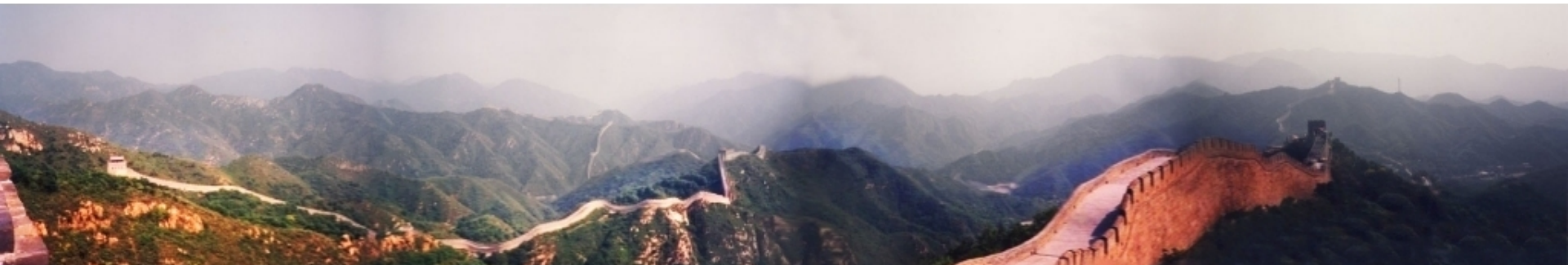


# **World Economic Forum Inaugural China Meeting**

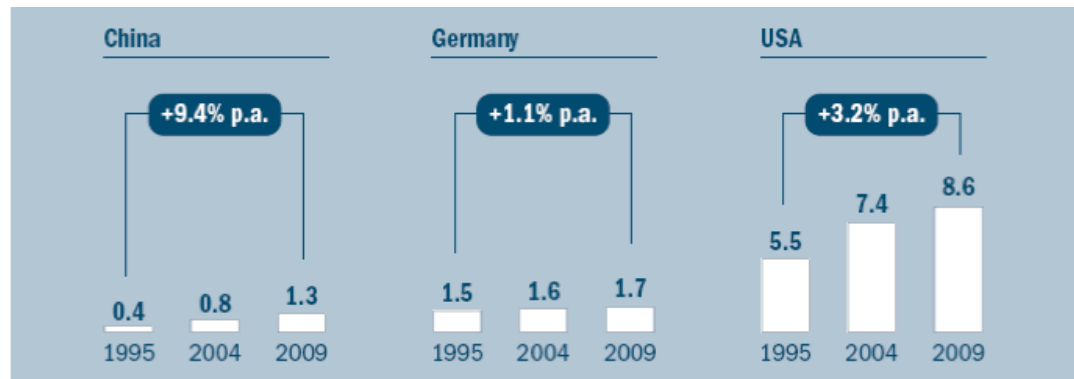
Dalian, September 2007



# No other country grew as fast as China in the entire world economic history.

- 1979-2004, China's economic growth per annum % 9.4
- 1990-2006 China's average purchasing power has risen sixfolds
- 2004, China's share in world GDP %4,1
- 2004, China's contribution to worldwide economic growth %8,8
- 2006, China's economic growth %13.6 (3 times the world economy)
- 2007, China will export more than the US
- 2008 will become world's largest net exporter (overtake Germany)
- 2008, China will become the world's third-largest economic power (overtake Germany)

Real disposable income (USD bn)



**China is a sales market with enormous potential, but companies must be aware of its limits, challenges and risks.**



## Limited Income

- Upper class of 13 million
- No middle class
- Average disposable income 889 USD per person in '05, 5% of Western Europe
- Relatively high savings rate of 40%

## Tough Competition

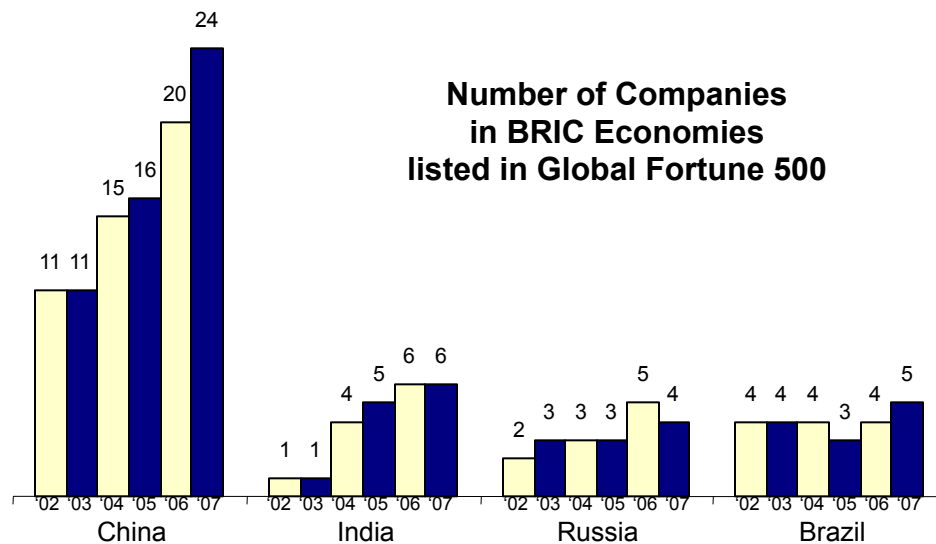
- Foreign providers, domestic providers and state-run companies lead to huge overcapacity, which in turn affects market shares and prices
- To win over Chinese customers, international companies must enter the market with the right offerings

## A Varied Market

- Climatic zones: polar to tropical
- 50 dialects
- 31 provinces with own government and laws.
- Peasants to urban dwellers lifestyles
- There is demand for every product but a national market probably for very few

Although the Chinese economy is a global giant, there are not much Chinese firms on the international scale.

