

Oaklins

# Voice from China

Quarterly update on the  
M&A market in China

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# Introduction

2019 was a troubled time for China, as its trade war with the United States affected the country's economy and the mass protests in Hong Kong created some tension with the central government. But the coronavirus outbreak that began at the start of 2020 has completely overshadowed these earlier events and is likely to have a much graver and more enduring impact on both China and the rest of the world.

It goes without saying that this holds true for all M&A activity into and out of China as well.

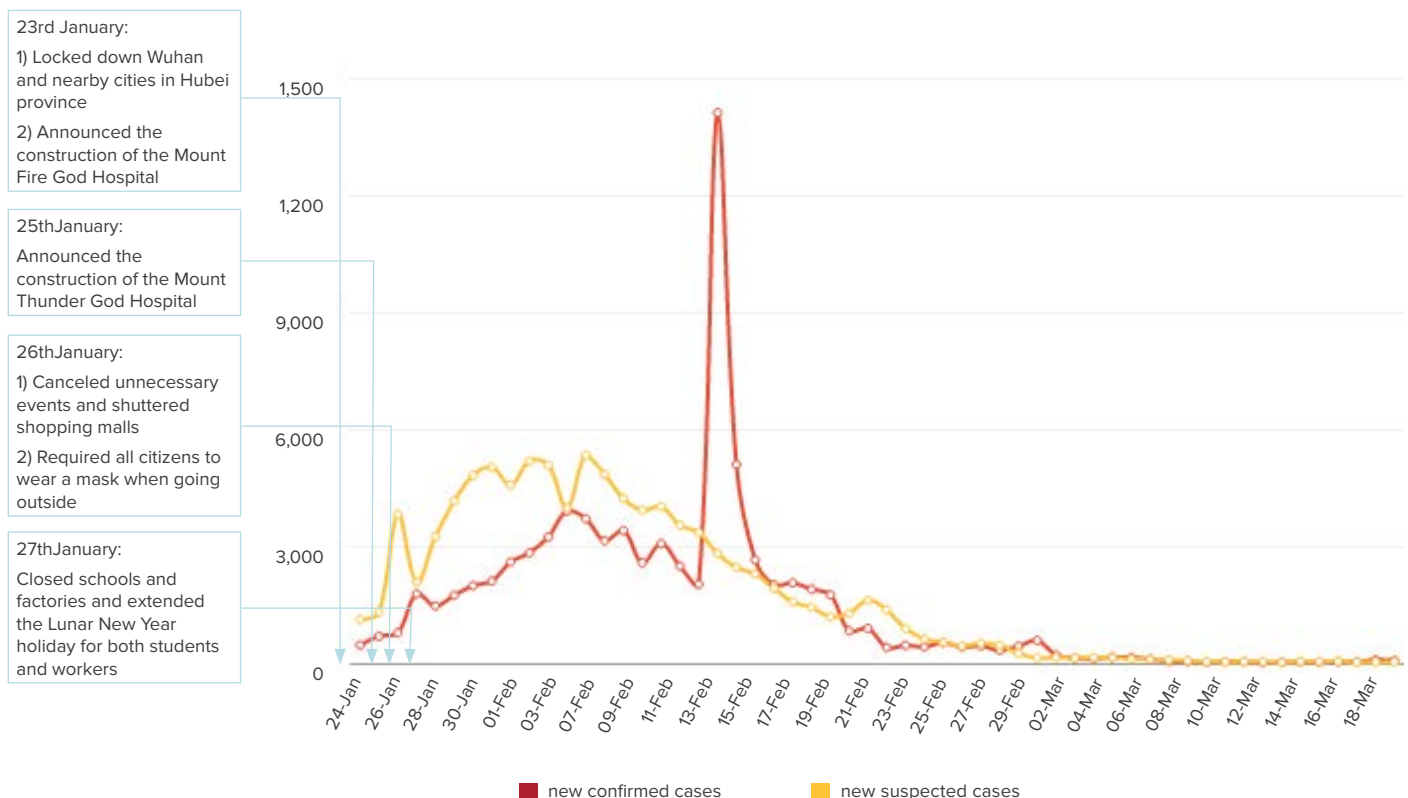
## SOME BACKGROUND ON THE OUTBREAK

Since the contagion first began in January, the Chinese government has taken a series of increasingly bold steps to contain the epidemic, and the latest indications are that these are working.

