KPMG

THE UNIVERSITY OF SYDNEY

Demystifying Chinese Investment in Australia

The new normal: health, happiness, lifestyle and services

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About our reports

KPMG and The University of Sydney formed a strategic relationship to publish research and insights on doing business with Chinese investors. Our first report was launched in September 2011 and this is the eleventh Demystifying Chinese Investment report in our series. This report examines Chinese investment in Australia for the calendar year 2015.

The catalyst for our report series is the historic lack of detailed factual information about the nature and distribution of China's outbound direct investment (ODI) in Australia. Without this information, there is misinformation and speculation. Our reports seek to set the record straight and debunk the myths associated with Chinese investment in this country.

Methodology

The dataset is compiled jointly by KPMG and The University of Sydney Business School and covers investments into Australia made by entities from the People's Republic of China through M&A and joint venture. Knight Frank has provided data on real estate transactions. "Real estate" referred to in this report does not include residential apartment and home sales. The dataset also tracks Chinese investment by subsidiaries or special purpose vehicles in Hong Kong, Singapore and other locations. The data, however, does not include portfolio investments such as the purchase of stocks and bonds, which do not result in foreign management, ownership or legal control.

Our database includes direct investments recognised in the year in which parties enter into legally binding contracts and if necessary, receive mandatory FIRB and Chinese Government investment approvals. In certain instances, final completion and financial settlement may occur in a later year.

For consistency, the geographic distribution is based on the location of the Australian invested company and not on the physical location of the actual investment project. Completed deals which are valued below USD 5 million are not included in our analysis, as such deals consistently lack detailed, reliable information.

Unless otherwise stated, the data referred to throughout this report is sourced from the KPMG/University of Sydney database, and our previously published reports[1]. The University of Sydney and KPMG team obtains raw data on China's ODI from a wide variety of public information sources which are verified, analysed and presented in a consistent and summarised fashion.

Our data is regularly updated and continually revised when new information becomes available. In line with international practice, we traditionally record deals using USD as the base currency. However, for 2014 and 2015 we use Australian dollars for our detailed analysis given the effect of exchange rate fluctuations.

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

[1] Includes *Australia & China Future Partnership*, September 2011; *The Growing Tide: China ODI in Australia,* November 2011; *Demystifying Chinese Investment,* August 2012; *The Energy Imperative: Australia-China Opportunities,* 25 September 2012; *Demystifying Chinese Investment in Australia,* March 2013; *Demystifying Chinese Investment in Australian Agribusiness,* October 2014; *Demystifying Chinese Investment in Australia,* March 2014; *Demystifying SOE Investment,* August 2014; *Chinese Investors in Australia Survey,* November 2014; *Demystifying Chinese Investment in Australia,* May 2015 Update.

Chinese investment in Australia in 2015: Ten things you need to know

Chinese investment rose very strongly to USD 11.1 billion (AUD 15.09 billion) – a 32.9% increase in USD terms, and 59.5% in AUD terms.

2015 was the second highest inflow year recorded in new Chinese ODI, behind the previous peak year in 2008.

2015 also saw the largest number of deals with 65 legally binding deals announced.

The 2015 sector profile confirmed the transition from mining to new industries, including health for the first time.

Investment in real estate continues strongly on from 2014 to dominate with AUD 6.85 billion or 45% of total Chinese ODI in 2015.

There were 12 agribusiness sector deals worth AUD 375.2 million.

Chinese investment is still driven by a relatively small number of mega sized deals. In 2015, there were 7 mega-sized deals of AUD 500 million or above. Two major deals constituted nearly half the Chinese investment volume for 2015.

NSW remains the top destination for Chinese direct investment in 2015, attracting 49.3% of the total.

The Northern Territory ranked ahead of South Australia, Tasmania, and Western Australia for the first time.

Chinese private sector investors are by far the most active.

By number of deals, we saw private investors dominate with 78% of the share.

Australia maintained its position as the second largest recipient country of aggregated global Chinese direct investment between 2005 and 2015, behind the United States.

Chinese global outbound direct investment in 2015 reached 118 billion USD, a 14.7% increase from 2014 (MOFCOM, 2016).

Globally Australia remains the second most favoured country for accumulated Chinese investment

According to official Chinese figures, Chinese global ODI in 2015 reached a record USD 118 billion, a 14.7 percent increase from 2014[2]. Based on our 2015 data, Chinese investment into Australia grew more than twice as strongly as the global trend.

The American Enterprise Institute's China Global Investment Tracker[3] shows that for cumulative investment from 2005 to 2015, the United States[4] ranks first with USD 99.92 billion, ahead of Australia with USD 78.68 billion and Canada with USD 43.45 billion.

Rhodium Group figures from the United States confirm these growth trends[5]. Australia has experienced a similar growth rate (above 30 percent) and industry sector distribution trend (into services) to the United States in 2015. Rhodium figures for 2015 in the United States show a concentration in real estate, financial services, ICT, autos, health and biotech, and entertainment. Sixty-four percent of total Chinese investment in the United States was made into services, compared to 14 percent in 2009.

While there may be differing measurement methodologies applied by MOFCOM, the American Enterprise Institute's China Global Investment Tracker and Rhodium Group there is no doubting Chinese investment in Australia continues to play a strategically important role.

Chinese direct investment in Australia and other major competitor countries (USD million)

Country	Accumulated volume 2005-2015
USA	99,920
Australia	78,680
Canada	43,450
Brazil	33,120
Britain	31,240
Russia	24,520
Italy	18,340
Indonesia	14,730
Kazakhstan	13,710
Singapore	13,680

Source: American Enterprise Institute China Global Investment Tracker, https://www.aei.org/china-global-investment-tracker/

[2] Ministry of Commerce, 2016, http://hzs.mofcom.gov.cn/article/aa/201601/20160101236264.shtml

[3] Formerly the Heritage Foundation

[4] American Enterprise Institute's China Global Investment Tracker figures differ in detail from KPMG/University of Sydney dataset. However, they constitute the best available dataset for international comparison.

[5] Thilo Hanemann and Cassie Gao, Chinese FDI in the US: 2015 Recap, Rhodium Group, January 19, 2016; http://rhg.com/notes/chinese-fdi-in-the-us-2015-recap

Chinese outbound M&A investment in a global context

KPMG's Global China Practice's *China Outlook 2016 report* covered China's economic transition towards consumer and services led growth, as well as trends in Chinese ODI and foreign direct investment (FDI) into China 2015.

Chinese ODI

Consistent with predictions in last year's China Outlook 2015 report, three trends characterised China's outbound M&A in 2015:

- First, China's outbound M&A activity continued to be focused on 'quality growth', with not only more but also larger deals being announced in high value-added and consumption-related sectors. For instance, 2015 saw 99 deals in the computer and electronics sector up from 57 in 2014, with their total disclosed value almost doubling from USD 9.0 billion to USD 11.8 billion.
- Second, and consistent with the first trend, Chinese companies did more deals in developed markets in 2015 compared with prior years. This translated into 408 deals or 81.3 percent of the total, with a value of USD 67.8 billion in 2015 – up from 277 deals with a value of USD 52.3 billion in 2014, and 225 deals with a value of USD 33.3 billion in 2013.
- Third, more deals were announced by privately owned enterprises (POEs), accounting for 75.9 percent of the total number of deals in 2015, which was up from 68.0 percent in 2014, and 55.1 percent in 2010. State-owned enterprises (SOEs) are still doing the majority of the largest deals.

GROWTH in China's ODI flows by sector

	2014 YoY	Compound Annual Growth Rate (CAGR) (2011-2014)
Secondary industry		
Mining	- 33.3%	4.6%
Manufacturing	33.2%	10.8%
Construction	-22.2%	27.2%
Supply of electricity, gas and water	159.3%	-2.0%
Tertiary industry		
Wholesale and retail	24.9%	21.0%
Transport, storage and post	26.2%	17.6%
Hotels and catering services	3rd 197.9%	27.9%
Financial intermediation	5.4%	37.9%
Real estate	67.1%	49.6%
Leasing and business	36.1%	12.9%
Health, social security and social welfare	1st 800.6%	1st 188.5%
Culture, sports and entertainment	67.0%	2nd 70.4%
Information transmission, computer services and software	126.3%	3rd 59.8%
Scientific research, technical service and geologic prospecting	-6.9%	33.2%
Management of water conservancy, environment public facilities	2nd 280.6%	29.3%
Other services	68.4%	43.0%

Source: 'China Statistical Database', NBS, http://data.stats.gov.cn/english/easyquery.htm?cn=C01; KPMG analysis

TOP 10 countries attracting Chinese overseas investment in 2014

	ODI Flow			ODI Stock		
		YoY	CAGR 2011-2014		YoY	CAGR 2011-2014
1	US	96.1%	61.3%	US	73.6%	61.7%
2	Luxembourg	259.0%	53.5%	Australia	36.9%	29.3%
3	Australia	17.1%	8.6%	Singapore	39.9%	24.9%
4	Singapore	38.4%	-4.9%	Luxembourg	50.3%	30.3%
5	UK	5.6%	1.8%	UK	8.5%	71.7%
6	Germany	58.0%	41.1%	Russia	14.7%	32.2%
7	Indonesia	-18.6%	29.0%	France	89.9%	31.4%
8	Netherlands	332.0%	83.1%	Canada	25.7%	27.8%
9	Laos	31.4%	30.8%	Kazakhstan	8.4%	38.2%
10	Pakistan	520.1%	44.9%	Indonesia	45.9%	59.1%

Source: '2014 Statistical Bulletin of China's outward foreign direct investment', MOFCOM, NBS and State Administration of Foreign Exchange, China Statistics Press, Beijing, September 2015

Vaughn Barber
Global Chair of KPMG's Global China Practice

Consistent with the findings in Australia, Chinese companies have increasingly invested globally in services, advanced manufacturing, technology and other high value added and consumption related sectors as well as in assets providing high and stable returns.