- China is the **world's largest producer** of many products (copy machines, cameras, textiles, refrigerators, paper, shoes, toys, etc.) **but it is usually foreign companies** that are responsible for much of this production.
- **Western firms control around 85% of all high-tech exports** such as motherboards and routers.



- **Fortune 500 ('07) has only 24 Chinese companies** that generates most of their **revenues on the domestic market**.
- It is no easy for Chinese companies to make the jump to the global arena since they generally lack the expertise in **sales, marketing** and **development** necessary to become a global success.

**This is set to change:**  
**China's hidden companies are taking actions to be active in the global arena.**

# **“Go Global” is Chinese governments current strategy to encourage its companies to invest overseas.**

## **WHY**

- **Increase China's political influence**
- **To have the pride of having world class companies**
- **To employ foreign reserves by acquiring assets overseas**
- **To balance dependence on export-led development**
- **To equip the domestic firms with international experience**

## **HOW**

- **National policy in 10th Five year plan for '01-'05**
- **Support 50 Chinese companies to be listed on the fortune 500 before '10.**
- **Benefits from the government including information-sharing networks, domestic tax breaks, cheap land and low-interest funding**
- **Draw capital from foreign currency reserves**

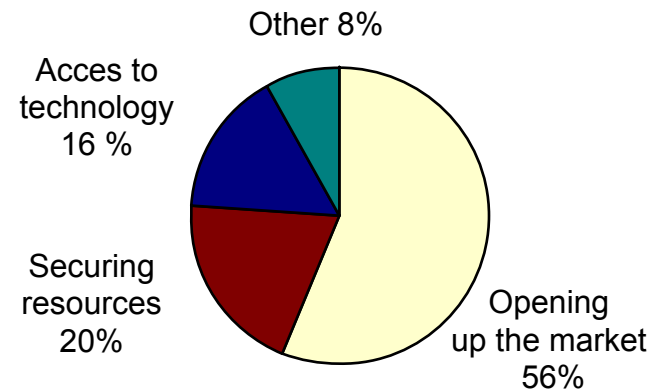
## **RESULTS**

- **73 billion USD invested outside**
- **Between '00 – '04, China's FDI increased by more than %70**
- **Invested in 160+ countries, The largest recipients were Asia and Latin America**
- **China's companies are still at the initial stage of "going out."**
- **Small and medium companies account for 70% of the outward investments**

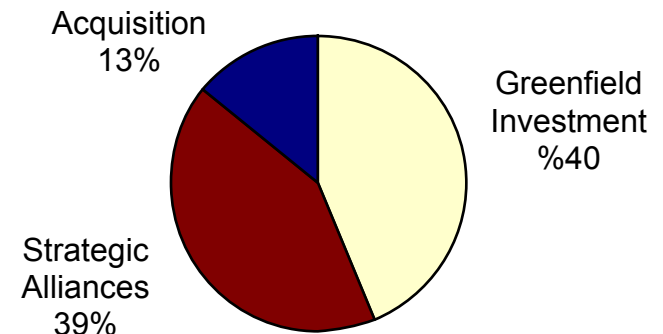
**For sustainable growth, Chinese companies have many reasons to develop relationship with the global economy beyond a simple export-driven model.**

- To work behind the trade and tariff barriers
- To capture a larger portion of the value chain
- To develop products and services to fit China.
- To bring new knowledge and capabilities
- To master new skills
- To gain access to technology and bring operations to international standards.
- To have global brands
- To secure the energy and resources
- To play a key role in the hightech and service industries
- To accumulate global operational experience before the fierce domestic competition

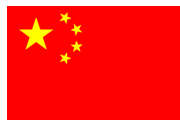
### Reasons for Expansion (\*)



### Ways of Expansion (\*)



# Chinese companies that want to expand internationally mostly prefer to move in two different destinations.



**Highly competitive companies enter European, Japanese and North American markets.**

**Small and medium companies start with emerging markets in Russia, Eastern Europe, Southeast Asia, Australia, Latin America, and Africa.**

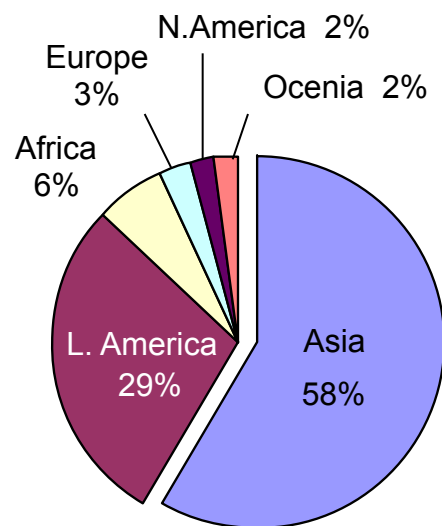
- Better understanding of emerging markets is a guarantee of success in initial overseas expansion plans
- Improve chances of a smoother entry into more developed western markets later.
- Companies like Huawei and ZTE have used their experience in building China's own markets to develop new ones in other emerging economies before tackling developed economies.

