September 4, 2017

Chinese capital outflow restrictions give way to new opportunities for CIS countries

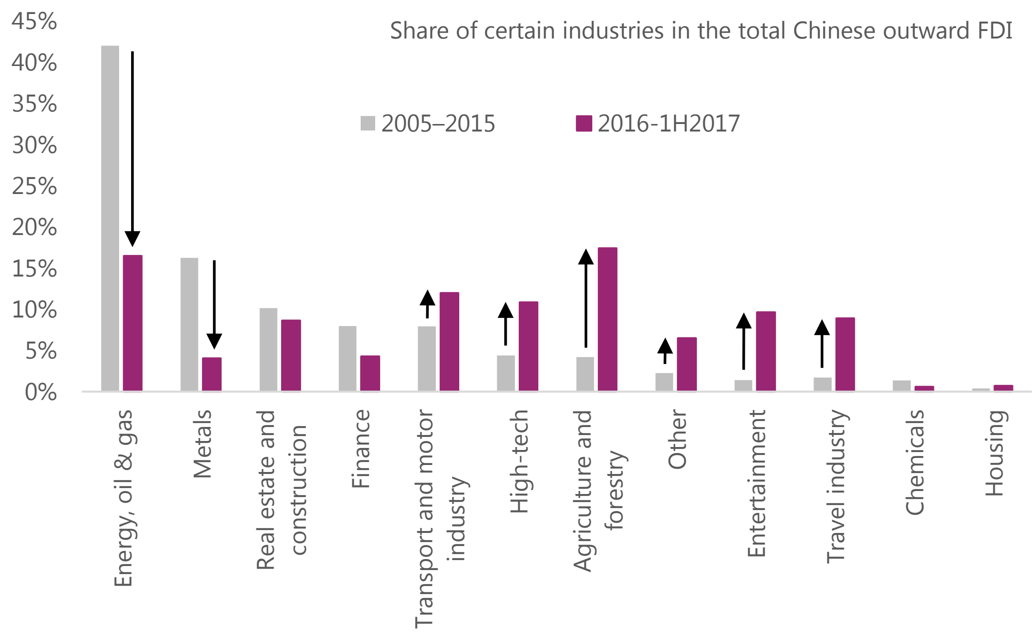
China's foreign direct investments analysis

In 1H2017, the foreign direct investments of China grew by mere 9% against 39% seen in 1H2016.[1] The key reason of such deceleration is the decision to restrict FDIs, which was taken in the end of 2016 by the Chinese government to rise the effectiveness of the People's Bank of China's control over the FX rates, fight the corruption and give a boost to domestic manufacturers. On August 18, 2017, further restrictions were introduced with respect to FDIs in specific industries (construction, sports and entertainment). Another reason for investments deceleration is the slowdown of Chinese economy: the real GDP growth is expected to be about +5.6% in 2017 and +4.8% in 2018 (against the average of +6.8% in 2014–2016).

See ACRA commentary [China no longer invests in raw materials] dated August 9, 2016

However, those processes have not hindered certain major investments that took place in the first half of 2017. For example, after ChemChina purchased a 95% share in the Swiss agrochemical company Syngenta[2], the share of Chinese direct investments in the agriculture sector reached its 12-year maximum of 45%. The purchase price is about USD 41.2 billion, the all-time peak for China.

Figure 1. Chinese investors prefer high tech, transport, entertainment and travel industries



Source: MOFCOM, American Enterprise Institute, ACRA estimates

Restrictions on investments[3] into construction and entertainment industries may decrease the shares of Europe[4] and the USA in the Chinese outward FDI. Today, the amount of investments into such regions is the largest (70%), while the share

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[1] 2005–2017 data provided by China Global Investment Tracker. Unless stated otherwise, hereinafter, the paper deals only with USD 100+ mln gross outward FDIs in equity.
[2] The company focuses on development and production of GMO, plants and fertilizers.
[3] Capital outflow restrictions do not affect priority projects like One Belt, One Road.
[4] Main European counterparties of China are Germany, the Netherlands and the UK.