As of 8 March, fewer than 200 new cases of COVID-19 (now the official name of the coronavirus) were being reported daily — down from a peak of 4,000.

These containment measures, however, also significantly impaired China's economy during the first quarter — although the slowdown is now abating. By the end of February, work at 80% of all businesses had resumed, and schools are expected to reopen in April.

Measures taken by the Chinese government and the growth of new coronavirus cases



Source: <https://i.snssdk.com>

If, as hoped, the Chinese government can fully contain the outbreak within a six-month period, then we expect demand to rebound and the virus' negative economic consequences to be reversed the following year. Such a scenario would be similar to what took place in the wake of the 2003 SARS outbreak.

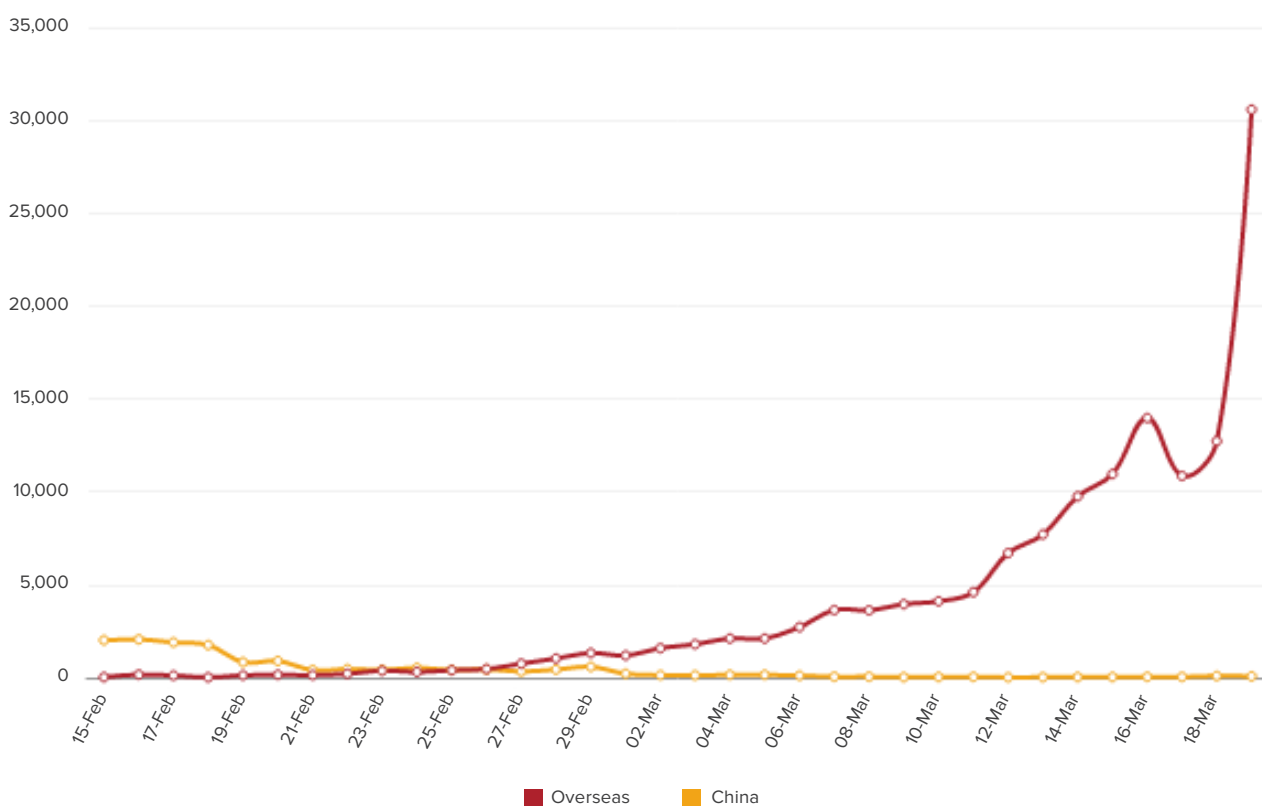
The consensus view is that fallout from the contagion will reduce China's

gross domestic product (GDP) growth by around 2% for the first quarter and 0.5% for all of 2020. These projections, however, are based on Chinese market conditions and could be upended by international developments.