- Securing energy and resources

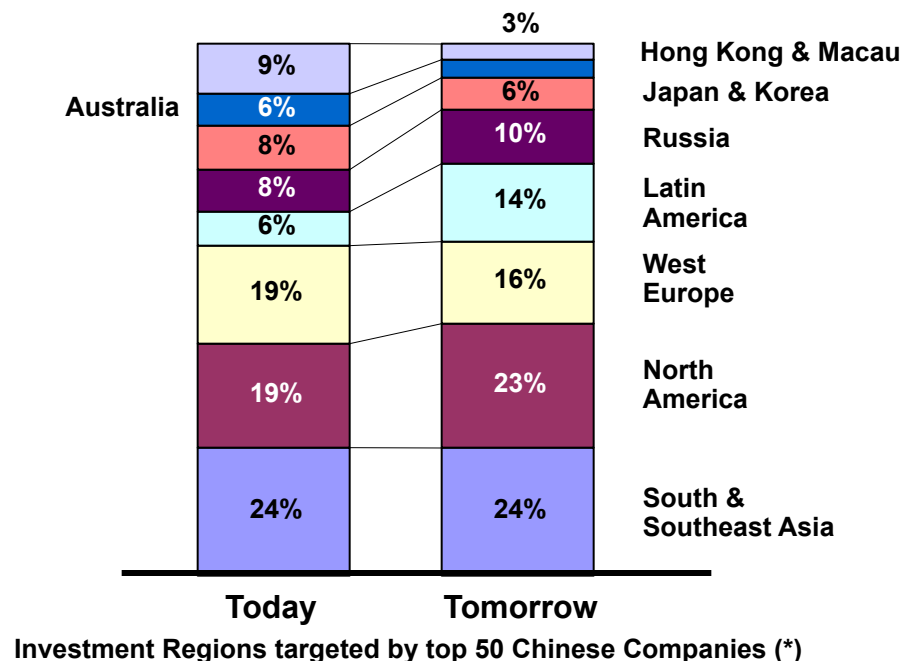
Figure 2: Focus on developing countries and energy

Africa	Latin America	Central Asia	Middle East
<ul style="list-style-type: none"> <li>• China has struck trade deals with 40 African countries and has established a China-Africa Business Council to boost mutual trade and development.<sup>1</sup></li> <li>• China sources nearly a third of its oil from Africa<sup>2</sup> and currently has oil interests in Sudan, Chad, Nigeria, Angola, and Gabon.</li> <li>• Construction, telecoms, timber and fisheries also are common sectors for cooperation.</li> </ul>	<ul style="list-style-type: none"> <li>• China has signed more than 400 trade agreements and projects with Latin American countries<sup>3</sup> and plans to invest US\$100 billion over the next 10 years.<sup>4</sup></li> <li>• While concentrating on natural resources, China also has been investing in manufacturing, textiles, food production and joint satellite projects.</li> <li>• China's major investments have been in Brazil, Mexico, Chile, Argentina, Peru and Venezuela.</li> </ul>	<ul style="list-style-type: none"> <li>• China has trade missions in every Central Asian country and forms part of the Shanghai Cooperation Organisation (SCO), with Russia, Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan.</li> <li>• China has invested in energy projects throughout the region, with large investments in Kazakhstan.</li> <li>• Central Asia has been used to balance China's dependence on Middle Eastern energy sources.</li> </ul>	<ul style="list-style-type: none"> <li>• China signed a "Framework Agreement" with the Gulf Cooperation Council in July 2004 and agreed to negotiate a free trade zone via the China-Gulf Cooperation Council.<sup>12</sup></li> <li>• The Middle East accounts for more than 50 percent of China's oil imports. Saudi Arabia, Iran and Oman are the top three exporters to date.</li> <li>• China is also interested in the potential of the region's oil services. By 2001, nearly 3,000 service contracts worth US\$2.7 billion had been signed.</li> </ul>
<p><b>Noteworthy Deals</b></p> <ul style="list-style-type: none"> <li>• Nigeria - In 2004, PetroChina signed a one-year oil-supply contract worth US\$800 million with the Nigerian National Petroleum Corporation, which will supply 30,000 barrels of oil per day.<sup>5</sup></li> <li>• Angola - In March 2005, China signed nine cooperation agreements with Angola, mainly for the development of Angola's oil and gas sectors. A US\$68 million agreement between Angola's MundoStarTel and China's ZTE Corporation to develop telephone networks in Angola was also signed. Angola is China's second-largest trading partner.<sup>6</sup></li> </ul>	<p><b>Noteworthy Deals</b></p> <ul style="list-style-type: none"> <li>• Venezuela - CNPC, which already operates two Venezuelan oil fields, has agreed to spend more than US\$400 million<sup>7</sup> in developing 15 declining oil fields in eastern Venezuela.</li> <li>• Brazil - Sinopec signed a US\$1 billion agreement with Brazil to build a gas pipeline across the country<sup>8</sup> in September 2004.</li> <li>• Brazil - Sinopec is exploring opportunities for joint operations with CNOOC in China, Brazil and other regions in the world.</li> </ul>	<p><b>Noteworthy Deals</b></p> <ul style="list-style-type: none"> <li>• Kazakhstan - China and Kazakhstan agreed in May 2004 to build a 1,000-kilometre pipeline, worth US\$3.5 billion, from the central Karaganda region to Xinjiang.<sup>9</sup></li> <li>• In August 2005, CNPC agreed to buy Petro-Kazakhstan for US\$4.2 billion.</li> <li>• Uzbekistan - Uzbekistan and China signed an oil deal in May 2005 to set up a joint venture and attract US\$600 million in direct investment to Uzbekistan.<sup>10</sup> CNPC is also expected to invest in 23 oil fields in the country in a 50:50 joint venture.<sup>11</sup></li> </ul>	<p><b>Noteworthy Deals</b></p> <ul style="list-style-type: none"> <li>• Iran - a preliminary agreement was signed in November 2004 for China to buy 10 million tonnes of Liquid Nitrogen Gas per year over the next 25 years<sup>13</sup>, a deal worth at least US\$100 billion.<sup>14</sup></li> <li>• Saudi Arabia - Saudi Arabia signed an agreement on natural gas drilling and production with Sinopec in March 2004. The spending in the first phase of the project was US\$300 million.<sup>15</sup></li> </ul>

**Currently Asia is the top destination of FDI, but bigger companies are heading for developed markets in Europe and N. America.**



