The China Analyst
中国分析家

A knowledge tool by The Beijing Axis for executives with a China agenda

March 2011

Doing Business in a Fast Changing China

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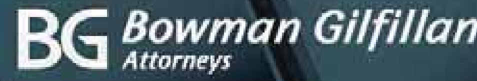

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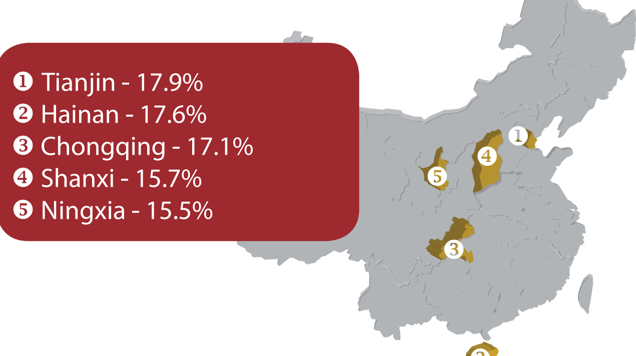
The Westward Shift of Growth in China*

Five Largest Provincial GDP, USD, Q3 2010

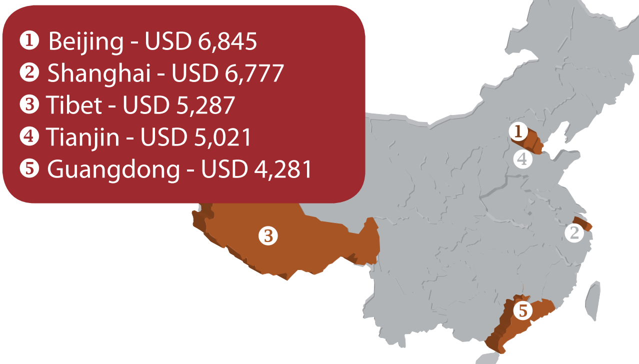
1. Guangdong - USD 473.6 bn
2. Jiangsu - USD 440.7 bn
3. Shandong - USD 424.3 bn
4. Zhejiang - USD 281.7 bn
5. Henan - USD 254.3 bn

Five Fastest Growing Provincial GDP, % y-o-y, Q3 2010



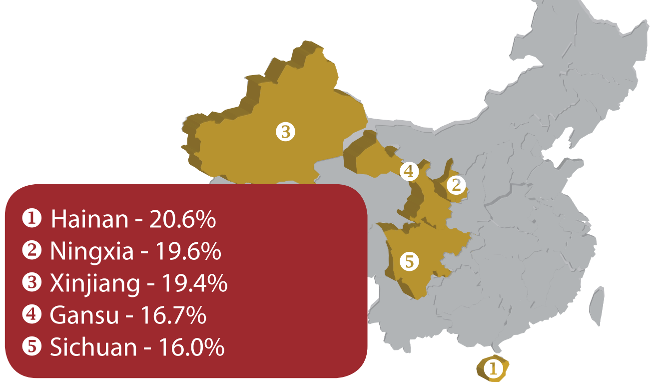
1. Tianjin - 17.9%
2. Hainan - 17.6%
3. Chongqing - 17.1%
4. Shanxi - 15.7%
5. Ningxia - 15.5%

Five Highest Provincial Average Urban Wages, USD, Q3 2010[1]



1. Beijing - USD 6,845
2. Shanghai - USD 6,777
3. Tibet - USD 5,287
4. Tianjin - USD 5,021
5. Guangdong - USD 4,281

Five Fastest Growing Provincial Average Urban Wages, % y-o-y, Q3 2010[2]

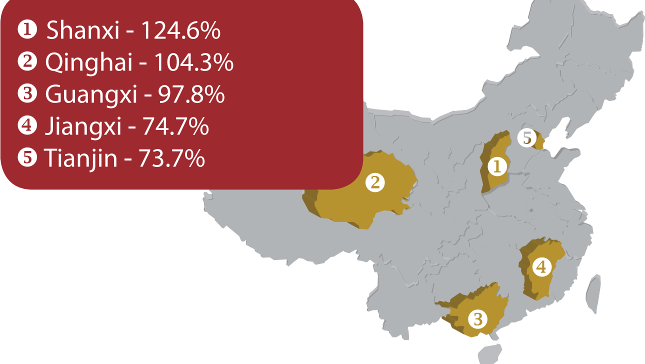


1. Hainan - 20.6%
2. Ningxia - 19.6%
3. Xinjiang - 19.4%
4. Gansu - 16.7%
5. Sichuan - 16.0%

Five Highest Provincial Total Profits of Industrial Enterprises, USD, Jan-Nov 2010

1. Shandong - USD 81.1 bn
2. Jiangsu - USD 71.1 bn
3. Guangdong - USD 55.9 bn
4. Henan - USD 41.3 bn
5. Zhejiang - USD 39.1 bn

Five Fastest Growing Provincial Total Profits of Industrial Enterprises, % y-o-y, Jan-Nov 2010

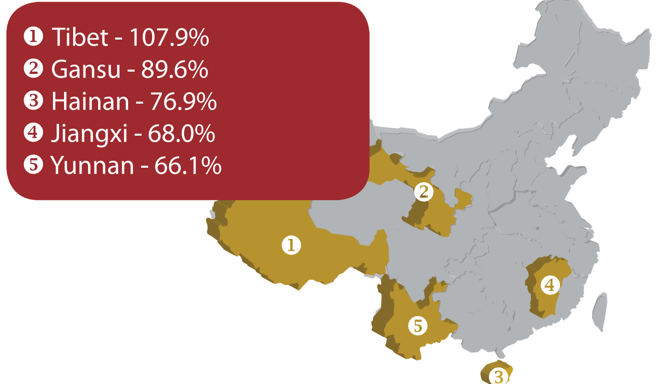


1. Shanxi - 124.6%
2. Qinghai - 104.3%
3. Guangxi - 97.8%
4. Jiangxi - 74.7%
5. Tianjin - 73.7%

Five Highest Total Provincial Foreign Trade, USD, 2010

1. Guangdong - USD 786.6 bn
2. Jiangsu - USD 465.7 bn
3. Shanghai - USD 368.8 bn
4. Beijing - USD 301.4 bn
5. Zhejiang - USD 253.4 bn

Five Fastest Growing Total Provincial Foreign Trade, USD, 2010



1. Tibet - 107.9%
2. Gansu - 89.6%
3. Hainan - 76.9%
4. Jiangxi - 68.0%
5. Yunnan - 66.1%

Source: China Monthly Economic Indicators (National Bureau of Statistics, China). * 'Provincial' here refers to all China's provinces, municipalities and special administrative regions, but excludes Hong Kong, Macao and Taiwan.
Notes: 1 - Refers to 'Average wages of employed persons in urban units'. 2 - Jiangsu is level in fifth place.

At the Highest Level

Current forecasts for the long term future of China's economy paint a stellar picture of how large and prosperous China is set to become, and in this edition of *The China Analyst* we look at how foreign firms can be a part of this future. Over the short to medium term, however, China still grapples with the economic challenges of a new chapter of its modernisation.

In 2010, The Beijing Axis celebrated eight years of providing China business solutions. During this time, we witnessed the transformation of China and its ongoing integration with the world. We have worked to understand and to engage the various opportunities for foreign businesses, and in this edition of *The China Analyst*, we have directly outlined some of our experiences in this regard.

In the features that follow we provide our insights on three key industries in China, namely construction, machinery, and clean coal technology. While there are substantial barriers to entry facing foreign firms in China's construction industry, there are opportunities for firms who are able to utilise advanced technology in areas such as power generation and transportation. There are also opportunities in partnering with Chinese firms in foreign markets, and the firms able to establish synergistic partnerships with Chinese entities in these markets will be able to reap the benefits. China's machinery industry has advanced in leaps and bounds in recent years, and our third feature discusses opportunities for foreign firms to export to and invest in this area in China. Our fourth feature discusses the latest developments in China's 'clean coal' revolution, another area where significant opportunities exist for foreign firms.

Yet if the future seems overly bright, over the short to medium term China faces a number of key challenges. With the very present danger of inflation and potential asset price bubbles, as well as the need to adjust the structure of the economy in order to increase the contribution of consumption to GDP, all current indications are pointing toward the need for slower and hence more sustainable growth in the coming years. Inflation and especially rising food prices is a pressing concern over the short term and has inspired three interest rate increases since October 2010, with more expected in the course of 2011.

Amid a still uncertain global economic outlook, a fundamental transformation is underway in China to reconfigure the economy to reflect a greater emphasis on domestic consumption. This is a complex and multi-faceted process that is impinging on virtually every aspect of Chinese society. It will witness the emergence of an immense middle class in China's urban areas, increasing imports and a decreasing trade surplus, and increased government expenditure on education, health care and pensions. All of this is, in short, a new chapter of China's modernisation, and it has various implications for the strategic approach foreign businesses will need to adopt in China now and in the future.

The need for such a strategic approach has never been greater, and in this first *The China Analyst* edition of 2011, we have turned our focus directly on the changing opportunities for foreign businesses in an evolving China.

I trust our readers will enjoy this edition of *The China Analyst*, and as always we welcome your feedback.

Kobus van der Wath
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China in 2030: Outlines of a Chinese Future

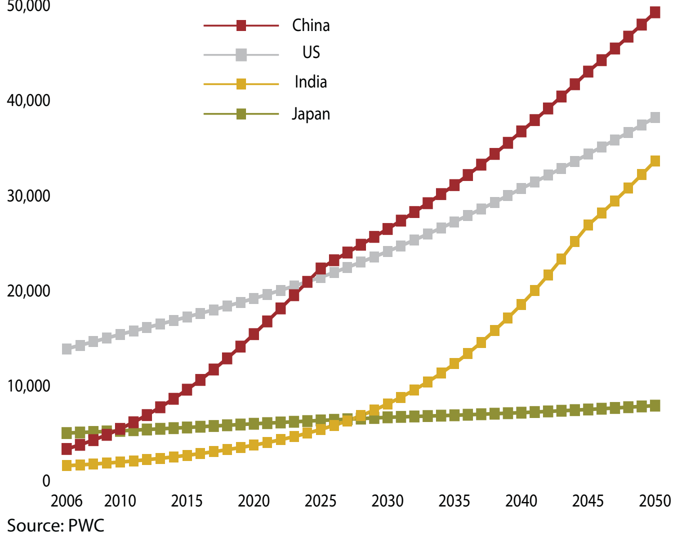
From current perspectives, China appears to have an awe-inspiring future ahead of it. In the next two decades, its economy is set to attain dimensions of size unparalleled in history, with a massive new, richer Chinese generation emerging in sprawling urban areas. If the future is going to be anything like current projections, China - unlike Japan - will fulfil enormous expectations. Yet even though the future rarely, if ever, turns out exactly as expected - China *is* different. *By Barry van Wyk*

The largest economy

The question is just when, not if. Yet this question - like all attempts to predict the future - is open to debate and constant revision. Depending on what is measured to make the projection, the answer ranges from imminently (within a handful of years) to the near horizon (within two decades). Using an estimation of purchasing power parity (PPP), the Conference Board, a global research association, have suggested that China's economy will surpass that of the US by as early as 2012. When it comes to actual size measured in simple dollar terms at market exchange rates, predictions for when China will eclipse the US stretch slightly further into the future.

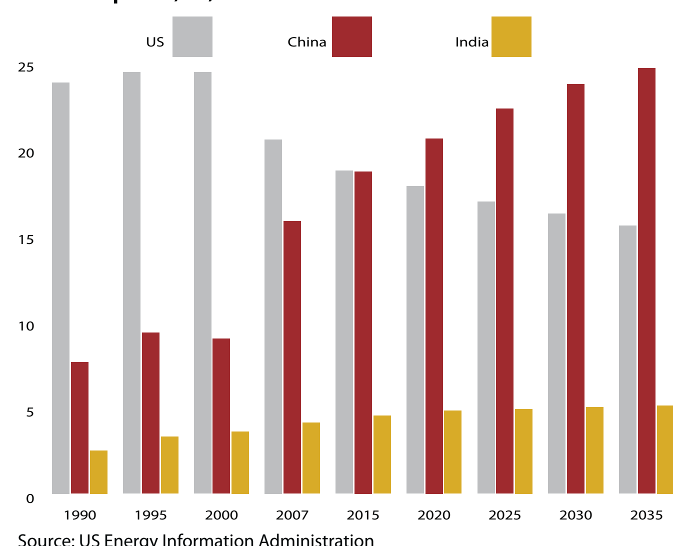
In 2003, Goldman Sachs estimated that China's economy would be the biggest by 2041. After five years in which the BRIC economies of Brazil, Russia, India and China all grew faster than Goldman Sachs had initially forecast, in 2009 the bank brought forward its prediction by 14 years to 2027. Accounting firm PricewaterhouseCoopers has put the date at 2025, and expects China's economy to grow to around 130% of the US economy by 2050 (see Chart 1), while Deutsche Bank and Standard Chartered have gone as early as 2020. Using its best guess of expected growth rates and inflation in both China and the US in the next decade and accounting for the expected appreciation of China's currency, *The Economist* newspaper expects China to surpass the US by 2019.

Chart 1: Forecast of Relative Size of Major Economies, GDP at Market Exchange Rates, Constant 2006 USD bn



Source: PWC

Chart 2: US, China, India Shares of World Energy Consumption, %, 1990-2035



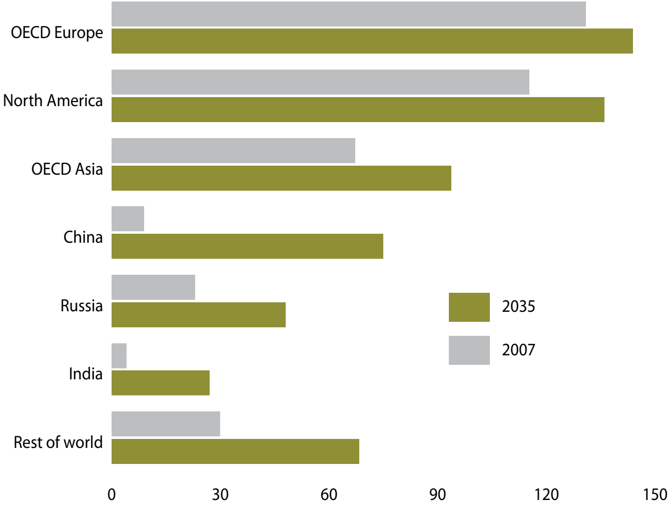
Source: US Energy Information Administration

The largest consumer of energy, including oil

In its *International Energy Outlook 2010*, the US Energy Information Administration (EIA) projected China's share of global energy consumption to increase from 15.76% in 2007 to 18% in 2015 (when it will draw level with the US), and will reach 23% in 2030, compared with the US' 16 (see Chart 2). Citing preliminary data in its *World Energy Outlook 2010*, the World Energy Agency (WEA) suggested that China had in fact already become the world's leading user of energy in 2009; its energy consumption in the period 2000-08 was more than four times greater than in the decade preceding that. Given that China's per capita consumption level stands at only one-third of the OECD average, its future prospects are immense, with the WEA projecting its energy consumption to increase by 75% to 2035 (constituting an increase in its global energy consumption share to 22% - slightly lower than the EIA projection of 24.62% for 2035 - from 17% currently). Electricity demand in China is expected to triple between 2008 and 2035; in the period of just 15 years from 2010 to 2025, China is projected to add generating capacity equivalent to the total current installed capacity of the US.

In its *Energy Outlook 2030* released in January 2011, oil and gas company BP expects China to surpass the US as the world's largest oil consumer by 2030, with its oil consumption reaching 17.5 Mb/d. By 2030, China's consumption of gas (43 Bcf/d) will be comparable to that of the entire

Chart 3: World Nuclear Generating Capacity by Region, gigawatts, 2007 and 2035



Source: US Energy Information Administration

European Union today, even though gas will constitute only 9% of China's total primary energy consumption (up from 4% currently). China's coal consumption is projected to increase only slightly from 47% of global consumption to 53% in 2030, by which time China's coal demand will level off. The EIA has also projected that China will add 66 gigawatts of nuclear capacity from 2007 to 2035, far in excess of any other country, compare for example India (expected to add 23 gigawatts), and Russia (expected to add 25 gigawatts) (see Chart 3).

A billion urban consumers

In the last decade, the individual wealth of China's citizens has increased significantly. In its *Global Wealth Report* published in Q3 2010, Credit Suisse reported that wealth per adult (defined as the added value of financial and non-financial assets owned by individuals, less their debts) in China tripled from USD 6,000 in 2000 to USD 18,000 in 2010, so that total household wealth in China is now the third-highest in the world, around 20% behind Japan in second place and 35% ahead of France in fourth.

In the coming decades, urbanisation will continue to be the main driver of the formation of a massive middle class in China's urban areas. In its report *Preparing for China's Urban Billion*, released in 2009, the McKinsey Global Institute (MGI) forecast that China's urban population will expand from 604 million in 2008 to 926 million in 2025, before topping a billion by 2030. By 2025, the distribution of disposable income in China's urban areas will have increased to such an extent that only around 10% of the projected 373 million urban households will have annual disposable incomes below USD 3,200. The largest income group will be just under 60% of urban households with annual disposable incomes ranging from USD 12,500 to USD 25,000 (see Chart 4).

Given the various ways of defining what exactly delineates the boundaries of the middle class, in her book on the subject, *The Chinese Dream*, Helen Wang defined the Chinese middle class as urban professionals in foreign companies, private businesses, or state enterprises, and government officials and entrepreneurs who have college degrees and annual incomes ranging from USD 10,000 to USD 60,000. Over three hundred million people, or about 25% of China's population, met these criteria in 2010. Based on an econometric forecasting model using data from the last 20 years, MGI has projected that the Chinese middle class (here defined as people with annual incomes, in terms of purchasing power, ranging from USD 13,500 to USD 53,900) will reach 612 million by 2025, or 40% of the entire population at that time.

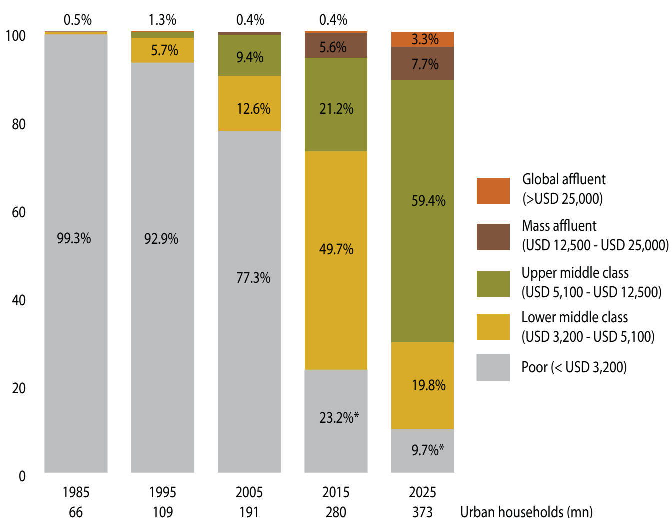
17 million automobiles and counting

As recently as the year 2005, only around five million vehicles were sold in China, compared to 17 million in the US. Yet in 2009 China became the world's leading auto market with 13.6 million vehicle sales, outstripping the 10.4 million sold in the US. In 2010, with 17.2 million vehicles sales, China raced ahead of the US, which registered only 11.5 million sales. What makes China's stellar growth all the more remarkable is that automobiles have penetrated only limited segments of the consumer market: in 2010, the ownership level for automobiles was only 12.7 units per 100 urban households, although this figure has more than doubled from 2007.

According to a 2010 forecast by JD Power Automotive Forecasting, by 2020 China will see almost 35 million vehicle sales, far in excess of the around 17 million sales in the US and around 7 million in India (see Chart 5). Some of China's auto manufacturers are even more optimistic than this. In January 2011, the president of Beijing Automotive Industry Holdings, China's fifth-largest auto manufacturer by sales, in January 2011 predicted that China's automobile market could triple in size to around 40 million by 2020, when it will account for around half of world production.

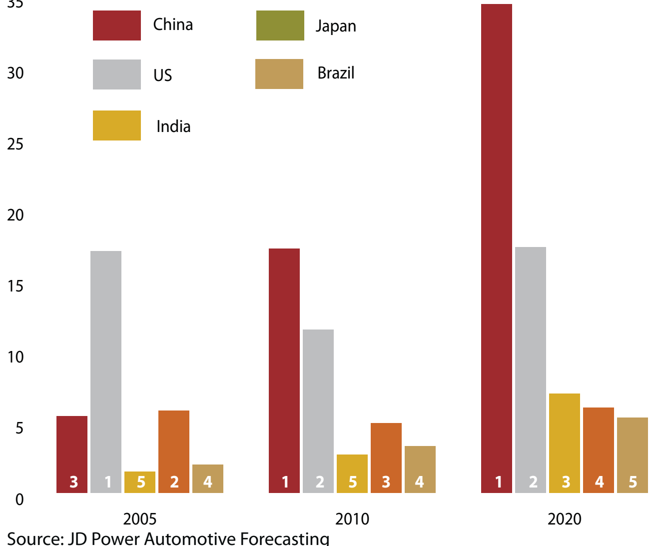
For some consumer goods like refrigerators (96.5 per 100 urban households) and washing machines (96.8), China is showing signs of saturation. Yet for a whole host of other

Chart 4: Chinese Urban Households Share of Annual Disposable Income, %, 1985-2025



Source: National Bureau of Statistics of China; McKinsey Global Institute Analysis; The Beijing Axis Analysis

Chart 5: Top Five Global Automotive Markets, Mn Vehicles Sold in 2005, 2010, and 2020



Source: JD Power Automotive Forecasting

products, prospects are still promising. At 70.5 units per 100 urban households, China's computer market still has good prospects, and the same is true for cameras (43.5), and hi-fi stereo systems (28.0). Mobile phone ownership increased from 3.3 units per 100 urban households in 1998 to 188.2 in 2010, meaning that multiple ownership in one household (on average 2.9 members) is still some distance away.

The phenomenal rise of China's middle class has led to a flood of new luxury store openings in the last few years. Beijing and Shanghai now have as many luxury point-of-sale locations per capita as New York and Chicago, and second tier cities like Shenyang and Harbin are not far behind. Based on the findings of a survey of Chinese consumer trends released in 2010, the Boston Consulting Group forecast that China is set to become the world's largest luxury market by around the year 2015, when it will account for 29% of global luxury product consumption. Research group CLSA Asia-Pacific Markets has forecast that China will become the world's largest luxury market a few years later, by approximately 2020. Interestingly, CLSA has found that - unlike any other luxury market - China's biggest buyers are men. Its not only Chinese retailers who are benefiting: increasingly numbers of high-end Chinese shoppers are heading overseas for luxury shopping sprees.

The busiest skies

By 2030, China is forecast to have taken the lead in air travel. According to the Federal Aviation Authority (FAA) in the US, 704 million domestic and international passengers travelled on US carriers in 2009. The FAA has forecast an increase of this number to 1.21 billion by 2030. The Civil Aviation Administration of China, on the other hand, has reported that 230 million passengers travelled on Chinese carriers in 2009, yet it projects this to increase to 1.5 billion by 2030, surpassing the US by around 300 million. In late 2010, US aircraft manufacturer Boeing forecast that China's airplane fleet will triple in size by 2030, and over the next 20 years China will need 4,330 new commercial airplanes valued at USD 480 billion.

The western frontier

While gaping at the broad outlines of China's spectacular future, it is apt to look westwards at China's vast interior. In the first thirty years of China's economic reform programme, the largest concentrations of wealth and income have occurred in the coastal areas, yet the coming decades will increasingly see vast new markets open up in China's interior, whose catch-up with the coastal areas could constitute decades more of growth and urbanisation potential. The pace of economic growth in the coastal provinces has already been eclipsed by other provinces like Inner Mongolia and Jilin in the north; Shaanxi in the west; Anhui and Hunan in the centre; and Chongqing and Guangxi in the south.

At the conclusion of the annual sessions of China's provincial legislatures in January 2011, the central and western provinces set growth targets of around 15%, planning to double their GDP in five years. More developed provinces like Beijing, Shanghai and Guangdong, on the other and, all declared growth targets of less than 9%. Retail sales growth is also the slowest in the coastal areas; the fastest retail sales growth is increasingly shifting towards second and third tier cities in provinces like Shandong, Jiangsu and Henan.

In 2010, The Economist Intelligence Unit released a report on China's 20 fastest-growing cities. The report pointed to 2007 as the birth of a 'new China' when for the first time in 30 years, inland China started to grow at a faster pace than coastal China. Unsurprisingly, the 20 fastest growing cities in China tend to be located in central provinces like Anhui and Henan with large rural populations fuelling urbanisation, and included rising mega-cities like Chongqing, Zhengzhou (in Hunan) and Wuhan (in Hubei). Also included are cities experiencing mining, construction or heavy industry investment booms in Inner Mongolia, Henan and the north-east. These fastest-growing central cities all share common features of rapid increases in population, income and infrastructure development.

Conclusion: China is different

Outlining China's likely trajectory in the coming decades suggests that China's growth is set to result in a new epoch in history. It is unavoidable to attribute China's economic success to the group of mostly engineers at the highest echelon of its government that have implemented economic policy and reform. Similarly, China's vast transformation over the last 30 years cannot but highlight the advantages of its peculiar system of government: too dominant for some, pragmatic and decisive for others; imperfect to be sure, but with a solid economic record. Nevertheless, whatever we may currently see in the future, it never quite turns out exactly like one expects. China's journey remains an amazing and unique story, yet the only thing we can say now for sure is that it is still incomplete.

Barry van Wyk, Senior Consultant
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China's Construction Industry: Strategic Options for Foreign Players

Within the next decade, China's construction industry will account for nearly one-fifth of all global construction output. Although entering the Chinese market presents challenges to potential foreign entrants, opportunities exist for those with high-tech capabilities and for those willing to look beyond China's borders to take on projects in the emerging economies of Asia and Africa. By *William Dey-Chao*

China's construction industry has been a driving force behind the nation's economic growth ever since it was targeted during the reform period of the 1980s as one of the cornerstones of China's plan for modernisation. After nearly three decades, construction activity in China continues to boom (see chart to the right), with the industry's output currently representing 24% (USD 1.4 trillion) of China's GDP.

China's sustained demand for residential, industrial and infrastructural expansion has generated the need for a multitude of new construction projects. The number of Chinese households grew by 9% from 2005 to reach 420 million in 2010, corresponding with population growth and less extended family living units. Industrial output has also expanded dramatically, and infrastructure needs have multiplied. Other drivers such as rising real per capita incomes, greater urbanisation and more investment in fixed assets have propelled China's construction market to its current place as the world's second-largest, accounting for nearly 14% of the global market (see table below). By 2020 China's construction industry is expected to obtain the top spot at 19% of global construction output.

Entry barriers

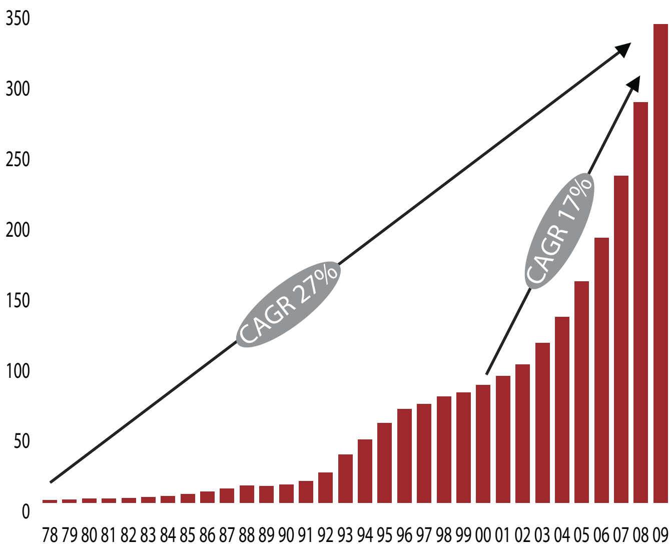
The challenge then for foreign construction firms is how to access this booming market. Although China's economy has become increasingly open, the construction industry remains relatively protected, with most construction activity

Top 10 Construction Markets in 2009 and 2020

Country	Market Size in 2009 (USD bn)	World Market Share in 2009	Predicted Top 10 in 2020
US	1,132	17.4%	China
China	1,034	13.7%	US
Japan	592	7.9%	India
Germany	303	4%	Japan
Spain	292	3.9%	South Korea
France	270	3.6%	Germany
Italy	262	3.5%	Spain
S. Korea	248	3.3%	Russia
India	247	3.3%	UK
UK	243	3.2%	Canada

Source: Global Construction 2020 Report

China Construction Industry Output, USD bn, 1978-2009

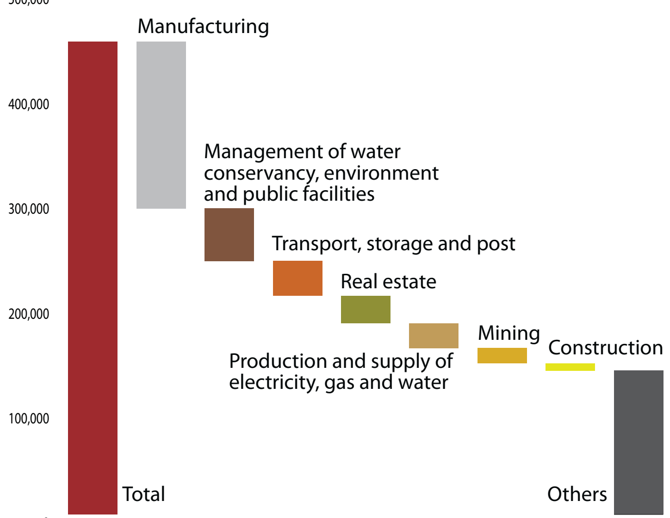


Source: China Statistical Yearbook 2010

undertaken by state-owned enterprises. As many as 9,000 state-owned enterprises are involved in Chinese construction, yet only 400 foreign-invested firms have registered activity in China. Foreign firms are only allowed to perform construction projects financed by international organisations such as the World Bank, the Asian Development Bank and by foreign governments, or those projects which are wholly financed by foreign companies. In addition, the government does not allow foreign-owned enterprises to undertake design, construction or consultation independently within China. To participate in projects that are subsidised by the Chinese government or by domestic banks, foreign firms are required to form joint ventures or corporations with domestic firms.

A case in point of the challenges faced by foreign construction firms is China's housing sector. There is certainly a lot of potential here. As of 2009, around 620 million people, or 46% of China's population, lived in cities. Some estimates anticipate that by 2020 the urban population will rise to nearly 50% of China's total population, and that by 2050 the percentage will rise further to 75%—a level comparable to that of developed economies. Accommodating this demographic shift will require even further expansion of China's already enormous cities, with equally impressive infrastructural upgrades necessary to facilitate the massive movements of people and goods that are to follow. However, due to the support of China's government for domestic companies, as well as

China Projects Under Construction, Unit, 2009



Source: China Statistical Yearbook 2010; The Beijing Axis Analysis

the general inability of foreign players to compete in terms of cost, foreign companies remain at the fringes of China's housing construction. The greatest potential for international companies lies in energy conservation, environmentally friendly building techniques and in the adaptation of modern materials—primarily in a consultant-type role.

Niche industries

Nonetheless, according to China's National Bureau of Statistics, there are around 400 foreign-invested joint ventures in China. These companies targeted China's civil and heavy engineering sectors. By partnering with domestic players, international companies have entered the Chinese market leveraging their intellectual property and value-added services—competencies which Chinese firms have not yet fully developed. Foreign companies have achieved the best results in providing some of China's power generation, transportation, water distribution and industrial needs.