It is the global scope of the outbreak that makes the situation so difficult to predict. Since the first case of COVID-19 was confirmed in Thailand on 14 January,

as of 11 March the total number of cases outside of China has grown to 125,815, and its spread in many countries is still accelerating. And given that the response of these countries and the containment measures taken by their governments is sure to differ from China's blunt and sweeping actions, it is impossible to know at this time just how effective they will be.

Confirmed cases of COVID-19



Source: <https://i.snssdk.com>

With more countries restricting travel and the shipment of goods, globalization has been thrown into reverse. Instead of greater integration, the world economy is becoming more fragmented and many companies in many countries are confronting supply-chain challenges.

## THE ECONOMIC IMPACT IN CHINA AND THE GOVERNMENT'S RESPONSE

Companies and industries have experienced disruption in China, too.

The coronavirus outbreak has put significant pressure on the wholesale, retail, hotel, restaurant, travel and entertainment sectors — industries that accounted for 54% of China's GDP and 60% of its GDP growth in 2019. The supply side of China's economy, including manufacturing and real estate, has been thrown into disarray as well.

But not all the news is so grim. The health crisis has also generated opportunities for online businesses, including online education (Tencent Class, NetEase Cloud Classroom), online conference systems (Zoom, DingTalk under Alibaba) and online shopping (Freshippo under Alibaba, MissFresh). The healthcare industry — and especially the medical consumables sector (Uvex green shield masks) — has also benefitted from the increased demand for masks, protective goggles and body suits. So have testing and pharmaceutical companies, which are receiving strong support from the government.

More generally, the crisis has led most industries to restructure, forcing out

some smaller players, while the bigger and more entrenched players, along with some new market entrants, have gained market share.

To support the economy, the Chinese government has indicated it will relax its fiscal policies for the remainder of the year, and the People's Bank of China has signaled that it may drop its base interest rate for the first time in 12 years.

China's central bank has also announced a series of policy changes aimed at increasing lines of credit and lowering financing costs. These include:

- dropping the one-year loan prime rate (LPR) by 10 basis points to 4.05% and the five-year LPR by five basis points to 4.75%
- injecting US\$174 billion worth of liquidity into the financial markets via reverse repo operations
- earmarking US\$43.17 billion in funds to support major national banks and some local corporate banks.

Government and private sector investment — which represented 31.2% of GDP growth in 2019 — is expected to play an even bigger role in 2020. Much of it will center on the “new form of infrastructure,” including 5G stations, smart-city and public facilities, as well as urban redevelopment.

## HOW WILL THIS IMPACT M&A ACTIVITY?

Given the global economic slowdown, our expectation is that outbound investment will continue to decline. The exceptions will be large, cash-rich companies seeking to mitigate the disruptions caused by the outbreak and adapt to new industrial patterns. These companies — some of which are also looking to reduce their production costs by shifting portions of their operations from China to lower-cost regions — are still eagerly searching out new opportunities abroad.

But even as outbound investment slows, interest in inbound acquisitions continues to grow on the part of foreign multinationals hoping to expand their Chinese presence. Drawn by the allure of the world's biggest population and its huge and growing consumer market, these companies recognize that business conditions in China are maturing and increasingly favorable for international investors. Anticipating a rebound, many of them are preparing to hit the ground running as soon as the crisis abates.

This, however, is not a one-way street. Driven by heightened local competition and the rising cost of labor, there are also numerous international players that have been active in China for years but are now seeking to exit the market.