**China's FDI Outflows (2004)**



Asia	Hong Kong, Indonesia, Singapore	2006, CNPC – Petro-Kazakhstan (Can.) 4,2 billion USD
L. America	Brazil, Mexico	2004, Baosteel – CVRD (Brazil) 1.5 billion USD – to operate a steel plant in São Luís.
Africa	Sudan, Nigeria, South Africa	2005, CNPC- Sudanese Oil 14.4 billion USD. Sudan provides half of CNPC's overseas oil.
Europe	Russia, UK, Germany	2004, TCL -Thomson Elec. formed the world's largest television manufacturer
N. America	US, Canada	2004, Lenovo- IBM's PC Business 1.75 billion USD
Ocenia	Australia	2003, Huaneng Group- OzGen 227 million USD - %50 share

(\*) Roland Berger survey among 50 top Chinese companies



# Lenovo, Haier, TCL, Huawei, CNOOC, Nanjing, CNPC are no longer unfamiliar names to global business executives outside China.

## Winners of "Most Globally Competitive Chinese Companies" award '2006

### LENOVO – Computer Best in Integration

- Global HQ in NY
- Principal locations in Beijing and Raleigh, NC
- Employs 19,000+ people
- Founded in '84 by 11 Chinese scientists
- '05 annual revenue is 13 billion USD, only after Dell and HP
- **'06 overseas revenue 8.6 billion USD, 65% of total sales**
- Together with Coca-Cola, will be the main sponsor of 2008 Olympic Games
- Lenovo became a household name with its landmark acquisition of IBM's Personal Computing Division in '05

### HUAWEI – Telecom Best in Europe

- Products sold in 100+ countries to 1 billion users
- **'06, overseas revenue of 5.3 billion USD, 65% of total sales revenue** and a 73% growth rate for the past three years.
- 12 R&D facilities; including 2 in USA, others in Sweden, India and Russia.
- Employs global consulting firms for marketing and branding strategies
- Invests strongly in training and lifelong learning.
- Sell products with own brandname
- Key strategies; Think global, act local, Customer-centered, innovation-driven company

### HAIER – Household Best in USA

- Production bases in China, Pakistan, Bangladesh, Indonesia, Philippines, Malaysia, Iran,
- USA production base established in '99 and first refrigerator was produced in '03.
- Owns total of 5.469 patent
- 30,000 outlets around the world
- The US branch is the 4th largest home appliances manufacturer in the world,
- '06 overseas revenue of 3.3 billion USD, 24.7% of total sales revenue and a 4.2% growth rate for the past three years
- '06, Forbes ranked the company as the **3rd largest in the global electronics industry** behind Samsung and Philips.

### ZTE – Wireless Com. Best in Emerging Mar.

- ZTE's India branch works on the design, development, production, distribution and installation of a range of telecommunications systems and equipment, including wireless communications, handsets and software.
- Strong commitment to local human resources policy.
- Strong innovative capacity: As of August '05 applied for around 3000 national or international patents, 90% of which are innovation patents with associated intellectual property rights.

# China's course on going global may be set, but the global business landscape will not be changed overnight.

## M&A is an advantageous but difficult option

Continuous growth without acquisition is almost impossible

But integrating companies is also difficult to execute

2/3 of M&A in any geography fail

Only a small proportion of M&A deals create value

## Size of outbound M&A's by Chinese companies is very small in the global context

China's total overseas acquisition activity is increasing; 3 / 8 / 16 billion USD in '04/'05 and '06 respectfully.

FDI abroad had reached 73.3 billion USD by the end of '06.

Mentioned amounts are a small fraction of the global M&A activities that reached a record of 3.8 trillion USD in '06

## 1/3 of Chinese companies had lost money on foreign investments and 2/3 of JVs had failed. (\*)

Most Chinese companies have limited experiences of int. M&A

"For Chinese companies, one of the more dangerous strategies to pursue is to go global just because of increased competition in your home market or that you are jumping onto a trend. "The best strategy to pursue is to ensure that they first build a strong position in their core business in the home market before going abroad," (\*\*)

Even Lenovo merger has limited cost reductions and synergies after the merger (\*\*\*)

**Although Chinese market is an ideal training ground, companies with international ambitions are aware of their weaknesses and trying to fill the gap before going global.**

### **PREPERATIONS**

- **Increase R&D investment:**
- **Improve marketing and branding abilities**
  - China the world's 3rd largest advertising market '05
  - Lenovo - Coca-Cola, main sponsors of 2008 Olympic Games
- **Overcome internal weaknesses in branding, marketing, sales and R&D primarily through takeovers and joint ventures.**
  - TLC (Schneider, Thomson and RCA )
- **Focus on local adaptation**
  - Haier, develop products in the countries where they sell

### **MORE CHALLENGES on the Internationalization Course**

**CULTURAL  
CHALLENGES**

**HUMAN RESOURCE  
MANAGEMENT  
CHALLENGES**

**EXPERIENCE  
CHALLENGES**

**PERCEPTIONAL  
& POLITICAL  
CHALLENGES**

# Of the failed Chinese JVs, %85 of CEOs attributed their difficulties to differences in managerial styles and corporate culture. (\*)