Chinese investment in Australia increased 32.9 percent in USD terms in 2015

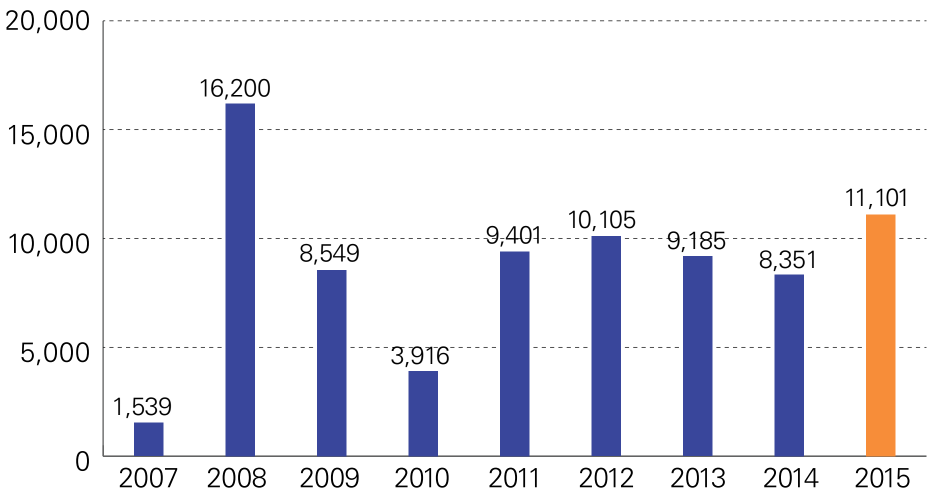
Based on the KPMG/University of Sydney database Chinese ODI in Australia for 2015 was USD 11.1 billion (AUD 15.09 billion), a 32.9 percent increase from USD 8.35 billion or a 59.5 percent increase in AUD terms from AUD 9.46 billion in 2014.

We are back into a positive annual growth trend after a 9.1 percent annual decline between 2013 and 2014. 2015 was the year with the second highest inflow recorded in new Chinese ODI, behind the previous peak driven by mining investment in 2008.

The drivers of this growth are a return to mega-sized deals by both SOEs and private companies, with seven deals of AUD 500 million or more; and a continuing increase in the number of investments, largely from Chinese private investors. 2015 saw the largest number of deals in any single year, with 65 legally binding deals announced.

The relative depreciation of the AUD has attracted Chinese investment and increased AUD equivalent results in 2015 significantly.

Historical trend of Chinese ODI into Australia by volume (USD million)



Source: KPMG/University of Sydney database

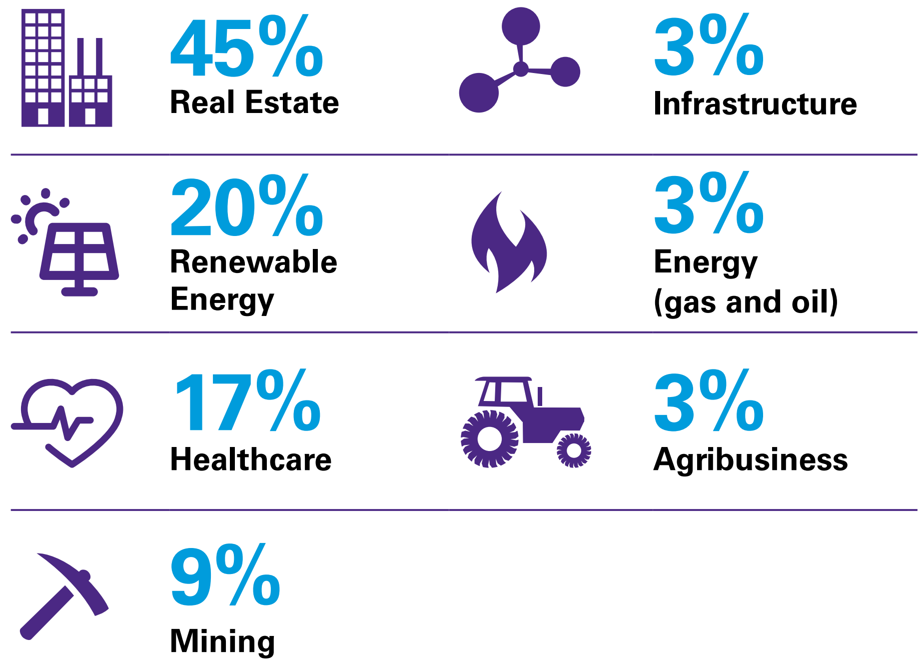
Chinese investment in Australia by industry

Overall, real estate continued to dominate with 45 percent of the 2015 total investment.

One very large renewable energy deal accounted for 20 percent of the total. 2015 was also a breakthrough year for the healthcare and agribusiness sectors.

From an industry sector perspective, Chinese investment in Australia now reflects the new normal: China's focus on middle class consumption – premium quality health, lifestyle and services.

Chinese ODI in Australia by industry in 2015 (AUD)



Chinese ODI by Industry in 2015 (AUD)

Industry	Value (million AUD)	%
Real Estate	6,852.70	45
Renewable Energy	3,000.00	20
Healthcare	2,550.00	17
Mining	1,299.00	9
Infrastructure	513.00	3
Energy (gas and oil)	500.00	3
Agribusiness	375.20	3
Total	15,089.90	100

Source: KPMG/University of Sydney database.

Industry sector analysis

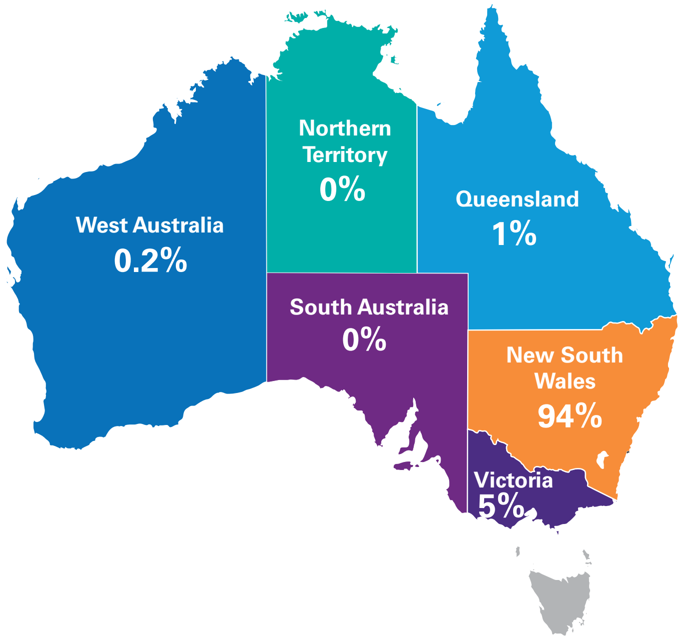
Real estate[6]

Real estate remains the sector attracting the largest proportion of Chinese investment, accounting for 45 percent of the investment volume in 2015.

Ninety-four percent of the total real estate investment was in New South Wales.

Together with the United States and Europe, Australia is a strategic investment destination for Chinese real estate investors who seek better returns and asset diversification overseas, driven by expectation of long term population and economic growth. Chinese investment in the real estate sector continues to have a geographic focus on NSW and Victoria.

After 2 years of rapid growth, Chinese developers believe the residential market is stabilising. In response, they're focusing more on long term development projects and balancing their portfolio of residential development projects and commercial properties including office, retail and hotels. China Investment Corporation's AUD 2.45 billion purchase of Investa Office portfolio is a good example of diversification of Chinese investment into alternative fields in the Australian real estate sector.



