

# **Mergers & Acquisitions in the domestic financial services sector**

December 1, 2006

# Why China?

## Market Potential

- A fast growing economy with approximately 1.3 billion in population

## RMB appreciation

- RMB appreciation is also fuelling investments into China (e.g. property sector)

## Market consolidation

- International foreign firms with the experience and expertise believe in becoming a consolidator in the China market

## Low production costs

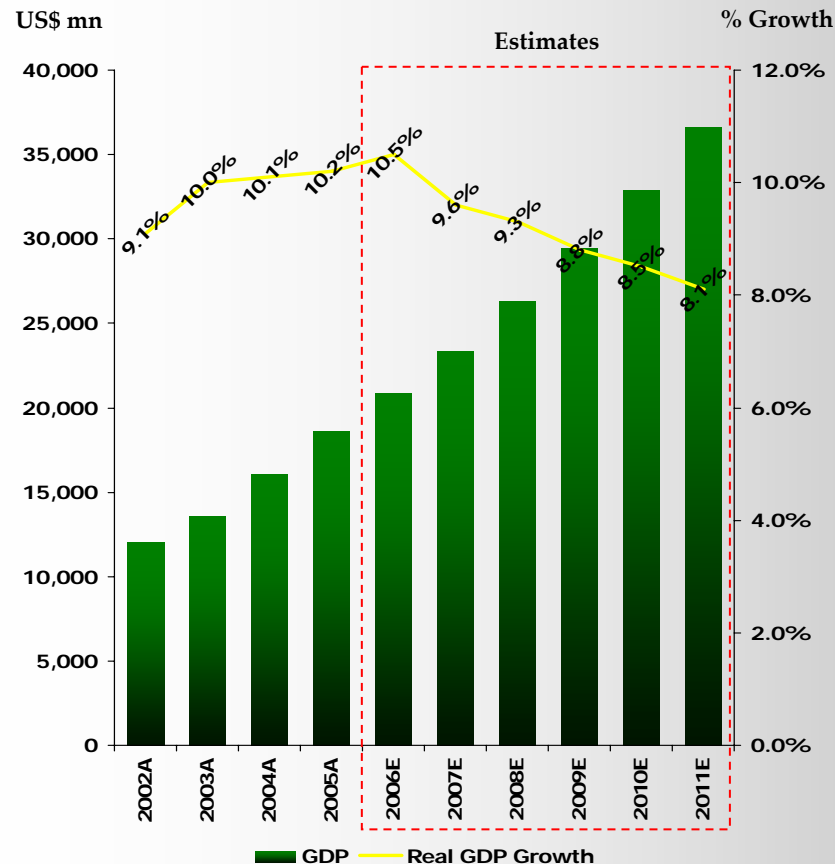
- Low labor costs, improving skill set and quality of production, China has become the world factory for almost anything and everything

## Educated workforce

- Government support together with overseas returnees have given China an educated workforce for growth

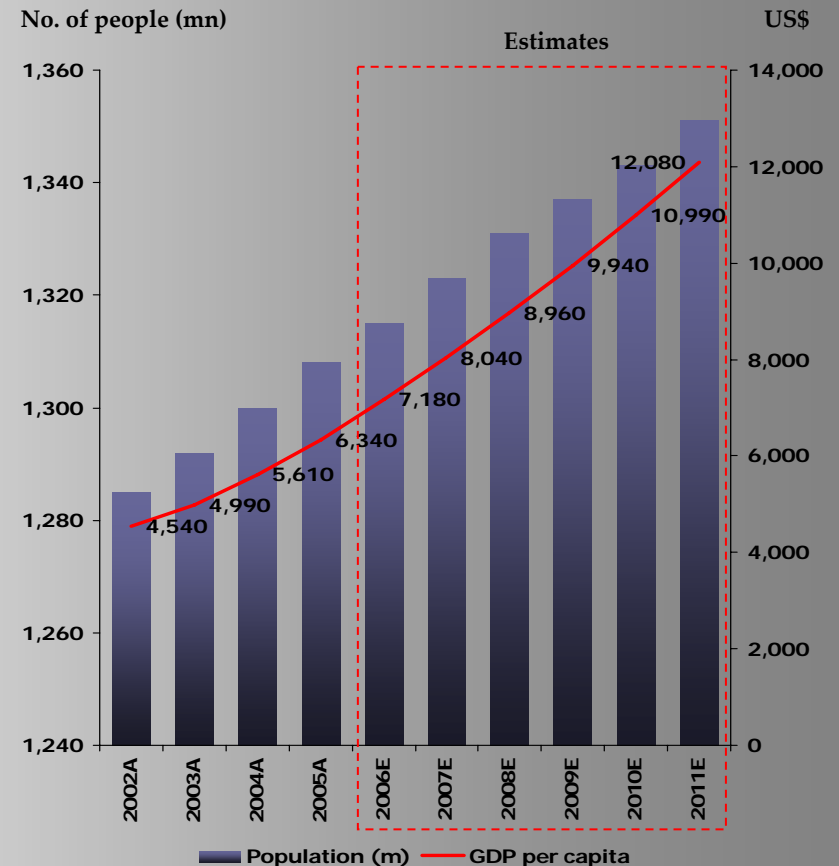
# China's recent development & outlook

- China's GDP will grow by a CAGR of 11.9% for the next 5 years



Source: EIU (at current market prices)

