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投英 Tou Ying Tracker 2016

THE LATEST TRENDS IN CHINESE INVESTMENT IN THE UK

The latest trends in Chinese investment in the UK

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Introduction

This is the fourth edition of the Grant Thornton Tou Ying Tracker, which identifies the fastest-growing Chinese companies in the UK. Over the last four years we have followed the fortunes of these trailblazing businesses, as well as looking beyond the headline numbers to tell the real story of Chinese investment in the UK.

This year the Tracker is divided into two categories, analysing the top 16 fastest-growing state-owned enterprises (SOEs) and the top 14 privately-owned Chinese companies in the UK separately. This reflects the changing pattern of Chinese overseas investment and shows that China's thriving private sector is increasingly forging its own path, following the lead of its more established SOEs.

With a combined turnover of £9.8 billion, these companies are making an important contribution to the UK economy and helping to create a sustainable environment in which existing and new Chinese businesses can flourish. This is very much in line with the Chinese government's 'one belt, one road' policy to create a new 'Silk Road' of trade links and markets.

This year's Tracker is based on analysis of the performance of Chinese companies in the UK prior to the EU referendum. However it provides some important insights into both opportunities and challenges of continued Chinese investment in the UK.

Harnessing the vast potential for investment from China may be one of the keys to a vibrant and sustainable economic future for the UK post-Brexit. According to a report by China's Administration for Industry and Commerce (AIC) there are around 77 million registered companies in China, of which an estimated 150,000 have the potential to grow into international businesses and invest overseas. The 280 companies currently established in the UK are therefore merely the tip of the iceberg.

Among the success stories included in this year's Tracker are the re-emergence of the 90-year old cornerstone of Chinese banking, a telecom company that has doubled its market share in the UK and France and a property group that continues to add to the London skyline.

We congratulate the Tou Ying Tracker companies on their achievements and their outstanding contribution to the UK economy.

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About the Grant Thornton 投英 Tou Ying Tracker

The Grant Thornton 投英 Tou Ying Tracker, developed in collaboration with China Daily, identifies the fastest-growing Chinese companies in the UK as measured by percentage revenue growth year-on-year, based on the latest published accounts filed as at 7 October 2016.

It includes companies with turnover of more than £5 million and a minimum two-year track record in the UK that are 50% or more owned by an entity in China.

Tou Ying Tracker 2016 overview

- The top 16 fastest-growing Chinese SOEs in the UK achieved average growth of 146% in 2015, while private companies grew by 210% on average.
- Together, these businesses had a combined turnover of more than £9.8 billion and employed over 20,000 people.
- The majority of the Tou Ying Tracker 2016 are new entrants, with the exception of Lenovo, PetroChina, China Telecom and China Unicom.
- The fastest-growing SOEs are focused mainly on the energy, financial services and technology sectors, while private companies are more diverse.
- Bank of China and ICBC Standard Bank are the only banks on the list of the 16 fastest-growing SOEs, although the three banks featured in last year's Tracker have continued to grow, albeit at a slower rate.
- All but two of the top 16 SOEs grew organically, while private companies are split between organic and M&A growth.
- 75% of the SOEs are based in London, while private companies are more dispersed around the UK.
- The boards of these top 30 Tou Ying Tracker companies include more women and have a younger age profile than the average for the FTSE 250.
- The lower total turnover of £9.8 billion compared to £35 billion in the Tou Ying Tracker 2015 is largely due to the fact that Sinochem, whose turnover was £30 billion, has not made the new list.
- 30% of Chinese companies in the UK failed to file their accounts in time for inclusion in the Tou Ying Tracker 2016.

UK's top 30 Chinese companies in brief

The top Chinese companies in the UK achieved average growth of **174%**

The top 16 state-owned enterprises (SOEs) grew by **146%**

While the top 14 private companies grew by **210%**

SOEs: 14 ORGANIC — V — 2 M&A

PRIVATE: 6 ORGANIC — V — 8 M&A

MANUFACTURING	TECHNOLOGY, MEDIA AND TELECOMS	LEISURE - BARS, RESTAURANTS AND HOTELS	RETAIL AND CONSUMER	FINANCIAL SERVICES	REAL ESTATE AND CONSTRUCTION	ENERGY AND UTILITIES	BUSINESS SUPPORT SERVICES
3	7	1	4	6	2	5	2