[6] "Real estate" referred to in this report does not include residential apartment and home sales.

Renewable energy

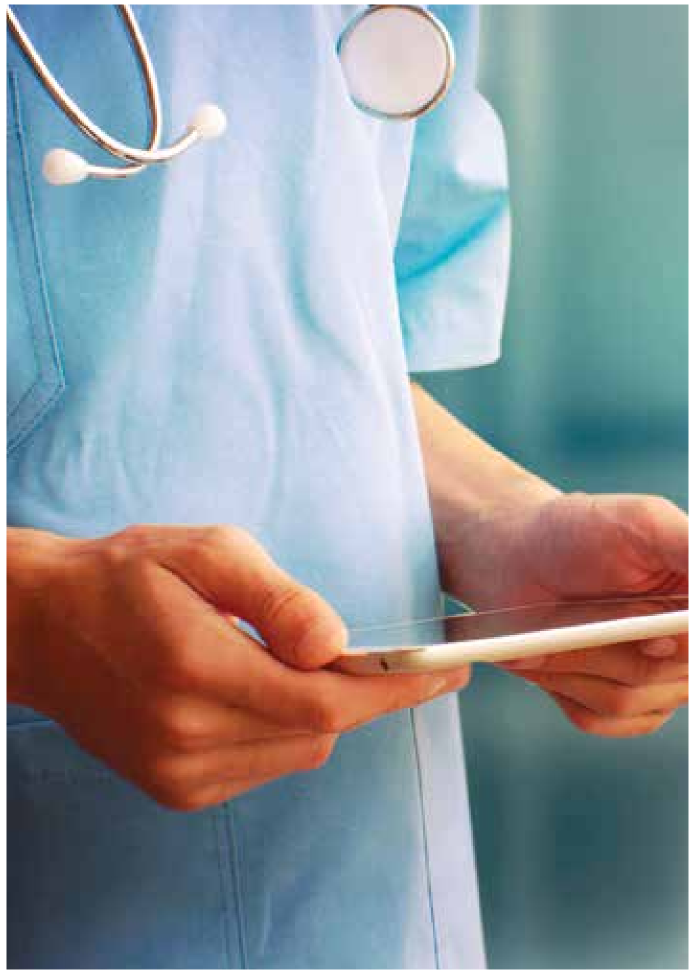
The outlook for Chinese investment in the wind energy sector is more positive than in previous years.

State Power Investment Corporation's acquisition of Pacific Hydro was the largest deal of the year. The deal made renewable energy the second largest sector receiving Chinese investment in 2015 and confirms China's return to the renewable energy sector in Australia, following a quiet few years since wind and solar were active sectors.

Agreement on the Renewable Energy Target (RET) was reached in 2015, creating a stable policy environment which has given Chinese companies renewed confidence to invest in Australia's wind energy sector.

Healthcare

Investment in healthcare has finally moved from the exploratory stage to realisation with four deals made during the year. These included Biostime's acquisition of the Swisse Wellness brand for AUD 1.38 billion and one major hospital deal close to AUD 1 billion with Luye Medical Group acquiring Archer Capital's Healthe Care.



Infrastructure

Chinese investment in the Australian infrastructure sector continued in 2015. The major deal was the 99 year lease of the Port of Darwin to the Landbridge Group for AUD 506 million. Chinese companies also participated unsuccessfully in the bid for the 99 year TransGrid lease in NSW.

Chinese companies with financial and technical expertise and financing capability in infrastructure provision are attracted by a strong local pipeline of attractive project opportunities offering relatively safe returns and a longer term investment horizon for cooperation.

Australia is a learning ground for Chinese companies intending to acquire international skills and knowledge, such as corporate governance and working with local stakeholders. Chinese investors cite China Communications Construction Company's 2014 AUD 1 billion acquisition of John Holland as an example of a large scale investment to acquire local skills, brand and credibility to enable better participation in infrastructure projects both in Australia and internationally.

Mining, energy, oil and gas

Mining investment was less than 10 percent of the total but remains on China's investment agenda with a shift towards non-ferrous metals.

Chinese investors have shown interest in non-ferrous metals including gold, lithium, and copper. In 2015, we have seen Guangdong Rising's AUD 1.2 billion acquisition of PanAust and Jiangxi Ganfeng Lithium's investment in Australian lithium mining company Neometals.

With expanded government infrastructure spending under the new 13th Five Year Plan (2016 – 2020), Chinese demand for iron ore and coal may prove to be stronger than originally expected.

Agribusiness

Chinese investment in Australian agribusiness remains a small but emerging story. In our 2013 report *Demystifying Chinese investment in Australian Agribusiness* we discussed the complimentary relationship between Australia's leading food production industry and China's rising middle class demand for high quality, safe and reliable food and beverages.

In 2013 we reported there was less than AUD 1 billion in total aggregated historical investment in the sector, and estimated that Chinese owned less than 1 percent of Australian land. In 2014, while there was lots of interest and activity, we reported very few completed agribusiness deals of a large scale commercial nature; and agribusiness investment only accounted for 1 percent of total Chinese investment.

2015 was the first year to show substantial growth in agriculture and agribusiness investment with a total volume of AUD 375.2 million spread across 12 deals including dairy, beef and cotton.

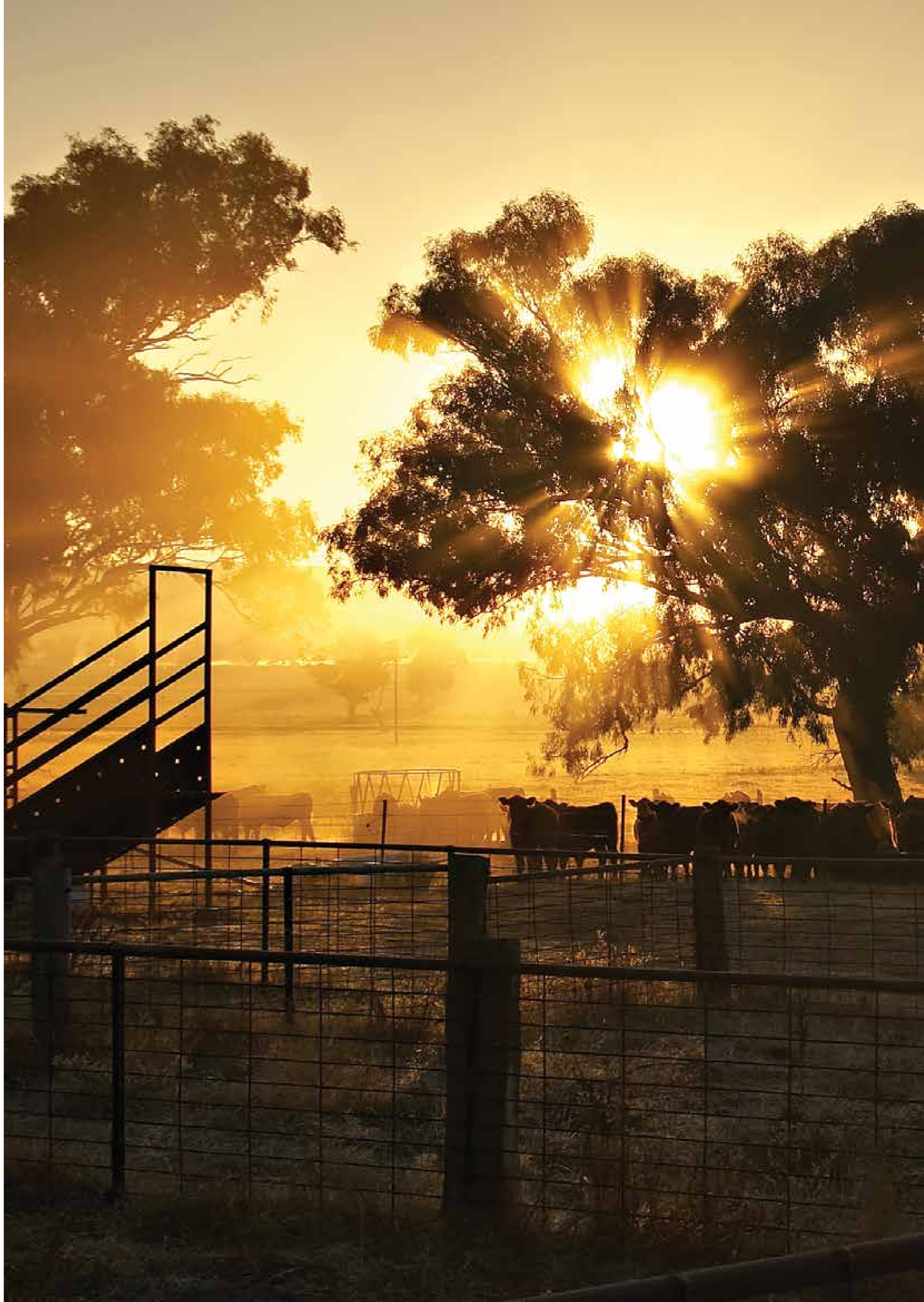
The largest deals with a combined value of over AUD 170 million were Beingmate's investment in Darnum/Fonterra in Victoria, Tianma Bearings Group's acquisition of Wollogorang and Wentworth stations in the Northern Territory, and Dashang's investment in Glenrock Station.