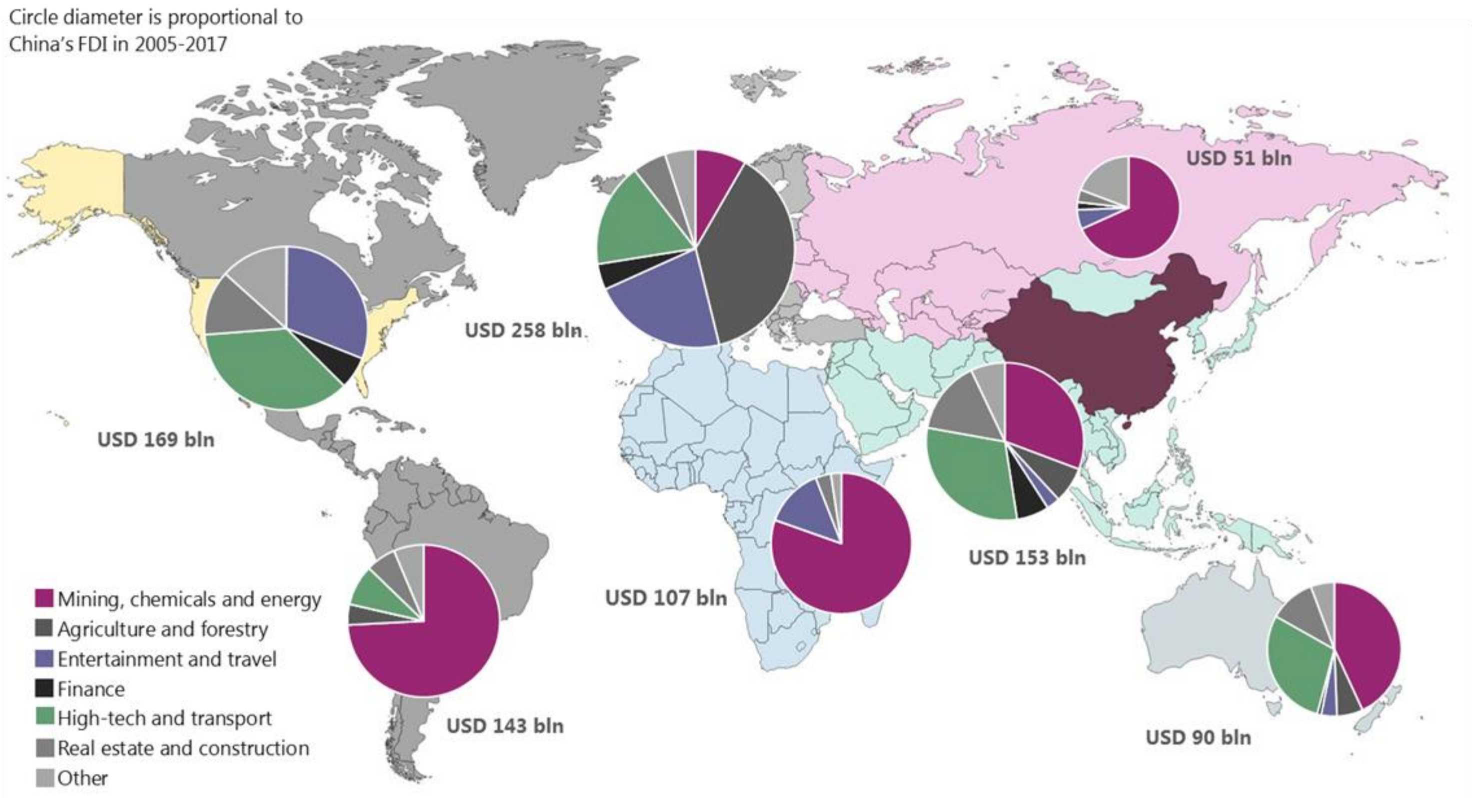
See ACRA forecast Russian Economy: Recession Knocked Out. What Next? dated March 28, 2017

of CIS countries is as low as 1%[5] (see Fig. 2). The geographical profile of Chinese FDI is driven by the growing focus of Chinese investors on the high-tech, entertainment and travel industries, most developed in Europe and the USA. But the capital outflow restrictions imposed by China may affect the shares of Europe and the USA in the Chinese FDI in the future.

One Belt, One Road is a China's project aimed at creation of new trade ways connecting East and West. The initiative was first announced in 2013.

Mineral resource sectors comprise about 68% of the total implemented FDI from China into Russia (see Table 1); for Kazakhstan, the share is 100% (see Table 2). In recent years, the share of Chinese investments into the CIS in the total foreign direct investments of China has dropped (from 6.6% in 2005-2015 down to 1.3% in 2016-1H2017) due to lower interest in mineral resources. However, the capital outflow restrictions and the measures driving investments into the One Belt, One Road project (having being implemented since August 18, 2017) give the CIS countries located within the project region a chance to increase their share.