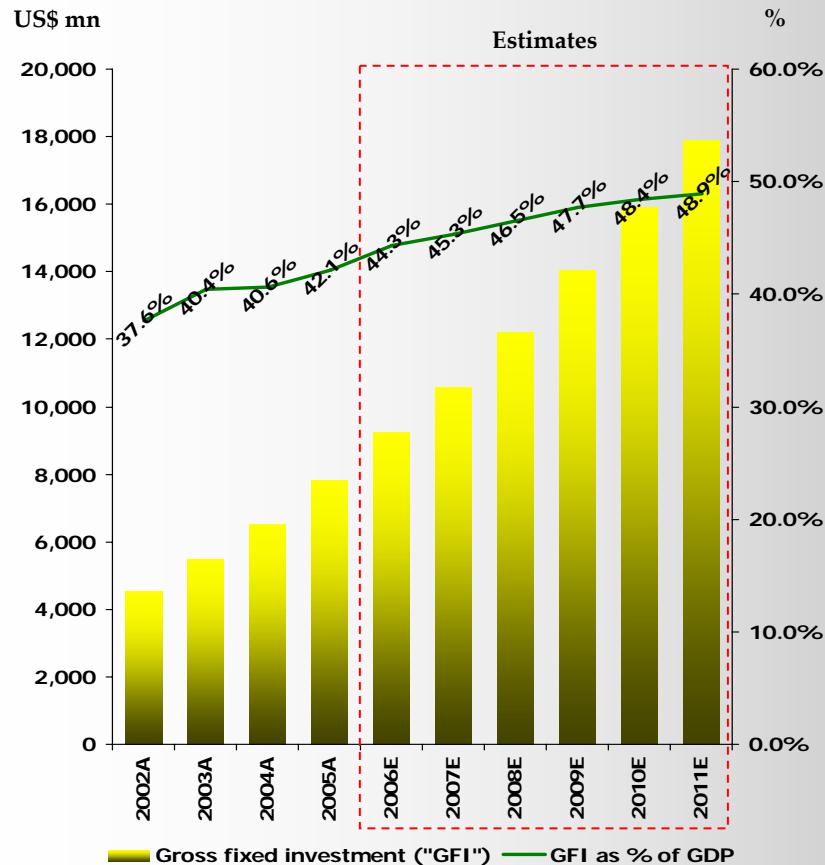
- China's growth is building wealth for its people



Source: EIU (US\$ at PPP)

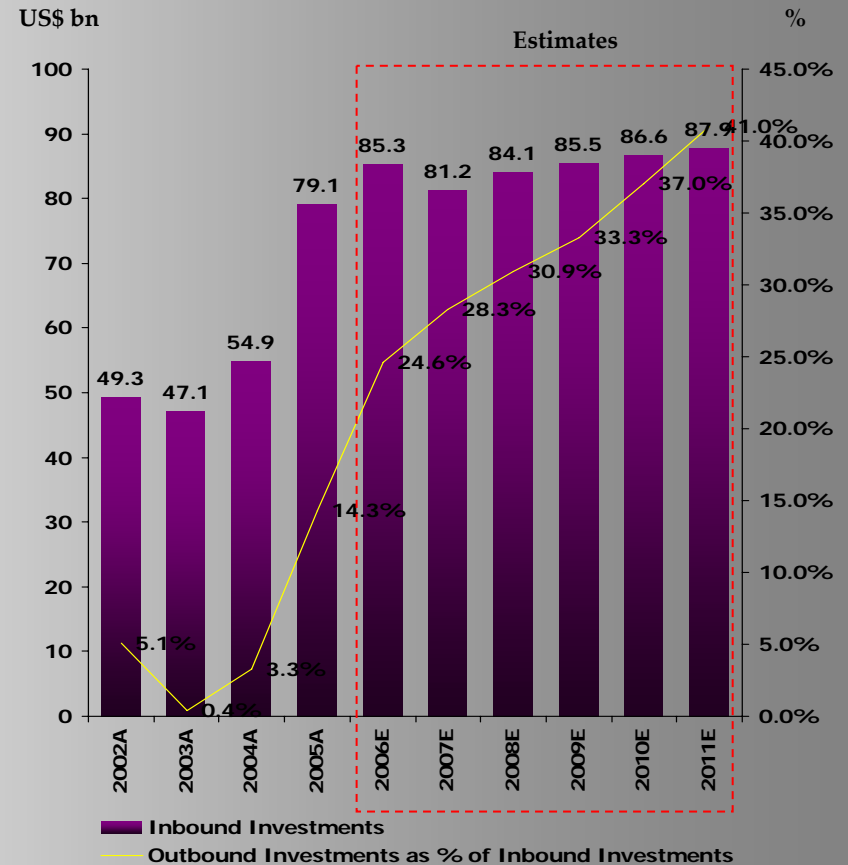
# China's recent development & outlook (cont'd)

- Fixed asset investments will continue to grow as GDP continues to rise



Source: EIU (at current market prices)