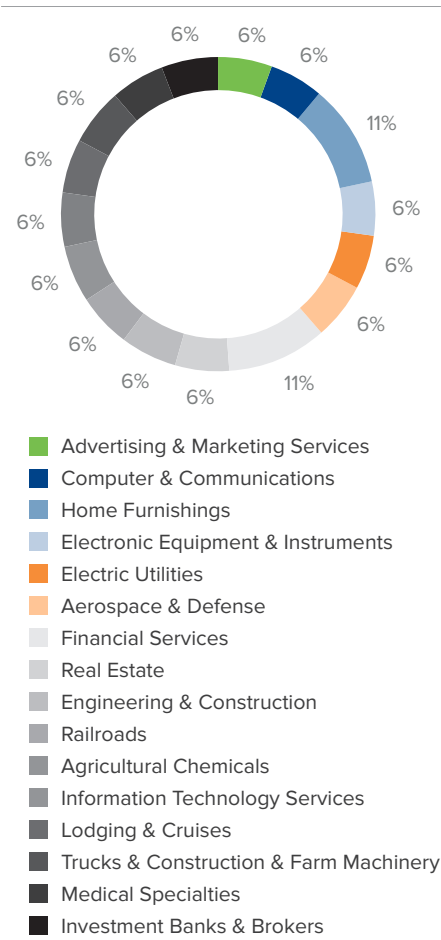


# Recent M&A transactions

## OUTBOUND M&A BY SECTOR

During the fourth quarter of 2019, 18 outbound acquisitions completed by Chinese companies were disclosed. The financial services and home furnishings sectors each represented 11% of the total.

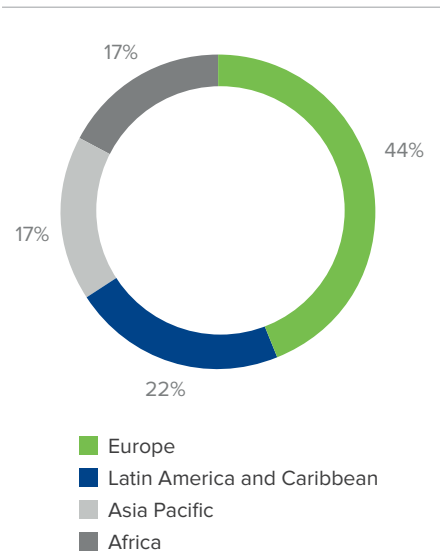
Transactions by industry



## OUTBOUND M&A BY REGION

In terms of geography, 44% of the transactions took place in Europe, followed by Latin America and the Caribbean (22%), and Asia Pacific (17%).

Transactions by region



Deal value was disclosed for seven of these transactions, with the largest pegged at US\$804.1 million for China Lodging Holdings Singapore Pte. Ltd.'s purchase of Steigenberger Hotels AG from the Travco Group.

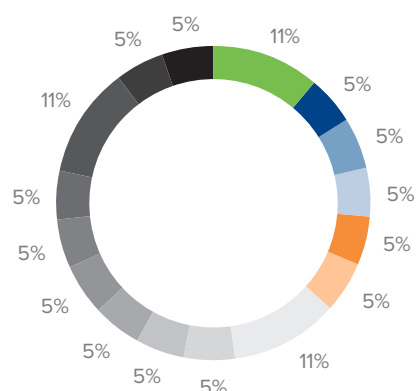
The breakdown for all seven deals was as follows:

Q1 2020	
Seven disclosed transactions by value	
Transaction size (US\$m)	Number of transactions
< 50	6
50–100	0
100–1,000	1

## INBOUND M&A BY SECTOR

In terms of inbound transactions, during the fourth quarter of 2019, 19 acquisitions (not including minority deals) of Chinese companies were recorded, with 11% of the deals taking place in the electronic components, miscellaneous commercial services and the consumer services sectors respectively.

Inbound by industry

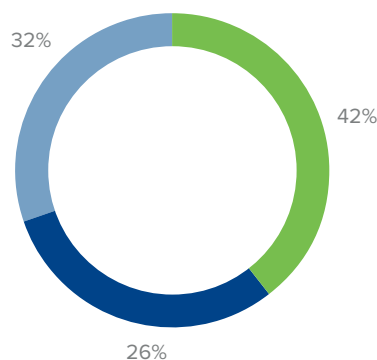


- Miscellaneous Commercial Services
- Food: Speciality & Candy
- Electronic Components
- Air Freight & Couriers
- Textiles
- Containers & Packaging
- Other Consumer Services
- Information Technology Services
- Industrial Machinery
- Industrial Specialties
- Advertising & Marketing Services
- Alternative Power Generation
- Data Processing Services
- Electronic Equipment & Instruments
- Pulp & Paper
- Hospital & Nursing Management

## INBOUND M&A BY REGION

European companies grabbed the lion's share of the inbound deals with 42% of the total, followed by the USA and Canada with 32%, and Asia Pacific with 26%.

