

The book cover features a light beige background with a subtle, repeating pattern of stylized clouds and waves. A black grid is overlaid on this background. A large, dark, rectangular area with intricate, swirling patterns is positioned in the center. A red circle is placed at the top center of this dark area. Several circular objects, resembling Go stones, are scattered across the grid: a black stone at the top left, a black stone at the top right, a black stone on the left side, a black stone on the right side, a white stone at the bottom left, a black stone at the bottom center, and a black stone at the bottom right.

THE
GLOBALIZATION
of
CHINESE
COMPANIES

**STRATEGIES FOR CONQUERING
INTERNATIONAL MARKETS**

ARTHUR YEUNG

KATHERINE XIN

WALDEMAR PFOERTSCH

SHENGJUN LIU

The Globalization of Chinese Companies

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**Arthur Yeung
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Preface

In the first half of 2010, the Chinese economy became the world's second-largest in gross domestic product (GDP) terms, behind only that of the United States. In 2009, China also became the largest exporting nation and is striving to consolidate this position into the future. Now more than ever, with the globalization of the world economy, the game is being played on the largest potential playground.

In the last 50 years, numerous companies have entered the global market and changed the market landscape in their home countries and around the world. After World War II, U.S. firms took the lead, with European companies following soon after. In the 1970s, Japanese consumer-electronics and auto companies entered the lucrative markets of the industrialized world. In the '80s, Korean companies followed and became serious competitors to new entrants and established players alike. Now, Chinese companies are using their competitive advantages to establish themselves as global players.

The subject of globalization, particularly for Chinese companies, contains many issues worthy of analytical research: Why do companies want globalization? How can they position themselves in the globalized economy? What paths are available to them and which paths are more suitable for specific businesses to follow? What kind of globalization fits the organization's capabilities, and how can they create the necessary capabilities quickly and effectively?

Facing these complex issues, firms in China and around the world may easily become blinkered in their thinking; for example, seeing only the benefits of globalization while ignoring the costs.

They may only see the opportunities and forget to examine the scope and strength of their capabilities. We have found that many experts and scholars indulge in cheering success and criticizing failure, but fail to provide constructive solutions. They introduce the best practices of multinational companies without providing systematic analysis and reflection.

In 2009, the number of Chinese companies listed in the Global Fortune 500 list increased from 34 to 43 (see Appendix 9), and their revenue growth was impressive. However, coupled with the gains, there were also pains that few people know about. In fact, very little is known about how China has managed to ascend to the position it occupies today. But one thing is certain: there were many hardships along the way.

The purpose of this book is to shed light on the current situation of Chinese firms and to help Chinese entrepreneurs who want to undertake the challenges of globalization. We offer a thorough analysis of the current developments in this area; help aspiring candidates to develop a systematic approach; and help them to avoid errors in their thinking by providing a “navigation map” and a set of practical tools and instruments for managing the task of globalization.

This book is designed to provide a systematic and pragmatic approach to global expansion and competition for Chinese entrepreneurs and is based on both clear frameworks and detailed case studies. We believe that the book will be of practical benefit to Chinese senior executives facing the challenges of both global expansion and competition, and to managers, scholars, and students around the world who are interested in understanding how firms in China are striving to emerge in the global arena.

At the end of the book, we provide a self-assessment questionnaire covering all of the issues raised in these pages (see Appendix 10), something that can be utilized as a practical reference to the content. Immediately following, we provide an action plan (Appendix 11) which gives the reader/manager an opportunity to assess the current situation of their company in the context of going global. This tool has already helped to focus the strategic discussion within many companies in the course of going global. It is also available through the authors in Chinese/English and they will gladly assist with the interpretation of the results.

We firmly believe that the globalization of Chinese firms in the twenty-first century will be one of the most noteworthy events in the development of the world economy, and sincerely hope that this book will be helpful in contributing toward the rise of China's own "Sony and Samsung."