Power generation has been an area of relatively heavy involvement by foreign players. China has doubled its power output in the last decade. Yet with per capita electricity consumption levels still well below that of developed nations, the coming decade will likely see further increases to China's power output. Such expansion requires the expertise of foreign construction firms, as do plans to diversify away from coal-dominated power generation by means of nuclear and renewable energy sources, areas in which foreign firms are more experienced.

An early example of international involvement in China's power generation was the work of Hochtief, a German company, which completed a 154-metre high rockfill dam near the city of Luoyang with a volume of 50 million cubic metres. The project was part of a larger commission from the Yellow River Water and Hydroelectric Power Development Co., and was completed in 2001. A more recent example is US-based First Solar, which announced a partnership with China Guangdong Nuclear Solar Energy Development Co. to build one of the world's largest solar power plants in Inner Mongolia in northern China. The plan is to install 2 GW of power generation capacity—the equivalent of two coal-fired plants—by covering 64 square km with solar cells to be built in stages through 2020.

Transportation is another promising area for foreign firms in China, particularly railway construction. Projects set forth in China's 11th Five Year Plan (2006-2010), which allocated USD 183 billion for railroad infrastructure, are still ongoing. This massive allocation of funds contributed less than half to the USD 441 billion worth of spending dedicated to railways in the five years up to 2010, all part of the government's goal to complete 90,000 km of operational railway track. The 12th Five Year Plan for 2011-2015 has allocated even more funding. This initiative has earmarked about RMB 3.5 trillion (USD 526 billion) for further railway construction, of which investment in urban rail transit is expected to surpass RMB 700 billion (USD 108 billion). According to China's Ministry of Railways, future railway construction will focus on the refurbishment of old railways and on the building of high speed rail lines.

It is this shift in focus to high speed rail that provides the greatest opportunities for foreign companies. In 2009 it was estimated that foreign companies were awarded around USD 10 billion worth of contracts related to China's high speed rail system. Canada-based Bombardier Inc., one of the world's largest rail equipment manufacturers, is one such company set to profit from this trend. In 2010 it was awarded a contract valued at USD 761 million to provide 40 high speed trains as well as signalling systems. The company operates in China through a joint venture, Bombardier Sifang (Qingdao) Transportation, and will be a key beneficiary of the 27,500 km in new high speed track planned by the Chinese government.

Then there is water distribution. Here, the Chinese government has earmarked USD 303 billion for water infrastructure projects over the next five years to secure access to safe drinking water for millions of rural residents. Urban areas too will benefit. USD 3 billion will be spent in 2011 on Beijing alone for water projects to sure up the city's water supply. A foreign player who is looking to act on water distribution opportunities in China is Suez Environment SA of France, Europe's second-largest water utility, which announced in 2010 that it was looking at expanding its operations in China through joint ventures. Opportunities exist in China's water distribution for companies willing to invest in concession-type structures, particularly in build, operate and transfer (BOT) projects. Opportunities also exist for international equipment providers to meet China's increasing water quality requirements via sales of high technology equipment.

New technology

As China's economy advances it is adopting new technologies in which foreign companies have been the forerunners, and hence have the ability to profit by conferring their knowledge to nascent Chinese industries. Bechtel of the US is one firm that has done just that. It has participated in various

Chinese projects over the years, including as a management contractor during the construction of 11 chemical plants. One was a major petrochemical project, an 800,000-ton-per-year naphtha cracker together with downstream plants, utilities, and infrastructure that was completed in 2005.

Siemens AG, a German company, also serves as an example in how to target emerging industries in China. The company is expected to finalise an agreement to supply charging infrastructure for electric vehicles to a still undisclosed Chinese city. The deal would see the engineering company install charging points for electric vehicles throughout the city as well as expansions to various green technologies throughout China such as wind farms, medical equipment and high-speed trains. The projects underway by Siemens AG symbolise the future of foreign involvement in Chinese building activity—it will be a shift away from the basics to technology intensive processes involving clean energy, environmental protection, technical controls and automation processes for machinery, logistics, and project management services to elevate China to the next level in its economic development.

Thinking beyond borders

Ultimately, when attempting to access China's construction prowess, foreign companies would miss many opportunities by narrowly focusing on China's domestic market. The real opportunities for partnering with Chinese construction companies are in developing markets, where Chinese players are expanding their presence. Chinese builders are not just expanding the infrastructure and housing blocks of their own cities but are some of the top international contractors in the developing economies of Asia and, even more so, Africa. Truly forward-looking international construction firms are now harnessing this trend for their benefit.

The Korean major Hyundai E&C has plans to do just that. It is currently considering opening several branch offices in China, and its CEO recently visited the country to forge closer relationships with Chinese builders and equipment suppliers. Hyundai E&C's Chinese branches, expected to open sometime in 2011, will seek cooperation with Chinese development companies and EPC contractors specialised in the development of oil, gas and renewable energies and in technology-intensive civil works. Through this heightened Chinese presence, the company also hopes to join forces with Chinese companies for projects in Africa, the CIS and in Latin America. Although China's government has impeded foreign companies from openly engaging in China's construction market, these restrictions stop at the Chinese border. Perhaps the best opportunities exist for foreign firms which incorporate China into broader, global-oriented strategies.

Building a synergistic relationship

Once an international company has determined that accessing the potential of China's construction industry is an essential component of its forward-looking strategy, the challenge of engagement then remains. A few critical success factors must be heeded in order to ensure successful execution both within China and abroad, and I include a few of them below.

Locate the right partner – In order to succeed in China's construction market, given domestic regulatory constraints, it is imperative that foreign companies establish a good relationship with the appropriate Chinese partner. Access to capital, political influence, and operational capabilities are aspects to consider when identifying potential partners. Although most of the Tier 1 players (Major state-owned enterprises) will be difficult to approach given their size and influence, Tier 2 (medium-sized provincial and semi-public companies) and Tier 3 (smaller private companies) are more readily approachable and to find synergies with.

Leverage core competencies – Foreign companies should utilise their core competencies in order to create synergies with Chinese companies (from Tiers 2 and 3) that will enable them to create value and directly compete with Tier 1 companies.

Employ a diversified China strategy – Incorporating strategic sourcing from China into the mix will allow foreign players to become more competitive global entities able to leverage China's status as a low cost country. In this way they will be able to utilise the partnership to engage reliable suppliers to obtain a competitive advantage through low cost sourcing.

Conclusion

For foreign construction companies, profiting from China's ongoing construction boom is essentially a question of partnership. There are distinct (and profitable) roles for foreign firms to play in specific niche industries in China, namely power generation, high speed rail, and water distribution, as I have outlined above. Various foreign firms have fulfilled such roles in China in the past, and more will do so in the future. Yet not only in China, but also in emerging markets in Asia and Africa where Chinese companies are so active, crafting the right partnership with the appropriate synergies with Chinese firms is the underlying challenge for foreign construction firms.

All the while, China's construction industry and those of other emerging markets are changing rapidly. The success of today's international companies relies on their ability to adapt to this phenomenon and the ability to craft new collaborative models to ensure success in the years to come.

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Gearing Up: Engaging China's Globalising Machinery Industry

The scale of China's manufacturing capacity and its domestic market for machinery are remaking the industry's international landscape. China's dynamism presents opportunities for foreign machinery makers as an export and investment destination, as well as an up-and-coming source of capital. *By Charles Avery*

Tucked away in the northeastern section of Beijing just outside the Fourth Ring Road stands what was once the pinnacle of Chinese industry. The Dashanzi factory complex, as it was called at its inauguration in 1957, saw the light of day with the assistance of Chinas's erstwhile communist allies: Soviet engineering and machinery imported from East Germany. In the early days of the People's Republic of China, the nation was heavily dependent on foreign technology, and its capacity to produce its own modern machinery desperately lagged behind the great economic powers of the day.

A lot has changed in the last fifty years. The manufacturers of Dashanzi have left and artists have moved in. The smokestacks and austere facades of yesteryear's fledgling manufacturing capacity contrast with the vibrant artwork within to create a surreal setting in what is now called the 798 Art District. China's machinery industry has progressed and moved on to more modern facilities elsewhere. Technology from the now non-existent Soviet Union and East Germany remain only as inspiration for oiled canvases. China has itself risen to become the world's largest machinery producer and the global industry's most dyamic player. It is the industry's most dynamic player with the greatest potential to impact coming generations. Now, just as travellers come to gaze at the paintings and sculptures of the 798 Art District, the whole world is taking a closer look at China's machinery industry to assess the repercussions of its rise.

According to the China Machinery Industry Federation, China's machinery output was valued at nearly USD 1.6 trillion in 2009, a four-fold increase from just a decade ago and now the highest machinery output in the world. The reach of this production is global, with around a quarter of Chinese-made machinery bound for export, constituting one of China's fastest growing export categories behind only electronics in terms of value. China's surge in internationally traded machinery occurred only recently, as until as late as 2003 it was a actually still a net importer of such goods. Since then its trade balance has shifted overwhelmingly toward exports. China finally surpassed Germany in 2007 to become the world's leading machinery exporter, and as of 2009, over 16%—or USD 243 billion— of the world's traded machinery was produced in China. A combination of low labour costs, a range of government incentives and the knowledge and technology imparted by foreign investment have made this rise possible.

China Net Machinery Exports, USD bn, 2000-2009

160
130
100
70
40
10
-20
2000 2001 2002 2003 2004 2005 2006 2007 2008 2009

Source: UN Comtrade

A cut cheaper than the rest

For the manufacturing of machinery it is very hard to beat China in terms of cost. For example, in 2009 China was the largest exporter of wood-sawing machinery, distributing these goods abroad at an average FOB price of USD 92. This price was less than one-fifth that of the number two exporter, Italy, at USD 585, and was even far below Mexico's USD 247. Similarly, China was both the largest and one of the cheapest manufacturing locations for refrigerator compressors, its USD 48 per compressor beating Japan, the US and Thailand at USD 113, USD 204 and USD 62, respectively. China also leads the way for 50-250 cubic centimetre spark-ignition reciprocating engines with an average FOB price of USD 129. Compare this to the USD 450 of Italy and USD 713 of Japan.

China's main cost advantage is, of course, inexpensive labour. As a corollary of having the world's largest population, China also has the world's largest labour force. The machinery industry alone currently employs around 20 million people, and they are paid wages far lower that those paid in any other major machinery producing country. Much of the resulting cost savings are then transferred to international consumers via lower product prices for exports. Although wages in China have increased substantially in recent years, the average rate of USD 0.40 per hour in 2008 was well below the rates of the US, Japan and Germany, all with hourly wages above USD 20.

China Machinery Industry Federation's 12 Sector Classification

Grouping	No. of Major Enterprises
Automotive	3,000
Electrical Equipment	2,000
Heavy Duty and Mining Machinery	1,000
Petrochemicals and General Machinery	800
Agricultural Machinery	4,000
Construction Machinery	500
Internal Combustion Engines	1,100
Machine Tools	1,000
Instruments and Metres	2,000
General Machinery, Basic Components	800
Environmental Protection Machinery	2,000
Food Processing & Packaging	1,600
Total	19,800

Source: China Machinery Industry Federation

Not only are there millions of workers available to craft Chinese machinery, there are also increasing numbers of engineers to design them. Educational reforms implemented at the turn of the century greatly expanded the availability of university-level training. New engineering graduates expanded from 200,000 in 2000 to over 700,000 in 2010. These new minds have greatly contributed to China's success in machinery manufacturing and have helped to advance its industrial output upward on the value added chain.

The power of policy

China's government actively supports the development of its machinery industry through various means such as subsidies, VAT export rebates, reduced interest rates on loans and tax credits which enhance manufacturers' competitiveness abroad. Consider the case of Shandong Molong Petroleum Machinery Company Limited. In 2009, it reported USD 5.5 million (RMB 37.2 million) in government subsidies. This included a USD 4.4 million (RMB 30 million) grant from the local financial bureau in Shouguang City. An additional USD 1.2 million (RMB 8 million) was received in the form of VAT tax rebates, in line with the standard Chinese VAT rebate rate of 15 to 17%. Furthermore, Shandong Molong is subject to a concessionary income tax rate of 15%, rather than the standard 25% rate as it was classified as one of Shandong's 'New and High Technical Enterprises'. The company was given yet more incentives in 2009, with around USD 147,000 (RMB 1 million) deducted from the company's tax bill as a 50% reimbursement for research and development costs, and USD 4.4 million (RMB 30 million) was removed as a 40% tax credit on expenses for qualified plant and machinery. In total, these government policies effectively provided Shandong Molong with around USD 16.3 million (RMB 112 million) in subsidies.

While China's tax policy has fostered domestic players, nuances in legislation elsewhere have deterred some outsiders. Chinese tariffs on machinery have fallen substantially since China's accession to the World Trade Organisation in 2001, from 14.4% to around 6.5% in 2010, yet are still above those of most of the developing world.

Impact of foreign investment

The support shown by the Chinese government to domestic manufacturers has not deterred a wave of foreign investment, a force which has made the greatest impact on China's machinery industry. Through foreign investment, China's manufacturing capabilities have rapidly progressed to world class standards. International customers have brought stringent international standards, thus improving the quality of Chinese products. Higher quality standards have spread incrementally among Chinese manufacturers and to a wider range of products, providing yet further incentive for foreign manufacturers to directly invest in China in order to fully take advantage of the country's low costs.

Of all the countries classified as developing economies by the United Nations, China has consistently been the top recipient of foreign investment since 1990, and in 2009 was behind only the US in terms of received foreign funds. Nearly half of this amount was directed toward China's manufacturing sector. In 2010, foreign invested firms, mostly wholly foreign owned enterprises and equity joint ventures, accounted for 55% of China's exports. Technological spillovers have occurred as Chinese firms have imitated some of the finer points of their international predecessors—at times infringing on intellectual property rights—and through the mobility of human resources. Through such subtle transfers of knowledge, foreign direct investment has propelled the recent success of China's machinery makers.

Gearing up for China machinery industry

As China's machinery industry continues to progress, the question for the international manufacturer is how to react. A number of strategic options are available for international firms to integrate their businesses with China's machinery-making potential. Although China is the world's largest exporter of machinery, the opportunity still exists to export to and invest in certain products to China, particularly for innovative products using cutting-edge technology. It is often a matter of pride for Chinese manufacturers and a symbol of quality to have foreign-made capital equipment. When touring a Chinese factory the manager will often boast of possessing a German or American-made production line. The reputations conferred by the brand names of international companies still outweigh those of Chinese brands—Caterpillar is far more renowned than Henan Hongxing. Foreign firms are also noted for their after sales service, an area still relatively unemphasised by Chinese companies.

An international firm that has successfully targeted China's need for high-tech machinery is Rolls-Royce of the UK. In November 2010 the company landed a USD 1.2 billion deal to supply and service jet engines for China Eastern Airlines. This

is only the most recent of many sales made to the expanding fleets of Chinese carriers. Over 300 Rolls-Royce engines traverse Chinese airspace, including 17 supplied for helicopters. Rolls-Royce has heavily integrated its operations with China through investment. It has formed a joint venture, Xian Rolls-Royce Aerocomponents, with Xian Aero Engine Company to develop high-tech parts for its engines. Additionally, Rolls-Royce operates a training facility in Tianjin with China's Civil Aviation Administration to train technicians and engineers, and conducts a number of research programmes at Chinese universities to develop new talent in aero-engineering.

General Electric of the US has also successfully entered China's machinery industry through investment. The company has established 36 wholly owned enterprises and joint ventures in China which employ 14,000 people. In 2010 it announced plans to expand yet further in China by investing USD 2 billion in high-tech joint ventures with Chinese state-owned companies, as well as in new research and development facilities. Machinery from these new US-China cooperatives will target China's growing energy and infrastructure needs.

Direct investment is often the best way for international manufacturers to benefit from China's machinery industry. The encouraged status of foreign-initiated machinery investments generally means a less stringent approval process accompanied with tax benefits. Besides more advanced technology, foreign-invested firms in China have a number of competitive advantages. The efficiency—as measured by sales per employee—of foreign manufacturing ventures in China is often substantially above that of domestic privately-held ventures, which in turn tend to be more efficient than Chinese state-owned enterprises. Foreign-invested manufacturers also have greater access to international markets; a large quantity of China's machinery output is exported back to the countries where the foreign investment originated.

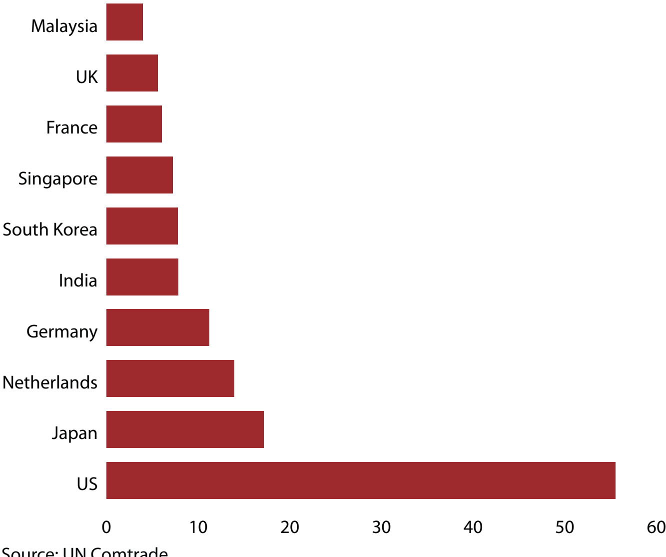
Rise of China Inc.

Despite the continued interest of international machinery companies in entering the Chinese market, the latest trend, still in its infancy, is one of Chinese companies going out. The continued success of Chinese firms in exporting their wares has given them the ability to take a more active approach in obtaining foreign technology and branding. This process began as early as 2004, just after China became a net machinery exporter.

In 2004, Shanghai Electric Corporation acquired a 75% interest in Japan's Ikegai, a manufacturer of lathes and machining centres, for USD 4.5 million. In 2005 Harbin Measuring Tool and Cutting Tool Group followed suit with a USD 12 million acquisition of Kelch GmbH, a German manufacturer of tools and pre-setting devices. Another German manufacturer, Grosse Webereimaschinen GmbH, was acquired in 2006 by Zhejiang Hongsheng Group for just over USD 5 million to expand the presence of its textile machinery abroad.

2006 also witnessed the expansion of two Chinese heavy equipment manufacturers into international markets, Sany

China's Leading Machinery Export Destinations, USD bn, 2009



Source: UN Comtrade

and Zoomlion, which represent the new archetype for China's outward development in machinery. Sany made its first big step abroad in 2006 by establishing a USD 60 million manufacturing facility near Mumbai, India. It then went on to set up a North American headquarters for construction machinery in the US in 2007, followed by a USD 130 million investment in Cologne, Germany, the location of a new factory and R&D centre. In 2010, the company expanded again, this time into Brazil via a USD 200 million manufacturing base, as well as with another Indian plant. Within the next few years Sany intends on creating a truly global footprint through further expansion into Indonesia, Russia and South Africa.

Zoomlion too has become an international force, yet through acquisitions rather than greenfield investment. In 2008 the company made an outright purchase of Italy's CIFA in a deal valued at USD 422 million. This more than doubled its overseas investment holdings, expanding its existing presence in the US, India and Brazil. Given the push abroad by companies such as Sany and Zoomlion, the greatest opportunities for international firms in unlocking China's potential may be through a globally-focused partnership, one with an eye not just on China but on emerging markets.

In time the names of Chinese manufacturers will likely be as ubiquitous as Caterpillar, Liebherr, or Komatsu. China continues to decrease its reliance on technology transfers from foreign investment and is honing its ability to compete directly with its international predecessors. The long term strategies of international firms must prepare for China as an equal. Once reliant on imported technology, China has rapidly progressed and will impart its own capabilities on today's developing nations. For the international machinery executive with some time to spare between meetings in China, its recommended to check out Beijing's 798 District, see the exhibits, and think not of the past, but the future.

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Clean Coal: China's Coming Revolution

Today, coal production in China provides more energy to the world's economy than the whole of Middle Eastern oil production.

—Nobuo Tanaka, Executive Director, International Energy Agency, *Cleaner Coal in China* report, 2009

You can think of China as a huge laboratory for deploying technology. [. . .] They can go from concept to deployment in half the time we can, sometimes a third. We have some advanced ideas. They have the capability to deploy it very quickly. That is where the partnership works.

—US government official, *The Atlantic*, December 2010

With the moderately successful conclusion of the Cancun round of multilateral global warming talks, the world has reiterated an agreement on the inevitability of dramatic climate change if significant counter-actions are not taken, and on the need to reduce emissions of greenhouse gases, especially CO_2, as one of the crucial mitigating actions. But clear mechanisms for emissions monitoring as well as clear reduction targets and funding arrangements are still outstanding, and these issues should still be high on policy makers' agenda. With the two largest emitters, the US and China, so reliant on coal for their energy supply, significant improvements in coal burning will have to be achieved if the world is to avoid further escalation of CO_2 concentration in the atmosphere.

In this article I will argue that China is very well positioned to promote the development, commercialisation and application of clean coal technologies both domestically and abroad. Foreign companies that will jump on this bandwagon early on could benefit tremendously by partnering with Chinese firms.

China has for the past 15 years paid increasing attention to the issues of environmental protection and resource utilisation. To minimise resource dependence, China has sought to work on both the domestic and international fronts: develop trade and investment relationships with new international suppliers of oil and coal while at home pushing for increased coal production, oil and gas field development, and major investment in renewables.

The escalating social costs of environmental degradation, combined with concern over global warming, the need to reduce dependence on commodity imports, and rising world commodity prices have motivated China's leadership to embrace policies that promote energy and resource efficiency, penalise polluters and encourage greener technologies, or any combination of these that ultimately promotes the continuing sustainability of China's economic growth from an environmental viewpoint. In addition, China's government is trying to steer the country's industrial development up the value chain: higher share of cutting-edge technology exports, higher share of services, and increasing utilisation of R&D and engineering human capital.

Old black magic: Coal is a big part of China's future, yet its a future of China as a global leader in clean coal technology (flickr / cindyt7070).

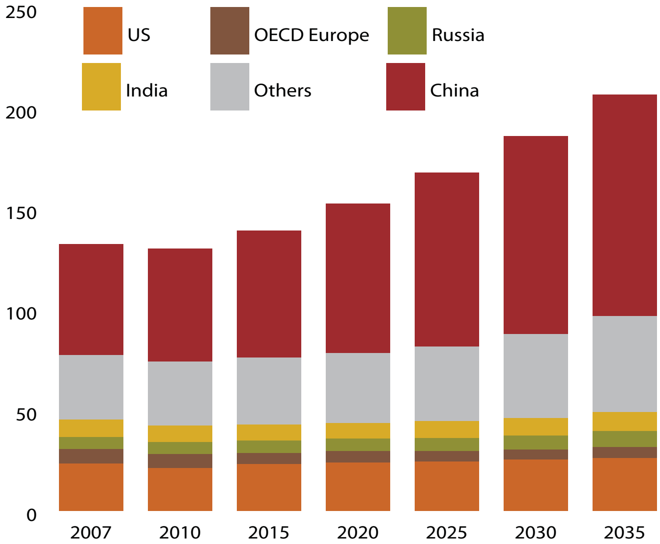
China is already a recognised leader in renewable energy such as solar, wind, hydro - both as equipment producer and as installed generation capacity. It is also making significant advances in the use of nuclear power. Of all the advanced technologies and investment areas that China has promoted in the 11th and 12th Five Year Plans and in its stimulus packages – renewables, high speed rail, electric vehicles, hydrogen fuel cells, nuclear power, etc. – 'clean coal' is perhaps the least talked about yet potentially the one with the highest economic and environmental impact.

Coal has a seminal place in China's economy. China generates around two-thirds of its electric energy from it, and in 2008 China produced 2.79 billion tons of coal (~43% of world

production). It is also the only fossil fuel China has in abundance, and the coal industry provides employment to around 5 million people. With a projected annual GDP growth rate 8-9% rate for the next 20-30 years, only coal can meet China's energy demand. No matter how fast new nuclear generation capacity is deployed (a targeted 5.3% of total installed capacity in 2020 vs. less than 1% in 2009), or how fast the energy efficiency of the economy increases (a 20% target reduction was achieved from 2010 to 2020), 2.6 times more coal will be consumed in China in 2035 compared to 2007, as projected by the US Energy Information Administration.

While coal will unquestionably be a big part of China's future, the adverse social impact of coal in the form of pollution (Linfen, according to the Blacksmith Institute, is the world's most polluted city and is located in Shanxi, China's foremost coal producing province), accidents and deaths due to coal mining, roads and railroads clogged by coal-transporting freight, and international pressure on the issue of climate change – all are pushing China towards revising its coal strategy.

World Coal Production by Region, Quadrillion Btu, 2007-2035



Source: US Energy Information Administration / International Energy Outlook 2010

Clean coal developments in China

China is very active in pursuing a host of clean coal technologies and initiatives, aiming at both mitigating the adverse effects of coal usage and at the same time advancing on the technology ladder and becoming a leading technology and engineering solutions provider in this space.

Below I summarise some of the most interesting recent developments in terms of 'clean coal' in China.

Inefficient capacity shutdown - As we have pointed out in previous issues of *The China Analyst*, the Chinese government has used this approach in a number of industries to shut down smaller producers in a number of industries such as coal and iron ore mining, steelmaking, chrome smelting, and others. The shutdowns typically affect older-technology, inefficient, high-polluting facilities and achieves a few different goals with one swipe: industry consolidation for more control and profitability, capacity management, and getting rid of typically the worst offenders in terms of pollution and mining accidents. An added benefit of these closures is reduced wastage of coal – small mines in China recover 15-20% of their coal reserves at best, while the larger ones are closer to international best practice of >50%.

Increasing proportion of washed coal - Nowadays, less than 30% of coal is washed in coal preparation plants (CPPs) in China. Given that washed coal is generally more profitable, burns better and generates less pollution, the trend is encouraged by the government. China boasted over 1,700 CPPs as of 2008, with an installed washing capacity of 1.4 billion tons, and it is in the process of constructing more. It is also the world's largest market for CPP equipment, creating a bonanza for domestic and foreign manufacturers.

Coal mine methane and coal bed methane - Chinese coal deposits are generally rich in methane. This is a safety concern as methane is the leading cause of accidents and deaths in mines, and an environmental concern since methane, a potent greenhouse gas, is released into the atmosphere during traditional mining. Yet this abundance of coal bed methane resources (China has the third-largest resources in the world with 37 trillion m^3) has already attracted foreign and domestic investors. It is considered a very attractive investment area due to a clear regulatory regime, and the high demand and price for natural gas. We consider it a 'clean coal' trend due to the drainage and usage of coal mine methane that would otherwise be released into the atmosphere, and because it has a lower CO_2 emissions profile than coal.

Coal-by-wire - A strategy of building more mine-mouth power plants in the coal-abundant central regions of China, and then transferring the produced electricity via efficient high-voltage lines (HVDC) to eastern and southern provinces has been on the agenda of Chinese policy makers for at least 15 years now as an alternative to 'coal-by-train'. The initiative has potential to decrease the environmental and economic costs of coal transportation, and is quickly gaining momentum. Over 100 GW of DC transmission capacity is planned in China by 2020, as part of a larger programme for interconnecting the six existing electricity grids and linking new traditional and renewable generation capacity to the national grid. Two major examples of such projects are the lines from coal-rich Ningxia province (2x4 GW, 2010) and Shaanxi via Shanxi (3 GW, 2011) to the populous and energy-poor Shandong province on the coast.

Advanced combustion technologies - Research into advanced burning technologies that allow for increased burning efficiency and significantly lower pollution from coal power generation have been high on the priority list of the Chinese government and state-owned companies. A number of projects utilizing circulating or pressurized fluidised bed combustion (CFBC and PFBC) and integrated gasification (IGCC) technologies have been or are being built. The leading

showcase project, led by Huaneng, and counting Peabody, Datang, Huadian and Shenhua as shareholders, is GreenGen, an IGCC plant that will also use Coal Capture and Storage (CCS). After some initial delays, the first 250 MW polygeneration (syngas, heat and electricity) plant will be online by the end of 2011, and the project will aim a total installed capacity of 650 MW by 2014. The projected is intended to serve as a testing bed and demonstration project for a host of 'clean coal' technologies that will hopefully inspire numerous follow-up projects in China and abroad.

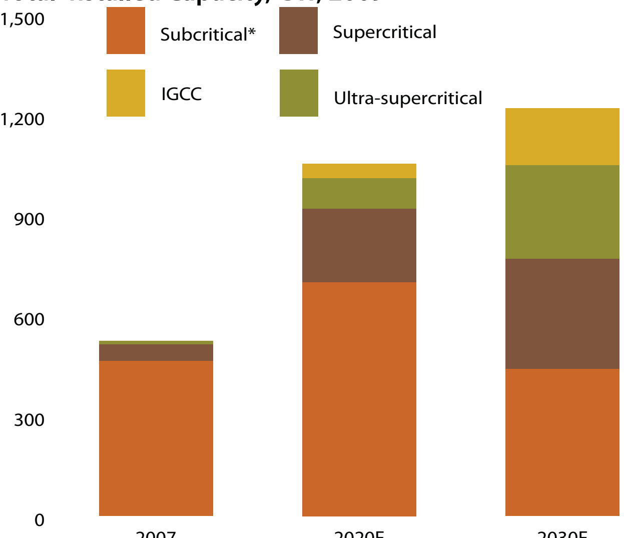
Underground coal gasification - China has been actively pursuing this old, complex, but potentially very rewarding technology since the 1980s. It would allow for safe (underground) production of syngas from marginal deposits, potentially providing cheap fuel to generate electricity or as feedstock for the chemical industry. China has over 15 projects underway, mostly in demonstration stage, and is the most active of all countries actively pursuing this area. So far, however, commercialisation has proven elusive.

Carbon capture and sequestration (CCS) - CCS is ultimately the only technology that can make coal burning 'green' – in the sense that it will allow for a dramatic reduction in CO_2 emissions and thus retard its climate change effects. China is endowed with significant CO_2 sources (chemical plants and power generation) near vast geological storage fields (China leads the world in the number and capacity of accessible saline formations, the most significant potential storage option for CO_2). While it has obvious benefits in the form of cleaner coal utilisation, the costs of CCS can be significant both in terms of up front investment in plant and equipment as well as coal utilisation efficiency. The technology is still in very early stages of deployment in China, and the Chinese industry and government are calling for more international assistance in this area in the form of technology transfer and financing support. Huaneng, Shenhua and the GreenGen project are all piloting the technology with both pulverised coal and IGCC plants, while PetroChina is exploring the potential of CSS in enhanced oil recovery projects for economic benefits and to gain green credentials.

Conclusion

China is busy with many 'clean coal' initiatives and a host of state-owned and private companies, research institutes and government departments are involved. In addition, foreign energy firms and equipment manufacturers, as well as NGOs are also playing a significant role. We already see increasing participation in these projects in China from foreign players such as Duke Energy or Peabody. Most projects are in fact not about discovering new technologies, but about practically deploying existing technologies on a commercial scale. China's advantage is that all the right ingredients are in place for its 'clean coal' revolution: government support and political will, cheap available capital (the government has recently earmarked RMB 5 trillion over the next five years for 'new energy' projects, including clean coal), plus domestic and international pressure to improve the environmental impact of coal. China has a history of experimentation with various policy options and successful infrastructure build-up via government policies, accessible financing and rapid deployment

Coal Fired Power Generation Technologies Used in China, Total Installed Capacity, GW, 2009



Source: *Cleaner Coal in China*, 2009; International Energy Agency / OECD
* Older technology, less efficient.

I do not doubt that China will lead the world in the sheer number of 'clean coal' projects deployment in the next couple of decades. We will see an increased number and sophistication of projects, as well as the emergence of Chinese companies among the leading global players for 'clean coal' equipment, technologies, and EPC project execution.

The question for other foreign companies, then, is: How to benefit from this trend? Who are the right Chinese partners? How will the cooperation unfold to benefit all partners?