Inbound by region



- Europe
- Asia Pacific
- United States and Canada

## Comparing inbound and outbound investments

In 2019, total outbound direct investment was US\$110.6 billion for a year-on-year decline of 8.2%. Inbound direct investment, on the other hand, was US\$138.1 billion — a year-on-year increase of 2.4%. That brought the total number of Chinese enterprises established with the help of foreign capital to 40,888.



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# Spotlight on: The medical consumables sector

Medical consumables are one-time-use devices for medical procedures. They are generally divided into two categories: high-value medical consumables include such items as orthopedic implants, vascular stents and specialized devices used in neurosurgery, while low-value medical consumables refer to disposable materials used during medical procedures. The humble surgical mask, which has received so much international attention lately, falls into the latter category and has become the single best-selling product in China since the outbreak began.

In 2018, China's market for medical consumables was valued at about US\$24.1 billion, or around 32% of the entire medical device market. Of this, the high-value medical consumables segment represented US\$14.94, or 62% of the total.

In the high-value medical consumable segment, the Chinese domestic market is generally dominated by foreign players, although there are a few exceptions, such as stents, some orthopedic implants and neuro-patches. The Chinese government is highly

supportive of this sector, providing both financial subsidies and fast-track approval procedures.

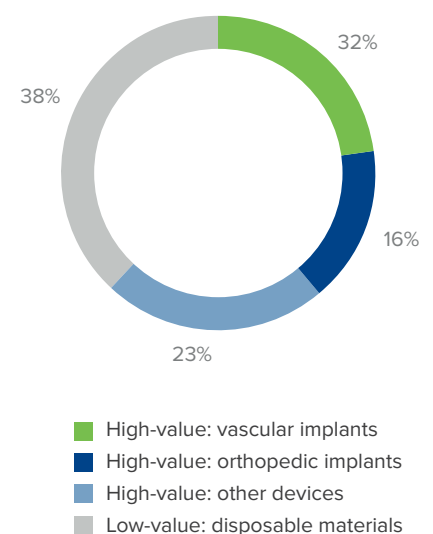
In the low-value medical consumable category, the barriers to market entry are much lower, and Chinese players dominate at home. Benefiting from lower labor costs, they also occupy a pivotal position in the global market. Chinese companies, however, are beginning to lose their cost advantage and face increasing competition from India and the Association of Southeast Asian Nations (ASEAN) countries. This has led some export-oriented players to refocus on China's fast-growing domestic market. But there, too, the competition is fierce, leading some of these companies to try and expand into other segments — especially the high-value medical consumable market.

To shore up and advance their positions, Chinese medical consumable companies are engaged in outbound acquisitions that support the following objectives:

- to acquire new technology and accelerate their in-house research and development (R&D)

- to help players in the low-value medical consumables segment expand into other categories, especially the high-value medical device segment.
- to help original equipment manufacturers (OEMs) and original design manufacturers (ODMs) acquire brands and distribution channels in the international market
- to shift production to lower-cost countries, in order to sustain a cost advantage in the low-value medical consumables segment.

Medical consumables by type





Deals struck earlier this year by two industry leaders are good examples of how these objectives are playing out

### Zhende

Zhende Medical Co., Ltd. is one of China's largest low-value medical consumables providers. In August, 2019, the company paid US\$6 million to acquire a 55% equity stake in Rocialle Healthcare through its wholly owned subsidiary.

**Company strategy:** Zhende Medical undertook the acquisition of Rocialle to create synergies in the field of surgical sense control by integrating the target's technology, production, sales channels and other resources with those of its own.

- market cap: US\$789.98 million
- revenue: US\$208.19 million
- EBITDA: US\$33.55 million

### Blue Sail Medical Co., Ltd.

Like Zhende Medical, Blue Sail Medical Co., Ltd. is one of the largest low-value medical consumables providers in China, but Blue Sail Medical also has a presence in the high-value medical consumables space. Last September, the company's board of directors approved the payment of US\$193 million to acquire a 100% stake in NVT AG.