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SHENGJUN LIU
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CHAPTER 1

Reaching Out

China is a sleeping giant. Let her sleep, for when she wakes she will shake the world.

Napoleon Bonaparte, 1803

China's position in the world economy has changed since the economic crises of 2008 and 2009. It is no longer simply perceived as the "production workshop of the world" and provider of cheap goods to the industrialized world. It is now recognized as the biggest holder of U.S. government bonds and a possible engine for global economic recovery. Without a doubt, China maintained its economic growth in this difficult time not only with the help of huge government stimulus packages but also with the strong commitment of Chinese entrepreneurs who have ambitions to be successful in the home market and beyond.¹

Five years ago, very few consumers outside China had heard of the home-appliance producer Haier or the computer brand Lenovo. Today, they are sold successfully in the United States, Europe, and elsewhere. For years, Chinese companies have been producing shoes, toys, light bulbs, consumer electronics, and much more on behalf of foreign brands. Many Chinese homegrown brands can be found in Asia, the Middle East, Africa, and Latin America. More than 700,000 passenger cars, light trucks, and heavy trucks were sold overseas in 2008, with car manufacturer Chery leading the way. But it is not only in consumer products that China offers competitive

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goods at low prices; it also produces industrial goods such as heavy construction equipment (Sany, Zoomlion, and Tengzheng, for example), ships and containers, heavy machinery, and mining equipment, and even airplanes.² The newly formed Commercial Aircraft Corporation of China Ltd. (COMAC) received 280 orders (including 25 from GE Commercial Aviation Services) for its first ARJ21 medium-range jet, and has plans to deliver 20 of its new mid-size (190-seat) C919 to Western and Chinese customers in 2016. Also, China has become one of the fastest-growing aviation markets, with more than 200 million passengers in 2009 and projected annual growth of more than 7.8 percent for the next 20 years (see Appendix 1). While the airline industry suffered in other countries in the aftermath of the economic crisis, Chinese competitors strengthened their position and are expanding aggressively.³

In the 1980s, Japanese companies plunged into what was referred to as the “buying the entire United States” spree,⁴ which saw the Wall Street Building, Rockefeller Center, and other U.S. landmark buildings swept up in its momentum. To the indignation of some Americans, Japanese companies acquired CBS and other industries that were part of the country’s cultural identity. Since the start of the twenty-first century, China has been doing the same. It is widely reported that Chinese firms have been actively engaged in overseas M&As to the tune of US\$0.2 billion in 2002, and US\$5.28 billion in 2005. These numbers continue to increase; according to statistics provided by the Chinese Ministry of Commerce, the amount in 2008 reached US\$20.5 billion.⁵ The TCL Group was widely known as the “pioneer” in aggressive overseas acquisition to realize its global aspirations. Many other companies, such as Lenovo, CNOOC, SAIC, and BenQ, undertook similar initiatives from 2000–08 and, most recently, Geely made a deal with Ford to acquire Volvo.

Burning Passion

In September 2002, the TCL Group, one of China’s largest appliance companies, announced that it had acquired the substantial assets the Germany company Schneider Electronics AG for €8.2 million (US\$8 million), creating a European production base for color televisions. The acquisition was cleverly made to bypass the

European Union's aggressive anti-dumping regulation against Chinese electrical-appliance firms. Few realized that this was just a warm-up for a series of overseas acquisitions by the TCL Group. In July 2003, TCL chairman Li Dongsheng formally announced the Group's "Dragon and Tiger Plan" to establish two competitive businesses in global markets (dragons) and three leading businesses inside China (tigers). This plan became the TCL-style "Great Leap toward Globalization."