## CHINESE CULTURAL DIFFERENCES

## IMPLICATION TO HR MANAGEMENT

Respect authority and favor centralized decision-making	<ul style="list-style-type: none"><li>• One sided objective-setting process</li><li>• Limited interaction between managers and their employees</li></ul>
Search for total group consensus before taking actions	<ul style="list-style-type: none"><li>• Agility is an important competency to realize the opportunities</li></ul>
Respect for hierarchy	<ul style="list-style-type: none"><li>• Limits development of individual responsibility and initiatives</li><li>• Managers may micromanage</li></ul>
Favor to act as part of a group	<ul style="list-style-type: none"><li>• Prevents individual creativity, achievement, reward and status</li></ul>
Distinction between “insiders” and “outsiders”.	<ul style="list-style-type: none"><li>• Unwilling to take personal responsibility at work</li><li>• Unwilling to give responsibility to outsiders</li></ul>
“Face” and harmony is a significant aspect of social life	<ul style="list-style-type: none"><li>• Indirect communication style may complicate communication between mainland and overseas facilities</li></ul>
Importance of Guanxi(*) (relationships)	<ul style="list-style-type: none"><li>• Guanxi traditions may seen as unethical business practices.</li></ul>
Reluctancy to communicate bad news	<ul style="list-style-type: none"><li>• Prevents timely decision making</li></ul>
Maintain greater social formality in the workplace	<ul style="list-style-type: none"><li>• May cause communication misleadings</li></ul>

**Chinese authoritarian executive styles are effective within the Chinese culture but don't translate well to the Western workplace,**

(\*) In China, gift giving is a prevalent social custom in strengthening Guanxi and dealing with political authorities, social institutions, and business people

# HR Management styles, experiences and competencies may be limited for western companies.

## IMPROVEMENT AREAS in CHINESE HR MANAGEMENT STYLES

- **Performance management** is relatively new issue for traditional HR management of China
- **Communication and conflict management** styles are not well aligned with western practices
- Even in China, talented professionals prefer to work in foreign companies, Chinese companies still **don't know and not able to attract the talent** to their company
- **Hiring habits** are not yet objective
- **Multinaional team development abilitiy is newly** developing

## Leadership capability is the most acute talent shortage in Chinese mainland companies, (\*\*)

- 203 major public and private companies in 7 Asia Pacific, countries are evaluated. (46 in China's mainland mostly wholly foreign-owned companies)
- Among the top 10 companies, 5 are Indian-owned. None of the companies operating in China's mainland were listed as outstanding firms for their leadership abilities
- Wipro Ltd of India, was named the region's top company for leadership expertise.
- Most top company managers in China's mainland lack know-how in building leadership and many focus on short-term development as they are under pressure to create the fastest returns for shareholders. Of Chinese companies
- %60 mentioned that they lack of a qualified talent pool for leaders internally
- %70 mentioned that on short-term operation is an impediment to leadership development %70
- % 23 mentioned that they lack of know-how and experience in developing leaders.
- Active involvement of CEO is a critical factor in building leadership quality and depth. It should be the chief executives to spot potential leaders within their companies, while in China this job is often carried out by human resource departments. At the top 10 companies listed in the study, all the chief executives were actively involved in developing leadership talent, compared with only %77 for other respondents.

# Experience and familiarity is an important challenge that may require different phases for investment.

- Lack managerial experience, knowledge and experience in dealing with newly enlarged transnational companies
- Insufficient understanding of cultures (as a result of close community)
- Lack the experience of managing global brands
- Mostly unfamiliar to international standards, regulations and systems
- Western styles of corporate governance is not well known, corporate governance framework remains undersdeveloped and most cases conflicts may occur between Western style corporate governance and Guanxi.
- Lack customer focused management

**China is not producing enough well-trained graduates who are suitably qualified to work for global companies. (\*)**

- Study involved interviews with eighty-three human resources professionals who hire local graduates in China.
- It concluded that less than %10 of Chinese university graduates had the skills necessary to work for foreign companies, compared with %25 of university graduates from India.
- Chinese graduates lack practical skills in areas of teamwork, project management, and software development, as well as proficiency in English, which are necessary to be successful in large global businesses.
- The research team attributed these problems to the fact that Chinese universities tend to focus on theoretical and textbook learning instead of emphasizing practical application of knowledge.
- Chinese universities are beginning to invite foreign professors to join their faculties and to improve research centers. (\*\*\*)

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**Chinese Managers lack the experience they need;  
to deal with very different management styles, cultures, prorities and minsets.**

# China's entry into global markets is often seen as a threat in political and business circles.



**The diaspora of Chinese talent – western-educated, and familiar with Chinese culture and values – provides a valuable resource for Chinese companies going global.**

## •Political Issues

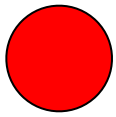
- USA and EU may increase protectionist moves against China's globalization
  - The political pressure that persuaded CNOOC to drop its bid for Unocal
- Resentment against Chinese companies, perceiving them as being government controlled (Lenovo vs. Dell)
- The fear of China taking assets, jobs, business and in this case, access to resources, can sometimes provoke an emotional response
- State influence on corporate planning may lead to goals beyond profit maximization.

## •Perceptual Issues from customer perspective

- Gaining acceptance in new consumer markets will take time
- "Chinese brands suffer from negative perceptions, and perhaps, negative realities (\*)
- Current perception of Chinese brands: cheap, poor value, low quality, produced by communists.
- Chinese companies also have to win over skeptical consumers
  - Much the same way as western firms have had to spend large amounts of time first understanding and then selling to the Chinese.
- Gaining acceptance in new consumer markets

## •Perceptual Issues from employee perspective

- Chinese companies need to take on more social responsibilities in local societies
- Gree Electronics aims to bring the Gree Chinese culture into Brazil, but the workers feel being deprived of human right under Chinese management.