THE MAJORITY OF SOEs ARE BASED IN LONDON, WHILE PRIVATE COMPANIES ARE MORE DISPERSED AROUND THE UK

16% OF BOARD MEMBER POSITIONS ARE OCCUPIED BY WOMEN

8yrs

BOARD MEMBERS OF UK'S TOP CHINESE COMPANIES ARE ON AVERAGE 8 YEARS YOUNGER THAN UK PEERS

WITH COMBINED TURNOVER OF **£9.8bn** IN 2015

THEY EMPLOYED OVER **20,000** PEOPLE

Grant Thornton 投英 Tou Ying Tracker 2016 - Top 16 SOEs (In alphabetical order)

Company name	Sector	Region
Bank of China (UK) Ltd	Financial services	London
BOC Aviation (UK) Ltd	Business support services	London
Boci Global Commodities (UK) Ltd	Financial services	London
Changan UK R & D Centre Ltd	Technology, media and telecoms	Central
China Bridge Group (UK) Ltd	Business support services	London
China International Capital Corporation (UK) Ltd	Financial services	London
China RE UK Ltd	Financial services	London
China Telecom (Europe) Ltd	Technology, media and telecoms	London
China Unicom (Europe) Operations Ltd	Technology, media and telecoms	London
Greenland (United Kingdom) Investment Ltd	Construction and real estate	London
ICBC Standard Bank PLC	Financial services	London
Nexen Petroleum U.K. Holdings Ltd	Energy and utilities	South
Nexen Resource Holdings U.K. Ltd	Energy and utilities	South
Petrochina International (London) Co., Ltd	Energy and utilities	London
Repsol Sinopec Oil Trading Ltd	Energy and utilities	North
Unipec U.K. CO. Ltd	Energy and utilities	London

Grant Thornton 投英 Tou Ying Tracker 2016 - Top 14 Private (In alphabetical order)

Company name	Sector	Region
Alipay (UK) Ltd	Financial services	London
Brecrest Fashion Ltd	Retail and consumer	North
Holroyd Precision Ltd	Manufacturing	North
House of Fraser Group Ltd	Retail and consumer	London
Huawei Technologies (UK) Co., Ltd.	Technology, media and telecoms	South
Hytera Communications (UK) Co., Ltd	Technology, media and telecoms	South
Lenovo Technology (United Kingdom) Ltd	Technology, media and telecoms	South
Mflex UK Ltd	Manufacturing	South
Precision Components Ltd	Manufacturing	North
R.F.S. (UK) Ltd	Technology, media and telecoms	South
RW Wentworth UK Ltd	Leisure (Hotels, bars, restaurants)	South
Shun DA (UK) Ltd	Retail and consumer	London
Shunfeng Imp-Exp Ltd	Retail and consumer	London
Yuanda (UK) CO. Ltd	Construction and real estate	London

Diverging fortunes?

SOEs laying the foundations

The top 16 fastest-growing SOEs on the Tou Ying Tracker 2016 reflect the more traditional strategies of Chinese companies expanding overseas. SOEs have focused mainly on the UK energy and financial services sectors to generate long-term sustainable returns or gain valuable experience of operating infrastructure projects. All but six of the 16 companies on the SOE list come from these two sectors, with the remainder coming from the telecoms, real estate, technology and business support services sectors.

Some of these SOEs, such as Bank of China, have been stalwarts of the UK economy for many years. Three of its subsidiaries – BOC Aviation, Boci Global Commodities and China Bridge Group – are also included in the top 16 SOE list, having outpaced the parent company's growth. Bank of China and ICBC Standard Bank are the only banks on the list, although the three banks included in last year's Tracker – Agricultural Bank of China, Bank of Communications and China Construction Bank – continued to grow, but at a rate below the cut-off for the Tou Ying Tracker 2016.

In the telecoms sector, the infrastructure being spearheaded by China Unicom and China Telecom is helping to open up a new 'information Silk Road' for private companies setting their sights overseas. Similarly, there has been rapid growth in business support services, such as visa provider China Bridge.

Private companies finding their way

By contrast, the top 14 private companies range across the manufacturing, technology, media, telecoms, leisure, retail, consumer, financial services and property sectors. This reflects the growing global presence of the Chinese private sector alongside its increasingly consumer-oriented economy, underlined by the move from 'Made in China' to 'Made for China'.

The strong performance of the technology companies on the list illustrates how they are delivering innovative products and services, rather than simply producing copycat western goods and services.

The likes of Lenovo and Huawei are becoming well established on the UK consumer scene, while Alipay has succeeded in bringing its home-grown mobile payments services to the UK market.