Later that year, TCL announced a joint venture with the French electronics giant Thomson (the originator of color-TV sets and the owner of more than 34,000 TV patents), with TCL owning 67 percent of the new entity (TTE). Remarkably, sales of TTE's color TV sets reached 18.5 million units in 2003, which established the company as the leader in this field and thrust TCL onto the world stage just 10 years after its entrance into the highly competitive color-TV market. In April 2004, TCL and another French company, Alcatel, announced the establishment of a joint venture that would engage in the production and sales operations of mobile phones. TCL injected €55 million (US\$67.7 million) for a 55 percent shareholding. With this, TCL became the world's seventh-largest mobile-phone manufacturer. Through the acquisition, TCL acquired core 3G technologies in network and wireless access systems. It thus became one of the few Chinese manufacturers of mobile phones with a core technology, which meant that it not only bought market share, but also acquired capabilities to prepare for the future.

Surging Forward

TCL was not the only one to make the "Great Leap Forward." In February 2003, BOE Technology Group Co. Ltd. announced the acquisition of the Hydis Company, the Hyundai Group's TFT-LCD business (the key component for flat-panel screens), in a transaction valued at about US\$380 million, a record for a Chinese acquisition at that time.

In October the following year, the Chinese auto-industry leader, SAIC, spent US\$500 million in acquiring a 48.92 percent stake of South Korea's Ssangyong Motor—the first overseas acquisition in the Chinese automobile industry. In May 2005, when the century-old British MG Rover company declared bankruptcy, with an

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attendant layoff of more than 6,000 workers, SAIC and the Nanjing Automobile Corporation stepped in to rescue the company. The latter bought the assets of MG Rover, including the MG and Austin brands, for £53 million (US\$101.1 million).⁶ Before Rover's bankruptcy, SAIC had spent £67 million (US\$127.8 million) on the purchase of part of the intellectual-property rights of the Rover 25 and Rover 27 models, which were introduced to the Chinese market in 2007 and 2008 as Roewe 550 and 750, respectively. Ironically, in 2007 Nanjing Automobile was acquired by SAIC, with support from the Shanghai and Nanjing governments, giving SAIC access to the precious MG and Austin Martin brands.

On December 24, 2004, the Lenovo Group gave itself a Christmas present by buying IBM's worldwide PC business at a price of US\$1.75 billion. The new Lenovo surged forward to become one of the global top three, increasing its global PC market share from 2.3 percent to 8.3 percent on the back of revenues of US\$13 billion and sales of 14 million PCs. This was a dream come true for Lenovo, whose market share in Europe and the U.S. had been close to zero before the acquisition. Yang Yuanqing, chairman of the new Lenovo, admitted that, when the possibility had been first raised by IBM a few years earlier: "I felt that it was just like the Arabian Nights."⁷

In January 2005, the smallest of China's three major oil companies, CNOOC, offered as much as US\$13 billion to acquire the ninth-largest U.S. oil company, Unocal, and subsequently increased the offer to US\$18.5 billion. The American public became unsettled with fears that national security would be threatened by Communist China's offer. Members of Congress were suspicious of the government ownership of CNOOC and exerted pressure against the acquisition, preventing the deal from going through.

As early as 2002, the Haier Group had spent US\$14 million in acquiring the Greenwich Savings Bank building—a New York landmark—as its North American headquarters. Haier was less successful, however, in its subsequent attempts to acquire U.S. companies. In June 2005, Haier announced a bid of US\$1.28 billion for the veteran U.S. appliance firm Maytag, and was turned down. At the 2005 Globalization Forum of Chinese firms, Haier Group CEO Zhang Ruimin pointed out that "Haier's internationalization is at the gateway, blocked by foreign competitors. If we pass this obstacle, we will make great success, otherwise we will become martyrs."⁸

In June 2005, BenQ acquired the global mobile-phone business of Siemens and emerged as the world's fourth-largest mobile-phone brand. In the process of the acquisition, BenQ did not spend a single cent, but rather received a "dowry" of €250 million (US\$454.2 million) from Siemens, scoring a big bargain compared to TCL and Lenovo's costs of their acquisitions. The newly formed BenQ-Siemens mobile communications subsidiary went on to win the most prestigious iF design awards in Germany's "red dot" competition.⁹

In August 2007, six months after announcing its acquisition of the Philips mobile-phone business, China Electronics Corporation (CEC) started to run the business with a team from Philips. This was the first time that Philips had enfranchised its brand to a third party. CEC also announced its intention to work closely with retailers and explore overseas markets, with an expected investment of RMB100 million (US\$13.2 million).