**Company strategy:** following a 2018 acquisition to gain entry into the high-value medical consumables market, Blue Sail Medical bought NVT AG to obtain market-leading heart-valve technology and expand its product line.

- market cap: US\$2377.21 million
- revenue: US\$620.15 million
- EBITDA: US\$162.53 million



## Case study



In August 2019, Zhende Medical Co., Ltd. paid US\$6 million to acquire a 55% equity stake in Rocialle Healthcare from Berendsen Healthcare.

### ABOUT THE BUYER

Zhende Medical is one of the largest low-value medical consumables providers in China, specializing in products for wound management, surgical procedures, infection prevention, pressure treatment, sports protection and rehabilitation. The company exports 68% of its products overseas, primarily as an OEM.







### ABOUT THE TARGET

Rocialle Healthcare is a UK manufacturer and supplier of medical devices and consumables that sells its wares under two brands: Rocialle and Guardian SU. Product lines include custom surgical procedure packs, bowl packs, polyware and dressing packs.

### SYNERGY

With overlapping product lines, Zhende Medical will benefit from the target's technology know-how and production facilities. Even more importantly, as an OEM, Zhende stands to gain from the target's brands and sales channels.

## 18 OUTBOUND ACQUISITIONS BY CHINESE COMPANIES CLOSED BETWEEN OCTOBER AND DECEMBER 2019

Date	Acquiror	Target	Target country	Industry	Transaction value (US\$m)
26-Dec-19	GDS Holdings Ltd.	MapletreeLog Integrated (Shanghai) (HKSAR) Ltd.		Real Estate Investment Trusts	8.22
26-Dec-19	Government of China; China National Nuclear Co. Ltd.	Nusim SA		Engineering & Construction	-
17-Dec-19	TL Natural Gas Holdings Ltd.	Jet Union Technology Ltd.		Financial Conglomerates	2.82
16-Dec-19	Weichai Power Co., Ltd.	Aradex AG		Electronic Equipment/ Instruments	-
13-Dec-19	Active Link Investments Ltd. /Private Group	Active Link Investments Ltd.		Advertising/ Marketing Services	0.06
6-Dec-19	OFC Commercial Carpet Co., Ltd	ANKER Gebr. Schoeller GmbH + Co. KG		Home Furnishings	-
21-Nov-19	Binance Holdings Ltd.	WazirX		Investment Banks/Brokers	-
19-Nov-19	Ingram Micro Inc.	Quosphere Inc.		Information Technology Services	-
11-Nov-19	Government of China; China Ocean Shipping Co. Americas Inc.; Ocean Rail Logistics SA	Piraeus Europe Asia Rail Logistics (PEARL) SA		Railroads	-

Date	Acquiror	Target	Target country	Industry	Transaction value (US\$m)
4-Nov-19	China Lodging Holdings Singapore Pte. Ltd.	Steigenberger Hotels AG		Hotels/Resorts/ Cruise Lines	804.09
30-Oct-19	City of Tianjin (China); Tianjin TEDA Group Co., Ltd.	Prentiss Química Ltda		Chemicals: Agricultural	-
30-Oct-19	Integrated Clinical Oncology Network Pty Ltd.; Pagoda Investment Advisors (S) Pte. Ltd.	Varian Medical Systems Inc./Ethos Therapy		Medical Specialties	-
28-Oct-19	Guangdong KinLong Hardware Products Co., Ltd.	Cifial SGPS SA		Home Furnishings	-
28-Oct-19	Sabart Aéro Tech SAS	Gardner Aerospace Mazeres SAS/ Balesta Site		Aerospace & Defense	-
21-Oct-19	Zhi Sheng Group Holdings Ltd.	Polyqueue Ltd.		Financial Conglomerates	4.50
16-Oct-19	FJ Dynamics Technology Co., Ltd.	Sveaverken Svea Agri AB		Trucks/ Construction/ Farm Machinery	-
8-Oct-19	Senba Sensing (International) Holdings Co., Ltd.	Alpha Instruments Inc.		Computer Communications	4.00
7-Oct-19	Astronergy Solar Korea Co., Ltd.	Dreamline Solar Power 4		Electric Utilities	0.41

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