



China Foreign-funded M&A Research Report 2010

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Special Issue

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Research on Foreign-funded M&A on Chinese Market

With the acceleration of global economic integration, the deepening of our country's market economy and the gradual perfection of policies regarding the utilization of foreign capital in recent years, foreign enterprises have become increasingly active in taking over Chinese enterprise. According to statistics from Zero2IPO Research Center, a total of 181 foreign-funded/inbound M&A deals were closed on Chinese market between 2006 and Q1'10, and 115 of them disclosed a total value of US\$15.417B.

Utilization of foreign capital constitutes a vital part of the opening-up policy--a fundamental national policy of our country. The executive meeting of the State Council on December 30, 2009 made it clear to "encourage foreign capital to participate in the reform, regrouping, merger and restructuring of domestic enterprises, expand the financing channel for foreign-invested enterprises and guide financial institutions to increase support for foreign-invested enterprises." In order to improve the quality of foreign capital utilization and tap into its advantages in advancing scientific innovation, industrial upgrading and coordinated regional development, the State Council again unveiled *Several Opinions on Further Improving Work on Foreign Capital* on April 13, encouraging foreign capital to be involved in the reform, regrouping, merger and restructuring of domestic enterprises via equity participation or M&A. The gradual recovery of world economy and a string of favorable policies on foreign M&A have created new opportunities for foreign-funded/inbound M&As. This special research provides an analysis on the development course of foreign M&A on Chinese market, the evolution of relevant policies and regulations as well as foreign M&A activities and its development trend. A summary and projections are also included in an attempt to provide valuable reference and suggestion for foreign acquisitions of Chinese enterprises.

1.1 Development Course and Policy Environment for Foreign-funded/Inbound M&A

1.1.1 Introduction to Foreign-funded/Inbound M&A

The so-called foreign-funded/inbound M&A refers to a kind of behavior wherein a foreign investor obtains the controlling rights or operation rights to a domestic enterprise through merger or acquisition.

According to the *Interim Provisions on Acquisition of Domestic Enterprises by Foreign Investors*, foreign-funded/inbound M&A falls into two categories: asset M&A and equity M&A. In an asset M&A deal, a foreign-invested enterprise is set up and then enters into an agreement to buy and operate the assets of a domestic enterprise, or foreign investors enter into an agreement to buy the assets of a domestic enterprise and then operate the assets through setting up a foreign-invested enterprise with the acquired assets. In the case of equity M&A, foreign investors enter into an agreement to buy the equities of shareholders of non-foreign-invested domestic enterprises or inject capital to a domestic company and turn it into a foreign-invested enterprise. Equity M&A is relatively simple in operation and the pricing is easy.

1.1.2 Development Course

Foreign-funded/Inbound M&A was first seen in the 1990s on Chinese market, featuring constant improvement and inadequate maturity. Based on the characteristics of foreign-funded/inbound M&A in different times, we have divided its development course into several phases:

Phase 1: 1992-1995 – A Start from Scratch

In the early 1990s, foreign-funded/inbound M&A remained new in China and both the number of deals and value involved were relatively small, so this phase the market was still in the budding stage. In 1992, the third plenary session of the 14th CPC Central Committee adopted the *Decision on Several Problems Concerning the Establishment of Socialist Market Economy System*, preliminarily establishing the framework for socialist market economy. Followed was the reform of tax-sharing system and the establishment of some equity exchange market and the stock exchanges in Shenzhen and Shanghai, which combined to lay a foundation for mergers and acquisitions in real sense. Along with the development of domestic M&A market, foreign-funded/inbound M&A also emerged, though of a small scale. At that time, foreign-funded/inbound M&A was mostly achieved through taking over or reforming old State-owned enterprise via joint-venture holding or property rights purchase. Joint-venture holding was the major means to achieve an acquisition or merger due to its low cost and ability to take over large and medium-sized State-owned enterprises in China. 1992 saw the first foreign-funded acquisition of a State-owned enterprise – China Strategic Holdings Limited's takeover of Shanxi Taiyuan Rubber Plant. Subsequently, China Strategic Holdings Limited acquired hundreds of enterprises from different industries in Chinese mainland, arousing concern for foreign-funded/inbound M&A.

Phase 2: 1995-1998 – Supervision Strengthened; Bumpy Road for Foreign-funded/Inbound**M&A**

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