- China ranks No. 1 globally for foreign direct investments

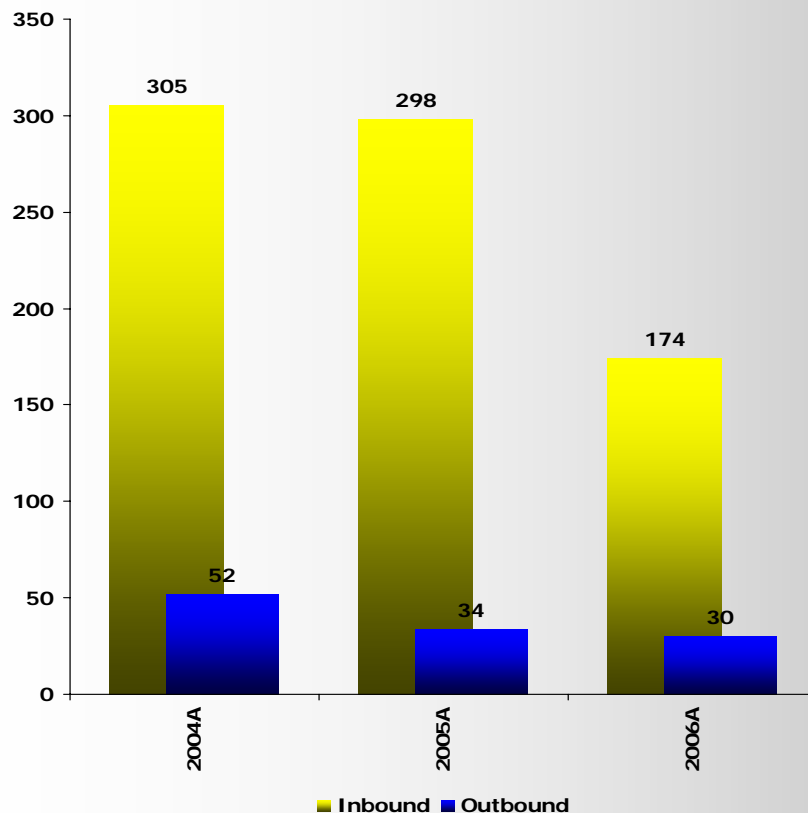


Source: EIU (US\$ at PPP)

# Inbound & Outbound Completed M&As

- Number of Inbound M&As has far outweighed outbound M&As for the past 3 years

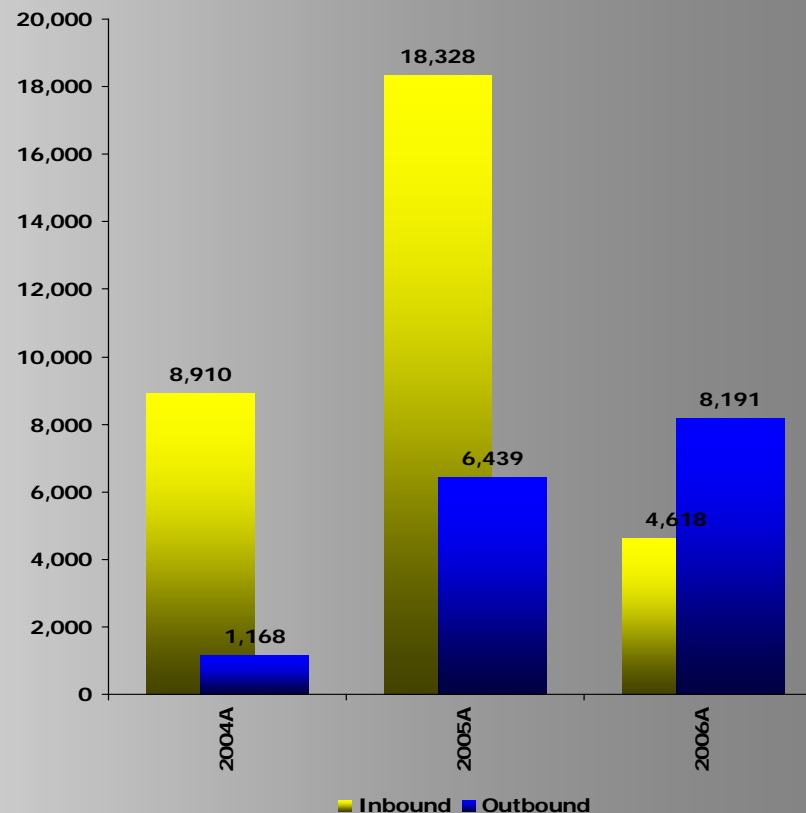
No. of deals



Source: Thomson One Banker (Jan 2004 to-date)

- Transaction value of outbound M&As completed is on an increasing trend

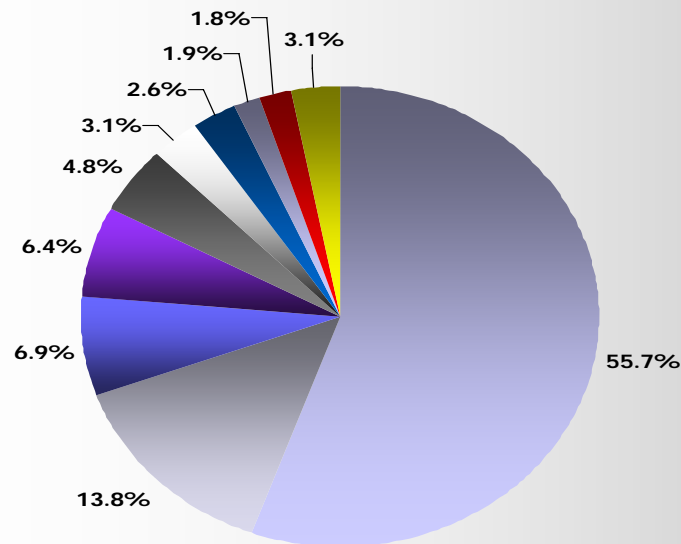
US\$ mn



Source: Thomson One Banker (Jan 2004 to-date)