# Will China age before it gets rich, or will it grow rich before it gets old.

**Development = *f***

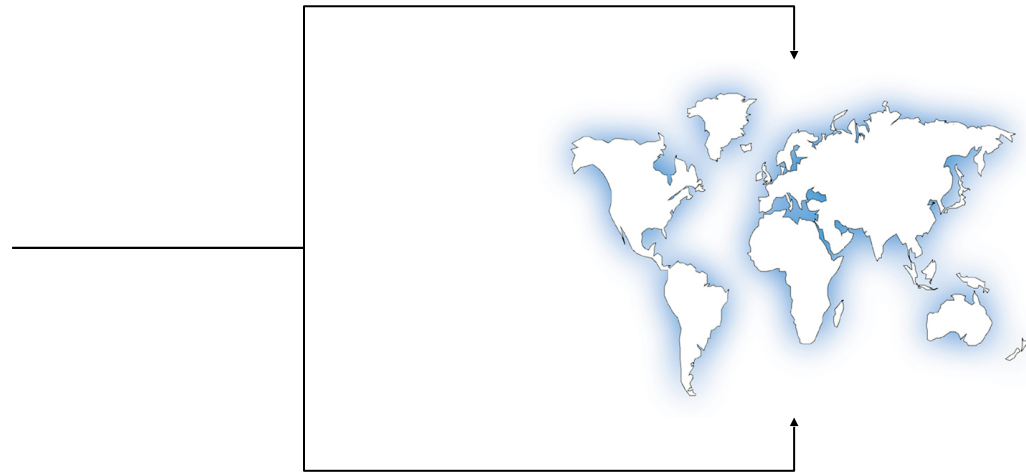
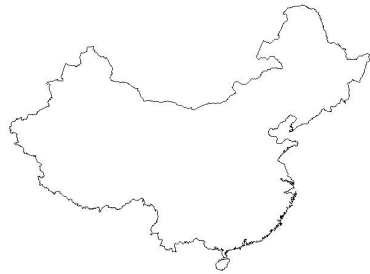
- 1. Investing in Physical Capital**
- 2. Demographics**
- 3. Acquiring & Using Knowledge**

- 102 million residents aged 65+, which is %20 of world's elderly population.
- By 2050, the worker to elderly ratio is expected to drop from 9 workers per elderly to 2,5 workers per elderly.
- Major cause is country's one child policy implemented in 1979 to control population growth.
- China is under the grip of the "4-2-1" problem, a single child has to take care of two parents and four grandparents
- The 4-2-1 problem means that the traditional systems of long-term care of elderly by adult children at home is breaking down.
- This problem is being reinforced by the highly skewed gender ratio in favor of boys, together with the rising female labor force participation.



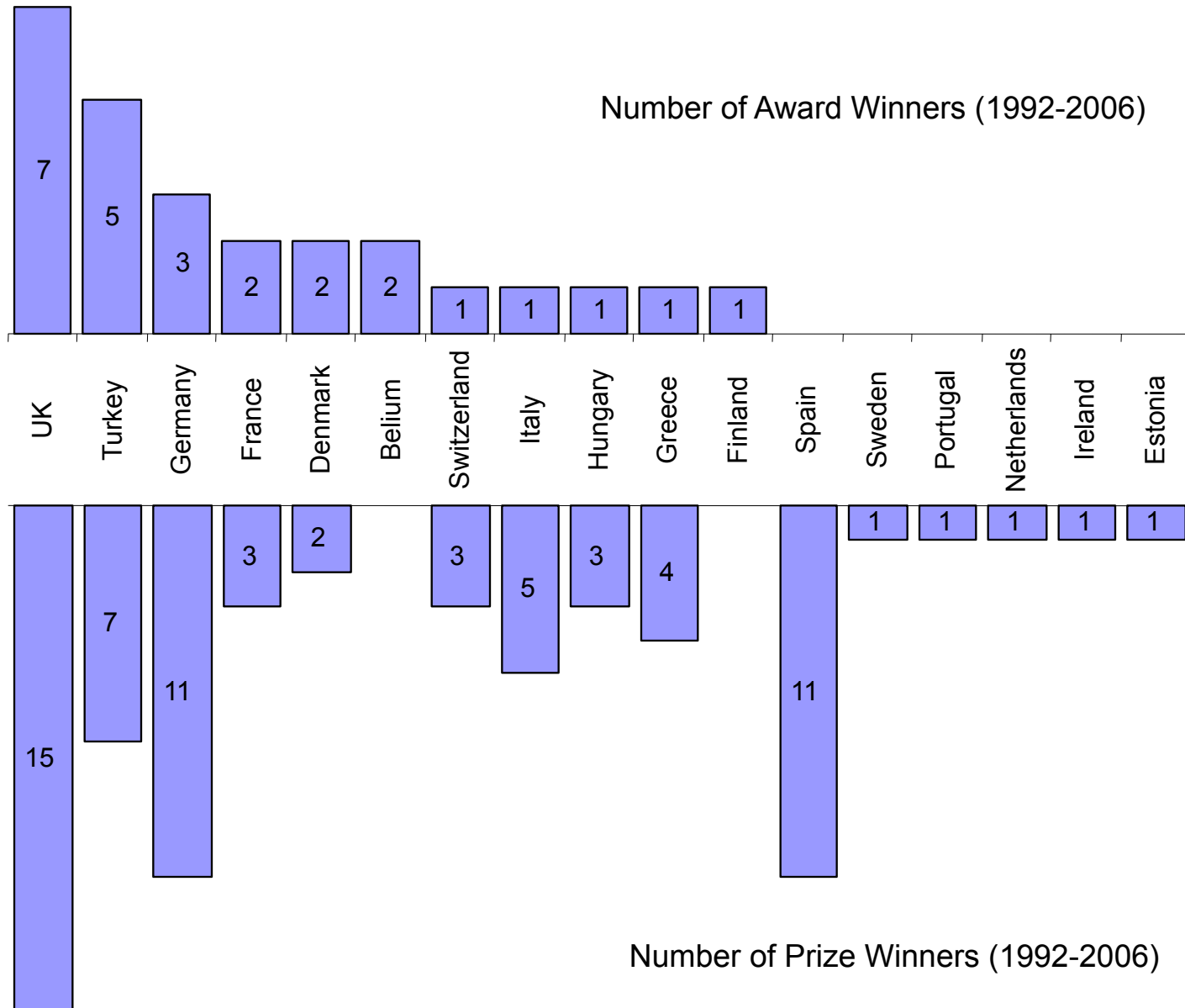
**Chinese companies has two routes to move, first one easier but longer, second one harder but shorter (can be easier with cooperation)**