There were also interesting investments in Moxey Farms by New Hope who co-invested with Australian partner Freedom Foods and JD.com's (an e-commerce platform) investment in the MG Unit Trust.

2015 also saw several larger sized cattle and cotton stations in New South Wales, Queensland and the Northern Territory sold to Chinese investors including Glenrock Station, Holymount Station, Elizabeth Downs and Undabri Cotton Farm.

During the year, the Foreign Investment Review Board (FIRB) limit for mandatory investment approval in agricultural land acquisition was reduced to a one off and aggregated level of AUD 15 million. In 2015, a FIRB application from a Chinese investor to purchase S Kidman & Co was rejected by Treasury on the basis of national security concerns relating to one part of the project. Both issues again reflect the sensitive issue of the sale of large scale productive agricultural land in Australia to foreign investors – a continuing and very public debate that Australians are having.

For 2016, there is strong interest from Chinese investors in Australian agribusiness. Chinese agribusiness companies see themselves benefitting from the signing of the China Australia Free Trade Agreement (ChAFTA) in the long term. Yet, they also find ChAFTA has raised expectations for the future growth of Australian agribusiness which leads to higher asset market valuations and prices.



Chinese investment in Australia by geography

New South Wales remained the top destination for Chinese direct investment in 2015, attracting 49 percent of the total.

While lower in percentage terms, NSW actually received more investment in absolute dollar terms increasing from AUD 6.8 billion in 2014 to AUD 7.44 billion this year.

Investment in NSW was mainly concentrated in real estate (86 percent), healthcare (13 percent) and agribusiness (1 percent).

Victoria's share improved from 8 percent (AUD 0.7 billion) in 2014 to 34 percent (AUD 5.1 billion) in 2015. Victoria attracted investment in renewable energy, healthcare, real estate and agribusiness.

The Northern Territory has attracted AUD 564.5 million of Chinese investment in 2015, placing it ahead of SA, WA and Tasmania for the first time.

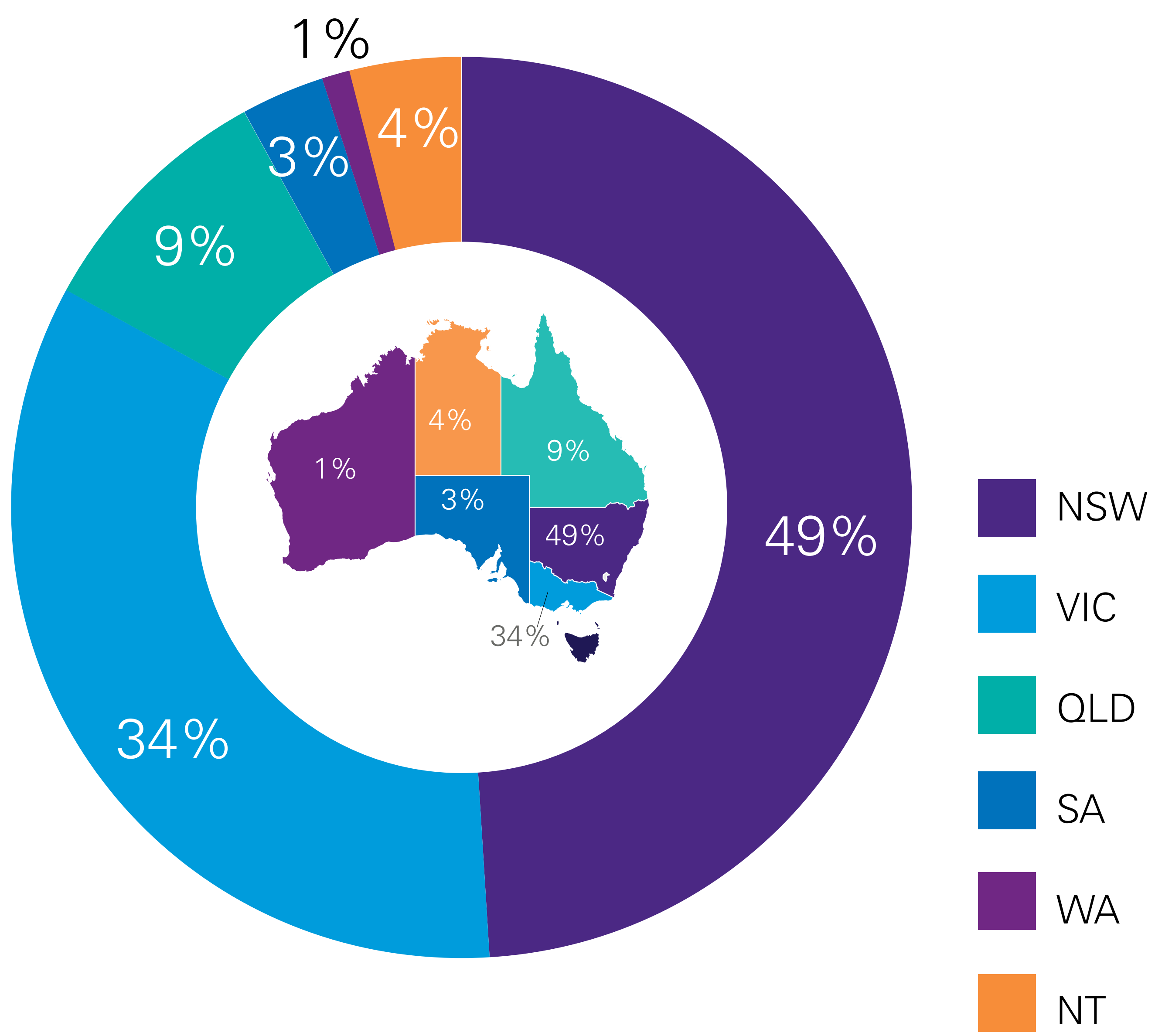
Reflecting the dramatic fall in global resource commodity prices, Western Australia attracted the least Chinese investment in 2015, with AUD 114 million and accounting for less than 1 percent of the total investment.

Chinese ODI by state and territory in 2015 (AUD)

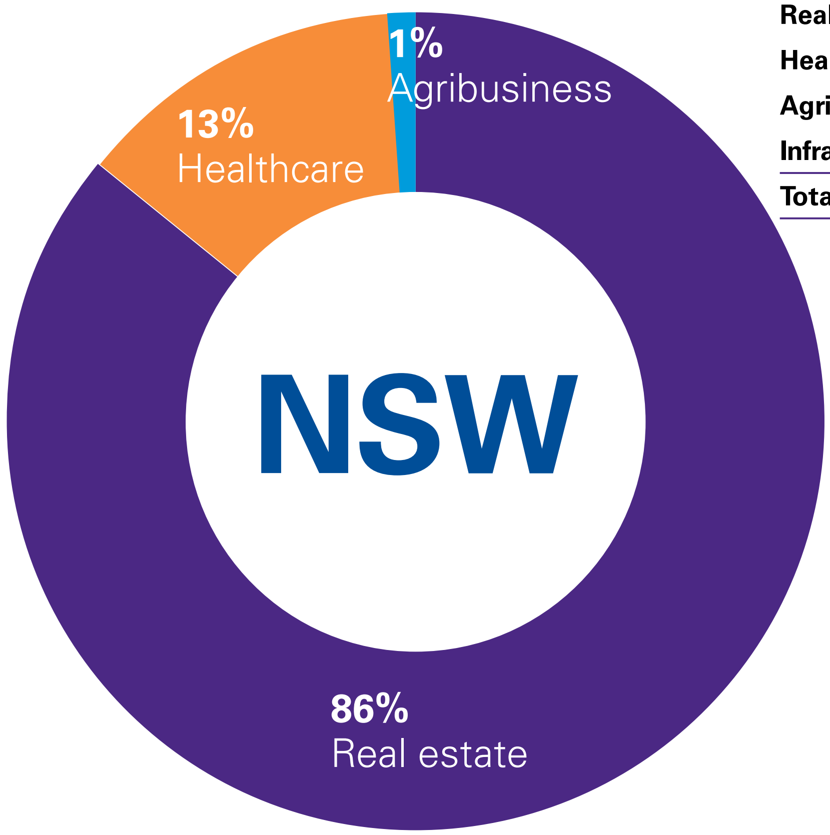
	Value (million AUD)	%
NSW	7,439.90	49
VIC	5,066.50	34
QLD	1,365.00	9
NT	564.50	4
SA	540.00	3
WA	114.00	1

Source: KPMG/University of Sydney database.