Figure 2. China invests heavily in high-tech, travel and entertainment industries in Europe and the USA*



Source: MOFCOM, American Enterprise Institute, ACRA estimates

* Announced FDI of China in 2005-1H2017 and FDI regional structure in 2016-1H2017

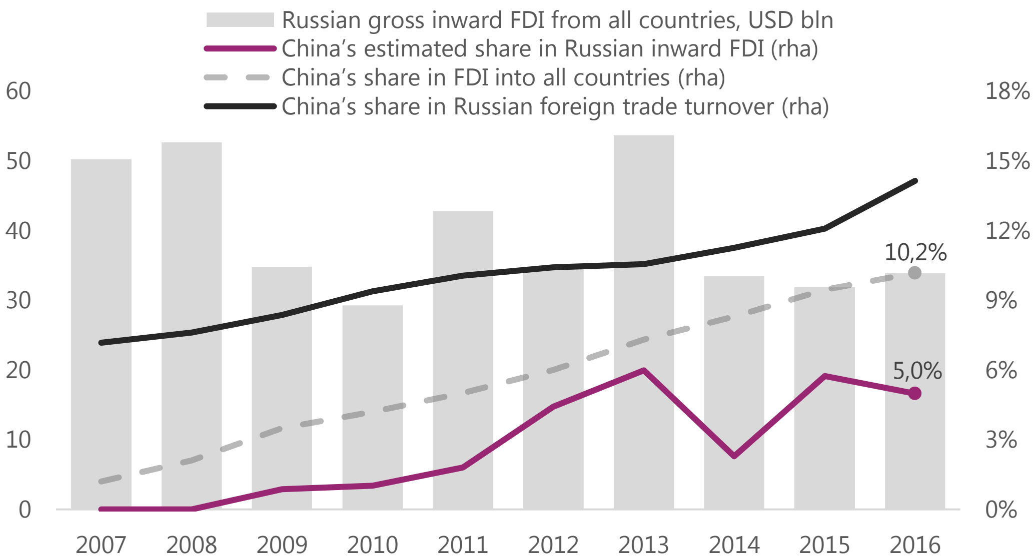
[5] In 2016-1H2017

See ACRA commentary [Russian foreign trade turns East] dated May 10, 2017

Financial flows between Russia and China are well behind the foreign trade flows: in 2015–2016, the share of China in the Russian foreign trade turnover was 10.1%, while the share of direct investments was as low as 5.4%[6] (see Fig. 3). This is caused by the Chinese interest in investments into high-tech, transport, machine building, entertainment, and travel industry, but in Russia, the focus is on raw materials. The Russia-China foreign trade turnover growth seen in recent years is explained, mainly, by western sanctions against Russia. In 1Q2017, Chinese FDIs into Russia grew by 7.9%, and the large Chinese FDIs into Russia[7] grew twice against 1Q2016. We expect that the China's share in the Russian inward FDI will grow on the heels of the growing trade turnover between the countries and the One Belt, One Road project.

In 1H2017, Chinese investors purchased shares in Russian companies for a record high USD 3.29 billion. But those investments are, again, connected with mineral resource industries: 20% share in Verkhnechonskneftegaz, a Rosneft subsidiary, was bought by Beijing Enterprises Group Company for USD 1.08 billion and a 10% share in Polyus was bought by Fosun Group for USD 0.89 billion. Nevertheless, many deals were closed in other sectors too, in particular, in chemical industry (purchase of 10% share in SIBUR by Silk Road Fund for USD 1.15 billion) and real estate (purchase of Voentorg building in Moscow by Fosun Group for USD 0.17 billion[8]). Those purchases are also caused by anti-Russian sanctions, as Russian companies seek for extra funding.

Figure 3. China's shares in Russian foreign trade turnover and inward FDI



Source: The Bank of Russia, American Enterprise Institute, MOFCOM, UNCTAD, ITC, FCS, ACRA estimates

[6] Sometimes the contract price is paid not as a lump sum but in portions, over the period of several years. That is why this indicator differs from the official one. Here, the share of the announced FDI is taken from Table 1, as published by the Bank of Russia.
[7] With the value exceeding USD 100 million.
[8] ACRA estimates.