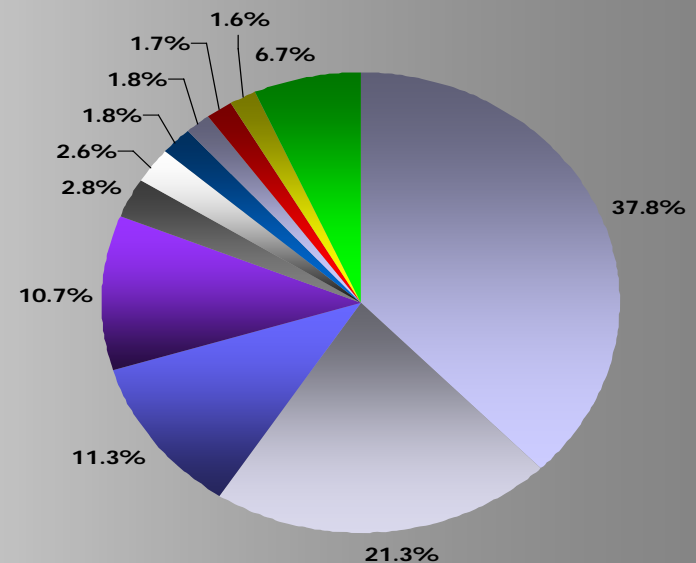
# Inbound M&As

- Inbound investments into China have been dominated by the financial sector for the past 3 years



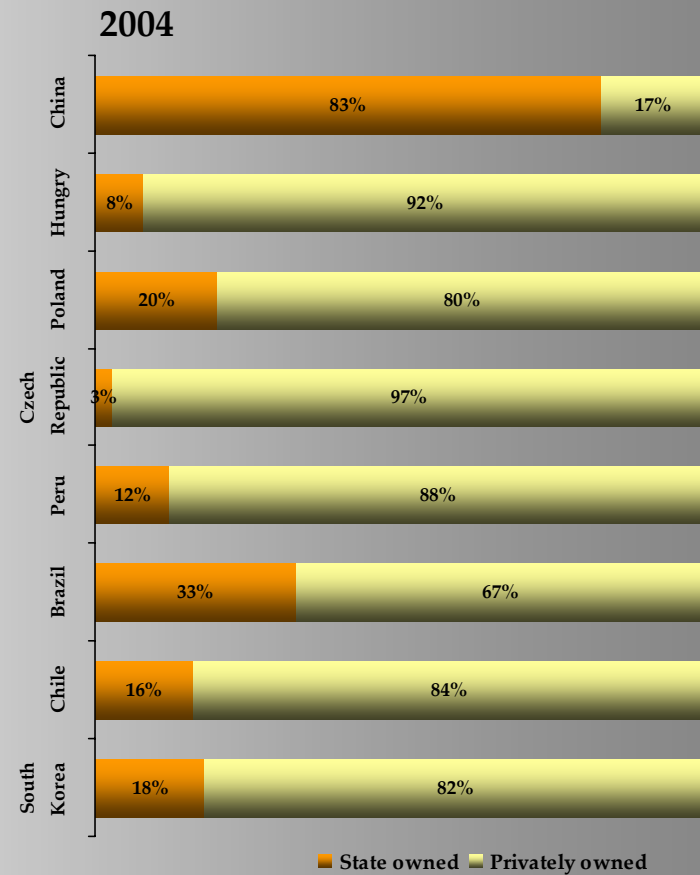
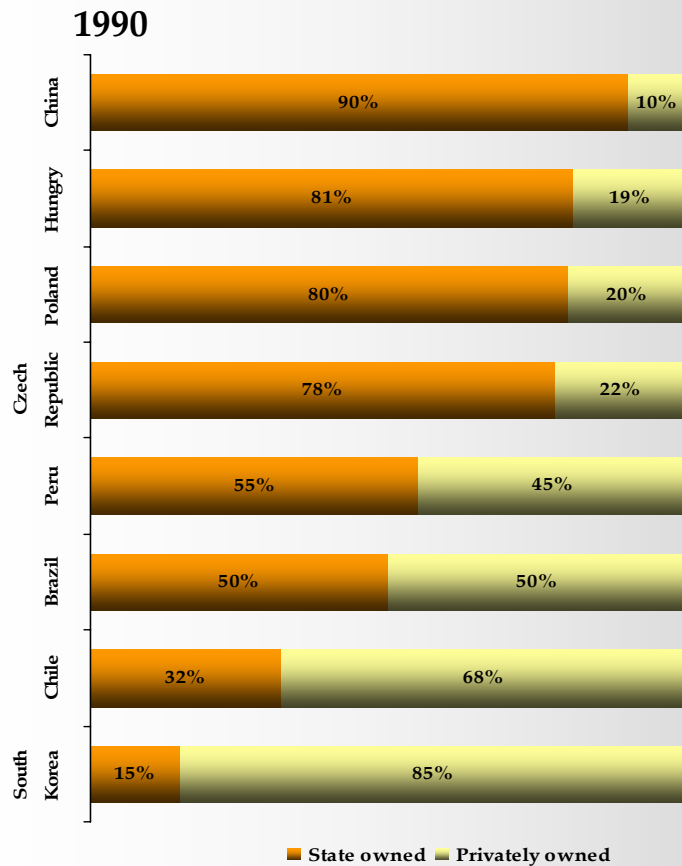
Source: Thomson One Banker (Jan 2004 to-date)