Increased investment in tourism and leisure reflects a boom in Chinese overseas travel and a growing expat community, which has fuelled the growth of prestige brands such as Wentworth golf and country club. The popularity of UK entertainment brands with Chinese audiences is demonstrated by ongoing interest in a number of famous English football clubs, although none of these make the top 30.

Future investment may focus on healthcare, the creative industries, real estate and infrastructure such as rail, airports and nuclear energy.

For example, UK and Chinese healthcare companies have recently signed deals with a total value of more than £250 million, following a visit to Shanghai by the UK Health Secretary as part of the UK-China Health Dialogue with Vice Minister Cui Li.

Five new UK-China commercial collaboration agreements were announced at the recent Creative Innovators Forum in Shanghai, strengthening the countries' creative industry ties, which are widely considered very important to future economic prosperity.

Strategies for success

The spectacular growth of the SOEs and private companies included in the Grant Thornton Tou Ying Tracker 2016 highlights a number of key issues for consideration by future Chinese investors.

Organic growth v M&A

The Top 16 Chinese SOEs are mainly the result of organic growth, whereas M&A accounts for more than half of the private company list and several of its new entrants.

This might reflect a more strategic approach to acquisitions than seen previously, particularly in the technology sector, with the emergence of a number of sophisticated, global and acquisitive businesses. Huawei, for example, has been particularly adept at adapting its products and promotion to specific western markets.

In the retail and fashion sectors, acquisitions such as babywear company Brecrest Fashion, included in the Tou Ying Tracker 2016, follow a long line of Chinese investment in UK heritage brands such as House of Fraser and Links. This underlines the importance of identifying target companies with an appropriate strategic fit and the ability to create long-term value in the domestic Chinese market.

By contrast, Bright Foods has struggled to crack the Chinese market with its Weetabix brand, following its acquisition of the cereal maker. Recent reports suggest Bright Foods will be looking for a buyer this year, less than five years after it took control of this famous British brand.

Successful acquisition strategies such as House of Fraser, which announced plans to open three large stores in China and Silver Cross also demonstrate the critical importance of effective post-acquisition integration. Fosun's acquisition of Silver Cross, for example, highlights the benefits of allowing the Chinese parent company to learn about the business alongside the existing UK management team without unduly interfering with its business model. By contrast, imposing a traditional Chinese management structure can sometimes hinder innovation.

A good example of the synergies that can be achieved through acquisition is Chongqing Machinery and & Electric Co's purchase of Holroyd Precision Limited. The company has benefitted from a stable shareholder base and long-term investment in R&D, achieving growth of 46% in its last financial year, a full seven years after its acquisition. Lenovo too has consistently delivered impressive growth figures since its acquisition as long ago as 2005 and is another excellent example of successful post-acquisition integration in our private company list.

More generally, post-acquisition integration involves sensitive handling of a raft of issues, such as aligning policies and systems, managing redundancies and maintaining good working relationships with minority shareholders – all demanding effective internal communication processes.

Dealing with these acquisition issues is likely to become even more critical in light of the Chinese authorities' tightening regulation of overseas M&As for both State-owned and private Chinese companies. During the past six years, the Bank of China has facilitated overseas acquisitions by extending $56.3 billion worth of loans for 188 deals involving Chinese companies. More recently, however, falling renminbi and forex reserves have reportedly led Chinese decisionmakers to consider restricting eight outbound mergers and acquisitions worth more than $10 billion and intensifying checks on the purchases of more than $1 billion, if the acquisitions are outside the investor's core business.

The informed strategic decisions exemplified by a number of the Tou Ying Tracker 2016 companies, however, should mean that they are unlikely to be affected by this policy. The road to sensible acquisitive growth is likely to remain very much open, but the full impact of this policy will become clearer during 2017.

Regulation and compliance

Trust and integrity in UK markets and businesses, regardless of their ownership, are fundamental to maintaining a vibrant UK economy. With all UK businesses under increased government and market scrutiny, it is more important than ever for Chinese companies in the UK to meet their responsibilities as good corporate citizens and to 'play by the rules'.

The large number of Chinese-owned companies that did not file their accounts on time for the most recent financial year – 30% in our analysis – should serve as a wake-up call to their boards of directors and finance teams.

All companies operating across borders need to recognise and adapt to a changing international regulatory landscape, this includes:

- The country-by-country reporting regime being rolled out as part of the OECD Base Erosion and Profit Shifting initiative, as well as the increasing co-operation and sharing of financial information between national governments in an attempt to crack down on tax evasion.
- The UK government's proposals on corporate governance and legislation such as the Modern Slavery Act.
- New rules that require all businesses that own more than 25% of a UK asset to disclose who has significant control over them, as part of the UK government's push for transparency.
- Overseas companies joining the UK business community are encouraged to support voluntary compliance, for example with the Financial Reporting Council levy for larger companies to fund its regulatory activities in the financial sector.