**Route 1 : First invest in emerging markets, acumulate experience, enter competitive markets.**



**Route 2 : Directly enter competitive markets by getting help on “Experience and Familiarity”, “Perception on Quality” and “Demographics”  
And also improving HR practices by overcoming cultural paradigms.**

# Commitment to quality for European companies is registered with EFQM Quality Awards.



## Composition of the the Board must be aligned with internationalization aims.

### HAIER

- 1.Yang Mian Mian (C)
- 2.Wu Ke Song
- 3.Chai Yong Sen
- 4.Liang Hai Shan
- 5.Cao Chun Hua
- 6.Cui Shao Hua
- 7.Song Chun Guang
- 8.Lam Kin Kau, Mark
- 9.Fung Hoi Wing, Henry
- 10.Lau Ho Wai, Lucas
- 11.Wu Yinong

### ZTE

- 1.Hou Weigui (C)
- 2.Wang Zongyin
- 3.Xie Weiliang
- 4.Zhang Junchao
- 5.Li Juping
- 6.Dong Lianbo
- 7.Yin Yimin
- 8.Shi Lirong
- 9.He Shiyong
- 10.Zhu Wuxiang
- 11.Chen Shaohua
- 12.Qiao Wenjun
- 13.Mi Zhengkun
- 14.Li Jin
- 15.Zhang Taifeng
- 16.Wang Wangxi
- 17.He Xuemei
- 18.Qu Deqian
- 19.Wang Yan

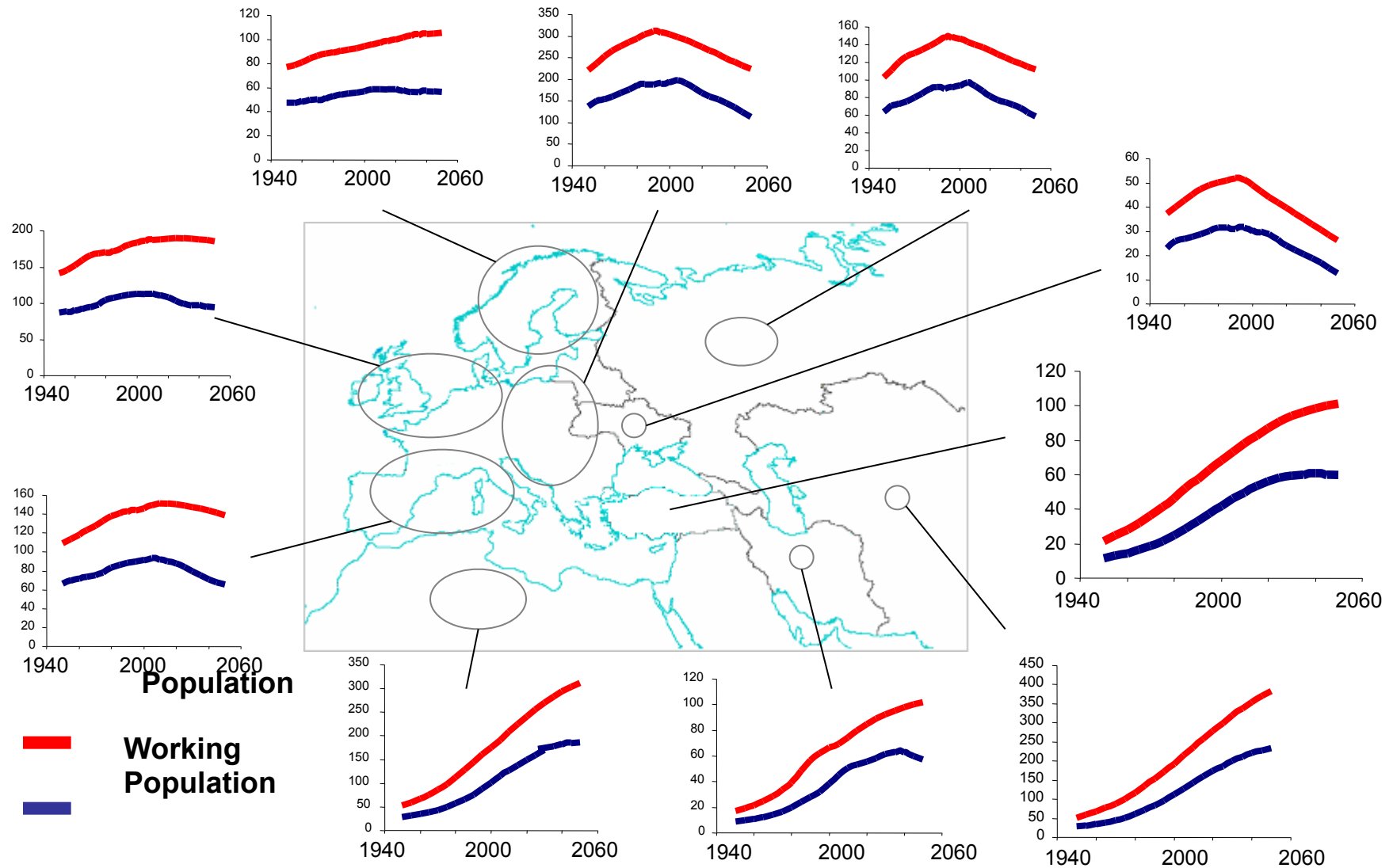
### BAOSTEEL

- 1.Xie Qihua (C)
- 2.Zhao Kun
- 3.Xu Lejiang
- 4.Wang Jinde
- 5.Ouyang Yingpeng
- 6.Ma Guoqiang
- 7.Liu Guosheng
- 8.He Wenbo
- 9.Chen Quanxun
- 10.Ai Baojun