Chinese ODI in Australia by state and territory in 2015 (AUD)

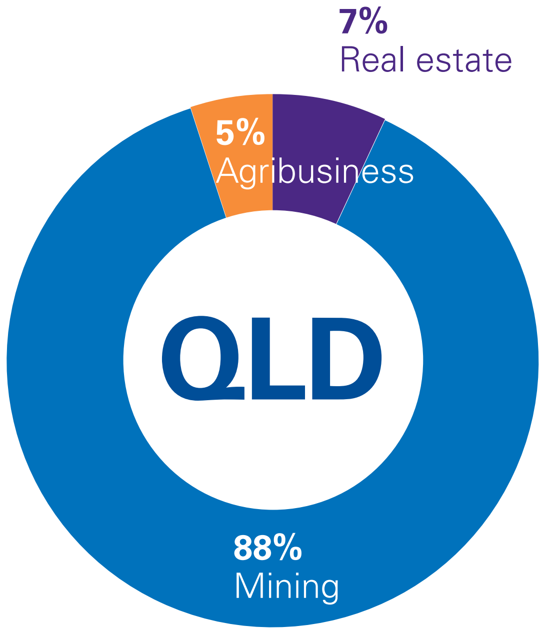


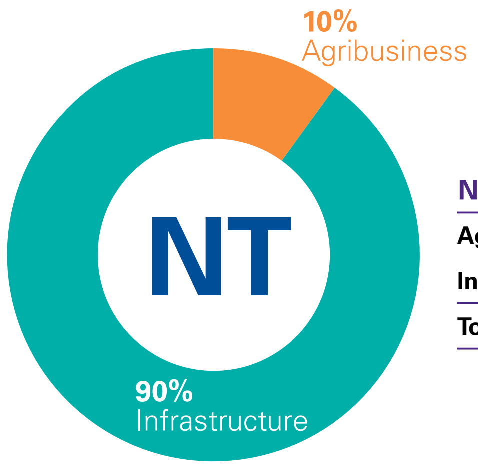
Total completed deals by state and industry



NSW Completed Deals	Value (million AUD)
Real estate	6,419.90
Healthcare	938.00
Agribusiness	75.00
Infrastructure – rail engineering	7.00
Total completed deals	**7,439.90**

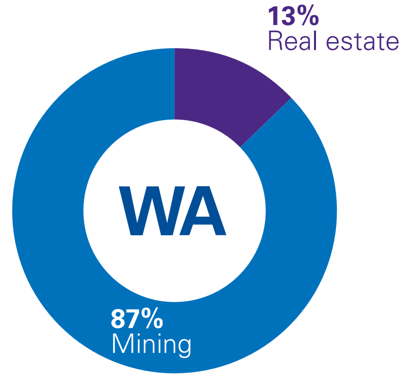
QLD Completed Deals	Value (million AUD)
Real estate	95.00
Mining	1,200.00
Agribusiness	70.00
Total completed deals	**1,365.00**

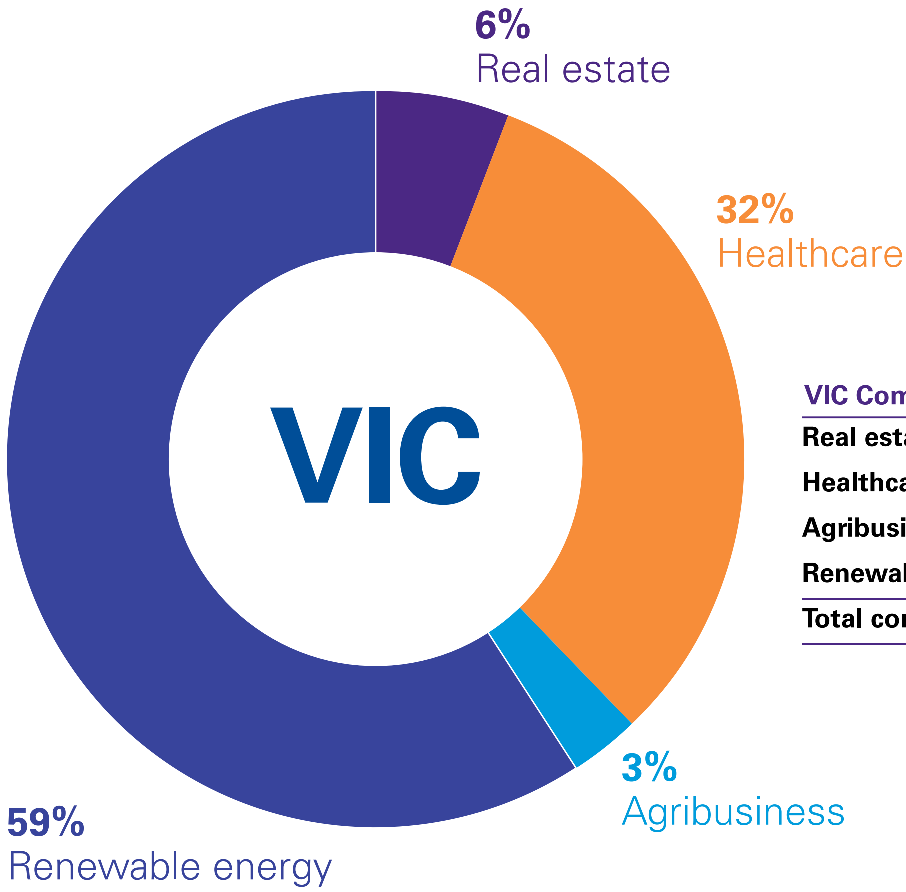




NT Completed Deals	Value (million AUD)
Agribusiness	58.50
Infrastructure	506.00
Total completed deals	**564.50**

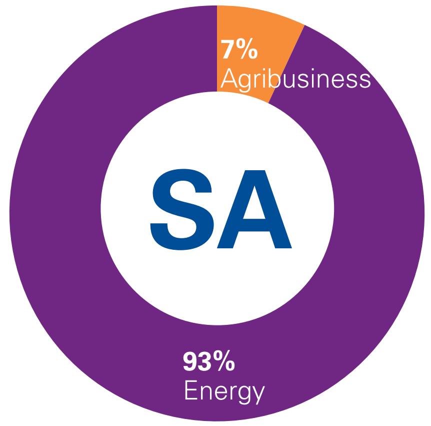
WA Completed Deals	Value (million AUD)
Real estate	15.00
Mining	99.00
Total completed deals	**114.00**





VIC Completed Deals	Value (million AUD)
Real estate	322.80
Healthcare	1,612.00
Agribusiness	131.70
Renewable energy	3,000.00
Total completed deals	**5,066.50**

SA Completed Deals	Value (million AUD)
Agribusiness	40.00
Energy	500.00
Total completed deals	**540.00**



Chinese investment by deal size

In 2015, there were seven mega-sized deals of AUD 500 million or more each, with four well over AUD 1 billion.

Major transactions included:

Selected major Chinese investments into Australia in 2015

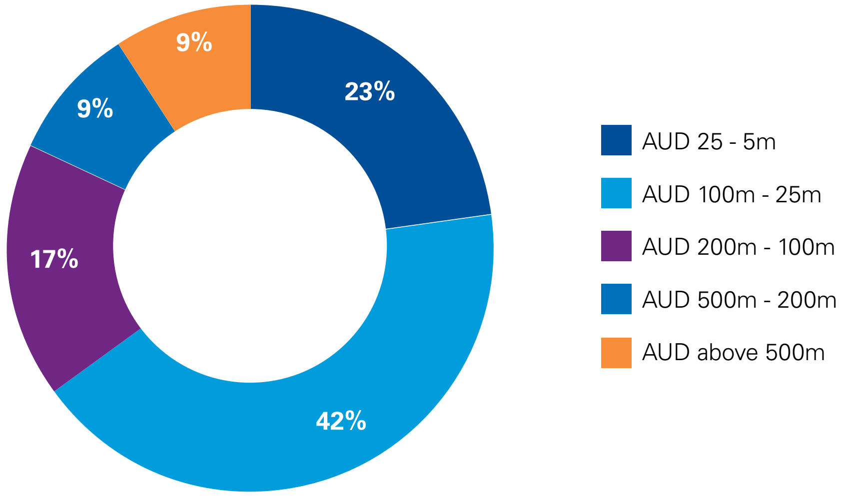
Target Name	Investor Name	Industry Sector	Location	Value of Transaction (AUD mil)
Pacific Hydro	State Power Investment Corporation	Renewable Energy	VIC	3,000.0
Investa office portfolio	China Investment Corporation(CIC)	Real Estate	NSW	2,450.0
Swisse Wellness	Biostime	Healthcare	VIC	1,380.0
PanAust Ltd	Guangdong Rising H.K (Holding) Limited. "GRAM"	Mining – copper and gold	QLD	1,200.0
Healthe Care	Luye Medical Group	Healthcare	NSW	938.0
Port of Darwin	Landbridge	Infrastructure	NT	506.0
Santos	Hony Capital	Energy	SA	500.0
Sydney Hilton	Bright Ruby	Real Estate – Hotel	NSW	442.0