The companies that answer these questions successfully will stand to benefit significantly in the future. Sitting at home and protecting one's own turf is no longer a viable option.

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Macroeconomic Monitor: China's Next Decade - More of the Same?

China finished off 2010 on a slightly higher note than expected with 9.8% GDP growth in Q4, but still achieved a much desired moderation and settled many of the earlier worries about possible overheating. As China enters a new decade, not only do we view it as highly capable of producing another ten years of strong economic growth, but we also ponder how far it can go in helping the developed world to overcome some of its problems. *By Kirill Riabtsev*

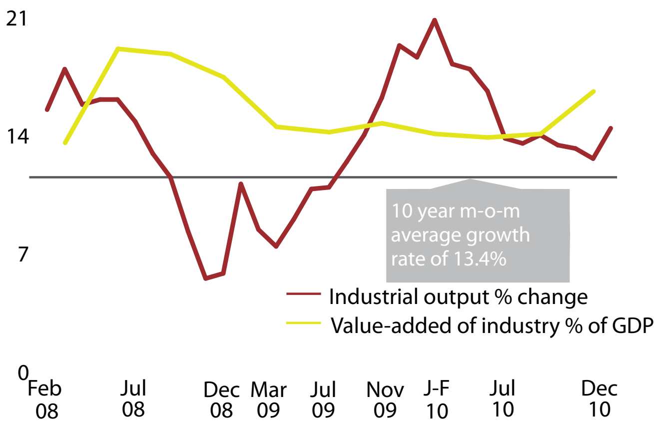
In Q3 and Q4 2010, China's economy cooled somewhat with growth declining to 9.6% in Q3 and 9.8% in Q4 from an 11.9% high in Q1 (see chart below, left). Slower growth was a necessary price to pay for economic stability – coordinated effort by the government helped wade off a growing real estate bubble and moderate bank lending, thus reducing the built-up excess capacity and preventing the formation of an inventory glut. Still, this managed regress gives China in excess of 10% annual growth in GDP for 2010.

As it closes the chapter on arguably one of the most phenomenal decades in its economic history, we can reasonably expect that China will continue along the positive development path for the next ten years. However, in order to sustain growth, it needs to maintain a delicate balance between central coordination and market principles, while gradually transforming itself from a net global producer to a major global consumer. The way it handled the global financial crisis of 2008, as well as the pressures of 2010, suggest that it is generally well positioned to do so, but must not overlook addressing some key structural obstacles.

Cooling but far from freezing

The slight cooling of China's economy in 2010 was led by a number of factors. Industrial production continued a steady decrease from the January peak of over 20%, reaching the

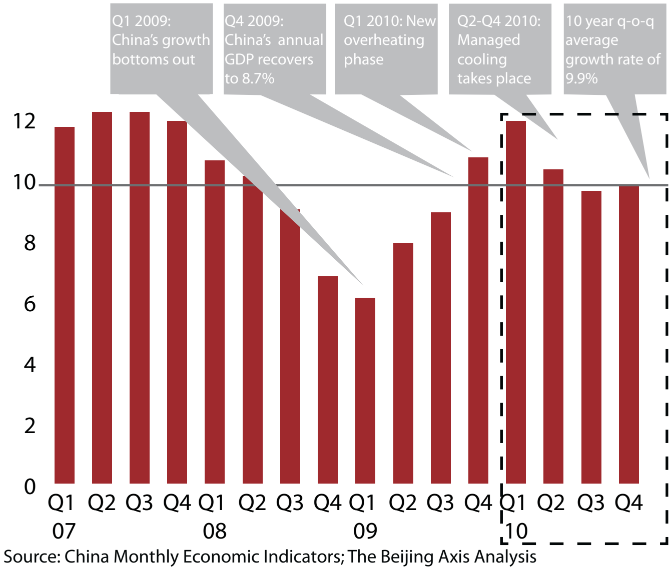
China Industrial Production, % y-o-y, Feb 2008-2010



Source: National Bureau of Statistics of China

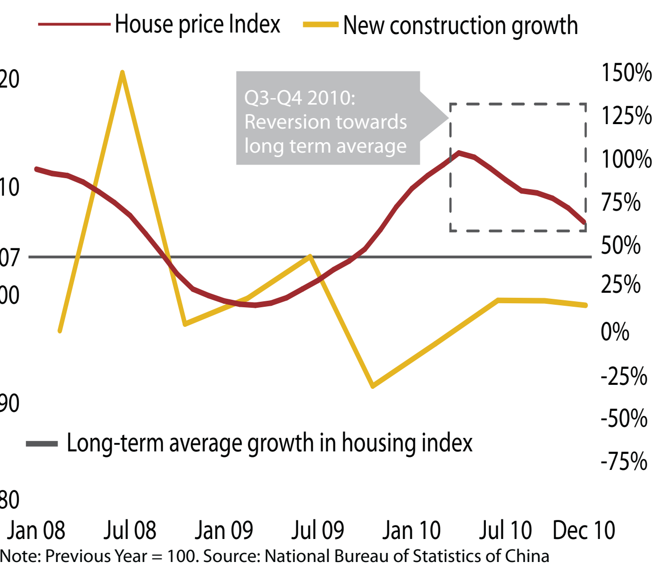
10-year average mark of 13.5% in Q3 and slightly below the mark of 13.3% in Q4. The average pace of decline has also slowed from -9% between Q1 and Q2 to under -3% between Q3 and Q4, pointing to a stabilisation around the 10-year average (See chart above). The same trend was observed in the value-added of industry (see chart above), which has shown a smaller ratio of around 13.5% per month for Q3, but rose to 15.7% in December to finish Q4 with an average of 14%, still lower by comparison with the 17% of H1 2010.

China Quarterly GDP Growth, % y-o-y, 2007-2010



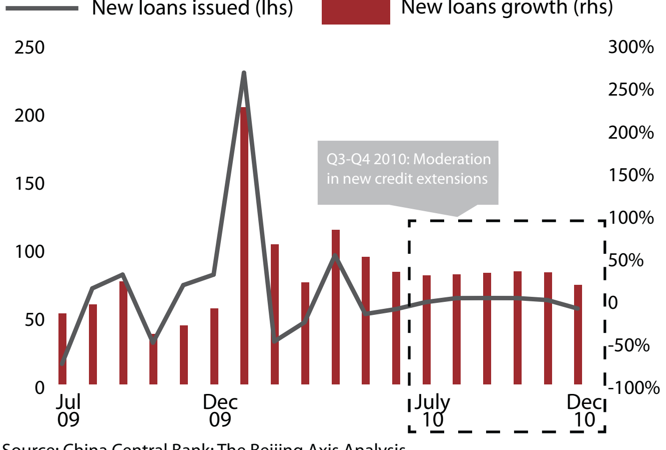
Source: China Monthly Economic Indicators; The Beijing Axis Analysis

China House Selling Price Index, % y-o-y, 2008-2010



Note: Previous Year = 100. Source: National Bureau of Statistics of China

China New Bank Loans, % m-o-m, USD bn, Q2 2009-2010



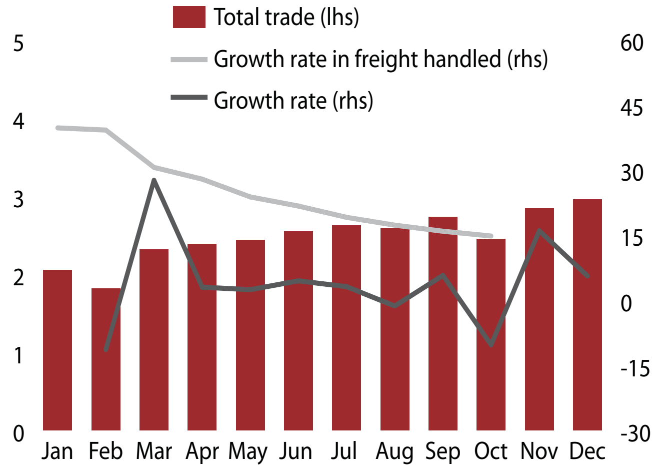
Source: China Central Bank; The Beijing Axis Analysis

Further moderation was also evident in the real estate sector (see chart below, right), with the housing price index shedding another 1.9% over Q3 and Q4, while the average monthly growth in new construction decreased to 18% for the same period from the 45% observed over Q1 and Q2. A slower pace of decline is also evident as for both series the average rate of change has been lower in Q3 and Q4 than at any time during the nine quarters before that.

In the banking sector the monthly growth rate in new loan issues was virtually flat over Q3 and Q4, following a drop of 10% per month for Q1 and Q2 (see chart above). The trend is also somewhat reflected in fixed asset investments (See chart to the right) for the same period which, although higher in absolute terms (USD 1.174 bn for Q3 and USD 1.387 bn for Q4), than for the first two quarters (USD 517 bn and USD 638 bn, respectively), have shown the slowest inter-periodic growth rate (25% on previous year) for the first time over the last 13 quarters. Fixed asset investment has, however, started to climb again in Q4.

Moderation is also evident in trade data (see chart below). Total trade by USD value remained fairly flat over Q3 and Q4 after a March spike, and total volumes of international freight handled at China's ports have been on a steady

China Monthly Total Trade, % y-o-y, USD bn, 2010



Source: China Monthly Economic Indicators; MOFCOM

decline month-on-month from the previous year. The trend could partly be attributed to the 2.6% appreciation of the Renminbi from Q3 – another necessary adjustment by the Chinese government following repeated international calls for the value of the currency to appreciate in order to better reflect the economic fundamentals of China.

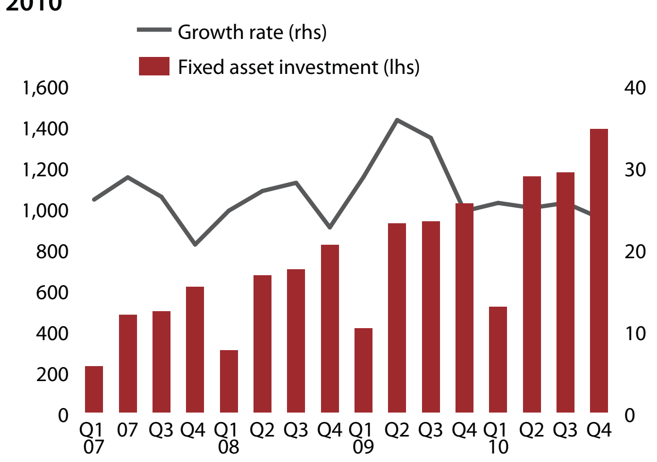
A welcome moderation

The cooling of China's economy is a necessary step, relieving much of the pressure inherent in breakneck economic growth. In the aftermath of the global financial crisis, a real investment bubble clearly emerged in China with too many infrastructure projects, excessive growth in the real estate market and a somewhat artificial stimulus of the banks and heavy industries, where the former were required to maintain lending to state-owned industrial enterprises while the latter would use the money to maintain fixed capital formation amid already high excess capacity.

As a result, a number of research agencies like RGE have estimated that China was ploughing as much as 50% of its GDP back into fixed assets at a time when developed economies were drastically cutting consumption and reducing inventories. Such levels of investment were perhaps more justifiable when the developed world – the main consumer of Chinese production – was enveloped in a binge of excessive consumption and China's factory floors were overheating in order to keep its seemingly insatiable foreign customers happy.

A sobering fact is that, now in the developed world austerity of one form or another is a daily reality. Stimulus packages may have prevented total collapse, but the economies are not yet reviving in a desirable manner. Europe is battling with the financial fallout of Greece and Ireland, with Portugal, Spain and Italy potentially next in line. There is already even a possibility - however distant - of a collapse of the single currency union itself. At the same time, the US is threatened with a deflationary trap, with a combination of massive direct liquidity injection and rock-bottom interest rates not resulting in much improvement in consumption and investment.

China Total Fixed Asset Investment, % y-o-y, USD bn, 2007-2010



Source: National Bureau of Statistics of China

In this new environment, increasing investment in new capital by a net supplier to the world like China is not only ineffective but also harmful, as it sets the scene for a hard fall in the future, when inventories adjust in response to falling consumption rates. Simply put, it makes no sense to expand the factory floor when the orders are not coming. This is why Q3 and Q4 moderation is a very welcome sign and yet another indicator of confidence in the ability of China's government to effectively manage the economy as and when required. But moderating the economy is only the first step towards sustainable development in the decade ahead. If China is to continue along the development path it has chosen, the next series of steps must be much more significant and much more definitive for the long-term future of the country.

The decade ahead

It is perhaps somewhat ironic that the same phenomenon which brought the US economy to its knees over the past decade can provide additional strength to the Chinese economy in the following one. As high as 70% of GDP, US household consumption fuelled a dominant portion of China's exports of manufactured goods. Capitalising on its massive labour force and weak currency, China comfortably supplied the developed world with the goods it demanded, while itself consuming very little and saving a lot. These savings were sustainable as long as the US and its peers were willing to finance their consumption through borrowing while spending at persistently high rates. At the end of the day, China's production was the developed world's consumption and China's savings were the developed world's borrowings. China became what Nouriel Roubini called "the lender of first and last resort".

Of course, this dynamic is now broken for the reasons described above. Continued investment in fixed assets is unsustainable and hence why the observed moderation is a very welcome sign. What China needs to do now is effectively leverage its accumulated capital. As it produced and sold to the world, it grew richer and amassed enormous capacity. It should now modify its strategy to utilise this capacity and continue along a relatively fast growth path in the following decade without overheating the economy.

It has all the right conditions in its favour to do so. An average Chinese worker is now many times richer than ten years ago, while still being one of the cheapest and most productive in the world. On top of that, various studies converge on the view that, alongside growing wages, aspirations are growing too – Chinese workers are no longer willing to accept any wage or any conditions, and are demanding greater balance between work and leisure, which is a strong indicator of the desire to enjoy the rewards of one's efforts.

At the same time, the government is evidently becoming more accustomed to the workers' greater assertiveness – a trend that strongly suggests that the government realises that consumption is going to be the key economic driver going forward and is willing to create an environment conducive to such development.

So all in all, it looks like China is set to continue to make the right strategic choices. Two decades ago it correctly anticipated that global demand is set to grow and skilfully crafted its economy to become a net global supplier. After the crisis, it reassessed its fundamentals and set out on a new direction. It knows that it has plenty of room to manoeuvre. With an approximate 36% consumption rate, 10% annual GDP growth, enormous capital reserves and the biggest population in the world, it is well positioned to continue along its phenomenal expansion path if it manages to steer its economy in the right direction and incentivise greater consumption and lower savings. Steering the economy, moreover, is what China has shown itself to be rather good at. A gradually appreciating Renminbi – a trend that has finally started to emerge – will help support the shift towards greater consumption by increasing the real purchasing power of the currency and boosting import demand.

These developments will not benefit China alone. In August, *The Economist* newspaper estimated that a 20% increase in Chinese consumption might lead to an additional USD 25 bn in US exports, which could create over 200,000 new jobs in the US. As China's population gradually becomes the world's biggest consumer, businesses around the world will get an opportunity to supply its growing consumption needs. The advantage of cheap labour that allowed the developed world to keep profits high may evaporate, but in place of the world's biggest factory floor is likely to emerge the world's biggest supermarket. Over the last 20 years, China helped the world enjoy relatively cheap consumption and an abundant choice of goods. Who knows, perhaps in its new guise it will once again become the backbone of global trade and may even save the developed world from a recessionary trap?

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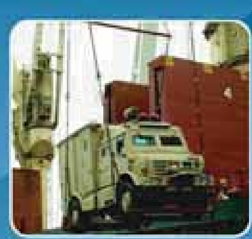
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China Business News Highlights

In recent months, China's leaders have been visiting the capitals of the world, with new business deals and even efforts to mitigate the European debt crisis following in their wake. In China, the aerospace industry is set to take-off, and foreign firms are optimistic about China's market potential, yet regulators worry about the immediate concerns posed by inflation.

Sector News

Inside China

A general outline of China's 12th Five Year Plan was released in October 2010. One of the key topics on the agenda is addressing income disparities. The focus is to be shifted away from export-led growth by raising the consumption levels of Chinese consumers. The formal release of the outline for the new Five Year Plan is scheduled for March 2011.

China raised its benchmark interest rates three times since October 2010. China's one-year base lending rate currently stands at 6.06% with a 3.0% one-year deposit rate, after its most recent rate hike on 8 February by the People's Bank of China—China's central bank—in an attempt to reign in excess liquidity and curb inflation.

In January 2010, China's consumer price index (CPI) reached 4.9%. This followed a lofty 5.1% n November and 4.6% in December. Chinese bond markets have indicated an expectation that policy makers will rein in inflation, as yields on 15-year bonds were lower than those maturing within five years.

In February 2011, China's State Council announced new rules for foreign investment. The National Development and Reform Commission and China's Ministry of Commerce are to oversee a new committee that will review foreign companies' attempts to acquire stakes in Chinese companies.

Headlines

All smiles: Chinese Deputy Prime Minister, Li Keqiang, with Spain's Prime Minister and Industry Minister (allvoices.com)

Business and diplomacy by China's leaders

In late January 2011, President Hu Jintao conducted a state visit to the US, a trip which served to shore up the bilateral relationship. Earlier in January, China's deputy premier, Li Keqiang, visited Spain, resulting in trade agreements for the sale of Spanish wine, ham and olive oil to China. It was also reported that China would work to bring stability to the European debt crisis by purchasing USD 7.9 billion of Spanish government bonds. A similar sum has been allocated for the purchase of Portuguese and Greek bonds.

A trip by Wen Jiabao, China's Premier, to Pakistan in December 2010 resulted in USD 35 billion in deals to further integrate bilateral trade. Agreements were signed in a range of industries via USD 20 billion in government-to-government contracts and USD 15 billion in private sector deals. Also on the agenda was the expansion of the Karakoram Highway which traverses the two countries' mutual border. Trans-Pakistan road and rail networks are planned to eventually connect China's north-western province of Xinjiang with Gwadar Port on Pakistan's coast.

China's big business in the Americas

In February, PetroChina signed a USD 5.4 billion deal in Canada. For this sum PetroChina entered into a joint venture with Encana to receive a 50% interest in the Cutback Ridge assets which contain an estimated one trillion cubic feet of natural gas reserves. This deal was the latest in a wave of Chinese invest deals in the Americas from 2010, notably oil in South America and in the US.

Sector News

Energy

In October 2010 it was reported that Sinopec, a major Chinese oil company, bought a 40% stake in Repsol Brazil for USD 7.1 billion. The funds will be used to develop Repsol's offshore assets which include some of the largest Brazilian oil blocks off the country's southern coast. Repsol Brazil has net resources of 1.2 billion barrels of oil equivalent.

In the first attempt by a state-owned Chinese oil company to invest in American oil since the failed bid for Unocal in 2005, China National Offshore Oil Company (CNOOC) successfully acquired a 33% stake in Chesapeake Energy's Eagle Ford shale project for USD 1.1 billion. CNOOC also agreed to pay for drilling and well completion costs of USD 1.1 billion. New techniques have cut the cost of extracting oil from unconventional sources, such as shale, prompting international oil companies to invest in such projects in the US.

Mining

The Chinese government again reduced the export quota for rare earths. 14,446 tonnes will be allowed to leave China in H1 2011, an 11.4% decrease from H1 2010 and 36.6% below the quota of H1 2008. In total, 31 companies, both foreign and domestically owned, are permitted to export rare earths. China accounts for 97% of world production in this mineral class which are utilised as key inputs for many modern electronic devices.

Retail

Tesco, the world's third-largest supermarket chain behind Wal-Mart and Carrefour, has announced that it will spend over USD 3 billion to establish 50 new shopping malls in China. The retailer intends to increase the number of its hypermarkets in China to over 200—a similar amount to what Tesco oversees in its home market, the UK. Tesco's increased presence is expected to raise the company's annual sales in China over the next five years to USD 6 billion, a level quadruple that of its current revenues in the country.

PayPal, the world's largest online payment platform, struck a deal with China's largest municipality, Chongqing. The deal entails a range of services including a foreign exchange settlement option for Chinese businessmen selling overseas. The new service is expected to increase the international presence of small Chinese vendors and is planned for launching throughout Mainland China in H2 2011. Approval from the State Administration of Foreign Exchange is still pending.

Pharmaceutical

The Swiss drugs company Nycomed will expand into China by purchasing a 51.3% stake in Guangdong Techpool Bio-Pharma for USD 214 million. The investment is intended to bring Chinese-developed medicines in touch with a global customer-base and highlights China's increasing role internationally in manufacturing and research and development. Through the deal, Nycomed also expects to double its sales in China to more than USD 150 million annually. The Swiss firm derived 30% of its earnings from emerging markets in 2010, and it hopes to raise this to at least 45% in 2011.

Tailwinds for China's aerospace industry - Helicopters the new luxury item of choice?

Boeing has released lofty expectations for China's airline industry. The world's largest aerospace manufacturer expects China to become the world's second-largest market for airplanes in the next two decades. In this time China is forecast to purchase over 4,300 new commercial jets valued at USD 480 billion, most of them smaller single-aisle planes. China's airline demand is currently growing at a pace double that of the global industry average. Boeing also indicated that it expects competition for Chinese market share to come from China's Commercial Aircraft Corporation with the release of its single-aisle model, scheduled for 2016.

In November 2010, Rolls Royce was awarded two major contracts to supply engines to Chinese airliners. The first, valued at USD 1.2 billion, was China Eastern Airlines' purchase of the company's Trent 700 engines to power 16 aircraft. Later in the same month, Air China agreed to fit 20 of its new aircraft with Rolls Royce engines at a total price tag of USD 1.8 billion. The deals raised the UK-based company's image after a range of problems earlier in 2010 with Rolls Royce-fitted planes in Singapore and after an emergency airworthiness directive for the company's Trent 900 engines was issued by the European Aviation Safety Agency.

The Civil Aviation Administration of China has opened airspace below 4,000 metres to all civilian aircraft. It is anticipated that this move may well proceed to trigger a rush in the purchase of privately-owned helicopters and light aircraft by Chinese consumers; as many as 3,300 helicopters may be purchased in the next decade, according to some estimates. This would mark a drastic increase to the mere 150 helicopters currently in use in Mainland China. Martin Lin, the president of Chinese aircraft manufacturer Texton, said the announcement "[Is] the beginning of a new chapter in China's general aviation development."

In early March 2011 it was announced that China's state-run Aviation Industry Corp. of China (AVIC), responsible for China's new stealth fighter, had agreed to buy the Minnesota-based private aircraft maker Cirrus Industries, the world's second-largest manufacturer of single-engine general aviation aircraft, behind Cessna, in terms of the number of planes delivered. While details of the deal were not disclosed, Cirrus is the first acquisition of an aircraft manufacturer in the US and Europe by a Chinese aviation company, and highlights the expanding ambition of China's aerospace industry. The deal is expected to close in mid-2011, and would give AVIC access to Cirrus' technology, which includes a small jet currently in development.

Finance

Two Chinese banks are among the world's top ten credit card issuers, according to a survey from October 2010. Industrial and Commercial Bank of China's 54 million credit card holders are the most of any bank based in an emerging economy and is gaining fast on the leader, JPMorgan, which has 96 million cards in service. China Merchants Bank also made it into the top ten list, as did three Brazilian banks. Asia is still catching up with other regions in credit card use with an average one-fourth of a credit card for every adult, a figure behind North America's 2.3, Western Europe's 0.7 and even Latin America's 0.6.

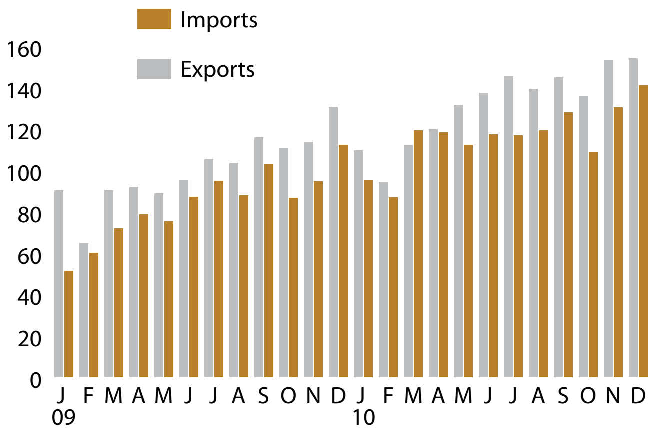
In December 2010, the German state-owned bank HSH Nordbank accepted a USD 500 million loan facility from China Development Bank. The German bank experienced heavy losses during the global financial crisis due to its exposure to property markets and international shipping. Chinese funding will expand the scope of HSH Nordbank's dollar business and is expected to help the German bank turn a profit in 2011 after negative returns in recent years.

The Swiss insurance company Zurich Financial Services AG has secured a 20% interest in New China Life Insurance in the run-up to the Chinese company's initial public offering, expected to occur sometime during the second quarter of 2011. For USD 420 million, the Swiss insurer purchased 280 million shares in China Life, China's third-largest life insurance company. Zurich Financial has been a shareholder in its Chinese counterpart since 2000, but decided to increase its holdings due to the insurance industry's rapid growth in China in recent years. The Swiss company has operated a branch in Beijing since 2006.

China Trade Roundup: China's Diversification

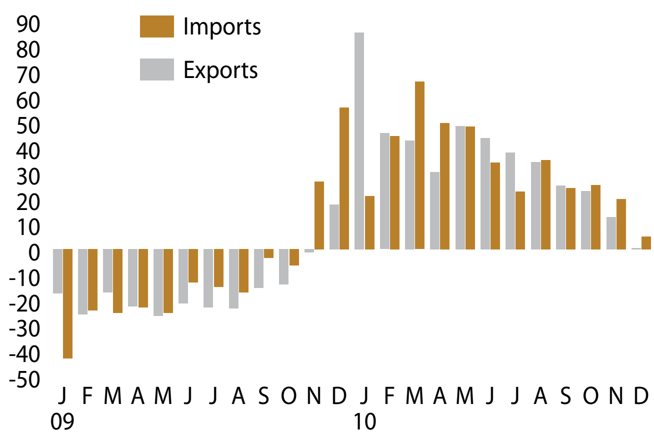
In this edition of *China Trade Roundup* we review the major trends of China's trade performance in 2010, a record year for Chinese commerce. China imported more automobiles in 2010 and displayed further diversification away from its more traditional trade partners in the countries of the West. *By Charles Avery and Jim Hu*

China Total Trade, USD bn, 2009-2010



Source: National Bureau of Statistics; China Customs; The Beijing Axis Analysis

China Trade Monthly y-o-y % Growth Rates, 2009-2010



Source: National Bureau of Statistics; China Customs; The Beijing Axis Analysis

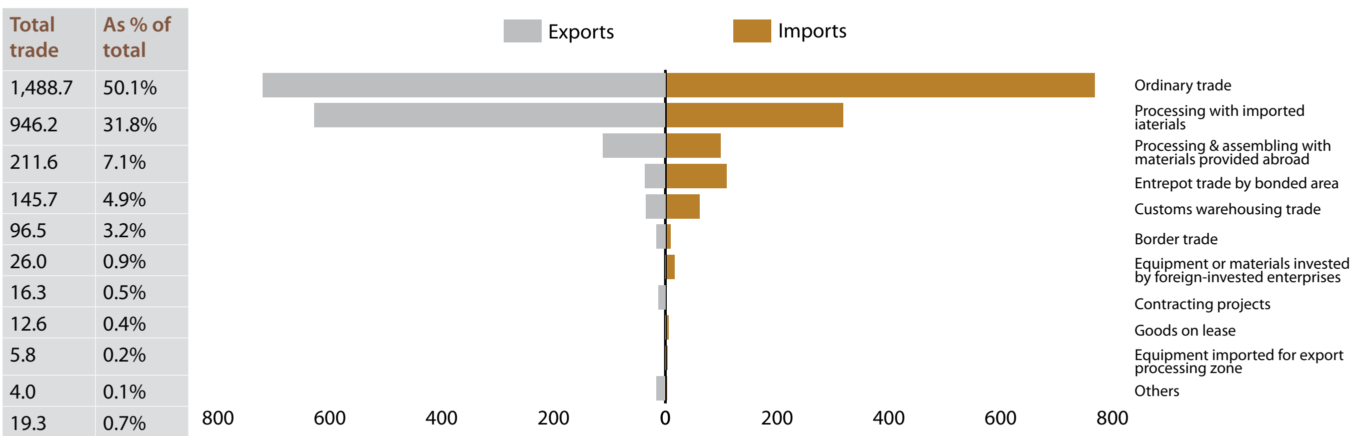
A new record for China trade in 2010

According to statistics from China Customs, the value of China's total trade reached USD 2.97 trillion in 2010, a 34.7% increase over 2009. The value of China's imports increased at 38.7%, a rate higher than the 31.3% growth in its exports, signalling the increasing purchasing power of Chinese consumers and a reduction in the nation's trade surplus—down 6.4% from 2009.

China's trade levels in 2010 reached a new record high, even surpassing the previous 2008 annual total trade of USD 2.6 trillion. China's trade deficit has contracted in this time period, dropping 38.0% between 2008 and 2010. China's trade has not only recovered from the lows of 2009 during the global financial crisis, but has exceeded previous levels in a more balanced state. In fact, in March 2010 the value of China's imports was greater than its exported value, resulting in an unusual trade deficit, although for only one month. The largest export and import totals for 2010 occurred at the end of the year. December set a new monthly high of USD 154 million in exports and USD 141 million in imports. The momentum from this impressive last month gives reason to expect greater trade figures in 2011.

Half of China's trade in 2010 was classified as 'ordinary' by China Customs. The second-largest segment involves both the processing and assembling of imported materials. The difference between the exported and imported values in these two trade categories (see chart below) equaled USD 310 million and loosely represents the value added of Chinese industry as an intermediary in the processing of goods. More common among imports for the year were entrepot trade using bonded areas and customs warehousing trade.

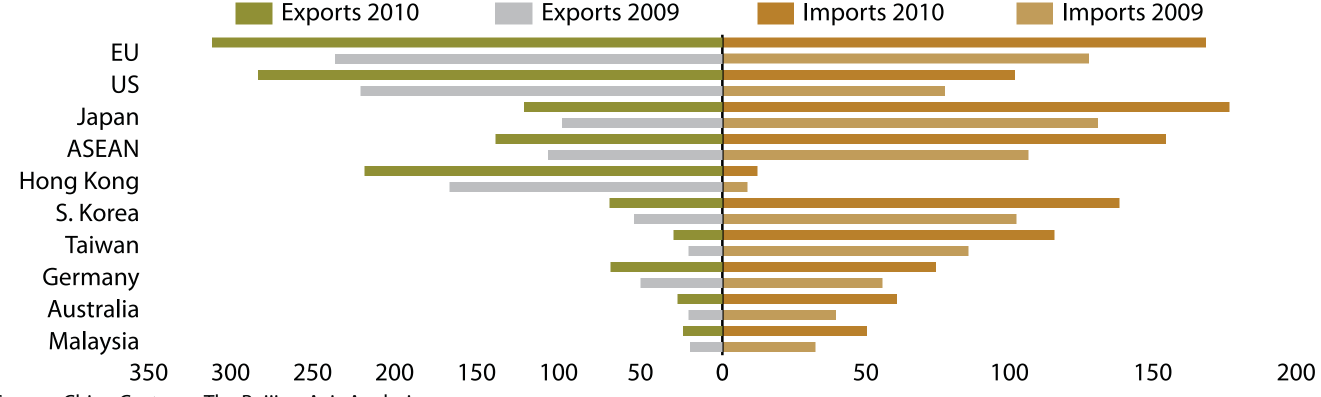
China's Trade by Type in 2010, USD bn



Total trade	As % of total
1,488.7	50.1%
946.2	31.8%
211.6	7.1%
145.7	4.9%
96.5	3.2%
26.0	0.9%
16.3	0.5%
12.6	0.4%
5.8	0.2%
4.0	0.1%
19.3	0.7%

Source: National Bureau of Statistics; China Customs; The Beijing Axis Analysis

China Total Exports & Imports by Country/Region, USD bn, 2009 vs. 2010



Source: China Customs; The Beijing Axis Analysis

China's major trade partners

China made huge gains in its overall trade during 2010 as its major trade partners recovered, albeit sluggishly, from the economic doldrums of 2009. Overall, trade with China's top ten partners (see chart above) increased from USD 1.7 trillion in 2009 to USD 2.3 trillion in 2010. Although this represents an increase of USD 600 million, the proportion of these ten countries in China's total trade fell from 80% in 2009 to 78% in 2010. The 2% difference represents an incremental shift by China toward the diversification of its trade partners.