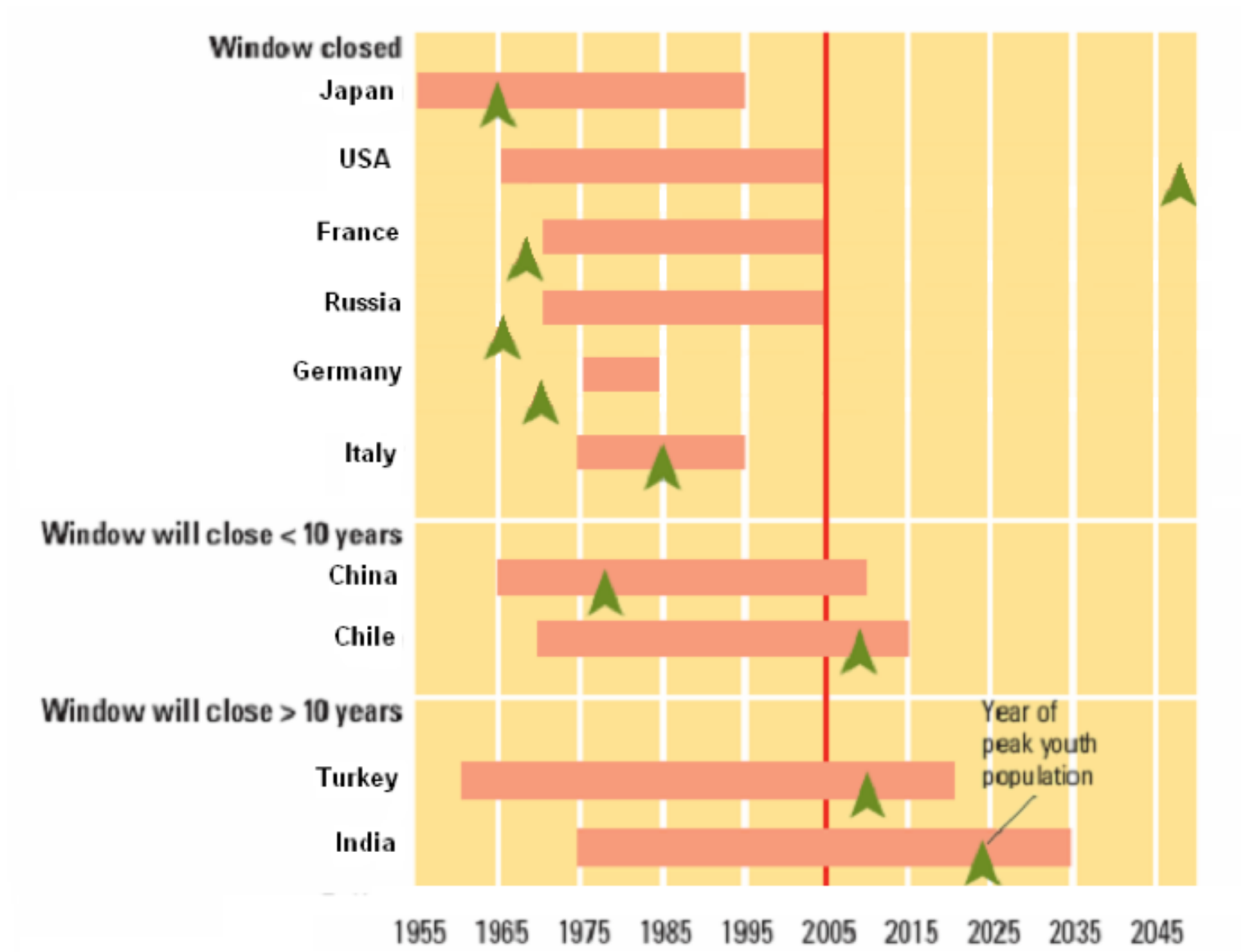
### NESTLE

- 1.Peter Brabeck-Latmathe, Austrian
- 2.Adreas Koopmann, Swiss
- 3.Rolf Hanggi, Swiss
- 4.Edward George, English
- 5.Kaspar Villiger, Swiss
- 6.Jean-Pierre Meyers, French
- 7.Peter Bockli, Swiss
- 8.Andre Kudelski, Swiss
- 9.Daniel Borel, Swiss
- 10.Caroline Müller-Möhl, Swiss
- 11.Jean-Rene Fourtou, French
- 12.Günter Blobel, German
- 13.Steven George Hoch, Swiss
- 14.Niana Lal Kidwai, India

# Current “under 15” population will be a scarce resource for the region.



# Golden Demographic Period is an opportunity for all nations.



# How to prepare for expansion in competitive markets.

## **CULTURAL CHALLENGES**

1. Gain new competencies for overseas expansions
2. More emphasis on HR functions
3. Develop HR Management with European practices
4. More emphasis on performance management
5. Change in communication habits
6. Utilization of more European employees and managers in overseas operations (also rotate)

## **HUMAN RESOURCE MANAGEMENT CHALLENGES**

## **EXPERIENCE CHALLENGES**

1. Support from consulting companies (branding, understanding customers, legislations)
2. Find suitable partners and learn from them

## **PERCEPTIONAL & POLITICAL CHALLENGES**

1. Improve quality image
2. More emphasis on corporate governance

## **DEMOGRAPHIC CHALLENGES**

1. Invest in countries with demographic advantages

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