- The U.S. continues to lead the way in making investments into China



Source: Thomson One Banker (Jan 2004 to-date)

# Assets by Ownership

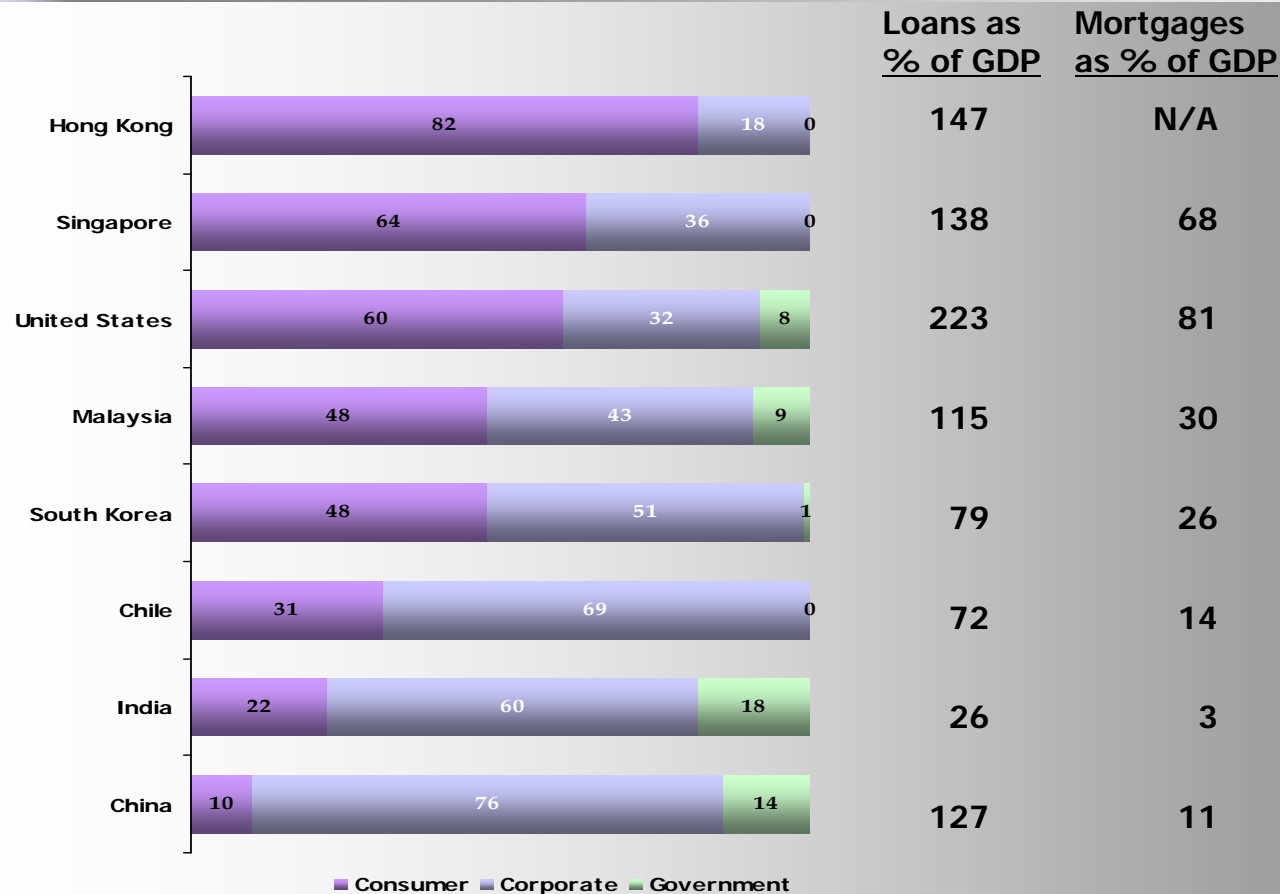


Source: Central banks of countries shown; McKinsey

# **Financial Institutions**



# Loans Analysis



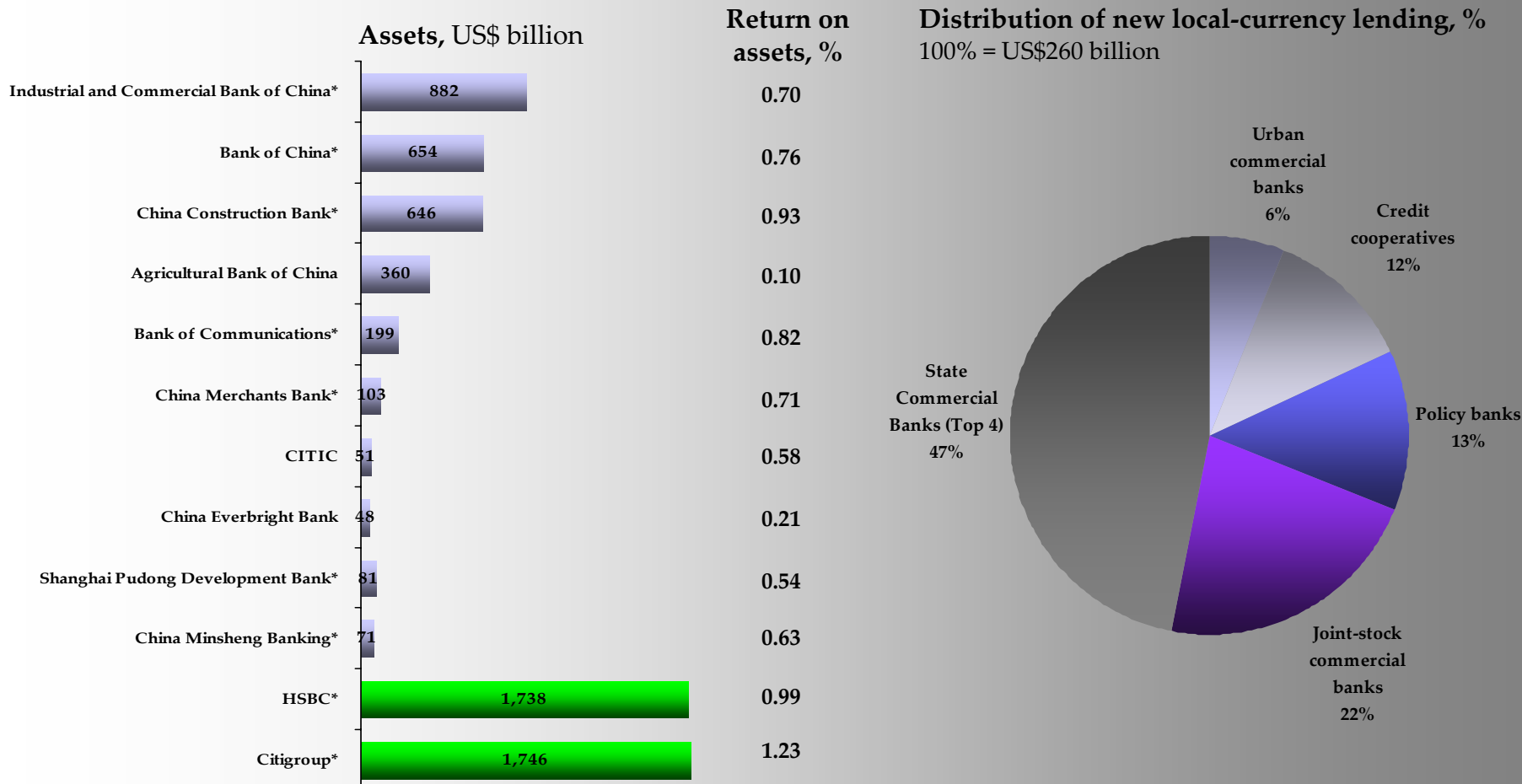
<sup>1</sup> For some countries, loan split not available at commercial-bank level – general data were normalized to match commercial-loan total

<sup>2</sup> Includes only government loans; figure would be significantly higher for India if government bonds were included

<sup>3</sup> 2003 data; includes securitized loans and loans from nonbanking institutions

<sup>4</sup> Figures do not sum to 100%, because of rounding

# China Banking Landscape



\* Based on latest available information

Source: Bloomberg, IBES estimates, "Top 200 Asian Banks 2004", The Banker; The Industrial Map of China 2004-2005, Japan; Nihon Keizai Shinbu; McKinsey