Source: KPMG/University of Sydney database

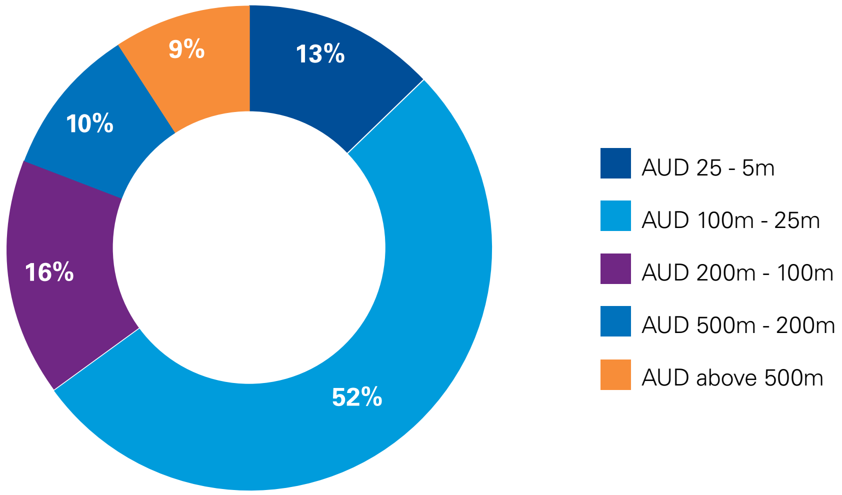
Forty-two percent of the deals were between AUD 25 million and AUD 100 million in size.

Sixty-five percent of the deals were below AUD 100 million in 2015, consistent with 2014.

Size of deals in 2015 (by number of deals)



Size of deals in 2014 (by number of deals)



Size of deals in 2015

Size of Deal (AUD)	number of deals	%	Value (AUD mil)	%
AUD 25m-5m	15	23	240.50	2
AUD 100m-25m	27	42	1,328.90	8
AUD 200m-100m	11	17	1,554.50	10
AUD 500m-200m	6	9	2,492.00	17
AUD Above 500m	6	9	9,474.00	63
Total	**65**	**100**	**15,089.90**	**100**

Source: KPMG/University of Sydney database.

Chinese investment in Australia by ownership

Last year's report showed that 2014 was the first year in which investment from China's private investors exceeded SOEs by total volume and number of transactions.

Our 2015 data shows a return by SOEs to claim a 49 percent share of investment volume, reflecting two major SOE investments by CIC in Investa Office Trust (and AUD 30 million on Daydream Island resort) and SPIC's investment in Pacific Hydro.

By number of deals, our data shows a continued domination by Chinese private investors which also correlates to the larger number of smaller deals – 65 percent of deals were below AUD 100 million. By number, 13 deals were by SOEs, while 51 were by private Chinese enterprises.

2015 deals by ownership

Ownership	Investment Value (AUD million)	%	no. deals	%
SOE	7,413.00	49	13	20
Private	7,226.90	48	51	78
SOE and Private JV	450.00	3	1	2
	15,089.90	100	65	100

Source: KPMG/University of Sydney database.

Chinese executive perceptions of Australia's investment climate

Chinese Investors Survey and Interviews

2015 is the second year that KPMG and The University of Sydney have reported on our *Chinese Investors in Australia Survey*. The survey provides insights into the perception of the Australian investment climate by Chinese investors and the key challenges they face in Australia.

The *Chinese Investors in Australia Survey* was conducted between September 2015 and February 2016 by KPMG and the University of Sydney with the cooperation of senior executives from 46 Chinese invested companies in Australia. These companies operate in a broad range of sectors including mining, gas, agribusiness, real estate, finance, infrastructure and engineering.

In addition, between 26 February and 4 March 2016, KPMG and The University of Sydney conducted in-depth interviews with 11 Australian-based Chinese companies, of which six were state-owned (SOE) and five privately owned (POE) enterprises in sectors including agribusiness, real estate, renewable energy, infrastructure, mining, and energy.

Profit is the main driver of Chinese ODI in Australia

Our results have shown that the top five motivations for Chinese investment in Australia are:

1. making profits
2. securing resources
3. building an international brand
4. accessing global markets and
5. gaining experience for operating in other markets.

Q: How important are the following points for your investment in Australia? (Importance on a scale of 0 to 10; 0=Not important, 10=Very important)

No. of respondents: 43

Source: Chinese Investors in Australia Survey 2015.

Our interviews indicate that investing in Australia is not opportunistic. Many of the businesses we interviewed completed detailed research before deciding to invest into Australia. One company studied over 20 overseas markets looking at the local economy, policies, migration data and more before choosing Australia for their first overseas investment. One agribusiness firm looked at nearly 100 projects in Australia but only a handful entered into feasibility and due diligence stages. Return on investment was quoted as the most important criterion for selecting projects.

For five out of the 11 interviewed companies, Australia was its first overseas investment destination. Before making decisions regarding which country to invest in, staff at headquarters in China usually conduct extensive desktop research to assess the advantages and disadvantages of each potential investment destination.

Among the key reasons that interviewed companies gave for choosing to invest in Australia were:

- long-term stable economic returns
- low sovereign risks
- a stable policy environment
- mature financial markets
- transparent legal system.

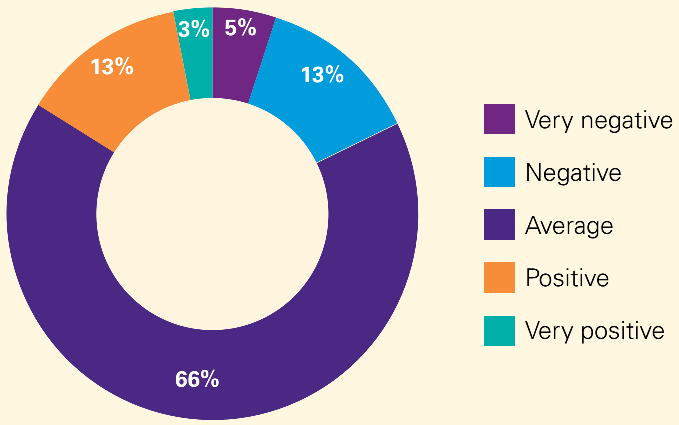
Australia is seen as a learning ground for entering other developed markets. The closer economic relationship between China and Australia has helped, as does the same time zone between countries (west coast Australia) and the sense that Australia is a preferred destination for Chinese students, tourists and migrants.

Despite perceptions of Chinese bidders offering much higher premiums in order to secure investments and projects in Australia, most very carefully consider the medium and long term future returns. Some SOEs mentioned they have recently withdrawn from projects that might have negative net profit regardless of other merits, as it is increasingly difficult to obtain relevant Chinese government approvals. Some POEs have higher expectations of investment returns and would not consider projects which do not bring adequate returns within 3 years.

Investment momentum set to continue beyond 2016

2015 recorded the second highest inflow in new Chinese ODI to Australia, behind the previous peak in 2008. Eighty-two percent of the respondent companies recorded average or above average profitability.

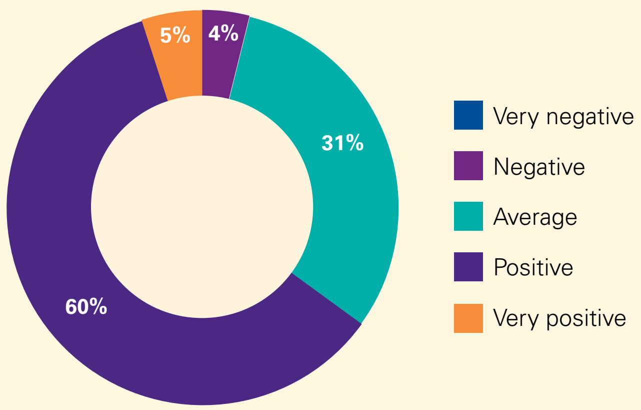
How was your profitability in 2015



Chinese investors in Australia have a highly positive business outlook for the next 3 years. Sixty-five percent of the respondent companies agree that their 3 year business outlook is positive, and 55 percent of the respondent companies are planning to expand their investments in Australia in 2016.

