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Chinese Companies Targeting Southern California for Growth Opportunities

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In 2016, Orange County has been at the epicenter of numerous major deals between U.S. and Chinese entities involving technology, entertainment, healthcare, and real estate. Despite China's current political and macroeconomic murkiness, there are many factors that continue to drive Chinese interest in U.S. investments. One of these drivers is the higher valuations for many U.S. assets by Chinese stock markets compared to Wall Street, which has encouraged Chinese public companies to aggressively pursue overseas targets using funds raised in China. The deceleration of China's economy has further intensified the hunt by Chinese firms for foreign value to bolster sagging balance sheets and diversify revenue streams.

Another deal driver is the Chinese government's adoption of various economic programs that encourage overseas investment. The 13th Five-Year Plan, adopted in 2015, promotes moving toward a fully developed economy defined by high-end technological innovation and has prompted Chinese companies to seek out cutting-edge foreign targets. The trends outlined above, coupled with last year's devaluation of the yuan that weakened acquisitive companies' cash reserves, help explain the record US$120 billion-plus of Chinese investments in the U.S. so far this year. Here are just a few examples of recent deals in 2016 that have a close nexus to Orange County:

- ▶ On February 17, Chinese shipping company Tianjin Tianhai announced that it would buy Ingram Micro, an Irvine-based wholesale provider of technology products and supply chain services, for US$6 billion.
- ▶ On March 12, Chinese holding company Anbang Insurance Group agreed to purchase Strategic Hotels & Resorts' 16 U.S. luxury resorts and hotels, including the Ritz-Carlton Laguna Niguel and Montage Laguna Beach, from Blackstone Group for US$6.5 billion.
- ▶ On March 28, Chinese investment holding company Fujian Thai Hot Investment completed its purchase of a majority stake in Alliance HealthCare Services, a Newport Beach-based medical imaging company, for approximately US$103 million.
- ▶ On July 26, Chinese technology firm LeEco agreed to buy Vizio, an Irvine-based consumer electronics developer, for US$2 billion.
- ▶ On August 9, NextVR, a Laguna Beach-based virtual reality startup, announced that it had raised US$80 million in Series B funding from a consortium of venture capital investors, many of which are based in China.
- ▶ On August 22, the Anaheim Planning Commission approved plans, originally announced in 2015, by Hong Kong-based LT Global Investment to build a US$450 million mixed-use project in Anaheim's Platinum Triangle.

Easing of Regulatory and Political Hurdles for Chinese Acquirers

While the dynamics described above will continue to lead Chinese companies to seek out investment targets overseas, regulatory, and political environments in the U.S. and China remain something to consider for cross-border deals. On the regulatory side, some acquisitions of U.S. businesses or assets by Chinese companies must clear both the Committee on Foreign Investment in the United States ("CFIUS") and an array of official approval processes in China. CFIUS is a U.S. government inter-agency committee, chaired by the U.S. Department of the Treasury, which determines whether particular foreign investment transactions raise potential national security concerns.

While CFIUS' review is not automatic, it reserves the right to investigate, as well as to block or even to unwind, any proposed foreign acquisition of control of a U.S. business (including through minority investments) that raises national security concerns that cannot be resolved without taking that extreme action. Transactions may raise national security concerns for a variety of reasons, including defense-related technology or contracts held by the target, or acquisition of assets that are considered critical infrastructure. While CFIUS rarely blocks a transaction, it has taken this action occasionally. Nevertheless, CFIUS has cleared most acquisitions of U.S. businesses by Chinese entities, in some cases by resolving the national security issues through agreements with the parties to implement mitigation measures.

It is important to keep in mind that notifying CFIUS is a voluntary decision by the parties, and that not every transaction warrants notifying CFIUS. In some transactions, the U.S. target business clearly has no relation to national security. In many cases, however, the potential for CFIUS interest is not clear, and it is wise to notify CFIUS in order to obtain deal certainty, in a timely way. A benefit of CFIUS review is that once CFIUS clears a transaction, then it will not re-open the decision (unless the parties provided materially inaccurate information).

On the other hand, in China, new regulations have simplified matters somewhat in recent years, as outbound investments have generally been encouraged, not only by state-owned enterprises, but by large, medium, and small private companies. Most cross-border investment projects now only need to be filed, post-closing, with the National Development and Reform Commission ("NDRC"), which removes a precondition for converting Chinese currency into U.S. dollars. Also, Ministry of Commerce ("MOFCOM") approval is only required for deals involving sensitive countries or industries; all other deals only need to be filed for recording purposes. Registration with the State Administration of Foreign Exchange ("SAFE") for remittance of currency outside China has likewise been streamlined. However, given SAFE's concerns regarding the significant outflows of capital from China in recent months, the currency conversion and approval process has been restricted as SAFE takes more stringent steps to review transactions. In some cases, this has led to delays in funding for outbound investment transactions. Nevertheless, given the easing of some restrictions in acquiring assets in the U.S. by Chinese companies, more private sector companies are driving China's mergers and acquisitions activity in the U.S. This marks a significant shift from just a few years ago, when the private sector accounted for a much smaller fraction of Chinese outbound deals compared to state-owned enterprises. Unless and until the Chinese economy rebounds dramatically, this trend should continue as private Chinese investors look to the U.S. as a way to balance their investment risks.

Structural economic dynamics continue to favor increased interest in U.S. assets by investors in China. No less important, Orange County's diverse business landscape (particularly in the fields of technology, entertainment, healthcare and real estate) offers a plethora of appealing prospects for investment, acquisition or partnership, so this is a market dynamic to watch in 2017.

The opinions expressed in this article do not necessarily reflect the views of O'Melveny & Myers LLP or its clients, and should not be relied upon as legal advice. For questions, please contact Mark Peterson at mpeterson@omm.com, Tony Wang at tonywang@omm.com or Michael Reynolds at mreynolds2@omm.com.

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