These obligations and the potential reputational damage with local stakeholders of non-compliance demonstrate the importance of experienced local advisers. This applies not only to financial reporting, but to disciplines such as strategy, law and media relations.

Governance and board diversity

According to a Cranfield School of Management report, just 5.6% of FTSE 250 board positions are occupied by women.

Our analysis of the board composition of the Tou Ying 2016 top 30 reveals above average gender diversity, with 6% of private company board positions and 12% of SOE board positions occupied by women. These are perhaps surprisingly high proportions, given that many of the companies concerned do not face the same level of scrutiny and shareholder pressure as their listed counterparts.

The proportion of female board members is highest among the technology, media, telecoms and financial services companies on the list. Noteworthy examples include Huawei (with 2 out of 7 female board members), ICBC Standard Bank (with 4 out of 13) and China Bridge (with an all-female board).

Looking at the age profile of company boards, a report by Spencer Stuart shows that the average age of UK listed company non-executives is 59 and executives 52. Compared to this group of UK peers, the companies in our Tou Ying Tracker 2016 top 30 have a younger average board member age of 48, although this covers a broad range between 25 and 75.

Chinese companies in the UK should find the results encouraging, especially considering the well-documented benefits of diversity at all levels of a business.

[1] https://www.ft.com/content/2511fa56-b5f8-11e6-ba85-95d1533d9a62
[2] http://uk.reuters.com/article/us-china-boc-boc-idUKKCN0WO08L

Retaining and incentivising talent

The companies in the Tou Ying Tracker 2016 employ over 20,000 people in the UK and are likely to continue growing. Attracting and retaining the requisite talent is an increasingly important issue, particularly given the relatively high levels of UK employment and possible restrictions on free movement of labour after Brexit.

Chinese companies are closely monitoring the UK's evolving immigration policy to gauge the likely impact of any visa restrictions on their home-grown executives who typically work alongside UK management.

These concerns aside, the way in which talent is typically rewarded in Chinese businesses is quite different to the 'total reward' approach increasingly adopted by many UK employers. There is generally a greater focus in China on a traditional salary-plus-performance-related-bonus model. Many Chinese businesses coming to the UK adopt this relatively traditional remuneration strategy, consisting of a package of salary, bonus and basic pension plan, sometimes with benefits such as medical insurance.

The companies implementing the most successful post-integration strategies are likely to be those considering alternative incentives in their remuneration packages. Particularly where the retention of a senior local management team is seen as key to success, Chinese companies may wish to implement suitable share option – or long-term remuneration – incentives to align their interests to those of the relevant management team.

Winning the talent battle is about more than financial reward alone. Chinese companies also need to create a working environment and culture that allows them to attract and retain the right people in a competitive job market. It also means catering for the different career aspirations of the millennial generation. This may require strategies such as flexible working or tailor-made benefits packages suited to specific groups of workers.

Another way to attract talented younger employees may be through offering apprenticeships. Chinese employers should note that there is currently something of a 'use it or lose it' opportunity to take advantage of financial assistance for employee training available through the UK's new apprenticeship levy on larger companies.

Breakdown of employment by sector

Sectors	Employees
Manufacuring	153
Technology, media and telecoms	1,616
Leisure (hotels, bars, restaurants)	243
Retail and consumer	17,509
Financial services	438
Real estate and construction	98
Energy and utilities	761
Business support services	43
Total	**20,861**

The Brexit factor

Formal negotiations to leave the EU are likely to start in March 2017 and may take two or more years to complete. Until then, the details of the UK's future trading relationships with the EU will be unknown. Different sectors will be affected to a greater or lesser extent by Brexit and the possible outcomes of these negotiations. Chinese investors should therefore consider the upside and downside impact on their specific sectors and businesses.

Brexit is just one component of wider global economic uncertainty. Elections in other EU countries in 2017, including France, Germany and the Netherlands may create further uncertainty and will probably determine the approach taken by the rest of the EU. In the meantime, the UK remains open for business and continues to provide a stable legal and regulatory environment, a large international talent pool and a competitive tax regime.