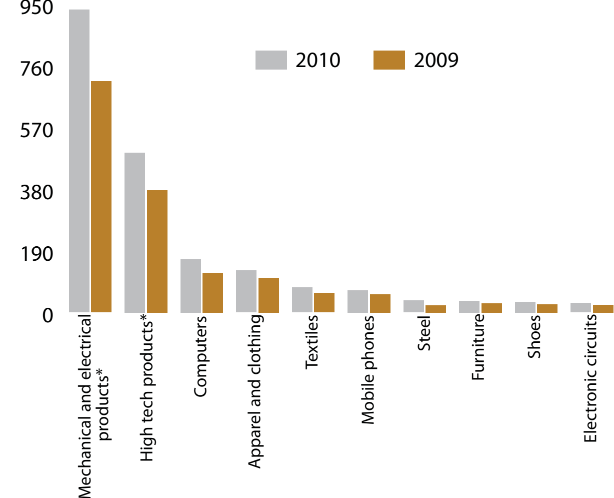
Of China's top trade partners, the greatest increase in exported value from 2009 to 2010 was in the goods and services exported to Taiwan, up 43% y-o-y. On the imports side, the greatest increase came from Australia. The resources shipped from Australia to China contributed to a 56% increase in the imported value of Australian exports to China. Closer East Asian countries also exported greater values to China in this time period. China imported 56% more from Malaysia in 2010 than it did in 2009, as well as 45% more from the ASEAN block as a whole.

With most of these countries China runs a trade deficit. Trade surpluses only exist with the European Union, the US and Hong Kong. The most dramatic shifts in trade balances were more exacerbated deficits with ASEAN countries which, although still small at only USD 17 billion in 2010, is a 17-fold increase from the previous year. With Malaysia, China's trade deficit doubled. Once again, the implication seems to be a shift in China's trade toward greater diversification and away from the traditional economic powers of the West.

The composition of China's leading exports in 2010 was relatively unchanged from recent years although at a higher overall value. The value of China's exported steel increased by 68% y-o-y in 2010, while 30-plus percentage increases occurred for mechanical and electrical products, high tech goods and computers.

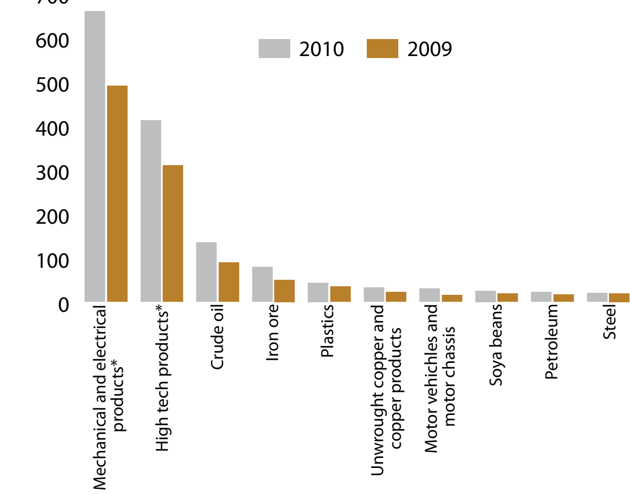
China's leading import category may have been mechanical and electrical products in 2010, but the largest increase was registered in imported motor vehicles and chassis, the USD value of which doubled between 2009 and 2010. The value of the imported crude oil used to fuel these vehicles rose to USD 135 million in 2010, a 52% increase over 2009.

Leading Chinese Exports, USD bn, 2009-2010



*May include duplicate data.
Source: China Customs; The Beijing Axis Analysis

Leading Chinese Imports, USD bn, 2009-2010



*May include duplicate data.
Source: China Customs; The Beijing Axis Analysis

China Sourcing Strategy

Chinese low-end steel products like billets and hot-rolled coils are no longer favourable targets for foreign buyers. Instead, China's steel industry is becoming a higher value-added supply base. In this edition of *China Sourcing Strategy*, we highlight new China sourcing opportunities for foreign steel players. *By Beijing Axis Procurement*

China is the world's largest steel manufacturer and is still growing fast in terms of output, product range and quality. It is becoming virtually impossible for overseas steel players to avoid a China agenda in their business estimations, either in the form of engaging China as competitor or as partner. Yet foreign steel players are now finding that China's steel industry is becoming a whole new entity.

No longer only a supplier of raw materials

Overseas buyers are finding that the competitiveness of Chinese low-end steel products (e.g. billets and hot rolled coils) is not as attractive as it was five years ago. The main reason for this is the government's restriction of exports and the growth of related industries.

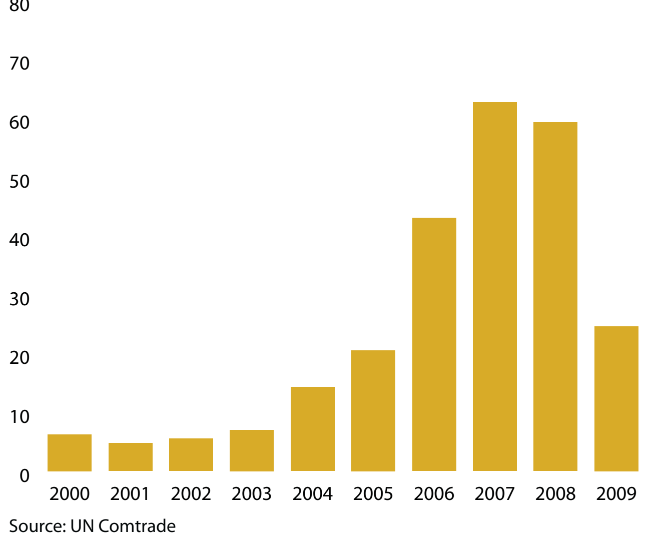
In 2005, the Chinese government raised the concept of 'highly-polluting, energy-intensive and resources-dependent industries' and determined to strictly control the expansion of these industries and their output of low-end products, including low-end steel products. Since 2005, several measures have been introduced to counter a rise in steel exports. These measures mostly took the form of reducing or cancelling export rebates. Although some export rebates were reinstated to secure exports during the global financial crisis, a new policy of removing the export rebates of hot rolled coils and profile steels was announced in mid-2010. The rebate cuts were intended to help the government 'control' the steel industry and improve energy efficiency by increasing the export costs of low-end steel products and driving obsolete mills out of production.

A higher value-added supply base for overseas steel players

Compared with crude steel production and exports, China's finished steel industry has been encouraged to grow. China's output of finished steel has exceeded crude steel since 2000, and in 2007 output of finished steel surpassed consumption for the first time (see chart above to the right).

Finished steel - China is now exporting an increasing amount of high value-added steel products such as pipes and rails. Overseas steel players are now able to cooperate with Chinese suppliers to source finished steel products to supplement their own supply in terms of both quantity and product range. If we take electric resistance welding (ERW) pipes as an example, in recent years China has imported more than 20 advanced technical production lines from abroad. As a result, China's manufacturing capacity of ERW pipes is set to attain leading international levels in terms of output, product range (from very thin wall thickness to very large diameter), manufacturing facilities as well as product quality.

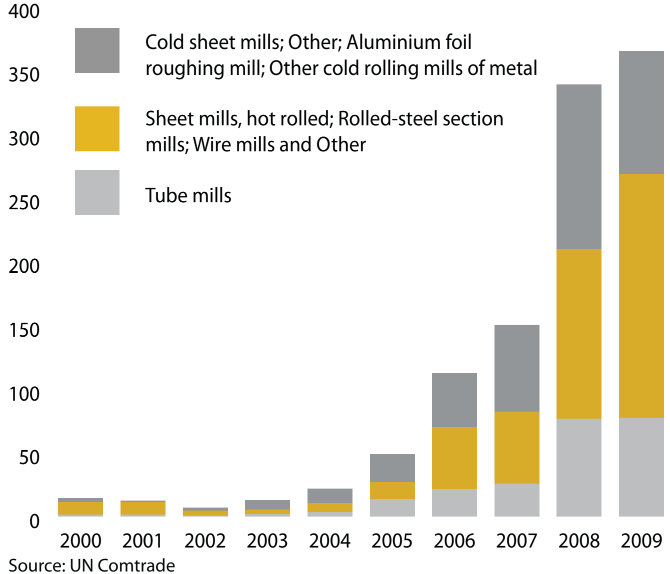
China Total Export Value of Finished Steel, USD mn, 2000-2009



Source: UN Comtrade

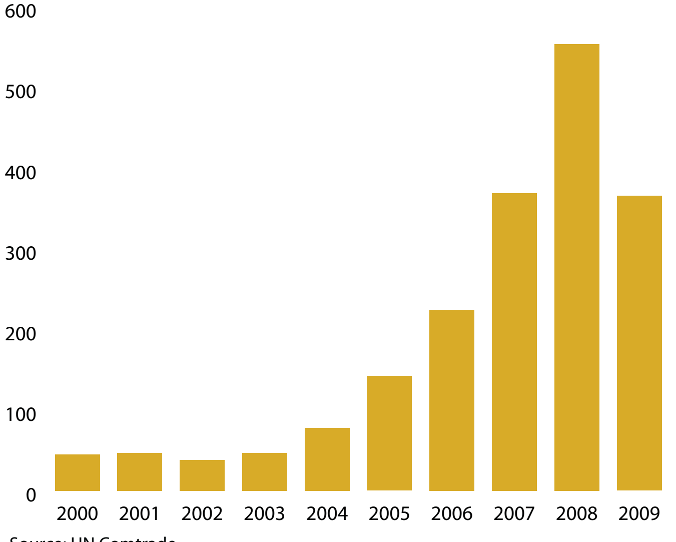
In addition, price and delivery times are remarkably still substantial advantages in China. Chinese pipes have been exported in large quantities to the US and other regions for years now and have encountered anti-dumping measures due to their competitive pricing, which has affected China's exports of these pipes. However, Chinese suppliers have been exploring emerging markets such as Latin America and Africa.

China Total Export Value of Metal-rolling Mills and Rolls, USD mn, 2000-2009



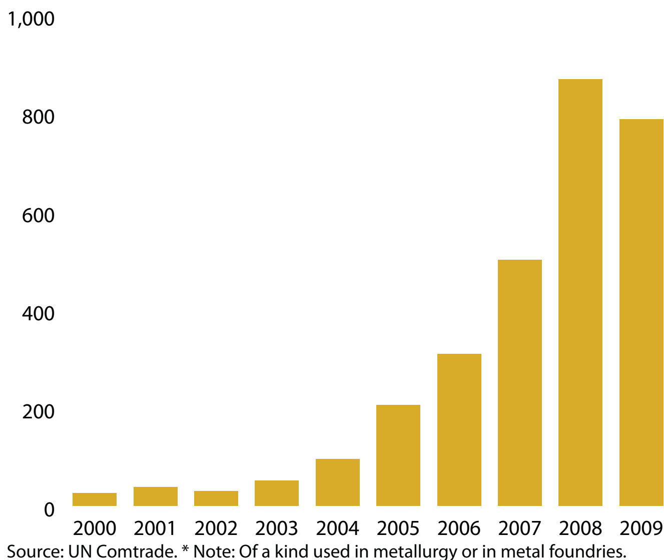
Source: UN Comtrade

China Export Value of Machine Tools for Working Metal; Presses for Working Metal or Metal Carbides, USD mn, 2000-2009



Source: UN Comtrade

China Export Value of Converters, Ladles, Ingot Moulds and Casting Machines*, USD mn, 2000-2009

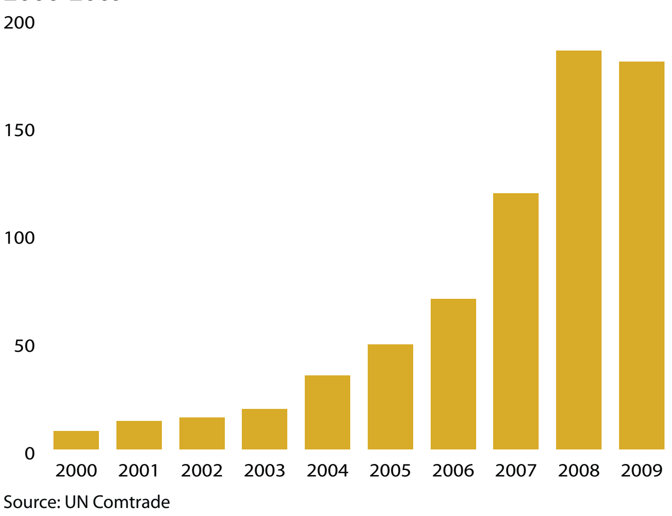


Source: UN Comtrade. * Note: Of a kind used in metallurgy or in metal foundries.

Equipment - The fact that the majority of Chinese steel mills were designed by Chinese engineering companies and are using equipment made in China is indicative of the fact that China has internationally competitive engineering companies and equipment manufacturers for steel mills. Many international metallurgy engineering companies such as Danieli, SMS, and VAI have established manufacturing bases in China and are also sourcing from OEM partners in China. Chinese metallurgical equipment and technology have been exported to many countries and to some of the world's major steel players.

China has a clear advantage in designing, producing and exporting the following equipment: long products rolling mills, thin strip rolling mills, complete line for seamless/welded pipe production blast furnaces, steel melting furnaces, secondary refining furnaces, continuous casting machines, roller tables, cooling beds, roll changing devices, coilers and uncoilers, cutters, shears, saws, cut to length lines, and slitting lines (see charts above and on previous page, right bottom).

China Export Value of Rolls for Rolling Mills, USD mn, 2000-2009



Source: UN Comtrade

Consumables - For overseas steel mills, there are big opportunities to source the following consumables from China: rollers (see chart below, left), side guides, continuous casting moulds (see chart above, right), refractories, hydraulic/pneumatic cylinders, pumps, valves, hoses, couplings, and cardan shafts.

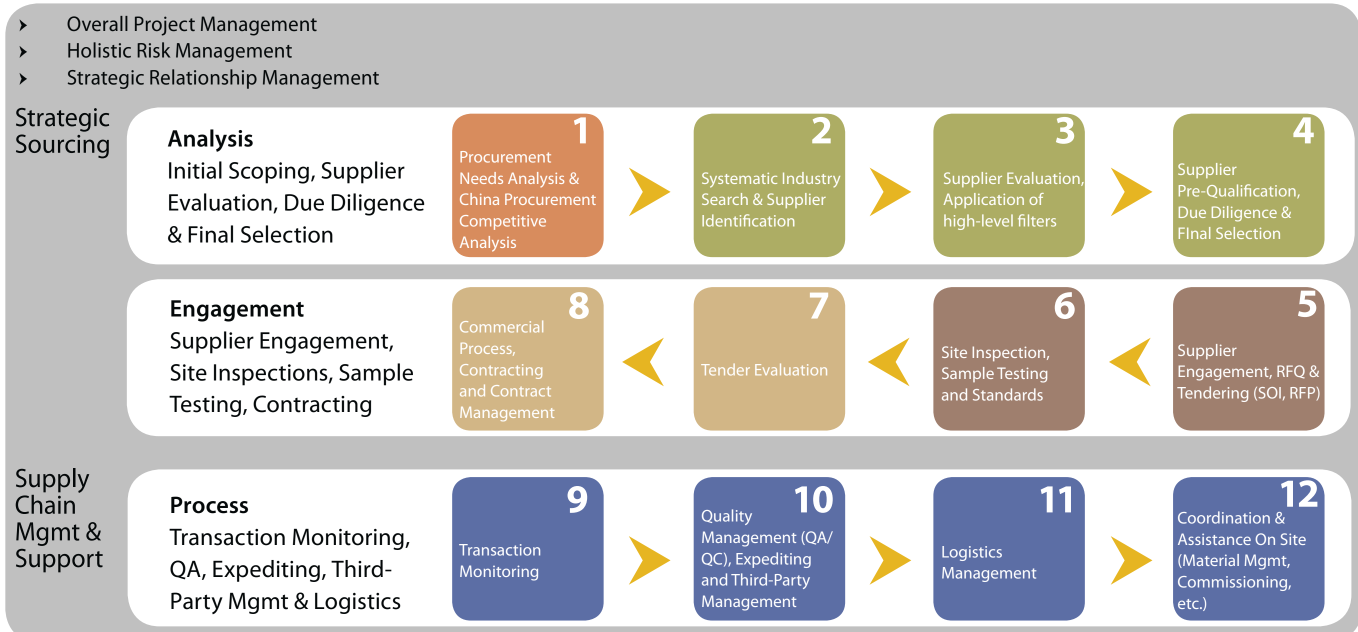
Taking rollers as an example, China's export volume was 32,287 tons in 2009, with an export value of around USD 180 million. The major export destinations were South Asia, the US, India, Korea and Turkey. There are about 300 roller manufacturers (with total annual capacity exceeding 700,000 tons) in China. More than 10 companies are capable of producing 10,000 tons per year. Since 2008, Chinese manufacturers have enhanced their manufacturing technology and facilities by means of joint ventures, restructuring and technological innovation. Chinese suppliers are currently also aiming to upgrade to international standards by using high quality raw materials or by shortening delivery times and providing more value added service.

With improving manufacturing conditions, cost competitiveness, maturing engineering capabilities, growing commercial capabilities, favourable policy from the government and enthusiasm of Chinese suppliers to expand in overseas markets, there is much room for overseas steel players to source from China and to include a strategic China agenda in their development plans for the 2010s.

How to Procure from China - #7 Tender Evaluation

The Beijing Axis Procurement Process Flow encapsulates the full extent of project engagement, from the point of first enquiry to the range of services in the solution process and benefits provided for the customer. In this edition we focus more closely on step 7 of the Beijing Axis Procurement Process Flow: Tender Evaluation.

The Process Flow and Service Delivery Platform of Beijing Axis Procurement



Beijing Axis Procurement has the ability to implement tenders in China on behalf of overseas buyers. After collecting all the tender documents from Chinese suppliers, *Beijing Axis Procurement* will carry out a pre-evaluation assessment before submitting the original documents to ensure that overseas buyers are able to make a thorough comparison of proposals from Chinese bidders.

Beijing Axis Procurement guidelines for Tender Evaluation

Evaluation **-** The following items need to be verified in the evaluation process:

- Documents - Due to language and culture barriers, even good Chinese companies can neglect to file several tables in tender documents. It is important to check whether the bidding documents comply with requirements
- Commercial information - For some bidders, tender documents may have information not properly or correctly displayed for use in China, e.g. terms, VAT, currency, and others. Chinese bidders can sometimes either ignore some of the requirements or comply without realising the potential risk involved. Therefore it is important to identify these discrepancies
- Technical specifications - Although buyers will be responsible for the final evaluation, *Beijing Axis Procurement* will preliminarily verify whether the proposed equipment/product meets the requirements. In addition, we will also check for other common mistakes such as when bidders misread coating requirements or the requirements of the motors with the equipment, or only provide partial data sheets, or provide unrealistic shipping solutions

Clarification - After identifying problems with tender documents, *Beijing Axis Procurement* will commence the clarification process with the Chinese bidders. The clarification documents will be provided in bilingual format and archived together with the bidders' proposal. Due to a lack of time or experience, only 10-20% of the bidding documents from Chinese bidders will usually meet the requirements of the tender documents. It is hence crucial to reconcile differences between Chinese and Western documentation and to enable the Chinese bidders to clarify and improve their documentation.

Classification - *Beijing Axis Procurement* will extract all the necessary information from the bidders' proposals and include these in our commercial evaluation summary table for the buyer to easily compare different offers. This summary will include quotation dates and validity, currency and exchange rates, packaging schemes and shipping costs (DDP/DDU if required), costs of key spare parts and 2-year spare parts, guarantee, VAT (Chinese government export VAT rebate), payment term, delivery time, etc. *Beijing Axis Procurement* will then submit the evaluation summary sheet, the bidding documents and the clarification documents to the buyer.

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Group Five is a diversified construction services, materials and infrastructure investment group

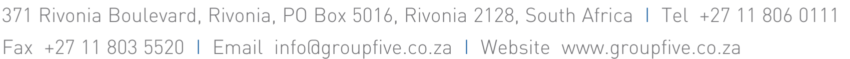
We have the skills and experience to deliver any aspect of an infrastructural project, including concept development, manufacturing, construction and operations and maintenance.
The group's capabilities have been honed to deliver comprehensive infrastructure solutions to sectors that have a high potential.

We operate in **Africa, the Middle East and Eastern Europe**

Ranked 4th in JSE SRI Index 2010
Winner of DEKRA **Ethics Award 2009**

9th in Financial Mail's top **empowerment companies 2010**
Construction Charter **Level 2 BBBEE rating**

Employing **14 050 people in 22 countries**
Celebrating **37 years as a listed entity**



China Capital: Inbound/Outbound FDI & Financial Markets

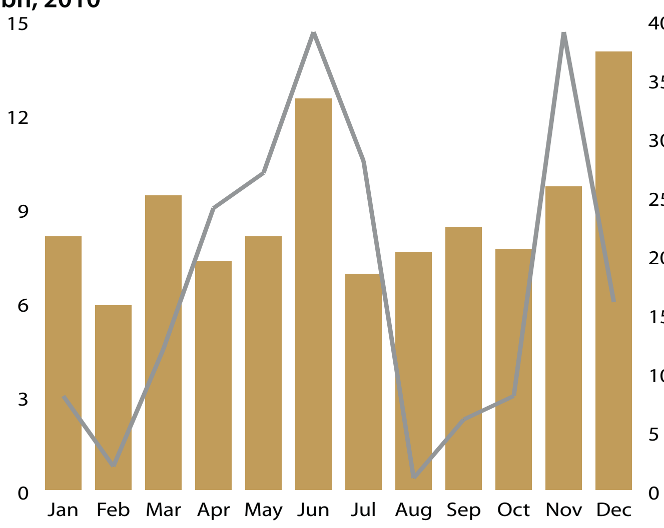
China remained an attractive destination for foreign investment in 2010, with FDI reaching USD 105.6 billion, 17.3% higher y-o-y. Chinese outbound investment in 2010 reached USD 59.0 billion, 33.6% higher y-o-y. From July 2010 to January 2011, *Beijing Axis Capital* tracked 103 of China's largest overseas M&A activities, which included 37 deals in the resources sector. *By Beijing Axis Capital*

Foreign Direct Investment in China

Summary

- Foreign Direct Investment (FDI) in China amounted to USD 54.3 billion in H2 2010. This figure represents a y-o-y growth rate of 15.5% (see chart to the right). This brought full year FDI utilised in China in 2010 to USD 105.6 bn, an increase of 11.7% y-o-y (see chart below)
- In 2010, wholly foreign-owned enterprises were the major vehicles of investment in China, accounting for 80% of approved cases of FDI and 77% of total actually utilised capital
- In H2 2010, FDI in China primarily originated from other Asian countries/regions. Hong Kong was still the largest investor in China, contributing USD 35.8 bn or 65.9% of total FDI. After Hong Kong, investment from Taiwan has become a notable source of FDI to mainland China (USD 3.2 bn or 5.9% of total FDI in H2 2010)

China Actually Utilised Monthly FDI and Growth Rate, USD bn, 2010

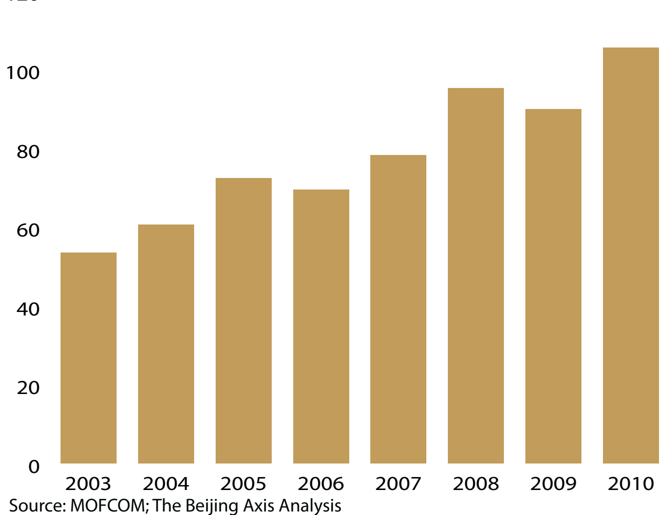


Source: MOFCOM; The Beijing Axis Analysis

Notable FDI deals in China in H2 2010

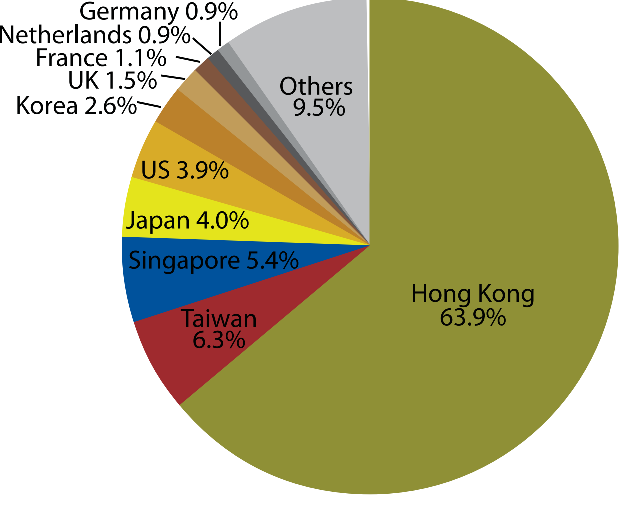
- Coty, the world's largest fragrance company, announced the acquisition of a majority stake in the Chinese skin care company TJoy for USD 400 mn (December)
- US health care giant Cardinal Health announced that the company had acquired the leading privately held Chinese drug distributor Zuellig Pharma China, also known as Yong Yu, for USD 470 mn (November)
- The French company Vallourec announced it had acquired 19.5% of Tianda Oil Pipe Company Limited, a Chinese seamless pipe manufacturer listed in Hong Kong, for around USD 100 mn (November)
- Pegatron, the manufacturing arm of pc vendor AsusTek, announced its acquisition of two electronic component companies in China for USD 220 mn (August)
- Discovery Holdings, a South African health care insurer, signed an agreement with Ping An Insurance Group Company of China (601318, 2318.HK) to acquire a 20% stake in Ping An Health Insurance (August)
- French hypermarket chain Carrefour SA announced the acquisition of a 51% stake in the Hebei-based hypermarket operator Baolongcang (July)
- Singapore's third-largest lender, United Overseas Bank (UOBH.SI), announced its investment of an additional USD 202 mn in China's Evergrowing Bank (July)

China Annual Actually Utilised FDI, USD bn, 2003-2010



Source: MOFCOM; The Beijing Axis Analysis

China FDI by Source Country/Region, USD bn, 2010



Source: MOFCOM; The Beijing Axis Analysis

Chinese Outbound Foreign Direct Investment

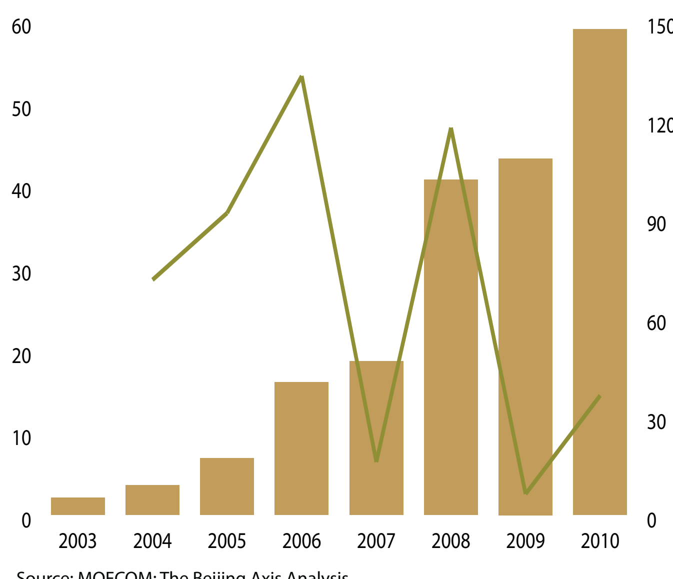
Summary

- In 2010, China's OFDI (non-financial) reached USD 59.0 bn, representing y-o-y growth of 36.3% (see chart, right)
- From July 2010 to January 2011, *Beijing Axis Capital* tracked 103 of the largest publicly announced overseas M&A activities conducted by Chinese companies
- According to our analysis, the region that attracted the most Chinese investment from July 2010 to January 2011 was North America, where we followed 28 major M&A activities, which included several mega deals
- In terms of deal size, Latin America witnessed two multi-billion dollar transactions in the oil & gas sector, which made this region the leading destination of Chinese capital outflow in H2 2010. Europe, Australia and Asia were the other main destinations of capital outflow from China. Interestingly, Africa saw a comparatively quiet period in terms of announced Chinese investment activities
- Although the largest deals in 2010 still mostly occurred in the resources sector, non-resource deals accounted for more than 50% in terms of numbers of deals. Manufacturing, light industry, the financial sector and technology were important sectors

Notable Chinese OFDI deals in H2 2010

- UK-headquartered BP agreed to sell its majority stake in Pan American Energy to its partner Bridas Energy, which is a 50% JV subsidiary of China National Offshore Oil Corporation (CNOOC), for about USD 7.1 bn in cash (November)
- General Motors' Chinese venture partner Shanghai Automotive has confirmed that it acquired a 1% stake in the Detroit auto maker for around USD 500 mn (November)
- China's Sinopec Group (0386.HK) agreed to buy 40% of Spanish oil major Repsol's (REP.MC) Brazilian arm for USD 7.1 bn (October)
- China National Chemical Corp has conducted talks to take control of MA Industries (MAIN.TA) in a deal which MA Industries' parent group Koor Industries (KOR.TA) said would value the world's seventh-largest agrichemicals maker at USD 2.7 bn (October)
- Multinational energy company Shell and PetroChina successfully completed their joint acquisition of the Australian coal seam gas company Arrow Energy Limited. The acquisition follows an offer in March 2010 to purchase 100% of the shares of Arrow by CS CSG (Australia) Pty Ltd, a 50/50 JV company owned by Shell Energy Holdings Australia and PetroChina (August)
- Zhen Hua Engineering Co. Ltd., a wholly-owned subsidiary of China Communications Construction Company Limited (CCCC), has completed the acquisition of a 100% stake in the US company Friede Goldman United (F&G) for USD 125 mn (August)
- China's Shandong Iron and Steel Group agreed to pay USD 1.5 bn for a stake in London-listed African Minerals' mine project in Sierra Leone. The investment would give Shandong Iron and Steel a 25% stake in the Tonkolili iron ore mine (July)

China Outbound FDI Flow (Non-financial) and Growth Rate, USD bn, 2003-2010



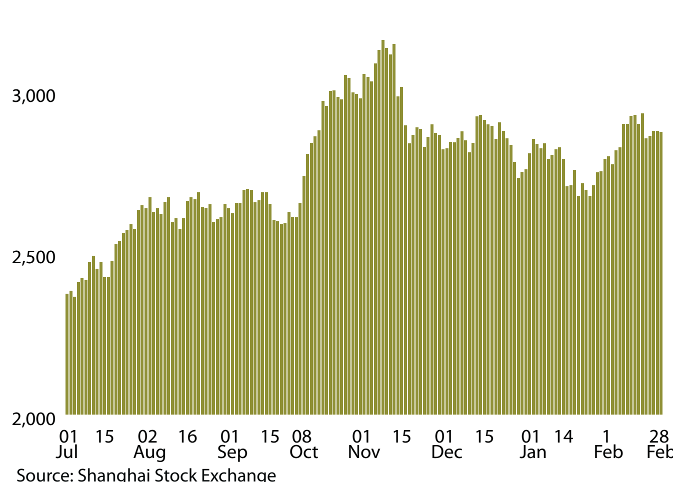
Source: MOFCOM; The Beijing Axis Analysis

China Financial Markets

China's stock markets since H2 2010

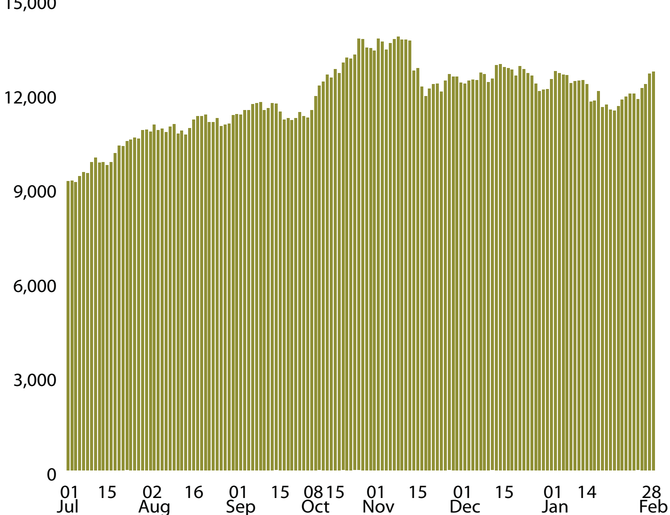
- After a long bear market since 2008, the Chinese stock market experienced a recovery in H2 2010 with a two-wave market rally in July and October
- China's main exchange, the Shanghai Stock Exchange, increased from 2,373 to 2,637 in July 2010, a rise of 11.1%. The second wave came later in 2010 after China's National Holiday week in October as the index climbed from 2,655 to 3,159 (a near-20% surge). This was followed by a sharp decline to 2,850 and a flat plateau period lasting until the end of 2010 (see chart below)
- The Shenzhen Stock Exchange Index experienced a surge from 9,171 in July to 13,807 in October, a remarkable 50% upgrade. Following the October holiday, however, Shenzhen shared a similar slump with Shanghai until January 2011 (see chart on next page)

Shanghai Stock Exchange Index, H2 2010-Feb 2011



Source: Shanghai Stock Exchange

Shenzhen Stock Exchange Index, H2 2010-Feb 2011



Source: Shenzhen Stock Exchange

- The launch of the Growth Enterprise Market in Shenzhen was one of the most important events in 2010, yet the market experienced major turbulence since its establishment in June 2010. In spite of the 30% increase through November, the index was back to its initial point of around 970 by the end of January 2011
- There were strong performances in H2 2010 in the Non-ferrous and Coal & Oil industries. The Non-ferrous sector outperformed the market with a dramatic surge from July to October, registering a 120% increase, on average. The Coal & Oil sector index experienced a 50%-plus increase at its peak point (11 November), and this significantly impacted the performance of the whole market
- Aside from Non-ferrous and Coal & Oil, other hot sectors in H2 2010 included Electronics, Pharmaceuticals, Machinery, Food & Beverage, and Agriculture. The worst performers were Real Estate, Financial, and Steel

IPO Watch: Hong Kong Stock Exchange

Given its close proximity to mainland China and the world's largest market for raw materials and mineral resources, Hong Kong has come to expand upon its traditional role as a conduit for investment into and from the mainland by serving as a capital market for Chinese mining and resources companies.