# Market Participants

As of December 31, 2004

	Number of institutions	Total assets		Total deposits		Total loans	
		Amount	% of total	Amount	% of total	Amount	% of total
(in billions of RMB, except for number of institutions and percentages data)							
Big Four <sup>(1)</sup> .....	4	17,859.5	54.8%	15,384.1	59.5%	10,667.5 <sup>(4)</sup>	54.6%
Joint stock commercial banks .....	12	4,803.4	14.7	4,143.6	16.0	2,926.1	15.0
Urban commercial banks .....	112	1,705.6	5.2	1,414.6	5.5	903.1	4.6
Rural credit cooperatives <sup>(2)</sup> .....	32,869	3,133.2	9.6	2,784.1	10.8	1,955.1	10.0
Urban credit cooperatives .....	623	178.7	0.5	158.9	0.6	101.5	0.5
Foreign-invested commercial banks .....	67	582.3	1.8	149.9	0.6	284.4	1.5
Others <sup>(3)</sup> .....	149	4,369.9	13.4	1,889.6	7.0	2,681.3	13.8
Total .....	<u>33,836</u>	<u>32,725.9</u>	<u>100.0%</u>	<u>25,849.9</u>	<u>100.0%</u>	<u>19,528.4</u>	<u>100.0%</u>

Source: CBRC, banks' annual reports.

(1) Amounts are on a consolidated basis.