Table 1. Large announced Chinese FDI projects in Russia in 2006–2017[9]

Industry	Agreement year (funding start year)	Investor	Investee (parent company)	Announced (implemented), USD million	Implementation[10]
Forestry	2006	MCC	-	250	
	2013	CIC	Russia Forest Products	100 (110)	+
Agriculture and fertilizers	2013	CIC	Uralkali	2,040	+
	2015	Zoie Resources Investment	-	436	
Oil and gas	2006	Sinopec	Rosneft	3,490	+
	2006	CNPC	Rosneft	500	+
	2009	CIC	Nobel Holdings Investments (NHI)	300	+
	2013	CNPC	Taas-Yuryah Neftegazodobycha (Rosneft)	620	
	2014	CNPC	Vankorneft (Rosneft)	990	
	2016 (2017)	Beijing Enterprises	Verkhnechonskneftegaz (Rosneft)	1,080	+
Energy	2010 (2011)	China Huadian Corporation	TGK-2	360 (323)	+
	2010	China Three Gorges Corporation	EuroSibEnergo	168	
	2011	China Three Gorges Corporation	EuroSibEnergo	2,290	
	2013	State Grid Corporation of China	Sintez Group	1,140	
	2013 (2014)	CNPC	NOVATEK	940 (425)	+
	2013	Shenhua[11]	En+	460	+
	2014	Power Construction Corporation of China (PowerChina)	RusHydro	1,460	
	2014	Harbin Electric	-	450	
	2015 (2016)	SRF	NOVATEK	1,210 (1,087)	+
Chemicals	2015	Sinopec	SIBUR	1,340 (1,338)	+
	2017	SRF	SIBUR	1,150	+
Metals	2009	Sinopec	-	480	
	2012	SRF	-	100 (114)	+
	2012	Xiyang Group	Basic Element	500	
	2012	Zijin Mining Group Company	Polyus	420	+
	2013	Norinco	IRC Limited	240 (238)	+
	2013	CIC	MBC	1,500	
	2015 (2016)	Minmetals Cheerglory, General Nice IRC	Norilsk Nickel	100	+
	2017	China Nonferrous Metal Industry's Foreign Engineering & Construction (NFC)	Polyus	890 (887)	+

[9] According to data from China Global Investment Tracker, adjusted to include information from Russian and foreign business media.
[10] "+" means the project is being implemented and funded, or the project has been implemented; no sign means the project has been announced, the agreement has been signed, but no further steps have been taken.
[11] According to ACRA estimates, total investments amount to RUB 15 billion, paid in phases.

Transport and motor industry	2011 (2013)	Highland Fund	-	200	+
	2014	Fosun Group	-	340	+
	2014 (2015)	Fuyao Glass Industry Group Co. Ltd (Fuyao Group)	-	290	+
Real estate and construction	2006	Group of Shanghai state companies	-	1,300	
	2011	China Chengtong Development Group Ltd.	Greenwood International Trade center	350	+
	2015 (2016)	Anhui Conch Cement Company	-	310 (500)	+
	2017	Fosun Group	Voentorg Trade House	172.5	+
Finance	2011	CIC	VTB	100	+
	2012	CIC	RCIF	900	+
	2013	CIC	Moscow Exchange	100 (50)	+
	2013	China Construction Bank	VTB	100 (110)	+
High-tech	2010	Tencent	Digital Sky Technologies	300	+
	2015	Cybernaut Invetment Group	Skolkovo	200	+

Source: American Enterprise Institute, ACRA estimates

Table 2. Large announced Chinese FDI projects in Kazakhstan in 2005–2017[12]

Industry	Agreement year (funding start year)	Investor	Investee (parent company)	Announced (implemented), USD million	Implementation[13]
Oil and gas	2005	CNPC	PetroKazakhstan	4,200 (4,180)	+
	2009	CNPC	MangistauMunayGas	2,600	+
	2009	CIC	KazMunayGas	940 (939)	+
	2012	CNPC	KazMunayGas	500	
	2013 (2014)	CNPC	KazMunayGas	5,300	+
	2014	Hainan Zhenghe Industrial Group Co Ltd.	Maten Petroleum	530 (525)	+
	2014	Sinopec	Caspian Investment Resources	1,090 (1,087)	+
	2015	Geo-Jade Petroleum	KoZhan (Maten Petroleum)	350 (340)	+
	2015	Geo-Jade Petroleum	Caspian Nature Resources (Caspian Oil)	120	
Energy	2006	CITIC	Nations Energy	1,910	+
	2008 (2009)	Xinjiang Guanghui	Tarbagatay Munay	250 (40.5)	+
	2010	Jinchuan	Kazakhmys	120	+
Transport and motor industry	2010	CITIC	KazMunayGas	150	+
Real estate and construction	2016	China Energy Engineering Corporation	-	180	
Finance	2017	CITIC	Halyk Bank	110	

Source: American Enterprise Institute, ACRA estimates

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[12] According to data from China Global Investment Tracker, adjusted to include information from Russian and foreign business media.
[13] "+" means the project is being implemented and funded, or the project has been implemented; no sign means the project has been announced, the agreement has been signed, but no further steps have been taken.

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