In 2010, there were 104 new IPOs and introduction cases at the Hong Kong Stock Exchange. Of a total of 15 mining, resource and raw material IPOs launched in Hong Kong in 2010, 12 were by mainland Chinese companies.

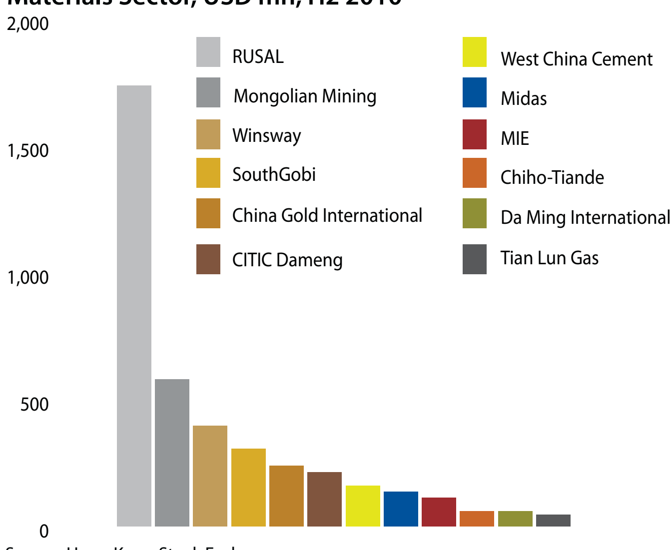
Prominent Chinese mining, resource and raw material IPOs in Hong Kong in 2010

- China Gold International Resources, a subsidiary of China Gold group focusing on the mining and development of gold and other non-ferrous mineral resources, with total funds raised of around USD 350 mn (December)
- CITIC Dameng Holdings, a subsidiary of CITIC Group specialising in Manganese mining and trading, with total funds raised of around USD 140 mn (November)
- Midas Holding, a leading manufacturer of aluminium alloy extrusion products and polyethylene pipes operating primarily in mainland China, with total funds raised around USD 180 mn (October)
- Winsway Coking Coal Holdings, one of China's largest traders of and investors in coking coal in Mongolia, with total funds raised of around USD 410 mn (October)
- West China Cement, a cement producer in Shaanxi province, with total funds raised of around USD 230 mn (August)
- Chiho-Tiande Group, a metal scrap recycler, with total funds raised of around USD 87 mn (July)

Other prominent IPOs in Hong Kong in 2010

- China Tian Lun Gas Holding, an urban piped gas distributor based in mainland China, with total funds raised of around USD 67 mn (November)
- Mongolian Mining Corporation, the largest privately-owned coking coal producer and exporter in Mongolia, with total funds raised of over USD 750 mn (October)
- Agricultural Bank of China (ABC), then the largest IPO by value in the history of the Hong Kong Stock Exchange, with total funds raised of over USD 13 bn
- Nine months later, the massive IPO of AIA Group exceeded that of ABC as the largest fund raising event ever in the Hong Kong Stock Exchange (also the third-largest IPO ever), with total funds raised of over USD 20 bn (July)
- RUSAL, the world's largest aluminium producer, with total funds raised of around USD 2.5 bn (January)
- South Gobi, the Mongolian coal producer, miner and explorer controlled by the Canadian mining giant Ivanhoe Mines, with total funds raised of around USD 124 mn (January)

Selected Hong Kong IPOs in the Resources and Raw Materials Sector, USD mn, H2 2010



Source: Hong Kong Stock Exchange

Major Chinese Outbound Investment Activity, July 2010 - January 2011

#	Date	Target / New Company	Target Country	Target Region	Acquirer / Investor (English Name)	Acquirer / Investor (Chinese Name)	Industry	Value	Stake	Status
1	31/01/2011	Chesapeake Energy Corporation	US	North America	CNOOC	中国海洋石油有限公司	Oil and gas	USD 570 mn	33.30%	Agreement Signed
2	26/01/2011	Belarusian Potash	Belarus	Europe	China Bluechemical	中海石油化学股份有限公司	Chemical	N/A	N/A	Agreement Signed
3	25/01/2011	BorsodChem	Hungary	Europe	Wanhua Industrial Group	万华实业集团	Chemical	USD 1.69 bn	58.00%	Concluded
4	22/01/2011	Bank of East Asia US unit	US	North America	Industrial & Commercial Bank of China	中国工商银行	Financial	USD 140 mn	80.00%	Ongoing
5	21/01/2011	Adriana Resources's Lac Otelnuk project	Canada	North America	Wuhan Iron and Steel Group	武汉钢铁	Iron ore	USD 120.7 mn	60.00%	Agreement Signed
6	12/01/2011	Aurobindo (Datong) Bio Pharma	India	Asia	China National Pharmaceutical Group	中国医药集团	Medical	N/A	80.50%	Concluded
7	11/01/2011	Orkla Group's Elkem (Silicon Business)	Norway	Europe	China Bluestar Group	中国蓝星集团	Chemical	N/A	N/A	Ongoing
8	21/12/2010	Valley Longwall International	Australia	Australia	Tianyuan Mining Machinery Group	中钢天源机械	Machinery	N/A	N/A	Agreement Signed
9	17/12/2010	Royal DSM's Antibiotic business	Netherlands	Europe	Sinochem Group	中化集团	Pharmaceutical	USD 280 mn	50.00%	Ongoing
10	14/12/2010	Energy Australia	Australia	Australia	CLP Holdings subsidiary TURenergy	中电控股澳洲子公司TURenergy	Energy	N/A	N/A	Ongoing
11	10/12/2010	Occidential Argentina	Argentina	Latin America	Sinopec	中石化	Oil and gas	USD 2.5 bn	100.00%	Concluded
12	28/11/2010	GMR Infrastructure's stake in InterGen N.V.	India	Asia	China Huaneng Group	中国华能集团	Power	USD 1.23 bn	50.00%	Agreement Signed
13	28/11/2010	Pan American Energy	Argentina	Latin America	Bridas Corp, a JV owned by CNOOC	中海油50%控股合资公司Bridas	Oil and gas	USD 7.06 bn	60.00%	Ongoing
14	25/11/2010	EuroSibEnergo	Russia	Europe	China Yangtze Power Co	长江电力	Energy	USD 168 mn	N/A	Agreement Signed
15	19/11/2010	General Motors	US	North America	Shanghai-based SAIC Motor	上汽集团	Automobile	USD 500 mn	1.00%	Concluded
16	11/11/2010	FerrAus and Brockman	Australia	Australia	Wah Nam International	华南投资控股公司	Mining	USD 930.6 mn	N/A	Ongoing
17	10/11/2010	Chesapeake Energy Corp's Eagle Ford shale	US	North America	CNOOC	中海油	Oil and gas	USD 1.08 bn	33,30%	Agreement Signed
18	04/11/2010	myTECHNIC	Turkey	Middle East	HNA Group and Bravia Capital	海航集团和Bravia Capital	Airline	N/A	N/A	Agreement Signed
19	29/10/2010	Kryso Resources	Tajikistan	Central Asia	China Nonferrous Metals International Mining	中色国际	Gold	N/A	29.90%	Approved by gov.
20	27/10/2010	M4S N.V.	Belgium	Europe	Huawei Technology	华为科技	High-Tech	N/A	N/A	Agreement Signed
21	16/10/2010	Nitel	Nigeria	Africa	China Unicom	中国联通	Power	USD 2.5 bn	75.00%	Approved by gov.
22	16/10/2010	Gandara Censa	Spain	Europe	CITIC Heavy Machinery	中信重工	Machinery	USD 70 mn	N/A	Agreement Signed
23	12/10/2010	Chindex International Inc	US	North America	Shanghai Fosun Pharmaceutical Group	上海复星医药集团	Pharmaceutical	N/A	51.00%	Gained gov. approval
24	11/10/2010	Koor Industries' subsidiary Makhteshim Agan Industries	Israel	MIddle East	China National Chemical	中国化工	Agrichemicals	USD 2.7 bn	70.00%	Completed
25	11/10/2010	South American Iron & Steel Corporation's Quince Iron Ore Project	Chile	Latin America	Henan Province Yukuang Xingyuan Mining	河南豫矿鑫源矿业有限公司	Iron ore	N/A	30,00%	Agreement Signed
26	10/10/2010	GlobeStar Mining	Canada	North America	Shenzhen Zhongjin Lingnan Nonfemet's subsidiary: Australia-based Perilya	深圳中金岭南澳洲子公司佩利亚	Mining	USD 182 mn	N/A	Ongoing
27	01/10/2010	Repsol's Brazilian projects	Brazil	Latin America	Sinopec Group	中石化	Oil and gas	USD 7.1 bn	40.00%	Agreement Signed
28	28/09/2010	ACL Bank	Thailand	Asia	Industrial & Commercial Bank of China	中国工商银行	Financial	N/A	19.26%	Agreement Signed
29	28/09/2010	Caspian Investments Resources	Canada	North America	CNPC	中石油	Oil and gas	N/A	50.00%	Concluded
30	17/09/2010	Continental Minerals	Canada	North America	Jinchuan Group	金川集团	Mining	USD 421 mn	100.00%	Ongoing
31	15/09/2010	Cambodia International Investment Development Group	Cambodia	Asia	Erdos Hongjun Investment	鄂尔多斯鸿骏投资公司	Power	N/A	51.00%	Agreement Signed
32	15/09/2010	Steel Development	US	North America	Anshan Iron and Steel Group	鞍山钢铁	Iron and Steel	N/A	14.00%	Ongoing
33	09/09/2010	Syria Shell Petroleum Development	Syria	Middle East	CNPC	中石油	Oil	N/A	35.00%	Gained gov. approval
34	08/09/2010	Kalahari Resources	Canada	North America	Shandong Gold Group	山东黄金	Gold	N/A	17.00%	Agreement Signed
35	07/09/2010	Haosheng Coal Mining	Mongolia	Asia	Yanzhou Coal Mining	兖州煤业	Coal	USD 980 mn	51.00%	Ongoing
36	06/09/2010	Daimler Trucks	Germany	Europe	Foton	福田	Truck	USD 411 mn	50.00%	Ongoing
37	31/08/2010	Morgan Stanley	US	North America	China Investment Corporation	中国投资有限责任公司	Financial	N/A	10.00%	Gained gov. approval
38	24/08/2010	Arrow Energy	Australia	Australia	PetroChina & Shell	中石油和壳牌	Oil	USD 3.2 bn	100.00%	Concluded
39	10/08/2010	Friede Goldman United	US	North America	Zhen Hua Engineering	中交股份的全资子公司香港振华工程有限公司	Engineering	USD 125 mn	100.00%	Concluded
40	03/08/2010	Volvo	Sweden	Europe	Geely	吉利	Automobile	USD 1.5 bn	100.00%	Concluded
41	16/07/2010	Philippines Alliance Mining	Philippines	Asia	China Daye Non-Ferrous Metals Mining	中国大冶有色金属矿业	Mining	N/A	61.00%	Agreement Signed
42	15/07/2010	African Minerals Tonkolili Iron Ore Project	Sierra Leone	Africa	China Shangdong Iron and Steel Group	山东钢铁集团	Iron ore	USD 1.5 bn	25.00%	Ongoing
43	14/07/2010	Toledo Mining Corporation PLC	Philippines	Asia	Jinchuan Group	金川集团	Nickel	N/A	N/A	Agreement Signed
44	05/07/2010	Loscam	Australia	Australia	China Merchant Group	招商局集团	Transport	USD 584.2 mn	N/A	Concluded
45	01/07/2010	AXA-Minmetals Assurance Company	France	Europe	ICBC	中国工商银行	Financial	N/A	60.00%	Ongoing

Source: Various media; Company reports; The Beijing Axis Analysis

China Shenhua: From Local Player to Global Champion

Supported by the largest and fastest growing coal market in the world, China's coal giants have progressively been gaining global market share and catching up with their foreign counterparts. China Shenhua, today the world's largest coal producer, was a pioneer of this trend. In this edition we take a closer look at this company's corporate strategy and its competitive advantages. *By Javier Cuñat*

Prior to 1978, China's coal production, sales and pricing were strictly controlled under a planned economy. In order to foster competition and promote efficiency in the industry, in the early 1980s a large number of small coal mines were established, operated and controlled by local/provincial government. Yet coal operations remained highly inefficient, required high levels of manpower and used obsolete technology. Under such conditions, domestic coal miners experienced difficulties in meeting growing demand, especially during the 1990s when industrialisation started hitting high gear in China. A solution presented itself in 1995 with the establishment of Shenhua Group, the flagship of a new, increasingly consolidated and vertically integrated corporate model for the industry.

Today, after only 15 years of the existence of Shenhua Group, the company ranks 356th in the Fortune 500 and one of its subsidiaries, China Shenhua Energy Company (CSE) is the world's largest coal producer. In 2009, the coal output of China Shenhua amounted to 210.3 million tons, coal sales volume reached 254.3 million tons and the company possessed 11.306 billion tons of recoverable coal reserves and 6.927 billion tons of sellable coal reserves. The same year, China Shenhua realised full-year operating revenue of USD 23.6 billion and profits of USD 3.37 billion.

The core advantage - Integration

Shenhua Group's vertically integrated business model is probably the company's strongest competitive advantage. Shenhua's coal business is strategically complemented by a large-scale integrated transport network (railway and port) together with an expansive power business. This has enabled Shenhua to implement a more efficient cost structure, dominate the seaborne coal trade and achieve sustainable supply despite logistics and infrastructure bottlenecks in China.

Shenhua's horizontal and vertical integration strategy was coherent with the highly fragmented nature of China's coal industry (China had around 64,000 coal mines in the 1990s, many of them being small operations). In order to generate better economies of scale, improve efficiency and bargaining power across the value chain, the government pushed for industry consolidation. This created enormous opportunities for companies such as China Shenhua, which achieved rapid growth through acquisitions in the sector. This facilitated both vertical and horizontal integration.

Horizontally, Shenhua Group started taking over the Shendong Mining Complex, the coal mining business of Huaneng. Huaneng, also state-owned and one of China's largest coal companies in the 1980s, is often considered the root of China Shenhua's success, as the latter took over many of its operations. Shenhua also acquired a number of other large-scale mining operations such as Zhunge'er Energy Company and Wanli Mines in 1998. In the 2000s, the company's expansion was further supported by ongoing industry consolidation fostered by the government, which facilitated numerous M&A deals and the shuttering of many of the country's inefficient smaller mines. This enabled China Shenhua and other large SOEs to achieve economies of scale in coal production, get rid of competition and rapidly enhance their control over prices.

Amid consolidation during the 1990s, Shenhua also started integrating vertically. By taking over Huaneng's railway and port facilities, China Shenhua was able to alleviate existing logistics bottlenecks, making coal more accessible and less regionally priced. The company also opened two additional rail lines in the 1990s (Shenshuo Rail in 1996, and Dazhun Rail in 1997), and opened its fourth leg, the Shuohuang Rail Line, in 2001. Today Shenhua operates five railways with a total length of 1,367 km, allowing it to connect demand and supply from eastern to western China.

By 2002, Shenhua had completed construction of its own port at Huanghua, an important component in the group's integration strategy. Huanghua port is the second-largest port in terms of seaborne coal transportation in China. Shenhua also operates Shenhua Tianjin Coal Dock, which together with Huanghua port enabled the company to complete seaborne coal sales of 99.5 million tons in 2009, accounting for 62.5% of the total seaborne coal sales of the company. Capacity expansion plans for both facilities are currently in operation.

Shenhua's vertical integration model was further enhanced in the late 1990s as it moved into power generation. It took over Huaneng's power generation operations and in 2000 created a dedicated subsidiary, Guohua Power, focusing on construction of power generation facilities at coal mines and ports. Today, the company controls and operates 55 units of coal-fired generators, 3 units of gas-fired generators and 21 units of wind power generators with a total installed capacity of 23,520 MW. With such a power generation business at its disposal, Shenhua was able to lower its production costs.

In order to raise funds to support the company's integration strategy, Shenhua Group carried out a major reorganisation of its holdings in the mid-2000s. In 2004, Shenhua created a new entity, China Shenhua Energy Company (CSE), which took over nearly all of the parent company's mining, transportation, and power generation operations. The restructuring

Table 1: Shenhua Coal Production, mn tons, 2006-2010E

	2006	2007	2008	H1 2009	2009E	2010E
Shendong	105.5	110.6	117.8	63.2	124.0	135.5
Wanli	4.8	16.0	27.7	18.5	39.0	47.5
Zhunge'er	23.5	25.2	29.3	18.8	44.0	45.0
Shengli	2.8	6.2	10.9	5.3	13.0	17.5
Total	136.6	158.0	185.7	105.8	219.0	245.5

Source: Deutsche Bank; Company data. Note: Production on 100% ownership

Table 2: Marketable Reserves, mn tons, 2005-H1 20009

	2005	2006	2007	2008	H1 2009	Mine life*
Shendong	3,551	3,804	4,140	4,022	3,959	31 years
Wanli	953	929	1,979	1,949	1,930	51 years
Zhunge'er	369	354	338	316	302	8 years
Shengli	872	869	863	852	847	80 years
Total	5,745	5,957	7,320	7,139	7,038	

Source: Deutsche Bank; Company data. *Mine life is determined by using marketable reserves at end H1 2009 and annualised H1 2009 production

quickly revealed itself as a prelude to a public listing of CSE, carried out in 2005 through one of the world's largest initial public offerings (IPOs) in that year.

Continuous expansion

China Shenhua is characterised by a strong production growth profile from low cost and high quality coal mines. The company's main mining assets (Shendong, Wanli, Zhunge'er and Shengli), have registered increasing production capacity on an annual basis (see Table 1 above). The company produced 219 million tons in 2009 and 246 million tons in 2010, respectively representing growth of 18% and 12% year-on-year with all four mining areas contributing to production growth. Shendong represents the largest as well as fastest growing operating asset. Shendong combines 17 mines, total production reached 149.9 million tons in 2009, almost 71.3% of the company's total production of 210.3 million tons of coal in 2009. Shenhua is also active in greenfield project development, and plans to double its capacity in only five years with two new greenfield projects (Xinjie in Inner Mongolia and Yulin in Shaanxi), each of these having the potential to produce 100 million tons per annum of high quality coal. Shenhua will also have to expand the capacity of its rail lines to Huanghua port to accommodate the added tonnage of coal.

It is important to note that most of Shenhua's mines started operation in the 1990s or later with mine-life of over 30 years (see Table 2 above). Moreover these mining assets are located in areas traditionally rich in coal. This provides room for further exploration, upgrades in reserves and additional capacity expansion in the future.

With a solid position in the domestic market and its booming demand for coal, China Shenhua has set its sights on developing overseas coal reserves. Driven by a strong balance sheet and government support, Shenhua has been actively exploring a number of opportunities outside China's borders. In Australia, Watermark was Shenhua's first overseas investment. In 2008, Shenhua paid nearly USD 200 million to acquire the exploration license for the Watermark mining area in New South Wales, where Watermark has around 1 billion tons of coal resources in an area of around 190 square kilometres. In Indonesia, Shenhua has embarked on the construction of a coal-fired power plant in the province of South Sumatra, the largest coal producing area in Indonesia. The power plant is a joint venture between Shenhua (which holds a 70% stake) and Indonesian PT. Shenhua is also pursuing opportunities in Mongolia, such as Tavan Tolgoi, the largest coal deposit in Mongolia, where Shenhua has been short-listed as a preferred bidder.

Challenges ahead

China Shenhua's financial performance, production capacity expansion and technological upgrading in the last three decades have been impressive but do not necessarily guarantee long term competitiveness. Difficult challenges lie ahead, such as rising environmental costs, tougher environmental protection regulations and enforcement, stringent energy efficiency targets, increasing production costs and local protectionism against China's consolidation plans, among others. It is uncertain how successfully China Shenhua will navigate these challenges, yet based on China's rapid economic growth, strong domestic demand and the importance of coal within China's total primary energy consumption outlook, China Shenhua can be optimistic on their long-term outlook.

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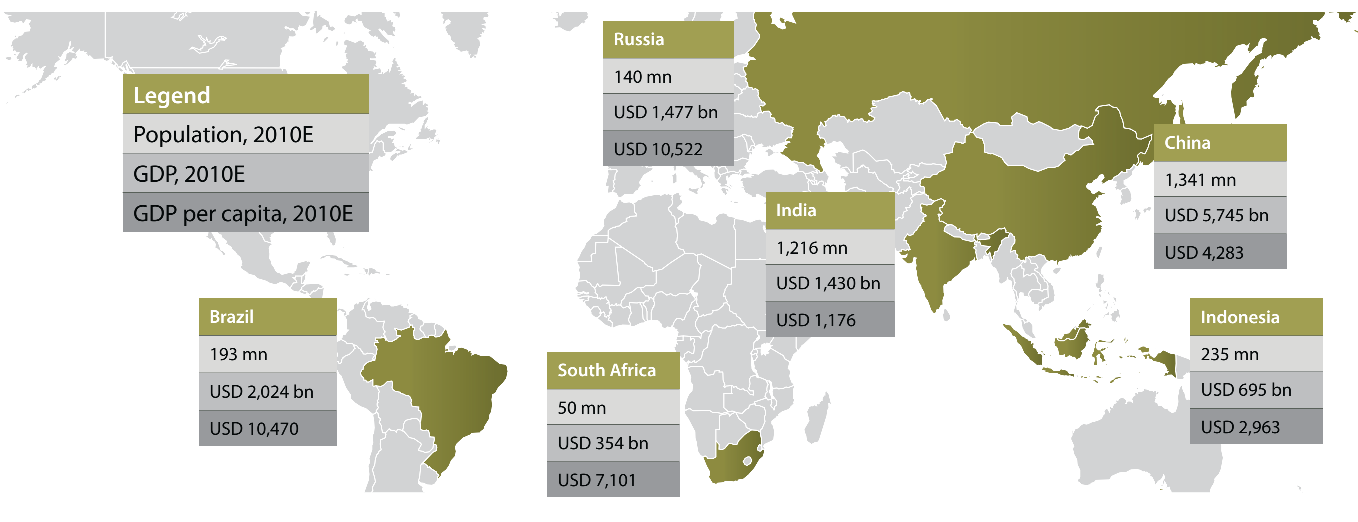
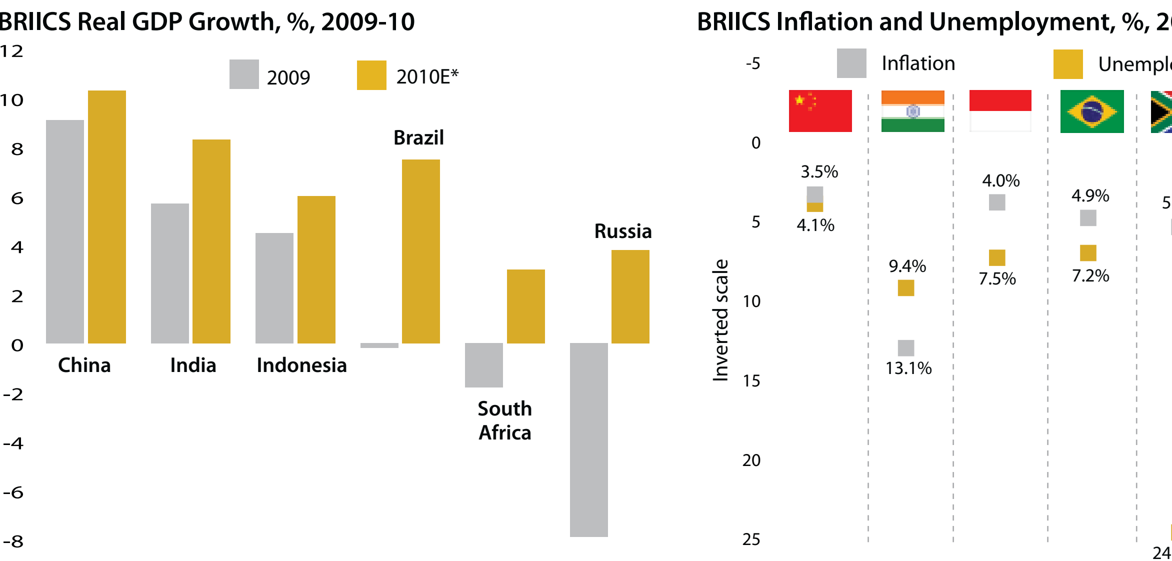
Regional Overview: BRIICS

Strong growth in Brazil, India, Indonesia and China; Russia and South Africa less dynamic but improving

- With the economy of Brazil doing so well in 2010 – with an estimated GDP growth of 7.5% – and much of the credit for this growth attributed to policies implemented in recent years by President Lula, his successor and political protégé Dilma Rousseff was elected to the position and inaugurated on 1 January 2011
- FDI inflows to Russia increased in 2010 to an estimated USD 40 bn, yet this is still significantly below pre-crisis levels. The mood among investors may be turning more upbeat, however: A UNCTAD survey found Russia to be the fifth most-popular planned investment destination for 2010-12. A first example of this new wave of investment is PepsiCo's plan to take over 66% (valued at USD 3.8 billion) of food & beverage giant Wimm-Bill-Dann, a deal which gained government approval in January 2011
- The Indian economy grew at an estimated 8.5% in 2010, fueled by sustained demand at home and increasing investment in infrastructure. The government, supported by loans from the World Bank and the Asian Development Bank, is actively promoting infrastructure investment, especially in the form of public-private partnerships
- Driven by strong global commodities demand, Indonesia experienced significant growth in exports in 2010. For the first three quarters of the year, exports grew by almost 40% compared to 2009. Realised FDI into Indonesia for Q1-Q3 2010 reached USD 16.7 bn
- In China the economy experienced continuing strong growth in 2010. Chinese investors have made significant overseas deals, primarily in extractive sectors, and OFDI soared to an estimated USD 60 bn in 2010. Labour costs are rising, however, driving potential investors elsewhere, but this is also encouraging Chinese manufacturers to move up the value chain. Consumer inflation, especially for food, and a potential housing bubble, are still the leading concerns
- The economy of South Africa grew slower in 2010 compared to the other BRIICS economies – an estimated 3%. Job creation remains a key concern and priority for the government. Driven by high global commodities demand, a weaker currency, and stagnating consumer demand at home, South Africa in 2010 experienced its first trade surplus since 2003, reaching ZAR 5 billion (USD 0.7 billion)





Source: Trading Economics; China NBS; IMF. *India, Russia, Indonesia, Brazil and South Africa are estimates based on Q1-Q3 2010 data. China figure released by NBS, Jan 2011

Source: IMF except unemployment figure for India, which is from Labour Bureau of the Government of India

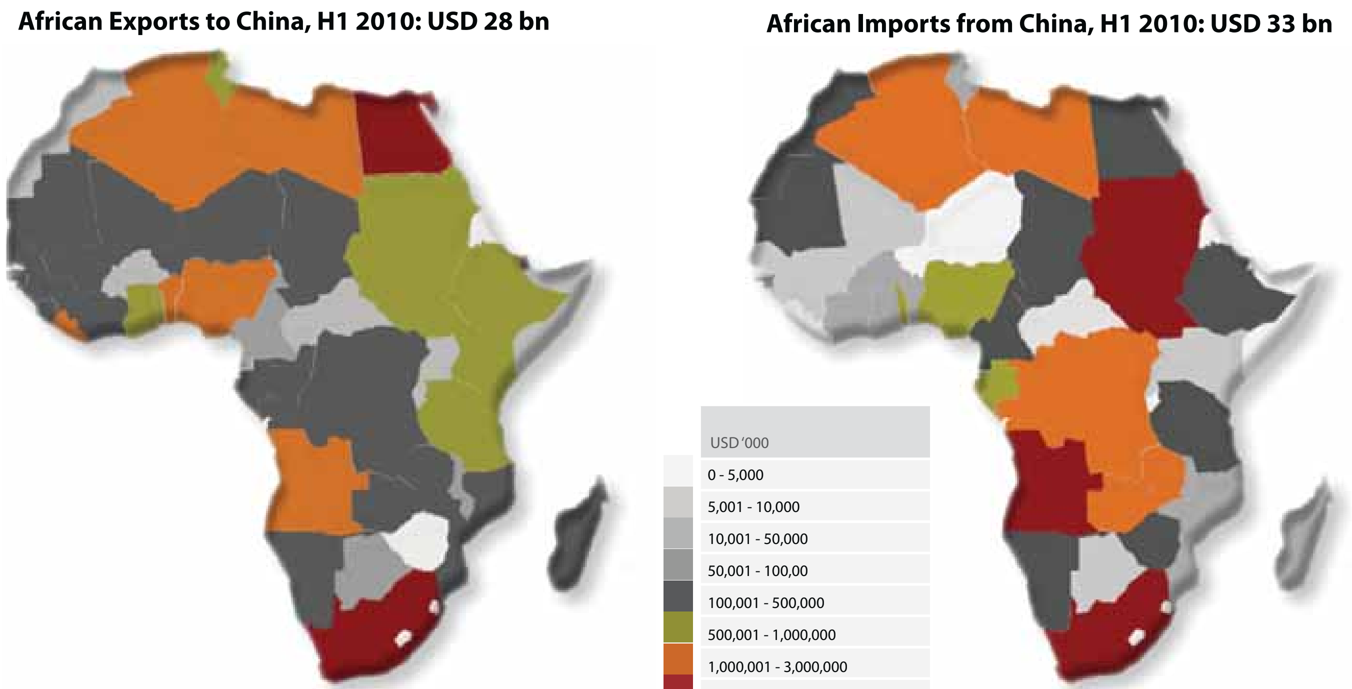
Regional Focus: AFRICA

China-Africa trade contracted by 15% in 2009 but 2010 was business as usual with full year China-Africa trade exceeding USD 100 billion. High level China-Africa delegation activity was vibrant, and with nearly 2000 Chinese companies now active in Africa, China-Africa investment is set to scale all time highs in 2011. This edition also features an in-depth assessment of China-sponsored Special Economic Zones in Africa.