# Big Four Snapshot

As of December 31, 2004							
	Total assets		Total deposits		Total loans <sup>(1)</sup>		Reported number of branches
	Amount	% of total	Amount	% of total	Amount	% of total	
(in billions of RMB, except for number of branches and percentages)							
ICBC .....	5,670.5	31.8%	5,060.7	32.9%	3,705.3	34.7%	21,323
Our bank .....	4,270.4	23.9	3,342.5	21.7	2,146.5	20.1	11,910
ABC .....	4,013.8	22.5	3,491.5	22.7	2,590.1	24.3	31,004
CCB .....	3,904.8	21.8	3,489.4	22.7	2,225.6	20.9	14,467
Total .....	<u>17,859.5</u>	<u>100.0%</u>	<u>15,384.1</u>	<u>100.0%</u>	<u>10,667.5</u>	<u>100.0%</u>	<u>78,704</u>

Sources: The 2004 annual reports of ICBC, our bank, ABC and CCB.

(1) Amounts for loans are before allowances for impairment losses.

# Recent Banking M&A

Bank	Assets (\$bn)	CAR (%)	NPL (%)	Timing	Investor	Stake (%)	Price (\$m)	P/BV (X)
CITIC Bank	88.4	9.2	2.8	Nov-06	BBVA	5.0	642	3.30x
CITIC International Financial Holding	11.9	16.0	2.7	Nov-06	BBVA	15.0	625	3.32x
Guangdong Development Bank	44.2	3.9	18.3	Nov-06	Citigroup Consortium	85.6	3,100	2.27x
Shanghai Rural Commercial Bank	17.0	8.1	3.0	Nov-06	ANZ	19.9	252	2.67x
China Citic Bank	76.1	8.2	3.9	Apr-06	Citic Int'l Financial	19.9	714	1.15x
Bank of China	584.5	10.4	4.9	Mar-06	NCSSF	3.9	1,233	1.17x
Ningbo City Commercial Bank	4.2	10.8	1.1	Jan-06	OCBC	12.2	70	2.10x
Shanghai Pudong Development Bank	70.7	8.0	2.0	Dec-05	Citigroup	15.3	-	-
Tianjin City Commercial Bank	7.3	-	14.7	Dec-05	ANZ	19.9	120	-
Huaxia Bank	43.9	8.2	3.0	Oct-05	Deutsche Bank	9.9	232	1.94x
				Oct-05	Sal Oppenheim	4.1	97	1.94x
Shenzhen Development Bank	28.3	3.7	9.3	Sep-05	GE Capital	7.0	100	-
Bohai Bank	0.6	-	-	Sep-05	Standard Chartered	19.9	123	-
Huaxia Bank	43.9	8.2	3.0	Sep-05	Pangaea Capital Management	6.9	125	1.50x
Industrial and Commercial Bank of China	699.2	5.8	14.3	Aug-05	Goldman Sachs	5.7	1,700	-
				Aug-05	Allianz	3.3	1,000	-
				Aug-05	American Express	1.0	300	-
Bank of China	584.5	10.4	4.9	Aug-05	Asian Development Bank	0.2	74	1.17x
				Aug-05	UBS	1.6	492	1.17x
				Aug-05	Royal Bank of Scotland	9.6	3,048	1.17x
				Aug-05	Temasek (Asia Financial HD)	4.8	1,524	1.17x
China Construction Bank	565.4	13.6	3.8	Jun-05	Bank of America	9.0	2,500	1.15x
				Jun-05	Temasek	5.1	1,466	1.19x
China Everbright Bank	64.0	4.7	6.1	Jun-05	Asian Development Bank	3.0	-	-

Source: Independent Analyst Reports

**M & A**

# Continuing driving force behind Inbound M&A?

Domestic restructuring

- Breakup of monopolies and consolidation in fragmented sectors

Private equity

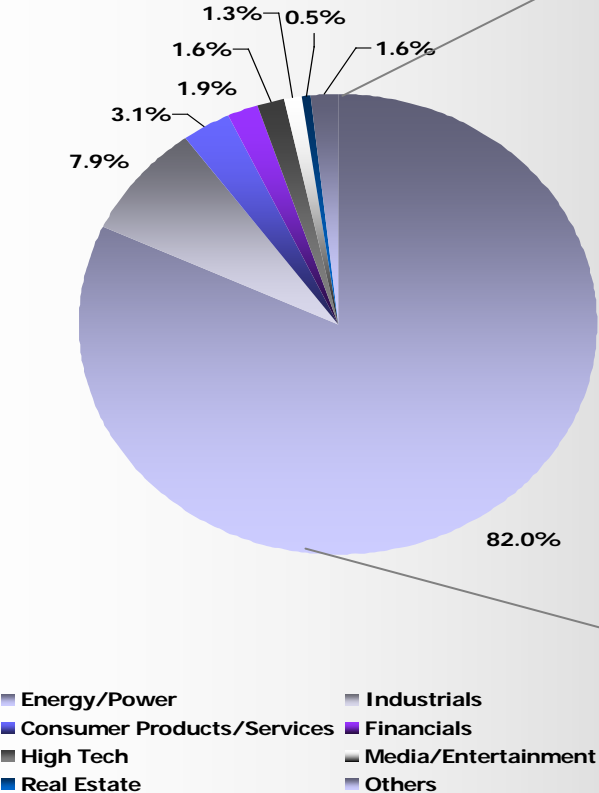
- Significance of private equity investing into China thereby continuing to fuel M&A activities

Regulatory Changes

- Regulatory changes has reinforced foreign investors' confidence in the market sparking M&A activities

