Horasis
The Global Visions Community

China Europe Business Meeting

15 November 2005, Geneva, Switzerland

a Horasis-leadership event

co-hosts:
Geneva Economic Promotion Office
China Federation of Industrial Economics

Horasis is a global visions community committed to enact visions for a sustainable future
(http:/www.horasis.org)

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Co-chairs:

Fu Chengyu	President, China National Offshore Oil Company, China
Guo Wei	Chief Executive Officer, Digital China, China
Armin Meyer	Chairman, Ciba Speciality Chemicals, Switzerland
Vincent H.S. Lo	Chairman, Shui On Group, Hong Kong SAR
Zhang Yue	Chairman, Broad Air Conditioning, China
Zhao Xizheng	Chairman, China Electricity Council, China

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Geneva Tourism
Office for the Promotion of Industries
UBS

Foreword

The China Europe Business Meeting was the first independent, international meeting of Chinese and European CEOs to conceptualize Chinese companies' rise to global eminence. By most accounts, this first China Europe Business Meeting was a real success. 100 participants from Europe had a chance to exchange views and ideas with about the same number of executives from China, led by the China Federation of Industrial Economics. The meeting provided a platform for potential cooperation between Chinese and European firms. This deliberately small, off-the-record event co-hosted by the State of Geneva was conducted in a highly interactive manner aimed at promoting business opportunities among participants.

Globalisation has become the key word for many Chinese companies with many aspiring to propel themselves from national champions to global winners. Be it computer maker Lenovo's acquisition of IBM's computer business, Nanjing Automotive buying Rover and TCL taking over assets of Thomson and Alcatel, Chinese firms are certainly showing their global ambition. And they are right to do so - with the opening of world markets and the continued globalization of services they might risk to fail if they do not have real global scale, continuing to build their strategies of home advantages.

Powerful forces of change are reshaping the competitive environment for Chinese companies and for many globalization will be a key to success in the new competitive game. But how can Chinese companies best advance globalization, avoid its pitfalls and build a sustainable global organization?

This question was high on the agenda of the China Europe Business Meeting, with a remarkable joining of forces among the business community, led by the six co-chairs, Fu Chengyu, CEO of China National Offshore Oil Company (CNOOC); Guo Wei, CEO of Digital China; Vincent H.S. Lo, Chairman of Shui On Group; Armin Meyer, Chairman and CEO of Ciba Speciality Chemicals; Zhang Yue, Chairman of Broad Air Conditioning; and Zhao Xizheng, Chairman of the China Electricity Council.

As this report shows, a tremendous amount of ideas and concrete proposals emerged from the very interactive, and often provocative discussions. Participants reached consensus that the perspectives for Chinese firms are compelling, but that the process of globalization needs systematic preparation:

- First, building a global company requires a determined campaign; one can advance globalization at the pace one chooses, but trying to skip steps might risk creating an unstable global edifice.

- Second is the idea that there is an over-arching sequence to building a global company – foundations come first, followed by the necessary capabilities to push on higher and further, crowned with the ability to become a socially responsible corporation which proactively interacts with the various global stakeholders.

- The third message is that climbing each step is an active process that involves institutional learning; the learning loop involved in taking each step will help companies to consolidate their position and to prepare them for the next ascent. Each step represents a major leap that shall be consolidated before moving on. For those Chinese firms with the right visions of globalization and the related implementation skills the future will be great.

Overall, the success of the China Europe Business Meeting will be determined by the months to come, as firms pursue the tasks that they have laid out. As one participant remarked, 'Chinese firms hold the seeds of economic dynamism in their hands already.' The challenge is now to convert this optimism into long-term sustainable growth.

The next China Europe Business Meeting will be held in Geneva, 25 September 2006, and is already taking shape around the theme of Chinese companies' steps towards 'sustainable globalization'. I look forward to welcoming you next year to an even more fruitful China Europe Business Meeting.

Dr. Frank-Jürgen Richter
President
Horasis: The Global Visions Community

Key Takeaways

By Werner Kreuz, Vice President, A.T. Kearney

The China Europe Business Meeting, held in Geneva, Switzerland, on November 15, 2005, significantly contributed to a better understanding for both the Chinese delegation, who got a clearer view about Europe's excitement and fears when investing in China, and the European top-managers, who got a lot of new insights into the fastest growing market in the world.