China-Africa Briefing: Xi Jinping in Africa; Enhanced role for South Africa

- During October 2010, the ten-year anniversary of the Forum on China-Africa Cooperation (FOCAC) was commemorated in Beijing. Since the launch of FOCAC in October 2000, China-Africa trade has increased ten-fold, and according to a forecast from South Africa's Standard Bank, Chinese investment in Africa is likely to reach USD 50 billion by 2015, an increase of 70% compared to the level of 2009
- In November, Chinese Vice President Xi Jinping visited South Africa, Angola and Botswana. The visit was intended to strengthen existing bilateral relations and mutually beneficial cooperation between China and the three countries
- In South Africa, Mr Xi met a number of business leaders and co-hosted the fourth plenary session of the China-South Africa Bi-national Commission with South African Deputy President Kgalema Motlanthe. Following the signing of the Beijing Declaration on the Establishment of a Comprehensive Strategic Partnership in Beijing between President Zuma and President Hu Jintao in August, further agreements were signed in the areas of energy resources, banking and trade
- Other recent high level delegations between China and Africa included Vice Minister Zheng Wenkai's visit to Ethiopia in November for the Africa-China Poverty Reduction and Development Conference; a South African Presidential delegation that visited China in August; and a delegation led by the South African Minister of Transport in November
- After paying official state visits to each of the BRIC countries in 2010, South African President Jacob Zuma in late December 2010 received a formal invitation from Chinese President Hu Jintao to attend the next BRIC summit, to be held in China in April 2011

African Exports to China, H1 2010: USD 28 bn | **African Imports from China, H1 2010: USD 33 bn**



China-Africa Trade

- Exports from Africa to China in Q2 2010 were approximately USD 13 bn, bringing the total for H1 2010 to USD 28 bn. The largest contributors were South Africa (USD 4.8 bn) and Egypt (USD 3.1 bn)
- Imports to Africa from China increased in Q2 2010 by almost USD 21 bn y-o-y, bringing the total for the year to June to USD 33 bn. The three largest African importers from China were Angola (USD 12.5 bn), South Africa (USD 6 bn), and Sudan (USD 3.5 bn)
- In August, China's Ministry of Commerce launched the China-Africa Research Centre, a think-tank focused on bolstering trade relations between the two regions. The new unit will analyse key economic issues pertaining to African nations and develop theoretical frameworks for future Sino-African trade policy development

Major Chinese Investment Activity in Africa, August 2010-February 2011

Ghana:
- USD 13 bn in new loans to fund energy, agriculture and transport development
- USD 500 mn to upgrade Korle-Bu Teaching hospital in Accra
- USD 42 mn for new gold refinery in Accra
- USD 25 mn for new palm oil refinery and processing factory

Nigeria:
- CADF and China Merchant Holdings joint venture to buy 47.5% stake in container terminal operator for USD 154

Angola:
- Framework agreement signed for joint venture worth USD 2.1 bn between Liaoning Huajin Tongda Chemicals and Sonangol

South Africa:
- New solar product manufacturing plant to be built by Yingli Solar worth USD 435 mn

Ethiopia:
- New USD 67 mn leather factory opened by Chinese firm Xinxiang Kuroda Mingliang Leather Co.

Uganda:
- Agreement signed for China to build 36 km toll road from Entebbe Airport to the capital Kampala for USD 350 mn

Zambia:
- China Non-ferrous Mining Corporation (CNMC) to invest USD 4 mn to upgrade and rebuild its Luanshya Copper

Mozambique:
- China's Henan International Cooperation Group hands over 100 km section of rehabilitated road between Gazza and Inhambane

China-Africa Investment: Major recent deals

- In December 2010, the Chinese Henan International Cooperation Group handed over a 100 kilometre section of road between Gazza and Inhambane in **Mozambique**. The project was a rehabilitation of the existing road and was jointly funded by the Mozambican government and the World Bank. The project was budgeted at USD 35 mn
- In November, Chinese company Yingli Solar signed an agreement to build a solar product manufacturing plant in **South Africa** to the value of USD 435 mn. Yinli will cooperate with an as yet unnamed South African partner
- In November, the China Africa Development Fund (CADF) entered into a 40/60 joint venture with China Merchant Holdings to buy a stake in a container terminal operator in **Nigeria**. The deal is worth approximately USD 154 mn and gives the partnership a 47.5% stake in the operator
- In November, **Uganda** and China strengthened ties by agreeing to a USD 350 mn deal to build and manage a 36 kilometre toll road from Entebbe's International Airport to the capital city, Kampala. The two countries are also in the process of agreeing further grants and loans, some of which will be used to construct office blocks for the Ugandan President and Prime Minister. China is Uganda's main source of FDI
- In November, Liaoning Huajin Tongda Chemicals, a Chinese manufacturer of industrial equipment, signed a framework agreement for a joint venture with Sonangol, **Angola's** parastatal petroleum conglomerate. The deal, reportedly valued at USD 2.1 bn, awaits approval from the governments of both sides
- In November, Chinese firm Xinxiang Kuroda Mingliang Leather Co. opened a USD 67 mn leather factory in **Ethiopia**. The project was 45% financed by CADF
- In early November the **South African** Embassy in Beijing and the China International Mining Equity Exchange jointly held the China-South Africa Mining Cooperation and Development Forum in Tianjin, China. During the Forum, Vice Provincial Governor of the Limpopo Province, Peets Moroto, invited Chinese mining corporations to explore potential investments in the resource-rich region of South Africa
- In October, the Luanshya Copper Mine in **Zambia**, which is run by the China Non-ferrous Mining Corporation (CNMC), is set to invest more than USD 4 million in upgrading and rebuilding the underground mine in an attempt to improve safety and efficiency. In the August 2010 edition of The China Analyst, our China Capital section featured an interview with the Head of Investment of CNMC
- Under the auspices of CADF, Chinese investors are to inject around USD 570 mn into three projects in **Ghana's** mining, health and agricultural sector. In November it was announced that a USD 500 mn project will upgrade the Korle-Bu Teaching Hospital in the capital Accra, USD 42 mn will be used to construct a gold refinery in Accra, and USD 25 mn will be used to construct an oil palm refinery and processing factory in the Cental Region
- In September, **Ghana** signed nearly USD 13 bn worth of loan deals with China to fund energy, agriculture and transport development in the country. Combined, the loans represent the largest commitment to an African country by China. Details of the loan include a USD 3 bn facility from the Chinese Development Bank to finance development of oil, gas and agricultural projects. USD 9.87 bn from the EXIM Bank was earmarked for road, rail and dam works

Game Changers: China-sponsored Special Economic Zones in Africa and Their Impact on Economic Progress

Special economic zones (SEZ) can take on many names, mostly in the form of free-trade, export-processing development areas; although by whatever name, the single most undeniable benefit offered to host economies via the SEZ is a spillover of technology and intellectual property. In Africa, China is putting its own experience with SEZs to good use. *By guest contributor Charlie Pistorius*

Special economic zones (SEZs) can take on various shapes and sizes, yet they are in essence demarcated areas given the full gamut of official support to turn the area into an industrial hub. These zones are designed to be 'industrial estates' unto themselves. They are governed through public-private partnerships under a tailored set of commercial rules and regulations created with the purpose of maximising the mutual benefits of the respective stakeholders. The equity partners of the SEZ will be (for instance) key Chinese state-owned enterprises (usually controlling the largest proportion), the relevant local government department, and (eventually) a smaller syndicate of local firms. The experimental purpose of the zone is to create a trade and investment gateway that attract (mostly foreign) manufacturers and fosters the spread of skills and know-how out into the local economy.

Producers are attracted to settle and operate within these zones because of a range of profitable incentives – from tax exemptions, duty-free imports, lax laws governing the cost management of wages, to preferential market access. The undeniable benefit reaped by the recipient African economy hosting the SEZ, is however a much-needed spillover of technology and intellectual property.

The SEZ in theory and practice

The practical theory behind an agglomerated industrial zone is well researched and has stood the test of time. Entrepreneurial producers are given preferential treatment to establish their operations within the zone, it benefits their bottom line and creates a cluster of capacity – think Silicon Valley or the Detroit Motor City – for sharing technological innovation, management know-how, and it crucially engenders a positive feedback of competition between firms that ultimately culminates in better and cheaper costs of production, allowing producers to exploit economies of scale. In most cases, foreign firms are the key variable to inject the requisite transfer of skills, knowledge, capital, and technological means of production.

The zones are often situated near or within good transport corridors to more readily facilitate trade. Although in Africa's case (as it was in China's leading SEZ, Shenzhen, and many of those first established in Asia), the earmarked region is a wasteland, devoid of proper (or any) roads and railways, without access to sea-or-airports, lacking usable ICT connections, and perhaps most critically, without a stable and secure source of power generation.

All these infrastructural needs are addressed, however, in the design of the SEZ; if connections do exist, improvements will make them great, and in most cases where the above infrastructure networks do not exist they will be developed in full to meet modern world-class standards. The capital contribution to the zones is thus immense, and assured under a private-public partnership with both sides having a vested equity and management interest to beget complete utilisation.

Producers reap significant rewards from all the above incentives. There is also a reciprocal benefit for labour, in that people are attracted to the zones via the promise and plentiful opportunity of jobs. Although in the initial phases of SEZ development, a race to the bottom for wages allows producers to garner the most benefit – they have the luxury of choice (an oversupply of labour), and they are also allowed to pay lower than average wages.

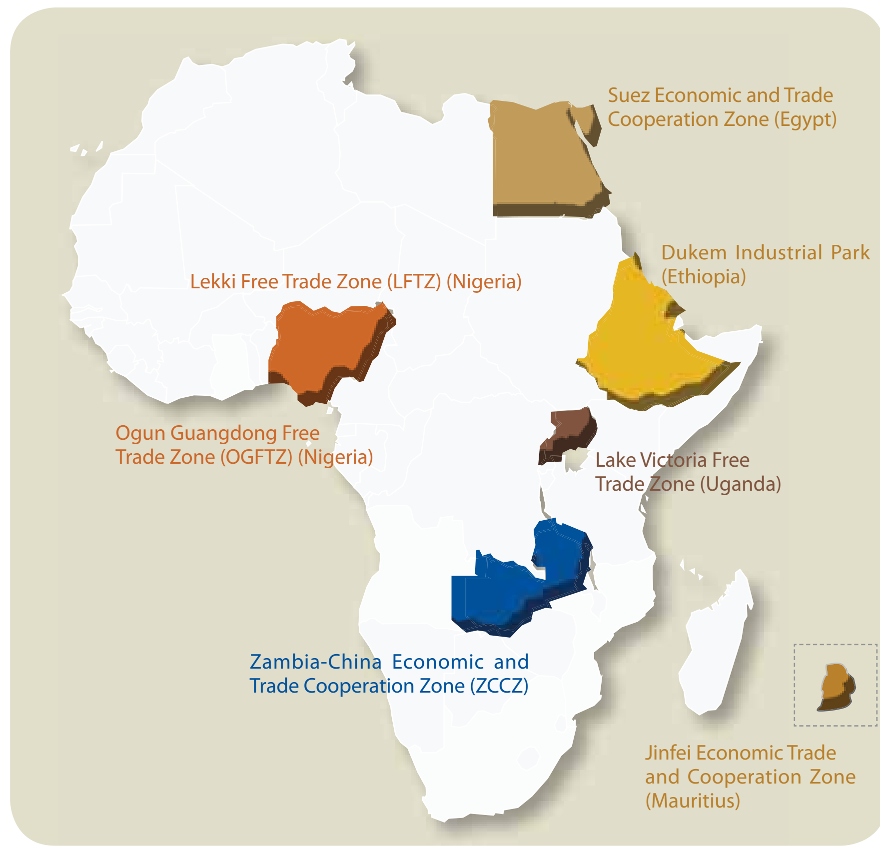
The development and growth of the SEZ cannot function without the hinterland's contribution of food and agriculture; output is increased on the back of growing demand, and with it, all manner of sophisticated agribusiness and farming support is brought in to secure supplies and the sustainable progress of the surrounding primary industry.

Yet the immediate positive impact on societal job creation is significant. The greatest social gain could be seen as that of building a community: as the SEZ moves to maturity, a concomitant township grows up around it, with dedicated social services injected - from housing, water and sanitation, to policing, schooling, medical care centres and even recreational clubs. In sum, the design of the SEZ draws in the productive effort of the domestic workforce as well as the individual capitalist.

The SEZ in China

China itself understands special economic zones (SEZ's) very well, China's own economic reform and gradual transition from a closed command-economy to a state-capitalist free-market global economy (with subsequent superlative growth) was to a large extent underpinned by the creation and success of these zone. In the early 1980s, four zones were created along the eastern coastline – Shenzhen, Zhuhai, Shantou (all in Guangdong province), and Xiamen (in Fujian province) - followed by Hainan Island as the fifth. These SEZs became areas where the government could experiment with

China-sponsored Special Economic Zones in Africa*



Suez Economic and Trade Cooperation Zone

Country	EGYPT
Size	6 km²
Planned Investment	USD 300 mn
Expected Completion	2018

This SEZ is strategically located close to European trade routes and provides direct access into Middle Eastern and North African markets. The SEZ will have an eventual USD 2.5 bn first phase investment to support manufacturing beneficiation geared towards automotive parts, logistics, textiles, and the electronics sector.

Dukem Industrial Park

Country	ETHIOPIA
Size	2-5 km²
Planned Investment	USD 700 mn
Expected Completion	2013

A 10 km² reservation area close to Addis Ababa has been earmarked for an SEZ that will be 2-5 km² in size. Beneficiation will be geared towards light manufacturing, focusing on textiles, food processing, construction and engineering materials, electrical equipment and metallurgy.

Lekki Free Trade Zone (LFTZ)

Country	NIGERIA
Size	30 km²
Planned Investment (1st Phase)	USD 820 mn
Expected Completion	2014-15 (1st Phase)

Industrial beneficiation will be geared towards light manufacturing, transport, equipment, telecommunication and home appliances. An initial USD 600 mn is being injected to establish most of the preliminary infrastructure, and the main Chinese partner and developer is the China Civil Engineering Construction Company (CCECC), which owns a three-quarter interest of the 60% share controlled by a Chinese consortium of enterprises, which includes CAD Fund.

Ogun Guangdong Free Trade Zone

Country	NIGERIA
Size	2.5 km² (Ultimately 100 km²)
Planned Investment	USD 500 mn
Expected Completion	2014-15 (1st Phase)

Located in the north of the country, beneficiation is mostly geared towards construction materials, furniture and wood processing, ceramics, ironware and electronic machinery.

China's engagement in Nigeria goes beyond resource extraction. The SEZs being set up in Nigeria will become manufacturing and assembly hubs for Chinese firms. Products will be sold domestically (in Nigeria) and then re-exported to West Africa.

Lake Victoria Free Trade Zone

Country	UGANDA
Size	300 km²
Planned Investment	USD 1.5 bn
Expected Completion	TBA

This SEZ will culminate in the USD 1.5 bn Ssesamirembe Eco-City, a 300 km² area geared towards overall industrial beneficiation.

Zambia-China Economic and Trade Cooperation Zone (ZCCZ)

Country	ZAMBIA
Size	41 km²
Planned Investment	USD 800 mn - USD 1 bn
Expected Completion	2014

The first Chinese SEZ established in Africa, ZCCZ is located in Zambia's Copperbelt region around a USD 250 mn copper smelter project. Planning already started in 2003, and up to 60,000 jobs have been created. Ancillary sectors of diamonds, tin and uranium have also received investment from Chinese firms. The Copperbelt's anchor enterprise, China's Nonferrous Metal Mining Company (CNMC), alone invested over USD 1 bn in the past decade to develop the copper-cobalt industry.

As a sub-zone of ZCCZ, a second SEZ has been established near the capital Lusaka. Only 5 km² in size, USD 350 mn has been injected to date. Beneficiation will be geared towards electronic component assembly and manufacturing, and completion is expected around 2011-2012.

Jinfei Economic Trade and Cooperation Zone (Jinfei SEZ)

Country	MAURITIUS
Size	2.1 km²
Investment to Date	USD 820 mn
Expected Completion	2012

China's second SEZ was established in the capital Port Louis as a strategically important hub in the Indian Ocean trading rim, with beneficiation geared towards light manufacturing. Up to 40 Chinese firms are expected to eventually settle in the zone, generating around USD 220 mn in annual export earnings and creating 26,000 local jobs. Manufacturers operating out of the Jinfei SEZ will enjoy a wider trading network and access to the Common Market for Eastern and Southern Africa (COMESA). Anchor investments here came from leading Chinese industrialists such as Taiyuan Iron & Steel Group, Shanxi Group, and the Tianli Group - all of whom located to Jinfei for trade, investment and tax reasons.

* Note: Discussions are currently underway for more China-sponsored SEZs in Tanzania, Mozambique, and Angola.

free-market practices, hence testing and sculpting the best method for their own system. Eventually the zones incorporated ethnic foreign ownership from Macao, Taiwan and Hong Kong, but also (an unprecedented) 100% ownership of 'other' foreigners (from US, EU, Japan etc.).

The SEZs were characterised by many tax and trade incentives to spur free trade and industrialisation. Such was the accomplishment of these zones that their experience was gradually extended (in various forms) to wider areas – encompassing fourteen other 'open coastal development cities' that spurred trade and export processing around the core manufacturing hubs of the Yangtze-and Pearl River Deltas, as well as the Liaoning Peninsula.

China-sponsored SEZs in Africa

The president of the World Bank, Robert Zoellick, recently stated that China's support for SEZs in Africa "is a very welcome initiative to expand China's investment in Africa beyond the minerals and infrastructure sectors, (and) into activities that are providing greater opportunities to create jobs." Although it is well understood among policy advisors that China must resolve local infrastructure constraints before ensuring that the zones in Africa are capable of attracting foreign investors, the ultimate hurdle (and victory in overcoming it) for China would not only be to inject the necessary infrastructure, power generation and ICT sophistication into Africa, but to show that through these zones China's enterprises can stimulate value-adding efforts. These would would include sharing and transferring knowledge and skills, creating domestic jobs, training the local workforce, and encouraging community service delivery for the future progress and maintenance of the Chinese-driven SEZs and free trade areas.

Africa's bounty of commodities make it the ideal candidate for Asian investors who have experience in managing state economies, dealing with ineffectual public institutions, being burdened by poor labour markets and shoddy handling of property rights and commercial laws. Paradoxically though, these 'inefficiencies' pave the way forward for rapid market participation and commercial opportunity – taking the view therefore that with increased economic activity the status quo can only improve.

Beijing's commercial priority and strategic interest in Africa can be better understood by scrutinising the Chinese-sponsored special economic zones already established to date or under construction (see page to the left).

SEZs and China's lasting commitment to Africa

It is useful to reflect on the fact that China's SEZ strategy in Africa emanates from its own economic reform path. The Chinese learnt from the successes and failures of various historical SEZs and applied it to the development of their own SEZs. These special economic enclaves became the leading trading hubs of the region and were the foundation for the wealthiest cities in China – Hong Kong, Guangzhou, Macao and Shanghai. China is therefore utilising what it learnt from history and its own experiences and applying these to good effect in Africa.

China is today Africa's largest trading partner as well as the largest buyer of and investor in African resources, and importantly, the most diverse player – China's trade and investment impact is expanding across all sectors. Development loans, training programmes and scholarships pledged by China to Africa under the aegis of the Forum on China-Africa Cooperation (FOCAC), moreover, provide a favourable platform for China to negotiate with African governments and secure favourable rights and allocations to precious natural resources.

In short, whether geared towards SEZs, facilitating bilateral trade, promoting job creation, commercial competition and entrepreneurial opportunity, or encouraging infrastructure development and holistic economic growth, the China-Africa model is grounded in a win-win pursuit. For instance, since 2004, Chinese enterprises alone have pledged over USD 23 bn in development aid to at least eight resource-rich African countries, with the funds being distributed directly to contractors and workers, and typically left untouched by corrupt bureaucrats. The sheer physical impact this money has on the economic progress and social confidence of the target countries is beyond comparison, and like SEZs, injects significant positive spill-overs into the local economy.

The China-Africa message is one of strong cooperation, and in stark contrast to Africa's usual dealings with the West. As Prof Deborah Brautigam, a leading Sino-African scholar states, "the West advocates trade liberalisation to open African markets; China constructs special economic zones to draw Chinese firms to the continent; Westerners [prop up] government and democracy; the Chinese build roads and dams."

China's role in Africa today is a game changer and it is most definitely not merely a myopic engagement for one-sided benefit and resource exploitation. Instead, this partnership has the makings to give Africans the hope and means to escape their resource-curse and dreaded 'forgotten' status, and hence cultivate their 'land of plenty'. By means of special economic zones in particular, China's engagement in Africa is translating into them taking a serious and long-term equity stake in Africa's future.

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Regional Focus: Australia

Sino-Australian relations experienced a challenging 2010 that was characterised by protracted iron ore negotiations, punitive resource tax measures, an unexpected leadership change and diplomatic tensions. Yet trade and investment activities remained robust with total bilateral trade for 2010 estimated to have breached the USD 80 bn mark. Despite a degree of regulatory uncertainty in Australia's mining industry, the investment climate for Chinese investment in Australia remains positive, as guest contributor Olatunji Pariola writes in this edition's longer feature.

China-Australia Briefing: Flooding in Australia and impact on China's steel industry

- Tropical storms that battered Australia's northeastern state of Queensland for protracted periods from November 2010 led to massive flooding that ruined the state's farm produce, shutting down coal mines and causing severe damage to transport systems. With coal and crop exports compromised, the overall impact on trade could be as high as USD 9 bn in lost income. The floods could also potentially trigger a rise in coal prices given reduced supplies, which would affect major coal importer China. The flooding in Queensland forced a number of mines to close and has affected Australia's output of both coking and thermal coal. As Australia is the key global seaborne supplier of these essential steel inputs, it is expected that China's steel producers may have to lower their steel production
- A rise in China's demand for food supplies has resulted in heightened interest in the Australian agricultural sector. Increased Chinese annual consumption of 4 million tons of grains, 800,000 tons of vegetable oil, and 1 million tons of meat has resulted in China purchasing more farm produce from Australia such as wheat and greater interest in Australian private farms, aggregation and processing businesses

China-Australia Trade

Total trade

- Sino-Australian trade total for 2010 is estimated to have been the largest yet with both the Australian Bureau of Statistics (ABS) and China Customs (v) data showing record levels in trade between the two countries during the first 11 months of the year. CC data put total trade at USD 78.75 bn from January to November, a 31.45% increase from the total trade figure in 2009
- Trade imbalances increased in 2010, however, with CC data showing an increase in the trade imbalance by 57.93% from USD 18.58 bn in 2009 to USD 29.34 bn in 2010 in favour of Australia. ABS data, while showing a more moderate trade imbalance of USD 15.00 bn, indicated a much more substantial increase of 204% from 2009's USD 4.93 bn

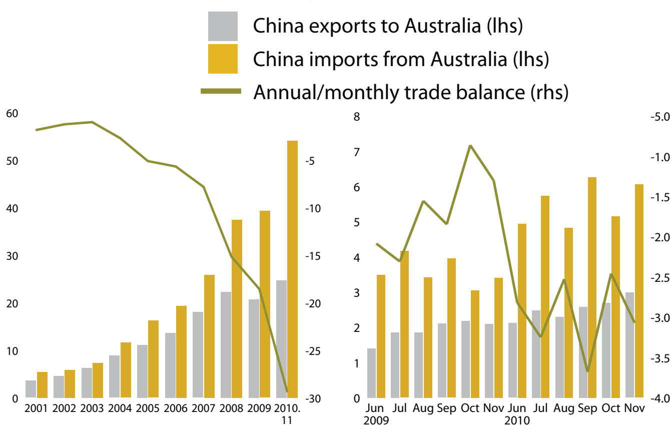
China imports from Australia

- As an indication of Australia's role as a supplier of commodities to China, ores, slag and ash remained China's leading imports from Australia in 2009, accounting for 59% or USD 23.17 bn of the total of USD 39.44 bn. Mineral fuels, oils, distillation products and copper were a distant second and third with USD 6.43 bn and USD 1.69 bn, respectively

China exports to Australia

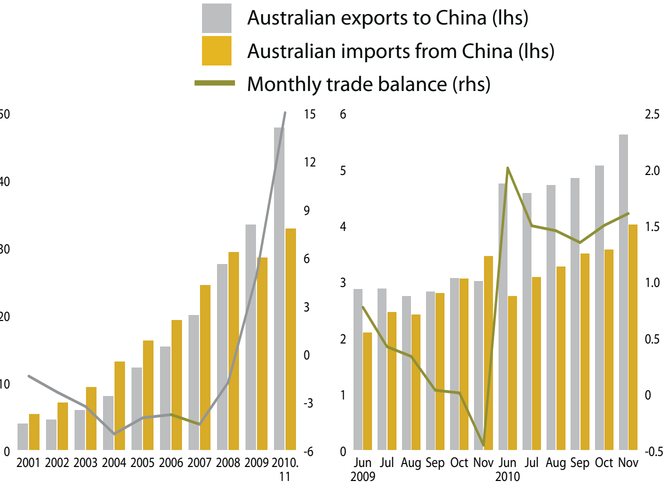
- Electrical & electronic equipment and nuclear reactors, boilers & machinery were China's leading exports to Australia, making up 19% each or USD 3.93 bn and USD 3.90 bn, respectively, out of the total of USD 20.65 bn. Articles of apparel & accessories and furniture, lighting, signs, and prefabricated buildings were the second and third-largest Chinese exports to Australia, with USD 2.17 bn and 1.34 bn, respectively

China Annual and Monthly Trade with Australia, USD bn



Source: China Customs; The Beijing Axis Analysis. Note: Balance = Chinese exports to Australia - Chinese imports from Australia, hence negative scale.

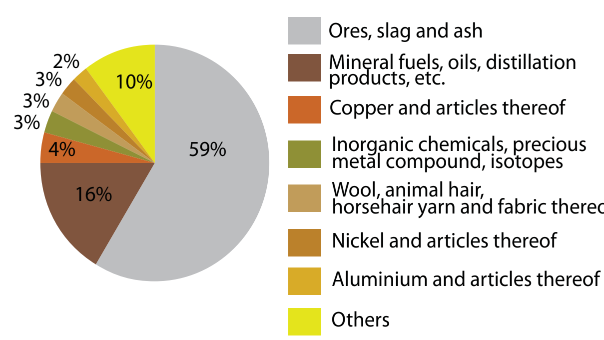
Australia Annual and Monthly Trade with China, USD bn



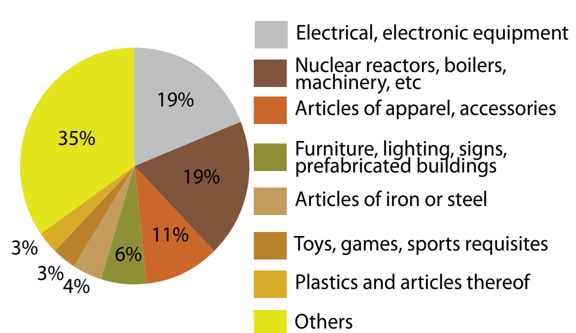
Source: Australian Bureau of Statistics; The Beijing Axis Analysis

China-Australia traded merchandise, 2009

China Imports from Australia



China Exports to Australia

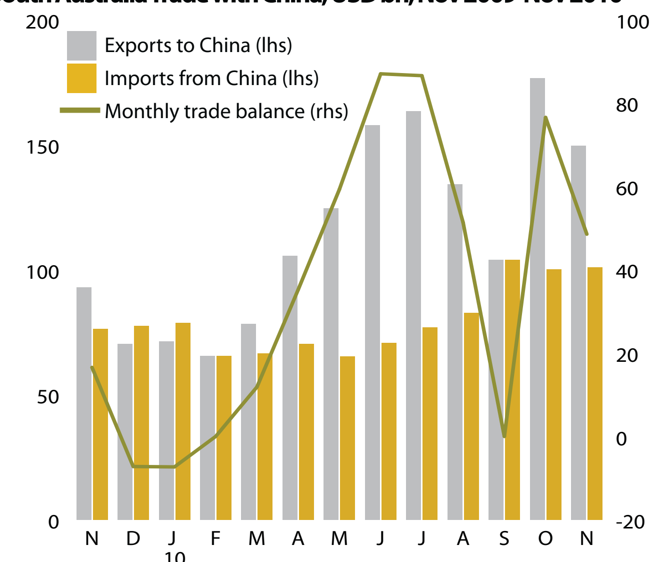


Source: UN Comtrade

State watch: South Australia

- With a real gross state product (GSP) of USD 58.15 bn in 2008-09, South Australia is Australia's fifth-largest economy
- It is a net exporter with exports of USD 7.10 bn and imports of USD 5.12 bn
- Main exports are wine, wheat and wool
- Main mineral commodities produced are copper, natural gas and uranium oxide
- Key industries as shares of GSP are manufacturing (10.7%), financial and insurance services (8.4%) and health care and social assistance (6.9%)
- In 2008-09, the US was South Australia's largest trading partner, with a total trade value of USD 1.74 bn. China was South Australia's second-largest trade partner with a total trade value of USD 1.65 bn, followed by Japan with USD 1.18 bn

South Australia Trade with China, USD bn, Nov 2009-Nov 2010



Source: Australian Bureau of Statistics; The Beijing Axis Analysis

China-Australia Investment

Major recent deals

- In March 2011, global mining giant Rio Tinto extended its USD 3.9 bn takeover offer for the Australian Mozambique-focused coal miner Riversdale Mining. On 4 March 2011, Rio Tinto disclosed that its interest in Riversdale had increased to 18.7% from the 17% disclosed earlier. Rio twice extended the deadline for its offer for Riversdale, and the latest deadline was given as 18 March after steel producers Tata Steel and Cia Siderurgica Nacional of Brazil both raised their respective holdings in Riversdale. China's Wuhan Iron & Steel Corp. (WISCO) is also interested in Riversdale, although for a minority stake. WISCO had earlier in 2010 signed a nonbinding agreement with Riversdale to take a 40% stake in Riversdale for USD 800 mn, yet this agreement expired in September
- In January 2011, China Huanqiu Contracting & Engineering Corp., a subsidiary of China National Petroleum Corporation, announced it will be purchasing a 19.9% stake in Australia's Liquefied Natural Gas (LNG) Ltd. The agreement will make Huanqiu the largest shareholder in LNG Ltd. and will give it preferential access to LNG Ltd.'s technology
- In January 2011, Australian Stock Exchange-listed Perilya, an Australian subsidiary of Chinese miner Shenzhen Zhongjin Lingnan Nonfemet, completed the acquisition of the Canadian GlobeStar Mining Corporation for USD 181 mn
- In December 2010, British-Australian diversified mining resources group Rio Tinto and China's Sinosteel Corporation agreed to extend one of the earliest mining joint ventures between Australia and China – the Channar iron ore project – in order to produce an additional 50 mn tons of iron ore from 2012 to 2017. Located in Western Australia's Pilbara region, the Channar iron ore project was initiated in 1987 and has since then supplied a total of 183 mn tons of iron ore to China
- In September 2010, the Perth-based iron ore company Cape Lambert commenced legal action against MCC Australia Sanjin Mining Pty Ltd and its parent company Metallurgical Corporation of China Limited (MCC) for failing to pay the final AUD 80 mn for its AUD 400 mn sale of the Cape Lambert Iron Ore project. MCC responded to the lawsuit by referring to the Australian company's failure to fulfil certain obligations required in the land leasing and related assets transference agreement

Ready for a Deal: The Current Australian Investment Climate for Chinese Resource Companies

As China continues to forge ahead with industrial expansion, iron ore remains an important part of its future. As a result, the investment climate between Australia and China has become ever more important. Yet how does this flood of investment actually play out on the ground? This article analyses an ongoing hostile iron ore takeover bid between a Chinese company and two Australian companies. It provides an overview of the players, the proposed bid and the rationale. More importantly, it looks at the current environment in Australia for Chinese investment and the possible factors that could encourage or hamper this flow of investment. *By guest contributor Olatunji Pariola*

The deal, the players and the rationale

Hong Kong-based Wah Nam International Holdings Ltd.'s (Wah Nam) recent bids to acquire shares in Australia's Brockman Resources Limited and FerrAus Ltd. are indicative of the growing level of interest that Chinese mining companies are showing in their Australian counterparts. Wah Nam is a Hong Kong-listed investment holding company active in the iron ore and copper industries. It is currently Brockman's largest shareholder, holding 22.63% of the issued share capital. In addition, Wah Nam is also FerrAus' largest shareholder, owning 19.8% of the issued share capital. Wah Nam also owns 90% of Luchun Xingtai Mining Company Limited in mainland China. Luchun Xingtai in turn owns 100% of the Damajianshan Mine, situated in Luchun County in China's Yunnan province. Through this subsidiary Wah Nam engages in the exploitation, processing and sales of copper ore.