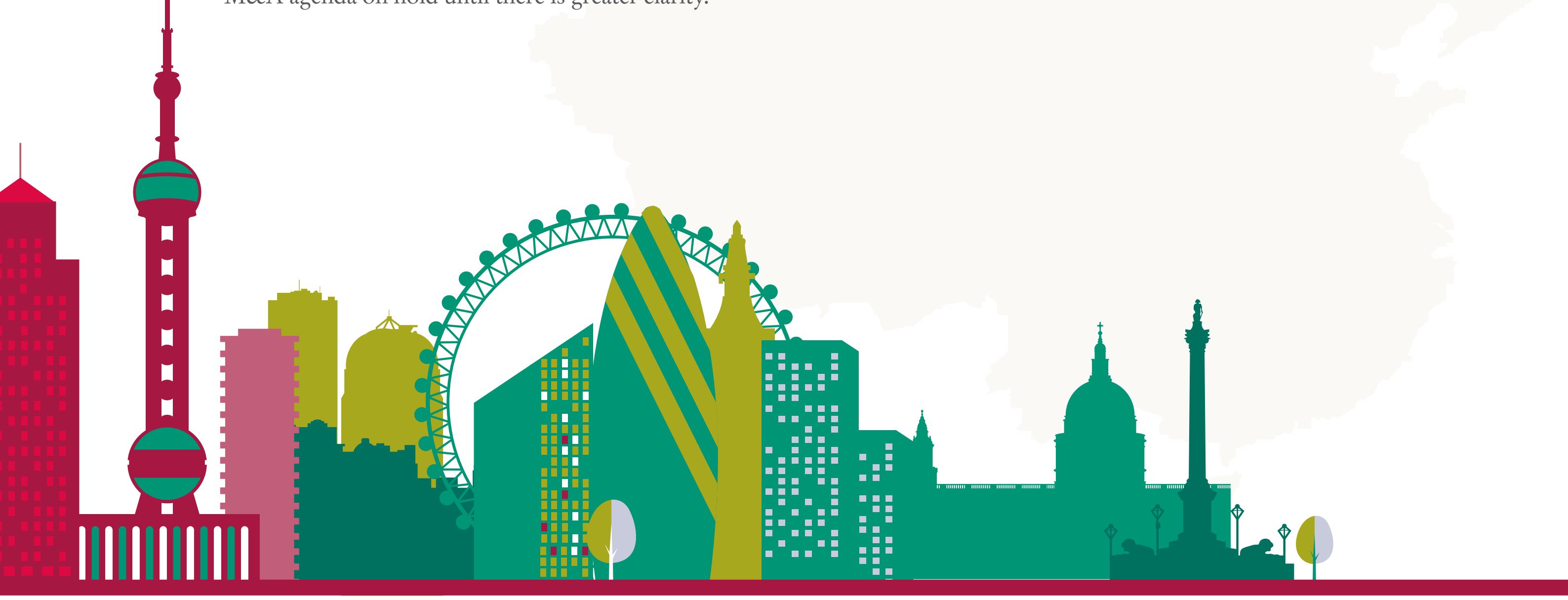
A survey by The China-Britain Business Council shows that UK companies are broadly confident in post-Brexit trade with China. Over half (56%) of respondents stated that leaving the EU would create "more" or "many more" business opportunities with China, while 88% said a Free Trade Agreement with China was either "important" or "very important".

Uncertainty surrounding Brexit will inevitably have an impact on M&A, causing some transactions to fail or be postponed, and some acquisitive groups may put their M&A agenda on hold until there is greater clarity.

However, Brexit negotiations may not be completed until early 2019 and both private owners and public companies cannot postpone their sale/acquisition plans for that long. Any slowing in M&A activity may therefore prove to be temporary. Overseas buyers were particularly active in the UK food and drink sector during Q3 2016. It is probably too early to draw negative conclusions regarding the impact of Brexit on M&A.

Since the result of the EU Referendum, there have been some significant projects involving Chinese investors and Chinese capital. Real estate deals – residential and commercial, investment and development, London and national – have continued to complete and projects such as Hinkley Point are evidence that the UK remains an attractive business destination for China. Once Prime Minister Theresa May had signalled her support for the nuclear project, it reignited a sense that the UK government recognises that encouraging a positive diplomatic and business relationship with China will be in the best interests of both countries.

The UK government will seek to maintain the competitive nature of the UK and its trading relationships and has signalled its intent to provide a smooth transition and to maintain legal and regulatory stability. In addition, the value of sterling may continue to offer opportunities for investors, as do government plans for increased infrastructure investment.



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China Britain Services Group

The China Britain Services group has extensive experience of assisting Chinese companies expand and set up in the UK. Whether you're looking to export, invest or do business with the UK, our advisers can help at any stage of your company's growth cycle.

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