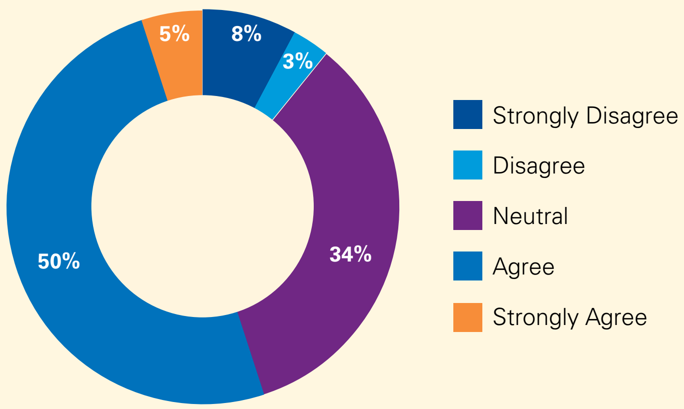
All businesses we interviewed hold a highly positive medium to long term view of Australia and are looking to increase their investments, including investors in the real estate sectors. Companies we interviewed emphasised their strategic motives for investing in Australia. They see Australia as an entry point into new markets.

What is your business outlook for the next 3 years?



No. of respondents: 45

Over the coming year, we are planning to expand our investment in Australia.



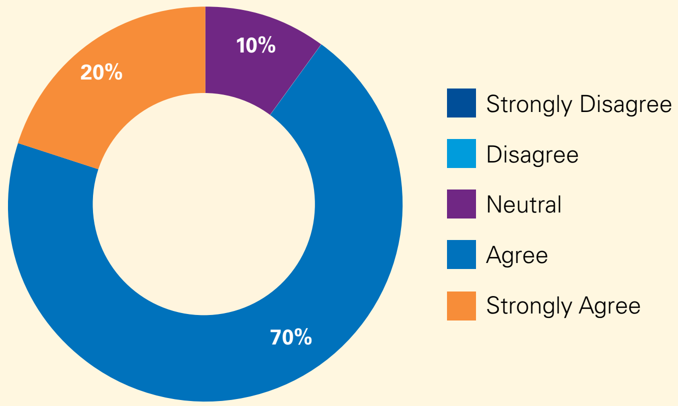
No. of respondents: 45

Source: Chinese Investors in Australia Survey 2015.

China-Australia FTA

An overwhelming percentage of Chinese invested companies in Australia believe that they will benefit from ChAFTA.

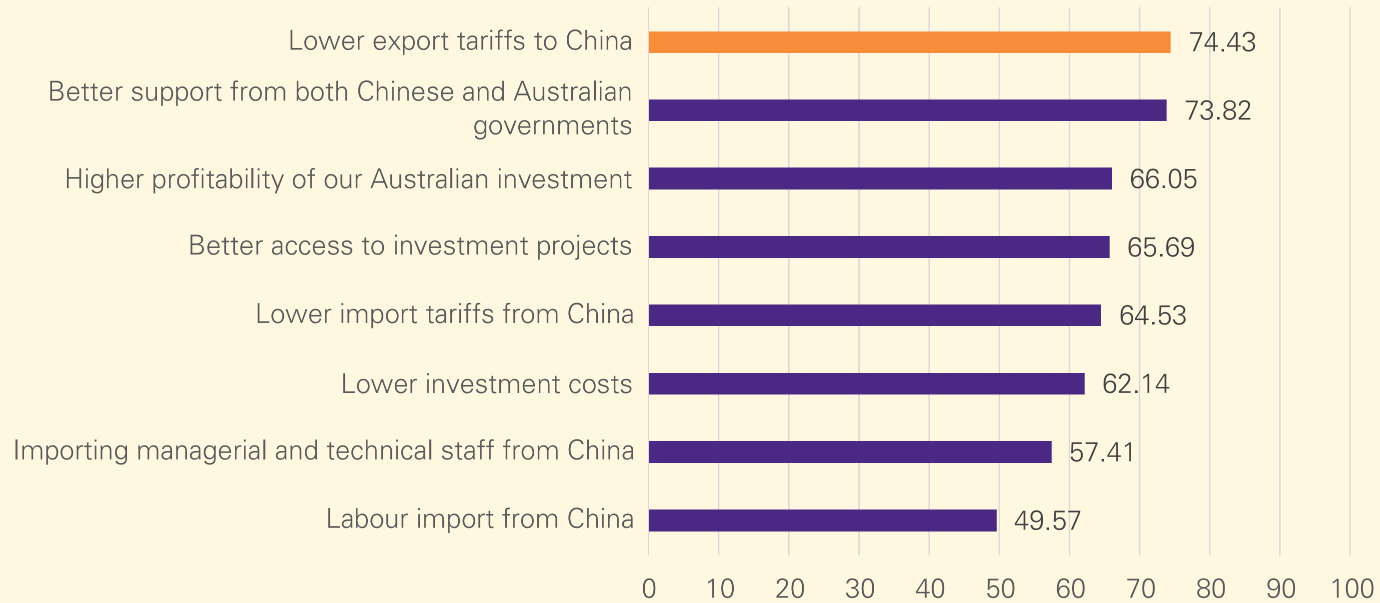
Chinese Investors in Australia would benefit from ChAFTA



No. of respondents: 46

For Chinese invested companies the benefits of ChAFTA are reduced export and import tariffs that will enhance the profitability and asset value of their operations in Australia. They also expect lower investment costs and easier entry for managerial and technical staff and to a lesser degree labour import from China.

Q: For your company, what are the benefits of the China Australia FTA? (Importance on a scale of 0 to 100; 0=Not important, 100=Very important)



No. of respondents: 38

Source: Chinese Investors in Australia Survey 2015.

Local integration

Interviewees stated that the initial investment is only one part of the overall investment strategic planning. For example, in real estate development, the total investment involves purchasing of land, developing the building program and design, obtaining necessary planning approvals and financing, building the structures, marketing and ultimately selling the property. Chinese property developers in Australia usually sub-contract with local partners which creates opportunities and jobs for local businesses. For instance, a real estate business we interviewed commenced a project in Southwest Sydney in 2015 which will complete in 2020. Design, construction, purchase of materials, marketing and advisory are all sub-contracted out to local businesses. The flow-on amount of new investment by Chinese real estate developers is much larger than the initial investment that is registered in investment data.

Based on information from the 11 interviewed companies, their overall number of local employees is 8,070, while the number of expatriate employees sent from China to participate in Australian operations is 58, accounting for less than 1 percent of their total employment.

Perceived challenges to local integration

From the interviews we learned that Chinese investors are making increased efforts to adjust to Australia's unfamiliar market and institutional environment. We have noticed a generational change from senior Chinese executives embedded in the traditional SOE culture to younger, internationally experienced and bilingual managers. We were also told of Chinese investors adopting localisation strategies to overcome local perceptions of being foreigners, by retaining Australian management teams and local employees; employing people with cross-cultural work experience; working with local contractors, designers and service providers including local banks, accountants, lawyers and consultants in many fields.

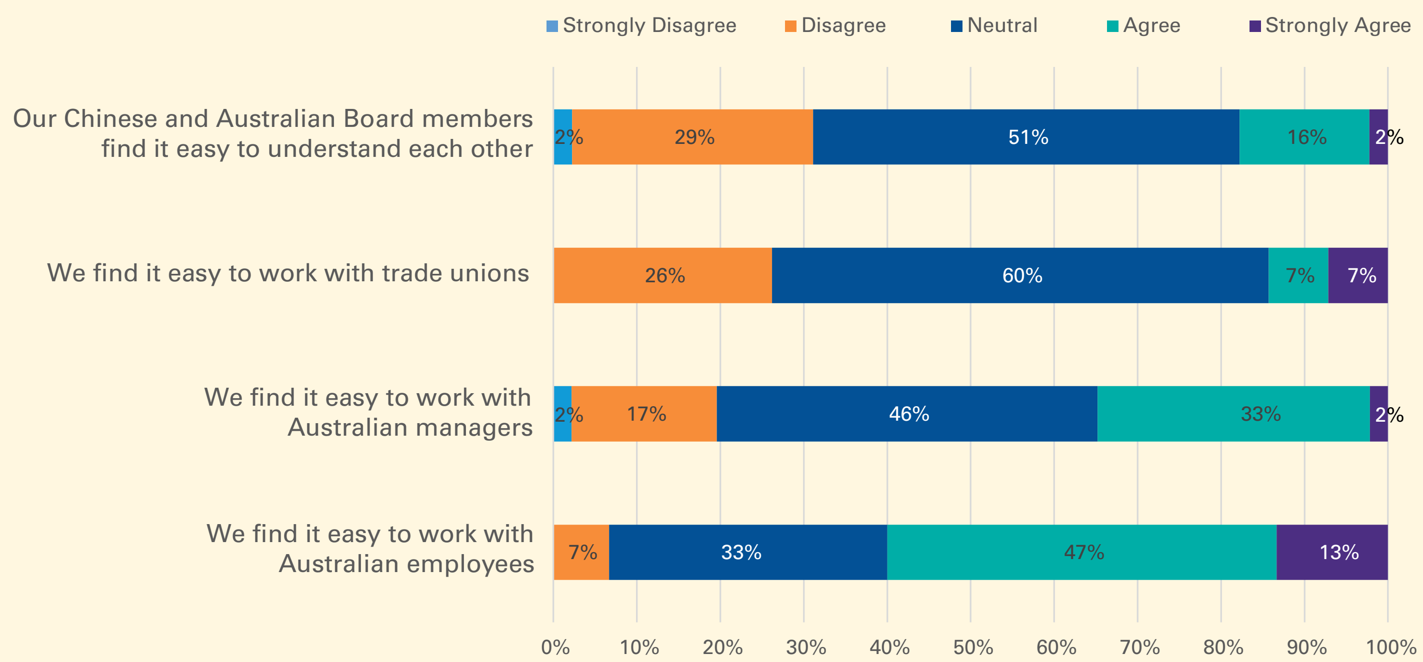
However, the change will take time and much effort. The corporate structure of Chinese companies is typically hierarchical, with strong control from the top and middle-level management expected to concentrate on implementation. This is quite different from the flatter structures and generally egalitarian culture in Australia.

