# CHINESE INVESTMENT SPECIAL FOCUS 2016: BUSINESS AS USUAL

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## China's economy may be slowing down, but fears that it could negatively impact on investment in Spain and Portugal appear to be unfounded with lawyers expecting the flow of capital from China to Iberia to continue

Chinese investment into the Iberian Peninsula has surged in recent years. State-owned enterprises and high-net-worth individuals are snapping up assets, while there has also been a significant increase in interest from private enterprises, according to lawyers in Spain and Portugal.

And while political uncertainty in Madrid and Lisbon – due to the result of last year's elections – may put a temporary brake on investment, the consensus is that it will merely be a period of 'wait and see' before the capital flows resume. Similarly, China's economic slowdown is not perceived as an impediment to continued investment in multiple sectors across the peninsula.

According to Fernanda Lomenso, partner at CCA Ontier in Lisbon, Portugal has seen three waves of Chinese investment. "The first was predominately from state-owned enterprises, targeting strategic industries, while the second wave was characterised by individuals investing in real estate, taking advantage of the 'Golden Visa' opportunity – the third wave came from privately held enterprises seeking to internationalise," she explains. While all three types of investment are continuing, Lomenso says it is private enterprises looking to expand internationally that is currently the most prominent trend and the one that is likely to continue growing.

Lomenso adds that China's economic slowdown has led to the adoption of a new strategy for growth, but not to a slowdown in investment. "The lower rate of growth for the Chinese economy is an additional incentive for Chinese entities to invest abroad as Chinese government policies incentivise internationalisation," she adds. Though some deals in Portugal may have been postponed or cancelled as a result of Beijing's economic slowdown, there has not been significant divestment, according to Ana Sá Couto, a counsel at Uría Menéndez's Lisbon office.

Similarly, Chinese investment in Spain has not been affected by the nation's ailing economy. Maite Diez, partner at Baker & McKenzie in Madrid, says: "Chinese foreign direct investment is not decreasing despite the deceleration of its economic growth." She adds that, on the contrary, data shows that Chinese investment in Europe and North America reached a record figure of $40 billion in 2015, with 73% of that injected into the real estate, hotel, automotive and financial sectors. Meanwhile, during first few weeks of 2016, M&A deals by Chinese firms totalling $70 billion took place in Europe and North America.

**New economic model**

Diez adds that the increase in Chinese investment will be long-term due to the accelerated change in the country's economic growth model, aimed at increasing domestic demand and the development of added value goods and services. This approach goes hand in hand with the liberalisation of regulations governing foreign investment.

While the surge in Chinese investment abroad coincided with Europe's worst financial crisis in decades, a drop in asset prices and the privatisation of public companies, large-volume Chinese investment is continuing even though there is a strong economic recovery now underway, Diez says.

Francisco Martínez Boluda, Uría Menéndez's resident partner in Beijing says this new strategy for growth has increased Chinese investors' appetite for investment in Spain. "Because of the shift of the Chinese economy toward a more consumption and services-oriented economy, there is more interest in Spain, although the amount of investment remains unsatisfactory," he says.

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> Fernanda Lomenso
> CCA Ontier

But the increase in investment also brings challenges for law firms who may face the problem of having to persuade Chinese clients regarding the need to use their services. "Traditionally, China's economy was not oriented towards service, especially legal advice, and this is still very clear when providing services to Chinese entities or individuals," Lomenso says. "The biggest challenge is finding the decision-making people, and then convincing the client of the necessity and the added value of having a reliable legal advisor when investing outside China."

While acquisitions remain Chinese investors' favourite modus operandi when entering foreign markets, over the last decade there has been an increase in greenfield investments, Lomenso says. Meanwhile, another trend has been the greater participation of Chinese investors as stakeholders as opposed to whole ownership through M&A. Lomenso also identifies a shift in Chinese investment trends, with private equity – in the form of venture capital – and insurance companies overtaking investment by state-owned firms. Indeed, private equity participation is on the increase, particularly in comparison with that of companies making long-term investments with a view to extending their global presence and increasing their market share. Lomenso highlights the purchase of Madrileña Red de Gas by Gingko Tree Investment and Dutch pension fund PGGM for €1.3 billion, last year's largest Chinese investment in Spain.

**Obstacles to investment**

Lomenso argues that Chinese investors face the challenge of improving their knowledge of foreign markets. Investments by other Chinese investors are often used as a benchmark, given that the language, culture and way of doing business will always be a challenge due to different expectations, timing, standards and ways of communicating.

Meanwhile, Diez comments: "The huge difference between the institutional frameworks of the Iberian Peninsula and China, as well as between business cultures, together with a lack of experience of international transactions, along with the language barrier, are among the biggest obstacles to entering and operating within the peninsula's mature market of complex regulations."

Challenges also arise due to each country's characteristics, as well as the nature of the specific sector or company targeted, Diez adds. However, she says that Europe is one of the world's most open markets with relatively few restrictions on investment. Chinese investors' biggest obstacle is the enormous regulatory and procedural differences that investing abroad implies, Diez argues. However, she adds that Chinese firms have demonstrated their ability to compete in the M&A market, including handling political negotiations when making acquisitions of state-owned companies, and have consequently made successful bids.

As time goes by and relationships strengthen, such challenges are mitigated, according to António Soares, partner in Linklaters' Lisbon office. Chinese investment in Portugal alone has totalled around €4 billion since 2011, including China Three Gorges' purchase of a 21.35 per cent stake in EDP, China's State Grid's 25 per cent purchase of Redes Energéticas Nacionais in 2012, and Fosun's acquisition of an 80 per cent share of Fidelidade, Multicare and Cares, Caixa Geral de Depósitos' insurance portfolio. In addition, Portugal's Banco Espírito Santo was wholly acquired by Haitong International Holdings in 2015, while the largest deal was Cheung Kong Infrastructure Holdings' (CKI) and Power Assets Holdings' 100 per cent acquisition of Iberwind for €1 billion. Such deals are examples of Chinese investors taking advantage of privatisations and asset sales in Portugal, Soares says.

**Brand recognition**

"When investing and conducting business in Iberia, it is important to achieve brand recognition and to deal with established local competitors," Soares adds. "Foreign investors must understand the market, business practices and the local consumers, and adapting their products and services accordingly is also a key challenge," he continues. "But Chinese investment in Portugal also represents a strategic way to strengthen the economic and financial capacity of the Portuguese companies and also their potential to grow, in both the domestic and international markets."

Soares dismisses concerns that China's economic slowdown will negatively impact deal activity in Spain and Portugal. "We are expecting Chinese investors to continue to invest in the Iberian market," he says. However, such investment cannot be taken for granted, according to Diez, who argues that the peninsula's ability to remain attractive to investors will depend on Lisbon and Madrid's capacity to boost their countries' economic growth and competitiveness.