# Outbound M&As

- The energy sector has been the biggest acquiror of offshore assets



## 2006



- CITIC Group announced the acquisition of Kazakhstan oil assets from Canadian-based Nations Energy for US\$1.9 bn



- CNOOC acquired a 45% interest in an oil block off the coast of Nigeria from South Atlantic Petroleum for US\$2.3 bn



- Sinopec acquired an oil-producing unit of BP Plc joint venture TNK-BP, OAO Udmurtneft in Russia for US\$3.5 bn

## 2005



- CNPC paid US\$4.18 bn to acquire PetroKazakhstan, but later sold 33% to Kazakhstan's state-owned firm KazMunaiGaz to assist in getting government approval

Source: Thomson One Banker (Jan 2004 to-date)

Source: Thomson One Banker, Factiva, Bloomberg



# M&A vs Organic Growth

	Pros	Cons
M&A	<ul style="list-style-type: none"><li>▪ Immediate expansion of product range, team, and geographical coverage</li><li>▪ Increase market awareness for foreign player</li><li>▪ Immediate increase in revenue base</li></ul>	<ul style="list-style-type: none"><li>▪ Difficult to identify and securing the right platform</li><li>▪ Difficulty in retaining skilled management</li><li>▪ Integration of team, culture and infrastructure</li><li>▪ Immediate increase in cost base</li><li>▪ Regulatory restrictions/hurdles</li></ul>
Joint Ventures	<ul style="list-style-type: none"><li>▪ Minimal outlay</li><li>▪ Immediate access to domestic market</li><li>▪ Good for markets with growth opportunities that a company either cannot or does not want to pursue on its own</li></ul>	<ul style="list-style-type: none"><li>▪ Difficulty in finding the right partner</li><li>▪ Difficult to harness the strengths of both sides</li><li>▪ Potential conflicts of interests</li></ul>
Organic Growth	<ul style="list-style-type: none"><li>▪ High flexibility</li><li>▪ Relatively quick process if regulations permit</li></ul>	<ul style="list-style-type: none"><li>▪ Require enormous amount of capital with no guarantee of success</li><li>▪ Alien operating environment</li><li>▪ Regulatory restrictions</li></ul>

# M&A Rationale

- Horizontal vs Vertical extension
- Geographic and/or product extension
- Industry consolidation
- Bargain Hunting (distressed assets)
- Strategic Alliance  
(normally coupled with a minority investment)
- Liquidity / Financing

# M&A Mechanics

## First steps

- Target identification / Business rationalization / restructuring

## Transaction structure

- Majority vs Minority; Share or asset acquisitions; Share subscription; Reverse takeover & Listing Status

## Shareholding vs management control

- Management retention; Veto power; Non-compete; Exclusivity

## Pricing vs Valuation

- Paid-Up-Capital vs Earnings driven valuation
- Industry specific valuations (project vs company)

## Due diligence

- Strategic; Operational; Technical (depending on industry); financial; legal; human resource

## Documentation

- Sale & Purchase Agreement; Share Subscription Agreement; Technical Assistance Agreement; Joint Venture / Strategic Alliance Agreement

# Trends

# M&A Trends

## 5 Trends Emerging

- I. Foreign companies continue to aggressively invest into China (e.g. Citigroup)
- II. Chinese companies buying offshore (e.g. CNOOC, CCB, Suntech Power)
- III. Consolidation in Chinese companies is beginning (e.g.   )
- IV. Investment into A Share listed companies
- V. Foreign companies disposing of their assets in China/Asia

# Recent Outbound M&A

## 2006



- CITIC Group announced the acquisition of Kazakhstan oil assets from Canadian-based Nations Energy for US\$1.9 bn (Pending)



- Suntech Power acquired two-thirds equity interest in MSK Corporation for US\$107 mn to tap into its extensive PV Module sales & distribution network in the key Japanese market (Pending)



- CNOOC acquired a 45% interest in an oil block off the coast of Nigeria from South Atlantic Petroleum for US\$2.3 bn (Completed)



- China Construction Bank acquired 100% of Bank of America's Hong Kong retail operations for approximately US\$1.24 bn (Pending)



- Sinopec acquired an oil-producing unit of BP Plc joint venture TNK-BP, OAO Udmurtneft in Russia for US\$3.5 bn in 2006 (Pending)

## 2005



- Lenovo acquired IBM's PC division for an enterprise value of US\$1.75 bn. Lenovo paid US\$650 mn in cash and US\$600 mn in securities and assumed all outstanding debt of the business (Completed)



- CNPC paid US\$4.18 bn to acquire PetroKazakhstan, but later sold 33% to Kazakhstan's state-owned firm KazMunaiGaz to assist in getting government approval (Completed)



- China Netcom acquiring 20% of Hong Kong based PCCW for US\$1 bn (Completed)

# Recent Outbound M&A (failed attempts)



- China Mobile's attempted US\$5.3 bn acquisition of Millicom International Cellular SA of Luxembourg, operator of mobile-telephone services in many of the world's poorest nations (Failed)



- Haier withdrew its attempted US\$1.25 bn bid for Maytag Corp of the U.S., a manufacturer of innovative and dependable energy efficient kitchen appliances and clothes washers (Failed)



- CNOOC's US\$18.5 bn attempted merger with Unocal of the U.S. was faced with strong opposition from the U.S. government on security concerns (Failed)

**Q&As**