Head offices in China are keen to play a key role in the operational decision-making but sometimes without detailed local knowledge. Many businesses interviewed felt they had to spend extra effort on communicating with their head office reporting lines in order to improve their understanding which can affect the efficiency of local operations.

Some of the Chinese businesses we interviewed admitted they found it challenging to balance the views and interests of different stakeholders. Our survey established a hierarchy of communication issues with Australian non-executive board directors and trade unions being the most difficult to deal with and less problems dealing with local employees.

Over regulation is perceived as a burden in some industries in Australia. Chinese investors feel the amount of regulations they face, ranging from acts of parliament, delegated legislation, legal documents, licences, judicial interpretations, rules, regulations to administrative policy, has become a hidden cost of doing business in Australia. However, with regards to working with Australian governments, the same Chinese investors generally view Australian authorities and regulators as supportive and professional towards Chinese investment.

The 11 interviewed companies had no experience of applications being rejected by FIRB in the entry phase, but some had concerns that FIRB was demanding disclosure of commercial information and imposing unexpected conditions on operational decisions. This included conditions imposed on board composition and decisions on business planning, such as capex discussions and monitoring the business.



No. of respondents: 38

Source: Chinese Investors in Australia Survey 2015.

Outlook for 2016: a continuation of the new normal?

China's economy: Chinese consumer services, e-commerce and innovation will be the 'fast track' growth drivers.

While China's economic growth rate is slowing and there are major challenges to resolve in the traditional state owned sectors – with alarmingly high levels of private debt, overcapacity, low productivity and pollution issues – there are also many positives.

While 6.9 percent gross domestic product (GDP) growth in 2015 represents a 25-year low for China, it is still one of the highest among the world's largest economies. The incremental economic output generated by China's 6.9 percent growth today is much higher than in the years when China was experiencing double-digit growth. According to forecasts prepared by the IMF, China is expected to continue being the largest contributor to world GDP – in purchasing power parity terms – and is expected to account for nearly 20 percent of world GDP by 2020, compared to 15.5 percent for the European Union and 14.9 percent for the US.

China's transition to an innovation-driven, service-oriented and consumption-led economy has led to the emergence of a two-track economy. One track – in basic manufacturing and traditional industries – is experiencing significant headwinds; while a second track – in services, advanced manufacturing and consumer markets – is exhibiting strong growth potential. Understanding the objectives for development of these industries helps explain policy settings and identify opportunities for foreign firms investing in China and Chinese firms investing abroad.

The services element of the economy has presented robust growth, offsetting the impact of the industrial slowdown. The resilience that the service sector has shown amid the global and domestic slowdown helps to underline its importance for China's long-term growth, and explains why its development is among the Chinese Government's top policy priorities.

Contribution from consumption as a percentage of GDP in China has been rising steadily and still has considerable potential to grow. We expect Chinese consumers will become one of the main drivers of China's growth in the future, especially given the country's current rapid urbanisation rate. E-commerce is turning into a pillar of growth: reducing costs and other barriers to entry, increasing competition, driving down prices, and unlocking new demand. E-commerce has become a dominant feature in the consumer spending landscape in China with online retail sales recording a 37.2 percent year-on-year increase to reach RMB 3.8 trillion in 2015, and this is forecast to almost double by 2018.

Over the course of 2015, the Chinese Government introduced a number of major policy initiatives to facilitate the country's transition into a high value-added economy, tackling issues such as overcapacity, increasing the productivity and international competitiveness of China's traditional industries, and promoting innovation and entrepreneurship.

Importantly, rather than focusing on the speed of growth, these initiatives place importance on the quality of growth, in order to achieve a more balanced level of development that is conducive to long-term prosperity. We expect this to continue being a feature of China's policies in the next few years, especially following the release of the 13th Five-Year Plan in March 2016. However the implementation is proving very difficult and slower than hoped by external observers.

Global Chinese ODI outlook: Agriculture and food, infrastructure, high-end manufacturing and real estate will continue to be important sectors in 2016

KPMG's Global China Practice expects China's ODI will continue to grow by more than 10 percent per annum, driven by factors including Chinese companies' desire to acquire experience, technology, brands and human capital to become more competitive, and to access high-quality products and services that can be deployed in China to meet its evolving consumption trends. Agriculture and food, infrastructure, high-end manufacturing and real estate will continue to be important sectors in 2016, while ICT, healthcare and transportation are new 'hot' sectors to watch.

KPMG also predicts more overseas investment by POEs and financial investors, as well as more win-win cooperation between Chinese and foreign companies. A key feature of the 'new normal' for China's relations with the rest of the world is 'cooperation' and 'collaboration', both in China and in markets outside China, to the mutual benefit of China, the partnering countries and the third-country markets.

North America, Europe and other developed economies are expected to attract more investment as the availability of high-quality targets in those regions can help Chinese companies upgrade, transform and boost their competitiveness. More projects and investments will be undertaken along the 'Belt and Road', as the objectives come to be better understood and the mode of implementing this initiative continues to evolve over the coming year.

Careful attention should be paid to three positive drivers of Chinese ODI in 2016, namely China's advancement of a new paradigm of international cooperation – through its 'Belt and Road' initiative for example, the emergence of new funding sources, and the implementation of the recent free trade agreements with Australia and South Korea.

Already in 2016, we have seen some absolutely massive deals in the technology sectors announced globally, including:

- ChemChina's USD 43 billion agreement to acquire Syngenta, a Swiss agrochemical and seeds company
- HNA Group's USD 6 billion acquisition of Ingram Micro, a US supply chain and technology solutions company
- Haier's USD 5.4 billion acquisition of General Electric's appliances business in the US
- Wanda's USD 3.5 billion acquisition of US film studio, Legendary Entertainment
- ChemChina's USD 1.0 billion offer to Krauss Maffei, a German manufacturer of machinery for rubber and plastic products and
- Ningbo Joysun Electronic Group's USD 0.92 billion acquisition of Key Safety Systems, a US advanced engineering company specialising in automotive safety.

What this all means for Australia: a continuation of 2014-15 trends?

While there are genuine concerns locally for the impact of China's slowing economy and the risks and potentially negative impacts of China's comprehensive reform agenda, including the impacts of treating the alarming private sector debts, foreign exchange devaluation and outflow controls, we see no reason to be concerned by a sudden fall in Chinese ODI to Australia. In fact we take great confidence that Chinese ODI has been increasing and there continues to be large investments by Chinese companies in 2016.

As clearly demonstrated, competition for attracting Chinese ODI (as well as tourists and students) is intense but Australia continues to offer many of the products and services that Chinese consumers desire – prestigious real estate, premium food, tourism, quality healthcare & life sciences, tertiary education. The fact we are in the same time zone as China, interestingly is often mentioned as another key factor in our favour.

New opportunities in 2016 for science and technologies

From above we can see Chinese investors are increasingly focused on acquiring science and technology to help solve their domestic challenges around ageing demographics, environmental pollution, food safety & supply, financial services & capital markets to name a few. One of our greatest opportunities and challenges is delivering on our national Innovation Agenda to develop and commercialise fintech, medtech, agtech, cleantech products and services which can help China to address its national objectives and therefore investment from Chinese strategic and capital partners.

Final word

All of this augers well for continuing Chinese trade and investment in Australia. As we've said in past reports, it is important that Australian companies, with strong leadership from directors and executives and support from institutional investors, continue to meet and seek partnerships with reputable Chinese companies, to leverage the best of eachothers' capabilities and invest together for long term success.

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