil Corporation Group (100% SASAC)	HK, NY, Shanghai	BG Group - Queensland Curtis Island at Gladstone	2012	equity in QCLNG Train 1 and reserves and resources	
86.5%	13.5%	China National Petroleum Corp. (100% SASAC)	HK, NY, Shanghai	Arrow Energy	2010	100%	50% Shell joint venture
86.5%	13.5%	China National Petroleum Corp. (100% SASAC)	HK, NY, Shanghai	Woodside (WPL) Petroleum Ltd.'s proposed Browse LNG project in WA	2012	8.33 % in East Browse JV, 20% West Browse	
75.84%	19.35% + 4.81%	Sinopec Group (100% SASAC)	HK, NY, London, Shanghai	Australia Pacific LNG	2011 2012	15% 25%	
71.56%	28.44%	China Minmetals Corp. (100% SASAC)	HK	OZMinerals Ltd	2009 2010		



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