Despite that both Wah Nam's bids have so far met with little success, what is most intriguing about these bids is not only their cumulative total – approximately USD 920 million - but also the audacious nature with which Wah Nam made simultaneous takeover bids for both companies. The Brockman bid was based on an all–scrip offer of 30 Wah Nam shares for 1 Brockman share, which values Brockman at approximately USD 921 million. An all–scrip offer effectively means that the buying of Brockman and FerrAus shares would have been purchased through the exchange of Wah Nam shares. This effectively amounted to about USD 6.41 per Brockman share. Similarly, the FerrAus offer is based on an all–scrip offer of 6 Wah Nam shares for 1 FerrAus share, which values FerrAus at approximately USD 265.4 million, and about USD 1.29 per FerrAus share.

Brockman and FerrAus are both representatives of an emerging group of junior iron ore producers who are gaining prominence in Australia's resource rich Pilbara region. Wah Nam's takeover bids, had they been successful, could have provided Wah Nam with an opportunity to capture great future benefits from the increased output in the iron ore industry. Iron ore production in Australia is estimated to increase to about 580 million tonnes over 2015–16, which is 29% higher than the 450 million tonnes of iron ore expected during 2010–11 period, with the increased output coming from new mining operations such as the emerging iron ore juniors in the Pilbara region. Any successful future bids like Wah Nam's would be a significant step by them towards consolidating the industry among Australia's iron ore juniors. A major challenge which most of the juniors are faced with is gaining access to complete end–to–end rail, road, port and ship infrastructure to transport their iron ore output. This leaves them with the option of either negotiating access to existing infrastructure or alternatively constructing their own infrastructure, such as railway lines. Existing railway lines are largely owned and controlled by the major iron ore producers in the industry, BHP Billiton, Rio Tinto and recent entrant Fortescue Metals Group. BHP and Rio have both been vocal about restricting other parties from using their rail, road and port access. Yet Fortescue has been more flexible with regard to negotiating third-party access and Brockman is currently in advanced negotiations with them to this effect.

Wah Nam's move to acquire Brockman and FerrAus is aimed at giving Wah Nam a significant supply of iron ore output in the Pilbara region. Brockman's flagship Marillana Project is estimated to provide 17–20 million tonnes of iron ore when production commences in 2013. FerrAus' current iron ore mining exploration assets would also increase Wah Nam's supply of iron ore output. If successful, this deal could create the fourth-largest mining company in the Pilbara, after Rio, BHP and Fortescue. However, what is the current investment climate in Australia towards Chinese investment and is it conducive for these types of deals?

All that glitters is not gold

Chinese investment in Australia has grown significantly over the past few years and this is likely to continue in the foreseeable future. Data from the Australian Embassy in China shows that Chinese investment in Australia grew by over 150% in 2009 from the previous year, with investments in the resources sector accounting for most of this increase. According to Australia's Foreign Investment Review Board 2008–09 Annual Report, China was Australia's second-largest investor during this period. Chinese investment in Australia was about USD 19.83 billion, - up 256% from the previous year - with investments in mineral exploration and development making up USD 19.58 billion. The Australian government reportedly approved 160 China-Australia deals

at approximately USD 59.4 billion. Australia's iron ore exports to China in 2009 were an estimated 266.2 million tonnes, up 45.2% from 2008. At the highest level the Australian government has indicated that they welcome Chinese investment in Australia. Yet there are certain issues that could potentially deter Chinese investors from making investments in Australia, and one of these is the perceived uncertainty of regulations in the mining industry.

The Mining Resource Rent Tax (MRRT) continues to create uncertainty within the industry. As a tax on the earnings of iron ore and coal miners, the MRRT has naturally received mixed reactions from the mining companies. The heads of major mining companies such as BHP, Rio and Xstrata Coal were at loggerheads with the government of Julia Gillard, believing that they were misled earlier in 2010 with regard to certain details of the agreement. According to a previous agreement during the Rudd government, royalties paid by the mining companies as of 2 May 2010 would be refunded. Yet under the new tax - due to come into effect in July 2012 – mining companies will have to continue paying state royalties which could be credited against their MRRT liabilities.

The perceived inability of the Australian government to provide a clear and unambiguous stance on the mining tax has led to a 'wait and see' attitude amongst Chinese investors. This uncertainty has affected Wah Nam as well. In a recent announcement the company issued a comment highlighting the level of uncertainty around the MRRT, stating that "the full extent to which the MRRT may impact the company and/or its operations is yet to be determined." Such uncertainties could cause Chinese investors to consider other investment destinations with less complex regulations in order to substitute their Australian assets. However, this is not the only issue that could affect the level of investment between China and Australia, other points to consider are notions of national security.

A 2010 Lowy Institute foreign policy poll revealed that 57% of Australians believed that their government had allowed too much investment from China in Australia. The Lowy Institute is an independent think tank conducting policy research of an economic, political and strategic nature from an Australian view point. This figure was up by 7% from the same poll in 2009. Similar sentiment has been expressed at a higher level about the loss of key national assets. A USD 2.48 billion proposed takeover bid by China Minmetals of OZ Minerals in 2009 was initially vetoed by the then Federal Treasurer Wayne Swan before he ultimately approved an amended offer. Swan cited 'national security' and the proximity of the investment to a military facility as a reason for initially rejecting the deal. Several potential China–Australia deals also fell through in 2009 before Yanzhou Coal Mining Co.'s landmark USD 3.47 billion purchase of Felix Resources.

It is estimated that 10% of deals submitted to the FIRB in 2009 were withdrawn without a ruling. In the past year more Chinese and Australian companies have been seeking clarity from the FIRB. A number of Chinese companies have raised concerns that their deals are being subjected to more stringent scrutiny by the FIRB than those of other foreign investors. As an indication of their appreciation of the need for a greater depth of knowledge of the Australian mining industry within their business, Wah Nam recently recruited a senior Australian mining executive with considerable experience.

Conclusion

The boards of Brockman and FerrAus have since put forward detailed target statements in response to Wah Nam's bidder statement, articulating why they believe the bids should be rejected. Brockman is currently in advanced negotiations with Fortescue to gain third party access to their rail, ship and port infrastructure. There is no guarantee regarding the outcome of these negotiations, yet Brockman's management – in a recent Australian Securities Exchange (ASX) announcement – indicated that they are "highly encouraged with the progress of negotiations."

FerrAus is in the process of seeking shareholder approval for a proposed capital raising of USD 35 million. If approved, this capital along with cash in hand would provide FerrAus with the opportunity to conduct a decisive feasibility study in the Pilbara region. For its part, Wah Nam has indicated that they will continue with their conditional offer for Brockman. They have also indicated that they will seek advice regarding FerrAus' decision to raise capital in light of Wah Nam's conditional offer. However, FerrAus' executive director Bryan Oliver confirmed in late January that they are in possible merger talks with Brockman. Oliver stated that he believed the merger would make sense as both parties require the transport services that BHP, Rio and Fortescue have access to.

China is and will remain a key investor and partner for Australia. Despite some of the possible factors that could encourage or hamper this trend, the current climate in Australia is one that sees Chinese investment as a viable relationship that contributes greatly to both nations. Despite the possibility that Wah Nam's bids for Brockman and FerrAus might not succeed, it is unlikely that either China or Australia will be deterred from negotiating future deals from which both nations will benefit.

Olatunji Pariola *is a management consultant for a global consulting firm. Opinions expressed in this article are those of the author.*

Regional Focus: Latin America

In 2010, China's trade with and investment in Latin America reached all-time highs, reaffirming China's importance for the region. Highlighting major recent China-LatAm trade and investment events, in this edition we turn the spotlight on China's bilateral trade and investment relationship with Colombia, including an interview with Alejandro Ossa Cárdenas, Director of the Colombian Commercial Office in Beijing.

China-LatAm Briefing: Strengthened political relations; New leadership in Brazil

- In November 2010, a visit to Argentina by China's farm minister helped mend relations strained by a recent Chinese boycott of Argentine soy oil, highlighting Beijing's drive to bolster trade ties with a major global food exporter
- Also in November, Brazil elected its first female president, Dilma Rousseff, from the Workers Party. Dilma Rousseff will inherit a robust economy yet will have to face the consequences of increased spending and rising public debt to fuel consumer spending and provide subsidized loans to public and private companies. The new president is set to make her first official visit to China in April 2011 during the BRIC summit scheduled to take place in China
- China and Costa Rica signed a cooperation agreement in November 2010 for the construction of the National Stadium in the Costa Rican capital San Jose, to be paid in full by China. The technological cooperation and economic agreement is the fourth signed between the two countries since the establishment of diplomatic relations in 2007. Future projects between China and Costa Rica also include the construction of a four-lane highway between San Jose and the port city of Limón. Trade between China and Costa Rica in 2009 reached USD 3,180 million, 10.8% higher than in 2008
- In October 2010, the Fourth Latin America-China Business Summit was held in Chengdu in China's Sichuan province. At this year's event it was announced that Inter-American Development Bank (IDB) had signed an agreement worth USD 200 million with China Exim Bank to support trade activities in Latin America. IDB also agreed with China-based Alibaba, the world's largest electronic trading platform, to promote SME trade between China and Latin America

China-LatAm Trade

Total trade

- In 2010, China's total bilateral trade with LatAm reached around USD 183 bn, far exceeding the total amount of 2009 of USD 107 bn (see chart below). Brazil and Chile were China's largest trade partners in the region
- In 2004, Hu Jintao predicted that China-LatAm trade would reach USD 100 bn in 2010 (compared to USD 12.6 bn in 2000), yet that goal was already achieved in 2007

China-LatAm Trade, 2003-2010, USD bn

China exports to LatAm
China imports from LatAm

0 20 40 60 80 100

2003 2004 2005 2006 2007 2008 2009 2010

Source: China National Bureau of Statistics

China imports from LatAm

- China's total imports from LatAm in 2010 amounted to USD 91 bn
- Approximately 90% of LatAm's exports to China in Q3 2010 emanated from just four countries: Brazil (41%), Chile (23.1%), Argentina (15.9%) and Peru (9.3%)
- Brazilian oil exports to China averaged 241,000 barrels/day (b/d) in September 2010, up 32% y-o-y. Sales from Latin America's biggest economy to China averaged 183,000 b/d in 2010, over double the 2009 average of 78,000 b/d. LatAm supplied China with 8% of its oil consumption in 2010 through September
- Chilean mineral exports to China totalled USD 2.96 bn in October, equivalent to 58% of the country's total exports for the month. Copper exports amounted to USD 2.59 bn in October, up 2% y-o-y. The increase was principally due to the higher copper price, which was 22% higher y-o-y. The copper price averaged USD 3.761/lb (pound) in October 2010, mainly underpinned by strong demand from China and recovering consumption in Europe

China exports to LatAm

- China's total exports to LatAm in 2010 reached USD 92 bn, far exceeding the USD 45.57 bn of 2009
- Bolivian imports from China in Jan-Sep 2010 increased by almost 39% y-o-y, increasing from USD 262.58 mn to 364.79 mn
- In Jan-Nov 2010, Peruvian imports from China totalled USD 4.6 bn, growing 58.1% y-o-y. Cell phones, computers, motorcycles, colour television sets and telecommunication apparatus were the main import products

China-LatAm Investment

Trends

- In 2004, Hu Jintao predicted that LatAm would receive USD 100 bn in foreign investment by 2014. Until 2009, China's investment in the region had reached around USD 30 bn. In 2009, less than 1% of foreign direct investment received by Latin America came from China
- In 2010 there was a significant change in this scenario, however, with Chinese investment in LatAm reaching an all-time high. Nine operations totalling USD 22.74 bn were announced during the first ten months of the year covering the extraction of metals and oil, the steel and automotive industries as well as the installation of high voltage power networks

Major recent deals

- In February 2011, China Petrochemical Corp. (Sinopec) announced that it had completed the takeover of the US oil company Occidental Petroleum Corp.'s (OXY) **Argentinean** subsidiary. Sinopec reached agreement with OXY on the USD 2.45 bn deal on 10 December 2010, marking the Chinese oil major's expansion in oil and gas exploration in Argentina. The transaction will give Sinopec access to 23 oil and gas blocks
- In December 2010, Bridas Corp., which is 50% owned by China National Offshore Oil Corporation (CNOOC), completed the acquisition of a 60% stake in Pan American Energy, **Argentina's** second-largest oil company, in a deal worth USD 7 bn
- In November, **Brazil's** Embraer, the world's fourth-largest plane maker, signed a USD 1.5 bn aircraft finance agreement with Aviation Industry Corp. of China (AVIC) Leasing Company to help boost sales in China
- In November, Perusat, a **Peruvian** telecoms operator acquired by ChinaTel in March 2009, signed a contract with Chinese company ZTE in which ZTE became the exclusive supplier of infrastructure equipment, consumer terminals, and engineering and management services for Perusat's wireless networks. The value of the contract is expected to be USD 48 mn over the next seven years
- In November, a new joint venture was formed between **Ecuador's** state-owned oil company Petroecuador, which will have a 60% stake, and China's Sinopec International Petroleum, a subsidiary of Sinopec Group, which will have the remaining 40%. The new company will be financed with USD 1 bn
- In October, Repsol, the Spanish oil company, sold a 40% stake in its **Brazilian** unit to Chinese oil giant Sinopec for USD 7.1 bn. The purchase was the largest acquisition in the sector in the country and the second-largest ever made by a Chinese oil company
- In September, Chinese auto maker Chery Automobile Co. announced it will invest around USD 400 mn to build its first production plant in **Brazil**
- **Chile's** second-largest bank, Banco de Chile, in August signed a USD 100 mn, five-year loan agreement with China Development Bank (CDB). The loan, the second signed between the two banks, aims to provide financing for Banco de Chile's customers doing business in China

China-LatAm Country Watch: Colombia

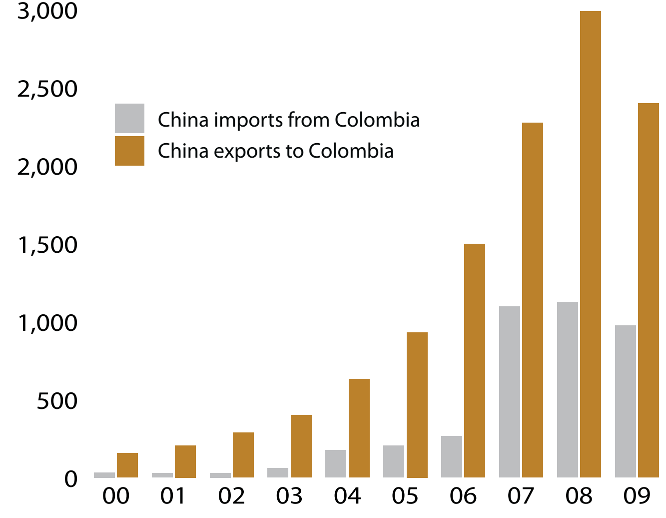
Brief country profile

- Colombia is the fifth-largest economy in Latin America with a GDP of USD 232.4 bn (2009) and a GDP per capita of USD 5,126
- Colombia's economy grew by 2.7% in 2008 and 0.8% in 2009. Growth in the first three quarters of 2010 was 4.5%, 4.4%, and 3.6%, respectively

China-Colombia bilateral ties

- In 2010, Colombia and China celebrated 30 years of bilateral relations
- In 2009, China replaced Venezuela as Colombia's second-largest trading partner
- China's total trade with Colombia reached USD 3.37 bn in 2009, a decrease of 14.08% y-o-y, yet bilateral trade between the two countries has been growing at a compound annual growth rate of 33% since 2000
- Colombia's total exports to China in 2009 amounted to USD 950 mn, or 3% of Colombia's total export market
- China's imports from Colombia decreased 13% y-o-y to approximately USD 950 mn. In 2009, 64% of China's total imports from Colombia were mineral fuels; 54% were oils and distillation products; 35% were iron and steel and 3% were copper and articles

China Trade with Colombia, USD mn, 2003-2009



Source: UN Comtrade; Beijing Axis Analysis

- Colombia imported USD 2.39 bn from China in 2009, representing a 20% decrease y-o-y. Colombia's imports from China mainly consisted of electronic equipment (which represented 44% of total imports), machinery and nuclear equipment (22% of total imports) and articles of iron or steel (5% of total imports)

Ready for Business: Expanding Colombian Commercial and Investment Ties with China

Alejandro Ossa Cárdenas is Director of the Colombian Commercial Office in Beijing. He is committed to enlarging the commercial and investment relationship between China and Colombia, which in 2010 celebrated its thirtieth anniversary. He told The Beijing Axis' LatAm Desk chief Javier Cuñat exactly how he goes about doing this.

Alejandro Ossa Cárdenas, Director of the Colombian Commercial Office in Beijing.

When did bilateral relations between China and Colombia commence and how have they advanced to the present stage?

In 2010 we celebrated the thirtieth anniversary of diplomatic relations between Colombia and China, which was first established in 1980. Since then, there have been regular bilateral agreements and exchanges of high-level visits. The last six years have seen rapid growth in these activities as China increased its focus on Colombia as part of its strategy of strengthening cooperation with Latin America.

What is the current commercial situation between China and Colombia?

Ten years ago, Colombian bilateral trade with China amounted to less than USD 100 million, yet by 2010 this figure had increased to approximately USD 2 billion, representing an amazing pattern of growth. Exports from China to Colombia have also been increasing at a tremendous pace. About ten years ago, the products Colombia imported from China consisted mostly of clothing. Yet over the years China made substantial progress in moving up the value chain, and nowadays Colombian imports from China mostly consist of telecommunication devices, computers, vehicles and machinery.

Since 2010, China is Colombia's second-largest trade partner, after the US. We are very glad and willing to continue supporting such imports from China because they provide Colombian companies with the means of accessing reliable technology at more affordable prices, which in turn contributes to the development of Colombian production capabilities.

Commodities used to be the main push factor of Colombian exports to China in the period before 2009, when oil and coal was not a major part of our commerce. Yet in 2010 we exported nearly USD 900 million in oil and USD 400 million in coal. Currently Colombia's trade deficit with China stands at USD 2 billion, but the deficit amount has been steadily decreasing. Five years ago, for each dollar Colombia exported to China, five dollars were being imported. Now this ratio stands at about one dollar to two.

Our challenge is to place less emphasis on commodities and more on value-added products. One of our main objectives in China right now as far as exports are concerned is to concentrate on agriculture and agro-industrial products, an area in which Colombia is in the process of developing a viable strategy.

The tremendous growth of Brazilian agriculture in the past ten to fifteen years has served as a roadmap to assist us in finding the appropriate approach for our country. Colombia possesses more than 10 million hectares of land available for the cultivation of agriculture. This land is available right now, without the need to fell one single tree.

What are currently the main opportunities and challenges for Chinese investors seeking to compete in Colombia?

Colombia sees a range of opportunities for Chinese small and medium sized enterprises that could benefit from the Latin American country's strategic location - it is located less than four hours from the US - and preferential market access to more than 1.2 billion consumers all over the world due to free trade agreements. Colombia also has a growing and flexible labour force and world class services for investors provided by Proexport, Colombia's investment promotion agency.

Colombia's interest in China is part of a broader programme of productive transformation to promote the flow of foreign capital that so doing ensures the transfer of new technologies and the modernisation of the economy. By carefully analysing global opportunities and local strengths, we have identified potential world class sectors in need of attracting foreign and domestic capital.

In some of those sectors, like for example automotive, textile and fashion design, graphic communication industries and electric power, Colombia has already reached a very competitive position. A good example of this is Colombia's hydro-electrical potential, which represents very lucrative opportunities as Colombia has already become a supplier of energy to a number of its neighbours.

But the need for investment has also been identified in new and emerging sectors like business processing and offshoring, IT services, cosmetics and health tourism. In cosmetics, for instance, Colombia holds the world's second-largest amount of species of plants and has a workforce of more than 200,000 professionals and 30,000 technicians available to work in that field.

What are the main new opportunities and challenges for Colombian companies doing business in China?
In terms of commodities, Colombia is currently doing very good business in China. However, looking at further potential options on the export level, the best opportunities are clearly going to lie in finding ways to produce products to meet the needs and tastes of the Chinese people.

As China modernises, Chinese people have started to consume products that conform to new habits. Milk, for example, is not a product that was historically entrenched in the Chinese diet, yet we are starting to observe an increasing level of importance attached to this product in the daily consumption habits of Chinese consumers.

The same thing has happened with wine. It took only a decade for China to become one of the largest wine consumers in the world. There is a similar story with coffee, chocolate and many other products. Therefore our job is to combine our efforts with Colombian companies and find the products that represent the greatest potential in China.

How do you see China-Colombia trade and investment relations going forward in the next decade? What is the strategic fit between China and Colombia?
Our government is increasingly seeing China as an ideal platform to reach an audience not only of professional investors, but also of very open and curious new consumers. Foreign direct investment and Chinese domestic consumption will be very important components of Colombia's agenda for growth in the long term. The Colombian government is considering the opening of more commercial offices around China in order to be closer to the most lucrative market opportunities.

Anhui Hongling:
Latest Chinese Investor in Colombia

After more than a decade of successfully exporting utility metres to LatAm, Anhui Hongli Intelligence Metering Device Equipment Co. Ltd. (a subsidiary of Hongling Group), in 2010 announced plans to build its first manufacturing plant in Colombia. Earlier in the year, Hongling had signed a joint venture with a Colombian partner for building Hongling's first LatAm manufacturing plant in the south-west of Colombia, the construction of which has already commenced. With a planned initial investment of USD 5 million, new plant will produce power, gas and water metres as well as LED lamps, and is expected to create 260 new local jobs. The plant will manufacture around 1 million metres annually and annual revenue is estimated at USD 20 million.

Hongling's decision to build in Colombia was the result of a proposal from Guillermo Osorio, Chairman of MTE SA-CI (Verifylab), a Colombian certifier and distributor of utility metres with a 10% stake of the Colombian market and long-time importer of equipment from Hongling. Hongling's strong relationship with Verifylab encouraged it to seek further opportunities in LatAm. In the words of Hongling president Lin Lusheng, "Before our business relationship with Colombia we had very little information about the country. But our assessment is very different now. Our partners are hospitable and sincere, as is the Colombian population at large."

According to Hongling's president, the Latin American market is very attractive to Chinese companies: "The standard of living on the continent is similar to China's, but there is a gap in terms of productivity and manufacturing. Chinese investment in the region will boost individual development in Latin America, while Chinese firms will take advantage of huge business opportunities."

He acclaimed the support provided to his company from the Colombian side: "The regime and the location of the Free Trade Zones are very favourable and the Colombian government helped us during the evaluation phase to understand the investment policies and initiatives, which gave us even more confidence in the project."

Hongling joins an increasing number of Chinese firms that have become active investors in Colombia. Other Chinese firms operating there include telecom and equipment manufacturers Huawei and ZTE, airport operator Capital Airports Holding Company (CAH), and oil giants Sinopec and Sinochem.

Regional Focus: Russia

Bilateral trade between China and Russia returned to pre-crisis levels in 2010, exceeding USD 55 billion. Russia is eager to attract Chinese investment in sectors such as energy and telecoms, while China seeks to secure long-term oil and gas supplies from Russia. In this edition's longer feature, Nikita Popov writes about China Investment Corporation's investment in the secondary public offering of Russia second-largest bank in February 2010, potentially the beginning of a new trend in Chinese investment in Russia.

China-Russia Briefing: High-level visits; Direct currency trading and an imminent gas price deal

- In November 2010, China's Premier Wen Jiabao undertook an official visit to Russia and Tajikistan. During high-level talks at the Gorky Residence outside Moscow on 24 November, the Chinese Premier announced the signing of 19 new deals between Chinese and Russian companies, collectively worth around USD 8.5 billion
- China and Russia have agreed to allow their currencies to trade against each other on spot inter-bank markets. The opening of direct trading was scheduled for 15 December 2010
- The European Union has backed Russia's entry to the World Trade Organization (WTO), clearing the way for Russia to join the trade body in 2011. China and India's foreign ministers also indicated their support for the move, according to a joint statement after a meeting of ministers of the three countries on 15 November
- China and Russia are expected to reach an initial agreement on natural gas pricing in early 2011. State energy firms China National Petroleum Corp. (CNPC) and OAO Gazprom have been locked in tense negotiations since 2006 regarding pricing for the 70 billion cubic metres of natural gas that Russia plans to supply annually to China

China-Russia Trade

Total trade

- Bilateral trade between China and Russia has returned to levels achieved prior to the global financial crisis, exceeding USD 55 bn for the full year 2010, an increase of 43.4% y-o-y

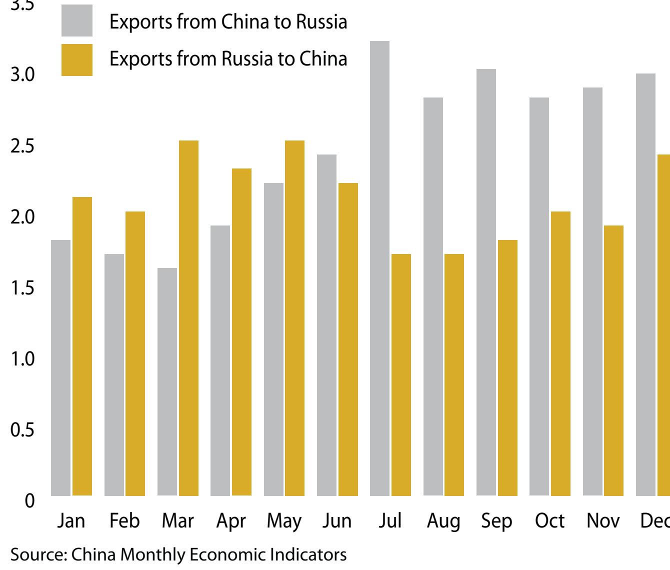
China imports from Russia

- Russia's exports to China in December 2010 amounted to USD 2.47 bn, up 26% y-o-y
- Russia's exports to China for the whole year 2010 amounted USD 25.8 bn, a y-o-y increase of 21.4% y-o-y

China exports to Russia

- China's exports to Russia in December amounted to USD 2.97 bn, an increase of 42% y-o-y
- China's exports to Russia for the whole year 2010 amounted USD 29.61 bn, an increase of 69% y-o-y

China-Russia Monthly Trade, USD bn, 2010



Source: China Monthly Economic Indicators

China-Russia Investment

Trends

- China's Outbound FDI flow to Russia in 2009 reached USD 348 mn, a decrease of 12% y-o-y
- China's Outbound FDI stock in Russia in 2009 reached a total of USD 2.22 bn, an increase of 20% y-o-y

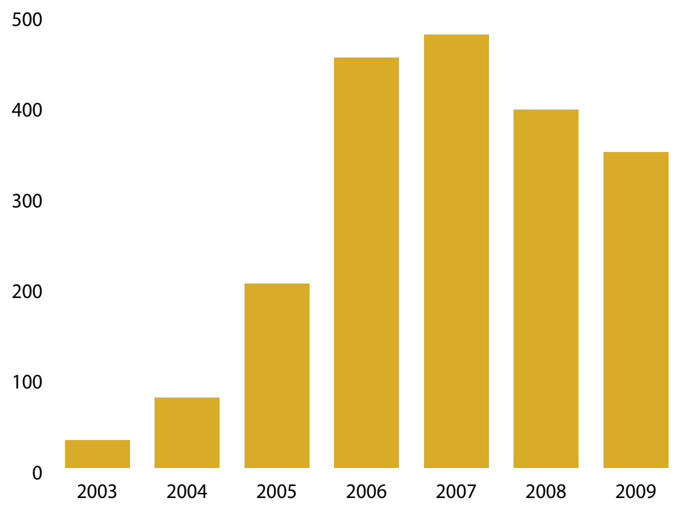
Major recent deals

- In February 2010, VTB, Russia's second-largest bank, launched a Secondary Public Offering (SPO) at the London Stock Exchange, raising USD 3.3 bn for 10% of its shares. China Investment Corp. invested USD 100 mn in VTB, the largest Chinese investment into the financial sector of the Russian economy (see longer feature on page 54)
- United Company Rusal, the world's largest aluminium producer, announced in November it had agreed to acquire a 33% stake in Shenzhen North Investments, a subsidiary of Norinco. Rusal also announced the creation of a joint venture in Russia with Norinco to produce aluminium alloys
- In November, the Russian investment bank Metropol signed an agreement with Metallurgical Corporation of China to build a mining and processing complex in Siberia. Construction of the plant is estimated at USD 1.33 bn
- Also in November, Russia's biggest lender Sberbank and the Export-Import Bank of China agreed to open a USD 2 bn credit line to finance joint projects

Major recent deals (cont.)