On October 25, 2007, the Industrial and Commercial Bank of China (ICBC) announced its purchase of 20 percent of the Standard Bank of South Africa for US\$5.6 billion in cash, the biggest foreign acquisition by a Chinese commercial bank yet. According to an ICBC report, it gained a US\$1.213 billion cash dividend and US\$589 million capital bonus from the Standard Bank in 2008, an annual rate of return on investment of 7.7 percent. By the end of March 2009, the ICBC and Standard Bank had completed nine out of the 65 joint projects based on the premise of their closer relationship.¹⁰

China Merchants Bank, one of China's most innovative banks, acquired 53.12 percent of Hong Kong's Wing Lung Bank for HK\$19.3 billion (US\$2.5 billion). In 2008, the Sinosteel Corporation, one of China's biggest steel companies, purchased the U.S.-based Midwest Corporation. This deal was adjudged the "Best Deal" and "Best Requisition Deal" of the year, respectively, by *Finance Asia* and *Assets*.

In 2008, China Metallurgical Group Corp. signed an agreement with Cape Lambert Iron Ore Ltd., an Australian company, to buy its flagship iron-ore project for A\$400 million (US\$376.6 million). In July 2009, it sealed a deal with Waratah Coal Inc., another Australian company, to fund up to 70 percent of a A\$5.15 billion (US\$4.2 billion) venture project and take a 10 percent stake.

In February 2009, Shenzhen Zhongjin Lingnan Nonfemet Co. (SZLN), a Shenzhen state-owned mining business, invested A\$45 million (US\$ 28.6 million) into Perilya, an ailing Perth-based metal mining company, and acquired a 50.1 percent stake in the business. As a result of the deal, in which it became the first Chinese metal company to acquire a controlling stake in an Australian mining business, SZLN is now China's largest zinc-lead producer. This move, seen by some as "the smartest deal with the most favorable price of any Australian resource acquisition by a Chinese mining company over the last two years,"¹¹ is very significant for SZLN and its "going global" initiative. On May 26, 2009, the state-owned Guangdong Rising Nonferrous Metals Group, SZLN's parent company, signed a deal with Pan Australian Resources Ltd. to become its largest shareholder, with the purchase of a 19.9 percent stake worth A\$140 million (US\$102.1 million). This is Rising's second acquisition in Australia.

In May 2009, Haier announced that it planned to acquire a 20 percent stake in Fisher & Paykel—New Zealand's largest home-appliance maker—and become its largest shareholder. The deal gives Haier exclusive rights to sell Fisher & Paykel's home appliances in China and Fisher & Paykel reciprocal rights to sell Haier products in Australia and New Zealand.

In June 2009, GM and Sichuan Tengzhong Heavy Industrial Machinery, a private Chinese firm, made an initial agreement concerning the latter's purchase of GM's famous Hummer brand.¹² On the same day, Shanshan, a Ningbo-based Chinese menswear brand, announced that it had reached an agreement with Australia Heron Resources Ltd. for a 70 percent interest in a joint development of the Yerilla nickel-cobalt project. As part of the agreement, Shanshan has proposed to acquire 12.045 million Heron shares, or 4.99 percent of the Australian company's outstanding share capital. By giving Shanshan a foothold in the raw-materials supply chain, the deal has secured the company's further development.

The Collective Ambition

For decades, the economy of China has maintained a growth rate faster than that of any other nation. From 1978–2008, China's average GDP growth rate was 9.83 percent.¹³ The growth rate of its leading

companies was even higher. However, as local challengers matured and foreign companies entered, industry competition became much more severe. In order to survive, many Chinese companies applied a price-war strategy to maintain market share.