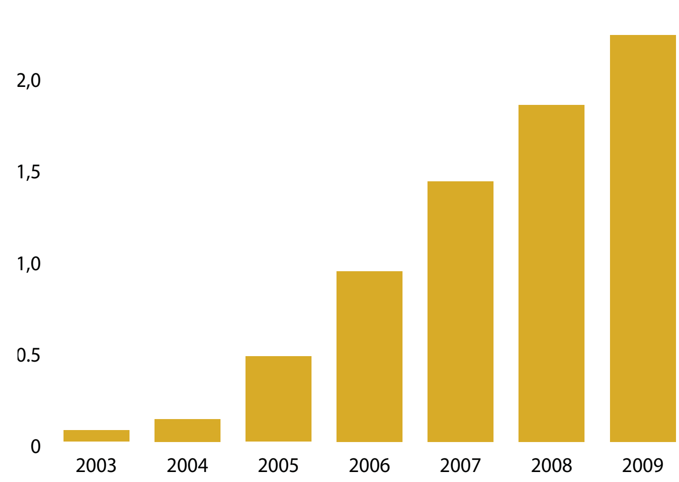
- In November 2010, the State Grid Corp. of China and Russia's Eastern Energy Co. signed an electricity supply contract for 2011. According to the agreement, electric power will be delivered to China via the existing inter-state 110 kV line from Blagoveschensk to Heihe and the 220 kV line from Blagoveschensk to Aygun. In order to increase Russian exports of electric power to China to a target of 60 billion kWh annually by 2020, Eastern Energy Co. plans to construct new generation facilities with aggregated capacity of 10,800 MW as well as AC and DC power transmission with a total length of over 3,000 km
- Also in November, China National Petroleum Corp (CNPC), the largest state-owned petroleum company in China, signed a memorandum of understanding with Rosneft to broaden cooperation between the two firms in the areas of exploration and development of oil and gas fields. CNPC and Rosneft also plan to jointly consider opportunities for acquisition of new assets for Vostok-Energy company, a joint venture between CNPC and Rosneft for operations in Russia in the upstream sector in which Rosneft has a 51% stake and CNPC, 49%
- In October 2010, another Chinese energy company, Shenhua Group, signed a memorandum of understanding with Russia's Inter RAO UES to conduct a study on the construction of a coal-to-liquid plant in Russia

China Outbound FDI Flow to Russia, USD mn, 2003-2009



Source: China Commerce Yearbook 2010

China Outbound FDI Stock in Russia, USD bn, 2003-2009



Source: China Commerce Yearbook 2010

China-Russia Resources Watch

China's new Siberian source of iron ore; Supply agreements

- China's coal imports from Russia are estimated to have exceeded 12 million tons in 2010, according to an announcement made by Chinese Vice Premier Wang Qishan during a Sino-Russian energy dialogue in St. Petersburg in November 2010
- China National Petroleum Corporation (CNPC) has announced that a test run of a 65 km cross-border pipeline was successful. The Sino-Russian crude oil pipeline was scheduled to commence operations at the beginning of 2011. The project is expected to become the most efficient and cost-saving crude oil pipeline from Russia to China ever launched. CNPC's partner for the project is Rosneft, Russia's largest oil company
- In November 2010, CNPC signed an agreement with Sovcomflot, a Russian maritime shipping company specialising in petroleum and liquefied natural gas shipping. The agreement includes delivery of transit batches to China of hydrocarbons as well as transportation of oil and gas from Russian Arctic fields to China. The agreement, signed by the CEO of Sovcomflot and the President of CNPC in St. Petersburg on 22 November 2010, forms part of a long-term partnership strategy between the two firms which also includes the construction of two large-capacity VLCC tankers of 320,000 dwt each for Sovcomflot, as well as cooperation on quality and safety standards and maritime specialist training. The two VLCC tankers will be constructed by Bohai Shipbuilding Heavy Industry Co.
- China National Electric Engineering Co. Ltd. has commenced construction of a USD 400 million iron ore dressing plant in the Evreyskaya Autonomous Oblast, 7 km from the Trans-Siberian Railway. With capacity of 10 million tons of iron ore and 3.2 million tons of iron ore concentrates annually by 2013, the plant is set to become an alternative source of supply for China, which imports large amounts of concentrates from abroad
- In November 2010, one of Russian largest mining-metallurgy holdings Metalloinvest signed an agreement with China's Baosteel for supplies of 2 million tons of iron ore and pellets in 2011, with a preliminary total value estimated at USD 320 million. Under the conditions of the contract, prices will be adjusted on a monthly basis. Delivery will be via maritime and railway transport, the expenses of which are included in the contract. Overall, Metalloinvest's iron ore supplies to Baosteel have risen sharply: in 2009 the Russian company supplied 420 thousand tons, and in 2010 over 550,000 tons

Branching Out: CIC's Interest in VTB's Secondary Public Offering

Russia's second-largest bank, the state-owned VTB, launched a secondary public offering (SPO) at the London Stock Exchange in February 2011, attracting attention from large institutional investors from Europe, the US, Russia and Asia. China Investment Corporation (CIC), one of the world's largest sovereign wealth funds, was also interested, and its investment in VTB turned out to be one of its largest ever in the Russian economy. *By Nikita Popov*

On 16 February 2011, VTB placed 10% minus 2 of its shares on the London Stock Exchange (LSE), allowing the Russian government to raise RUB 95.7 billion (USD 3.3 billion). Major investors were Italy's Assicurazioni Generali, Texas Pacific Group Capital (TPG) from the US, and the China Investment Corporation (CIC). CIC's participation in VTB's SPO is particularly noteworthy since it was one of the largest investments into the Russian economy by Chinese institutional investors, and the largest one in the financial sector.

'People's IPOs'

In 2006, the Russian government commenced with implementation of plans to privatise the largest state-owned companies. The intention was to attract not only large institutional investors, but also provide access to company shares for individual investors, i.e. common citizens. The purpose of this was to enlarge the share of retail investors in Russia, and also to distinguish in the public eye the current phase of privatisation from the chaotic sell-out in the 1990s, when a small group of entrepreneurs gained control over assets worth hundreds of billions of dollars. In 2006, Rosneft, Russia's largest oil company, was the first to go through this kind of public offering, so-called 'Peoples IPOs'. Sberbank and VTB, Russia's largest and second largest banks, respectively, followed suit in 2007.

The first round for VTB occurred in May 2007 when it launched an IPO, placing 22.5% of its shares on the London Stock Exchange (LSE) and Moscow Interbank Currency Exchange (MICEX). VTB was able to raise USD 8 billion, and the bank's capitalisation after the IPO amounted to USD 35.5 billion. The largest investor at that time (purchasing around 5% of the placed shares) was the Singaporean sovereign investment fund Temasek Holdings. The Russian government's share decreased to 75.5%. In 2009, however, the government decided to buy back 10% of the shares in order to help VTB cope with repercussions of the financial crisis.

VTB's secondary public offering (SPO) thus occurred in February 2011. With this SPO, the bank became the first company to participate in the second stage of the Russian government's plan for the divestiture of important state assets, scheduled for 2011-2013. The underwriters were Merrill Lynch, Deutsche Bank and VTB Capital. The SPO allowed VTB to raise USD 3.3 billion, and the Russian government share dropped to 75.5% once more. More than half of the SPO shares were purchased by European investors, 20% were purchased by investors from the US, 15% went to Russian investors, and the rest to investors from Asia. Major companies and funds that bought shares were the Italian Assicurazioni Generali (invested USD 300 million), TPG from the US (USD 100 million) and CIC from China (USD 100 million). This investment by CIC was the largest Chinese investment in the non-energy sector of the Russian economy so far.

CIC and Russia

CIC is a sovereign wealth fund that manages part of China's foreign exchange reserves. It was established in 2007 with around USD 200 billion of assets under management, making it one of the world's largest sovereign wealth funds. So far, CIC has mainly concentrated on investing in the power, energy and resources sectors. The company's Russian investments were no exception. CIC's first major investment in Russia dates back to 2009 when it purchased 45% of oil company Nobel Oil for USD 300 million. CIC's second attempt to make a large investment in a Russian company occurred at the beginning of 2010 during Rusal's IPO on the Hong Kong Stock Exchange. CIC planned to invest USD 300 million buying 10-15% of the total placement of shares of the Russian aluminium giant, yet at the very last moment CIC decided to cancel the investment, considering the deal too risky.

This time with VTB, CIC acted more resolutely. One of the reasons for this may be the fact that CIC was already familiar with VTB. In December 2008, VTB invited CIC and China International Trust and Investment Corporation Securities Co. (CITIC Securities Co., Ltd) to Moscow. A wide range of issues was discussed during the meetings, covering the current condition of the Russian economy, and prospects for expanding cooperation between the Russian and Chinese companies, including cooperation in the securities markets.

The CIC investment in VTB may be the beginning of an interesting trend of Chinese interest in assets outside the traditional focus area of Russia's resource sector, specifically in the banking sector. So far, Chinese companies have cooperated with Russian banks mostly in the form of granting credit. Some of the major deals so far was the USD 500 million credit extended by China Development Bank to Vnesheconombank, and the same amount extended by Agricultural Bank of China to VTB, both in 2009. The SPO of Sberbank, Russia's largest bank, is scheduled for H2 2011. Chinese companies will have the opportunity to further confirm or refute this trend.

Nikita Popov, Consultant
nikitapopov@thebeijingaxis.com

Upcoming Events

The Beijing Axis can assist delegates who wish to attend events in China as well as globally. The Beijing Axis' service set includes research, interpretation, negotiation and travel logistics. For more information, please send an email to *info@thebeijingaxis.com*, or for contact details see The Beijing Axis corporate profile on the backpage.

Date	Event	Location
14-16 March 2011	**Seventeenth World Steel Conference 2011**	Rome
The World Steel Conference is one of the world's leading events for senior executives in the steel industry		
22-24 March 2011	**Mines and Money Hong Kong 2011 Conference and Exhibition**	Hong Kong
As Asia's number one event for mining investment, Mines and Money is a platform for putting explorers in touch with operators, project managers in touch with financiers and technical experts		
24-25 March 2011	**China Iron Ore 2011**	Beijing
China Iron Ore 2011 will be an opportunity for the international iron and steel community to gather in Beijing and discuss the major issues in the industry		
4-8 April 2011	**Seventh Asia Mining Congress 2011**	Singapore
Asia Mining Congress is the region's definitive leadership forum for exploration, investment and development, convening major mining companies and the region's most influential investors to discover new investment opportunities		
5-7 April 2011	**MINEX Central Asia 2011**	Astana
As the region's largest mining and exploration event, MINEX aims to provide companies with information on key business / technical / investment and financial factors to assist them in managing their mining businesses in Central Asia		
13-15 April 2011	**Mining World Russia 2011**	Moscow
Mining World Russia is a leading exhibition for the mining and processing of metals and minerals in Russia. With a history of 13 years, this event gathers experts to discover the latest equipment, technologies and projects		
14-16 April 2011	**China International Mining Equipment Exhibition 2011**	Beijing
This event is a leading international mining equipment exhibition in China. Professionals from the mining, energy, power generation and engineering industry will participate and showcase their latest products		
4-6 May 2011	**ARMINERA 2011**	Buenos Aires
ARMINERA 2011 is the only international mining exhibition in Argentina. It will provide the possibility of sharing business scenarios with major mining companies to enhance business opportunities		
4-6 May 2011	**Zambia Mining and Energy Indaba**	
This event offers delegates the opportunity to get up to speed with one of Africa's most exciting resources destinations		
17-19 May 2011	**World Mining Investment Congress**	London
The World Mining Investment Congress provides and opportunity to network and discuss finance and partnerships in the industry. The Beijing Axis Director Matt Pieterse has been invited to deliver a presentation at the event		
18-20 May 2011	**IMEXPO SADC China Trade Fair & Investment Forum**	Johannesburg
The IMEXPO SADC China Trade Fair & Investment Forum provides investors and traders with a networking opportunity between the SADC region and China.		
24-25 May 2011	**The Sixth CIPSA Public Sector Procurement Forum**	Canberra
This event sets a strategic professional agenda for procurement through keynote plenary sessions, providing delegates with real practical and tactical deliverables		

Careers at The Beijing Axis

The Beijing Axis is looking for dynamic, performance-driven individuals to assist us in meeting our business challenges. If you believe you can make a contribution, please send a detailed CV with a letter of motivation and references to the Group MD, Kobus van der Wath: *kobus@thebeijingaxis.com* (Note: international relocation is possible).

Commodity Trader
Beijing Axis Commodities, Beijing (1 position)

Role

- Project manage transactions and execute commodity trading activities
- Analyse commodity offers and requests; understand prices, demand and supply pressures
- Analyse commodity trading market and instinctively understand current trends
- Verify the background of potential buyers and sellers
- Engage trading processes and negotiate trading terms
- Prepare contract documentation to meet client requirements; oversee contracting finalisation and signing
- Manage follow-up processes; supervise risk control management
- Develop extensive Chinese customer base
- Manage client relationships

Requirements

- Strong academic background – specialised trading, finance, or economics degrees preferred
- 3-5 years experience in a commodity trading environment
- Sound knowledge of trading transaction and contract management processes
- Thorough understanding of the logistics of commodity trading
- Proactive approach; ability to coordinate deliverables and teams across various locations
- Ability to multi-task and manage multiple responsibilities and projects simultaneously
- Customer-oriented and service-oriented
- Thorough understanding of Chinese and international business cultures
- Excellent English and Mandarin abilities, written and spoken

QA/QC Sourcing Engineer
Beijing Axis Procurement, Beijing (1 position)

Role

- QA/QC and expediting for mechanical and electrical equipment and fabricated steel for *Beijing Axis Procurement* team and clients
- Coordination with buyers in the *Beijing Axis Procurement* team and clients for inspection notifications
- Inspection in accordance with Inspection and Test Plans (ITPs) and instructions from clients
- Manage and monitor third-party inspection companies, if required
- Process all deviations from ITPs and Non-Conformance Reports
- Manage documentation related to all Inspection Reports, Inspection Release Notes and Inspection Waivers issued
- Performing expediting, if required, including setting up and managing delivery schedules, resolving delivery issues, etc.

Requirements

- Bachelor degree or above in mechanical or electrical engineering, metallurgy, mining or related major
- Minimum 5 years experience in QA/QC in mechanical or mining engineering and/or processing equipment industries
- Familiarity with relevant international standards and codes
- Thorough understanding of steel grades, engineering drawings, design aspects and AutoCAD software preferred
- Project management skills essential
- Quality engineering experience and/or certification preferred
- Good communication skills and team work ethic
- Excellent English and Mandarin abilities, written and spoken
- Willingness to travel

Buyer (Mechanical / Electrical Engineering Background)
Beijing Axis Procurement, Beijing (1 position)

Role

- Identify and evaluate suppliers/contractors; make recommendations for each enquiry/RFQ package
- Project manage sourcing schedules (i.e. ensure that specialised capital equipment is manufactured to required standards and delivered on time and within budget)
- Manage interaction and communication between suppliers and clients; ensure maintenance of good relations with clients and suppliers/contractors
- Ensure functional manager is kept informed of project status and any issues/problems
- Produce documentation to satisfy clients' requirements

Requirements

- Bachelor degree or above in mining, mechanical or electronic engineering or related field
- Minimum 3 years work experience in procurement, sales or other related fields
- Previous experience in mining or metallurgical industries preferred
- Sourcing or manufacturing project management knowledge and skills essential
- Ability to organise and present facts and arguments in a persuasive manner
- Good research and analytical capabilities
- Good communication skills and team work ethic
- Excellent English and Mandarin abilities, written and spoken
- Willingness to travel

Strategy Consultant
Beijing Axis Strategy, Beijing (1 position)

Role

- Analysis of clients' business needs and development of problem-solving methodologies; address complex problems by finding creative solutions
- Desk research and trend monitoring in various *Beijing Axis Strategy* business focus areas; including the Chinese mining and resources sector as well as the industrial and engineering sector; trade and investment relations between China and Africa, Russia, Australia and Latin America; China's OFDI and M&A; and government regulation
- Process, analyse, interpret and present relevant data in MS Office for external as well as internal projects
- Cross-checking data presented in Beijing Axis Strategy project documentation, ensure that information is accurate and updated
- Operational assistance for business exhibitions as well as commercial missions for companies, associations and chambers of commerce
- Authoring and co-authoring business articles

Requirements

- Business and/or technical degree with a post-graduate qualification
- Minimum 5 years experience in a consulting, research or analysis role
- Experience in the formulation and execution of research methodologies and analysis
- Sound analytical and problem-solving skills
- Thorough understanding of Chinese market and doing business in China
- Ability to work in teams with colleagues from diverse cultures and backgrounds
- Good communication skills and team work ethic
- English and Mandarin proficiency
- Willingness to travel

Analyst (Intern position)
Beijing Axis Strategy, Beijing

Role

- Desk research and trend monitoring in various business areas related to Beijing Axis project work, including the Chinese mining and resources sector; the industrial and engineering sector; trade and investment relations between China and Africa, Russia, Australia and Latin America; China's OFDI and M&A; and government regulation
- Process, analyse, interpret and present relevant data in MS Office software for external as well as internal projects
- Cross-checking data presented in Beijing Axis project documentation, ensure that information is accurate and updated
- Operational assistance for business exhibitions as well as commercial missions for companies, associations and chambers of commerce
- English/Chinese translation; fact-checking; proofreading; data processing

Requirements

- A business and/or technical degree with a post-graduate qualification (current study possible)
- Attention to detail and fast-learner
- Ability to work under pressure and multi-task
- Sound analytical and problem solving skills
- Ability to work in teams with colleagues from diverse cultures and backgrounds
- Good communication skills and team work ethic
- English and Mandarin proficiency

Business Development Consultant
Beijing Axis Global Business Development, Beijing (1 position)

Role

- Analyse and continuously enrich company client base
- Develop and manage relationship networks in China
- Build an effective consultative relationship with clients
- Identify and participate in job-related industry events to expand networks
- Undertake research and analysis of different project areas in order to support projects by providing consulting services, when necessary
- Provide assistance for the preparation of proposals and submission of tender documentation
- Support business development processes and carry out improvements on the system

Requirements

- Minimum bachelor degree or equivalent qualification
- Proposal writing experience essential
- 3-5 years experience in business development
- Excellent English business writing, communication, and analytical skills
- Ability to work within tight deadlines and under pressure
- Ability to work independently, to prioritise tasks and meet deadlines
- Strong negotiation and presentation skills
- Excellent knowledge of MS Office
- Knowledgeable in local media and experienced in business marketing
- Willingness to travel

The Beijing Axis News: August 2010–February 2011

Community

The Beijing Axis (TBA) was a sponsor of the inaugural *SA Inc Meets China Inc - Promise or Peril?* conference at the Sandton Convention Centre in Johannesburg on 16 Feb 2011. TBA staff delivered presentations at the event, namely Kobus van der Wath, Founder and Group Managing Director (*Formulating a China Strategy: Planning and Implementation Issues during Corporate Engagement*); Matt Pieterse, Managing Director: *Beijing Axis Capital* (*Attracting Investment from and Raising Capital in China*); Dirk Kotze, General Manager: Strategic Projects (*Unlocking Opportunities in the Resource Sector*); and Jackie Li, Business Development Manager (*Does Culture Matter?*). Nitesh Dullabh (General Manager: Africa) was the chairperson. The conference was well-attended.

Mining Indaba 2011

The Beijing Axis was active at this year's Mining Indaba in Cape Town, South Africa, on 7-10 Feb 2011. Kobus van der Wath was a keynote speaker, and delivered a presentation entitled *Africa in China's Orbit: Implications for Global Resource Companies* on 8 Feb.

During and after Mining Indaba, Kobus was interviewed by various print, online, radio, and television media, including interviews on Radio Netherlands Worldwide on 8 February, South Africa's Classic FM on 14 February, and ETV on 15 February.

On 9 February, Cadiz Corporate Solutions and The Beijing Axis hosted a Mining Indaba side event in the form of a cocktail evening at iArt Gallery in Cape Town to discuss new China business opportunities.

Learning and Getting Around

Greater China and Asia

CHaINA'10 Live - Shanghai, China
CHaINA'10 Live, the largest supply chain event in China, was held on 17-18 November 2010 at Renaissance Zhongshan Park Hotel in Shanghai, China. Lilian Luca (Managing Director: *Beijing Axis Procurement*) delivered a presentation on 17 November entitled *Low cost country procurement: Examining China as a High-value Capital Procurement Partner*. Luca also chaired a session at the event entitled *Stream: What's Next?* which assessed the current procurement outlook in China. Lilian subsequently won the award for Best Speaker of all the 45 speakers at the CHaINA '10 conference.

China Mining 2010 - Tianjin, China
The 12th annual China Mining Congress & Expo, hosted by the Chinese Ministry of Land & Resources and the Tianjin Municipal Government, took place at the Meijiang Convention Centre in Tianjin on 16-18 November 2010. Ben Zhang (Senior Manager: Corporate Finance), Jeff Dong (Analyst), Barry van Wyk (Senior Consultant), Charles Avery (Analyst); Lilian Luca and Javier Cuñat (General Manager, *Beijing Axis Strategy*) attended the event. Javier also chaired a session at the event entitled *Mining in Latin America* on 17 November.

Ninth Asia Pacific Mining Conference & Exhibition - Jakarta, Indonesia
On 13-14 October 2010, the Ninth Asia Pacific Mining Conference & Exhibition was held at the Shangri-La Hotel in Jakarta, Indonesia. Matt Pieterse delivered a presentation at the event entitled *China's Role in Resource Consumption and Overseas Investment*.

Tradewinds Shipping China 2010 - Beijing, China
On 28-29 September 2010, Javier Cuñat attended Tradewinds Shipping China at Park Hyatt Beijing, and delivered a presentation entitled *How China Seeks to Optimise the Security of Supply Through Diversified Investments in Overseas Ports, Mines, and Railways*.

Other events recently attended by The Beijing Axis in Greater China and Asia:

8-9 Jan 2011	China Foreign Trade Enterprises Development Forum 2011	Beijing, China
23-25 Nov 2010	The China International Nuclear Symposium	Beijing, China
25-26 Oct 2010	China Investment Summit	Beijing, China
25 Oct 2010	Coal Trading China	Singapore
16 Sep 2010	China-Africa Dialogue	Beijing, China
24-26 Aug 2010	President Zuma State Visit	Beijing, China

Upcoming events in Greater China and Asia where The Beijing Axis will be represented:

24-25 Feb 2011	Iron Ore Supply Chain Congress	Bali, Indonesia
22-24 Mar 2011	Mines and Money Hong Kong	Hong Kong
23-25 Mar 2011	Steel Market and Trade Conference 2011	Beijing, China
24-25 Mar 2011	China Iron Ore 2011	Beijing, China
29-30 Mar 2011	Asia Ferro-alloys Conference	Hong Kong
4-8 Apr 2011	Asia Mining Congress	Singapore
6 Apr 2011	Singapore Business Federation's Africa Business Group Dialogue Session	Singapore

Africa

Macquarie China Day Conference - Cape Town, South Africa
On 4 Feb 2011, Kobus van der Wath attended the Macquarie China Day Conference, held at the Mount Nelson Hotel, Cape Town. Kobus delivered a presentation on China's investment in Africa.

INSEAD Africa Initiative - Johannesburg, South Africa
On 4 November 2010, The Beijing Axis and leading South African corporate and commercial law firm Bowman Gilfillan sponsored the INSEAD Africa Initiative event in Johannesburg, South Africa. Nitesh Dullabh gave the welcoming address.

Electra Mining Africa 2010 - Johannesburg, South Africa
The Beijing Axis attended Electra Mining Africa on 4-8 October 2010 in Johannesburg, South Africa. During the event, *Beijing Axis Procurement* showcased its China procurement services as well as its commodity marketing and trading solutions. Jackie Li, Nitesh Dullabh and Barry van Wyk attended the event.

Third South African Ferro-alloys Conference -
Johannesburg, South Africa
On 29-30 September 2010, the Third South African Ferro-alloys Conference was held at the Hilton Sandton in Johannesburg, South Africa. Kobus van der Wath delivered a presentation at the event entitled *China's Influence in the Resource Sector: Consumer, Global Investor and Supply Chain Partner.*

Other events recently attended by The Beijing Axis in Africa:

2-3 Feb 2011	McCloskey South African Coal Exports Conference	Cape Town, South Africa
31 Jan 2011	Africa Mining Network	Johannesburg, South Africa
27 Jan 2011	The future of Technology: Tomorrow is here TODAY (business think tank)	Johannesburg, South Africa
26 Jan 2011	Gordon Institute of Business Science (GIBS) Economic Outlook 2011	Johannesburg, South Africa
11 Nov 2010	Supply Chain & Logistic Group - Powertech Plant Tour	Johannesburg, South Africa
3 Nov 2010	Gordon Institute of Business Science - Master Knowledge Forum on Africa	Johannesburg, South Africa
15-17 Sep 2010	Zimbabwe Mining Indaba	Harare, Zimbabwe

Upcoming events in Africa where The Beijing Axis will be represented:

1-3 Mar 2011	Energy Indaba 2011	Johannesburg, South Africa

Australia

Mining Investment and Reporting Seminar - Xstract - Perth
On 9 November 2010, Kobus van der Wath attended the Xstract Mining Investment and Reporting Seminar which was held at the Citigate Hotel, Perth, Australia. He delivered a presentation entitled *China's Role in the Resource Sector: Global Consumer, Investor and Supply Chain Partner*. This lunch-time technical seminar discussed current aspects of mining and exploration project investment and public reporting.

Sixth CIPSA Annual Conference - Melbourne
The Sixth CIPSA Annual Conference was held on 13-14 October at the Crown Conference Centre. This year's theme was *Managing Volatility*, and featured a host of mining and energy industry leaders like Woodside, Anglo American, Rio Tinto and Santos, along with contributors from other industries. The Beijing Axis had a booth at the event which was manned by Kobus van der Wath and Doug Horak (Business Development Manager).

Other events recently attended by The Beijing Axis in Australia:

27 Oct 2010	Annual Western Australia Consular Corps Reception	Melbourne
27 Oct 2010	CIPS Australia - Stainability Challenges in Low Cost Country Sourcing	Melbourne
19 Oct 2010	Western Australia Resources Overview	Perth
2-3 Sep 2010	Africa Down Under Conference	Perth

Upcoming events in Australia where The Beijing Axis will be represented:

1-2 Mar 2011	Engineering Australia's New Resources Boom	Perth
1-3 Mar 2011	Coal Seam Methane World Australia 2011	Brisbane
20-22 Mar 2011	The Mine Managers Show	New South Wales

Latin America

Third Annual Americas Iron Ore Conference -
Rio de Janeiro, Brazil
The Third Americas Iron Ore Conference was held on 9-11 November 2010 at the Intercontinental Rio de Janeiro, Brazil. Javier Cuñat delivered a presentation at the event entitled *China's Role in the Global Iron and Steel Sector: A Perspective on Demand and Strategic Capital from China*.

From Chile to China 2010 Forum - Santiago, Chile
On 27 August 2010, a business seminar entitled *From Chile to China* was held in the Great Hall of Casa Piedra in Santiago, Chile. Javier Cuñat attended the event and delivered a presentation entitled *China in 2020: Opportunities and Challenges for Chilean Companies*. After the conference, Javier Cuñat was interviewed by local business media.

Upcoming events in Latin America where The Beijing Axis will be represented:

26-27 Jan 2011	Minería Estratégica e Inversión Perú 2011	Lima, Peru

Europe and North America

Recent events attended by The Beijing Axis in Europe and North America:

25-26 Jan 2011	Global Mining Forum	London, UK
30 Nov - 1 Dec 2010	Mines and Money	London, UK

Upcoming events in Europe and North America where The Beijing Axis will be represented:

6-9 Mar 2011	PDAC 2011 International Convention, Trade Show & Investment Exchange	Toronto, Canada

The Beijing Axis Team Developments

In January 2011, Dirk Kotze joined the Johannesburg office as General Manager: Strategic Projects. Dirk was previously China General Manager at the Beijing office, and we are delighted to welcome him back to The Beijing Axis.

In December 2010, Christina Luo joined the Beijing office as Buyer for *Beijing Axis Procurement*.

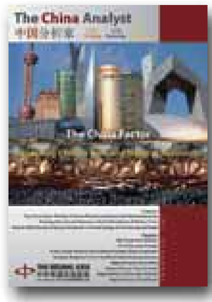
In November 2010, Shanshan Huang joined the Beijing office as intern for *Beijing Axis Strategy*.

In August 2010, Serena Wang joined the Beijing office as Receptionist, Guolin Liu as Sourcing Engineer for *Beijing Axis Procurement*, and Karah Wang as Consultant for *Beijing Axis Procurement*.

In October 2010, Paul Williams (formerly SGM: International Procurement), left The Beijing Axis after several years of service as he was returning to South Africa. We wish him all the best.

Previous Editions of The China Analyst

August 2010



Regulars
Macroeconomic Monitor
China Facts & Figures
China Trade Roundup
China Sourcing Strategy
China Capital
Mapping China
Regional Focus: China-Africa, China-Australia, China-Latin America and China-Russia

Features
The China Factor: Supplying China's Phenomenal Demand for Resources
How did the China Factor become a singular driving force of global demand for natural resources in the 2000s?

Road to 2020: Nuclear's Rising Contribution to China's Energy Needs
Nuclear power has entered a new era in China as China targets 2020 for radically ramping up inuclear production.

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Features
Upstart: China's Emergence in Science and Technology
After coming of age in China's domestic markets, Chinese are now replicating their domestic success in global markets.

Building by Design: How China Develops the Developing World
Chinese contractors and design firms have gone international and are shaping landscapes where its needed most: the developing world.

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Features
Fighting for Trade: China and the Threat of Protectionism
China's leaders are worried about protectionism, yet what is the real extent of the threat to China?

Rare Earths: China's Contribution to Modern Technology
A closer look at the history of the rare earths industry in China, the controversies surrounding it, and some upcoming trends to watch.

September 2009

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Features
Why, Who and Why Now? Chinese OFDI on the World Stage
Chinese OFDI has become fundamental to China's global integration, yet who is at the forefront of this drive and where is it heading?

Mining in a Downturn: What's in it for China?
The crisis hit the mining industry hard, yet Chinese companies have remained active with mining acquisitions and strategic stockpiling.

Other Recent Publications by The Beijing Axis

Unlocking Opportunities in the Resource Sector
SA Inc. Meets China Inc. - Promise of Peril? Conf.
February 2011

Attracting Investment From and Raising Capital in China
SA Inc. Meets China Inc. - Promise of Peril? Conf.
February 2011

China's Investment in Africa
Macquarie China Day Conf.
February 2011

Africa in China's Orbit: Implications for Global Resource Companies
Mining Indaba
February 2011

China's Role in Resource Consumption and Overseas Investment
Asia Pacific Mining Conf.
October 2010

China's Influence in the Resource Sector: Consumer, Global Investor and Supply Chain Partner
SA Ferro-Alloys Conf.
September 2010

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The Beijing Axis
中外商桥咨询服务

Commodities 大宗商品 · Capital 跨国投资 · Procurement 跨国采购 · Strategy 跨国战略

The Beijing Axis Group is a cross-border business bridge to/from China in four principal areas: Commodities, Capital, Procurement and Strategy. We work across various industries, but our core focus is on the mining, resources, industrial and engineering sectors. With offices in Beijing, Singapore, Perth, Moscow, Johannesburg and London, we support international firms as they act in unfamiliar territory in China and Chinese firms as they venture out and 'go global'. We are committed to safety and sustainability, and emphasise 'actions and transactions'.

The Group is organised along four synergistic cross-border business units:

Beijing Axis Commodities

Beijing Axis Commodities supports commodity producers with their international marketing efforts and the structuring of off-take agreements, and assists commodity consumers with their procurement efforts in securing supply.

Beijing Axis Capital

Beijing Axis Capital provides independent corporate finance advisory and transaction origination services. We have a specialist China-specific approach with extensive international and Africa-specific knowledge and experience.

Beijing Axis Procurement

Beijing Axis Procurement is a China-focused global procurement house and provides a comprehensive range of services across the supply chain.

Beijing Axis Strategy

Beijing Axis Strategy provides management consulting services to CEOs and senior executives in the areas of strategy formulation and strategy implementation.

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