The purpose behind Chinese companies going global is not simply about winning a global market; it is also about technology, brand, and sales channels. Most Chinese companies are at the bottom of the Stan Shih¹⁴ Smiling Curve (see Figure 1.1). For example, the Japanese zipper-producer YKK earns US\$15 for one meter of its zippers, while Chinese competitors earn only RMB0.7 (US\$0.1 in 2008) per meter.

When TCL decided to acquire Thomson, the company considered the move a “can’t miss” opportunity to turn itself into a real global player. This kind of short-cut mindset was not uncommon during that time. Lenovo and BenQ also had this mindset, with different degrees of disappointment. For example, in 2002 Changhong, then China’s leading TV manufacturer, exported televisions and DVD players to the value of US\$780 million to the United States. However, while it was enjoying great success overseas, its competitor, APEX, snared the domestic market. In the end, Changhong lost US\$472 million and suffered dramatically. This failure could be attributed to a lack of global experience and also to impatience on the part of Chinese companies’ to globalize.

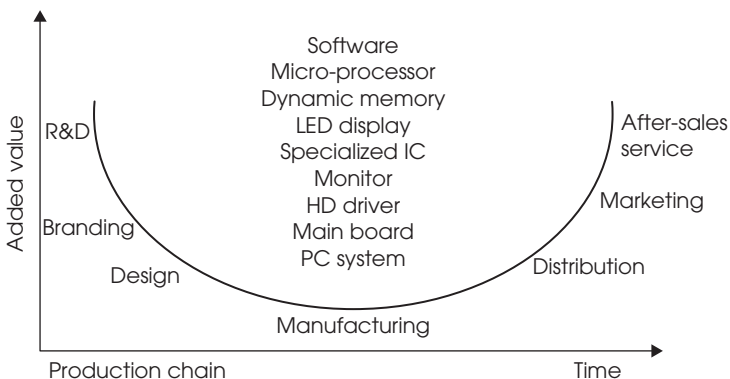


Figure 1.1 The Stan Shih Smiling Curve¹⁵

Things to Remember

The news that TCL had taken control of the valuable RCA TV brand in November 2003 caused a ripple in global consciousness, as did the sale of IBM's PC business to Lenovo in December 2004. Unfortunately, while China's acquisitions draw headlines, the outcomes are not always positive.

For many established names in the electronics business, TCL was a quiet assassin. Founded in South China in 1982 to make magnetic tape in response to the mainland's appetite for music from Hong Kong and Taiwan, TCL became a huge force in the television manufacturing industry, where its modestly priced, mid-tier product outperformed established Western competitors.

In spite of its great expectations of becoming the largest television manufacturer in the world, the iconic deal that led to the creation of TCL-Thomson Electronics (TTE) quickly turned to disappointment. The reality was that an increase in size and becoming a household brand name did not spare it from harsh competitive pressures. In its first year, the joint venture lost HK\$599 million (US\$77 million), followed by another HK\$1.5 billion (US\$220 million) in the first three-quarters of that year. Overall, almost half of its shareholders' equity quickly disappeared, and the value of TTE's shares on the Hong Kong stock exchange collapsed.

While TTE's business suffered all over the world, there were sharp differences between regions. Profits decreased minimally in China, where TTE had a particularly strong franchise, and in other developing countries, where manufacturers cleverly ship disassembled televisions to be then put together by local companies. In the United States, where both TCL and Thomson operated, the joint venture came close to breaking even, but in Europe, Thomson's home market, it was disastrous; TTE lost €159 million (US\$203 million) on sales of €328 million (US\$419 million) in 2006. In October that year, TTE announced that most of its European operations would be shrunk, sold, closed, or returned, including a factory in Poland and an expensive distribution network. Even the Thomson brand name would have largely disappeared within two years. TTE would instead concentrate on producing TV sets to be sold by other companies, with none of the cost of support and distribution that a brand requires. Even better, supervision for this kind of business would be based in China.

A big problem was that both TCL and Thomson focused on clunky old models that used cathode-ray tubes, despite the fact that