In the two plenary sessions "Rethinking Scenarios for China's Future – Assessing Europe's Strategic Options" and "China's Role in Global Trade", the discussion focused among other things on

- the incredible growth of the Chinese economy with an average GDP of about 10 % resulting in incredible business opportunities in China

- the continuously increasing flow of foreign investments into China (it is estimated that over the next 10 years more than $ 1.000 million will be invested in China by foreign investors) and the confidence these investors have that their investments will be successful (in 2004, China for the first time ever climbed to the # 1 spot in the confidence index and regained this position in 2005)

- the broad range of problems foreign investors experience when dealing with "China" including the availability of (trained and educated) resources, of energy and of an appropriate infrastructure

- the – still unclear – way how to protect Intellectual Capital and how to ensure that Intellectual Property Rights are enforced

- the often observed misunderstandings caused by lack of communication and by different cultural backgrounds

- the significant increase in global trade activities. In the last three years, we have already experienced some of the consequences of the exploding demand in China (e.g. for raw materials such as iron ore and alloys) when suddenly transportation costs skyrocketed by more than 250 % due to a shortage in shipping capacity

In addition, the audience agreed that the investment flow is not following a "one-way street". Chinese companies will invest more and more in Europe and the United States to get access to both latest technologies and to large, mature and high-priced Western markets.

This will have – for instance – severe impacts on the global allocation of production capacities and its related trade flows. New world-class and world-scale production facilities (based on latest technologies) will be built in China to fulfill the growing demand in China. However, there will be enough new capacity in China, so that finished goods – with an increasing share of high-end products – will be exported to Europe and the US. This will lead to three questions:

- Will (selected) European/US-based industries rapidly decline and relocate to China – and if yes, how fast?
- Will China continue to offer attractive factor cost advantages and develop new local (and future global) competitors?
- As a consequence, will we have to redesign entire industries?

In a series of roundtables the dynamics of Sino-Euro cooperation were highlighted for selected industries such as Energy, Information Technology, Consumer Goods, Capital Goods and Financial Institutions. In more detail, the participants were looking for answers to the following key questions:

- Which industries will outperform?
- What models of cooperation will generate future growth?
- How can barriers in cooperation be overcome?

China, which is already the second largest energy user, has recently experienced significant problems in providing Energy in a reliable way which is of immense importance especially for those industries whose production processes cannot be interrupted (such as all process industries incl. Chemicals, Pharmaceuticals or Steel). To overcome this problem, China is aggressively looking for improving the situation in the most flexible way incl. building nuclear power plants and importing energy from neighbouring countries. Gross investments will be one of the key success factors for Information Technology companies to bring China on a level similar to India. In addition, IT can play a major role in providing support in protecting Intellectual Capital.

For Consumer Goods the outlook given was "optimistic". Branding is critical to compete in the global market place and CEOs in China should set the standard of "living the brand". With the expected increase in consumer purchasing power over the next years, European/US consumer goods companies will have to serve a huge new market and will have to decide whether they can serve this market from their existing production facilities or will – more likely – have to build new plants in China.

Especially the Automotive sector within Capital Goods will "boom" over the next years. All major players will build production facilities in China to get both "their share" of the fast growing Chinese market and the opportunity to benefit from the low personnel cost in China by exporting parts, systems or entire cars from China to the Western world. It is expected that – at least – first and second tier suppliers will follow the car manufacturers to China.

Financial Institutions are going to China, too. They will face, however, the risk that an estimated 50 % plus of all credits will not be paid back and that several Chinese banks are in constant danger of being forced to file for bankruptcy. It was agreed that the capital market restructuring can and will go much faster than most people expect – the same is true for the floating of the RMB.

In a second series of parallel roundtables the focus was on "Internationalization of Chinese Firms". Questions that were discussed included:

- How does the Chinese firms' global future look like?
- What can they learn from their European peers?
- How can we create win-win situations with European partners?

Major challenges that were identified by the participants focused on Human Resources aspects and more specific on how to overcome the shortage of highly talented and well-educated professionals. One solution – at least medium-term – might be, to train not only Chinese students, but Chinese professors in the Western world. Especially the young Chinese people are "hungry" for education and many from the younger generation live in "two daily shifts" – one shift to earn money and a second shift to study foreign languages, economy or management.

A third series of parallel roundtables was looking for recipes for success in "Managing the Intangibles of Global Business". The audience agreed that the approach to Corporate Citizenship will be "Multiple Capitalism" with expanding diversity. To become "accepted" in the most innovative future world, China needs to drive into R&D and into High-Tech if it wants to have a successful Interaction with the World. And finally, adherence to "good" Corporate Governance is as desirable as adherence to high safety standards.

In summary: Armin Meyer, Chairman of Ciba Specialty Chemicals, said during the meeting "We can only win together". And let me add the following advice for both European and Chinese managers: "If you think doing business in China (or in Europe, if you are from China) is expensive … try ignorance!"

Selected Session Summaries

Energy

By Goran Mijuk, Dow Jones Newswire

Fu Chengyu, CEO, CNOOC, welcoming participants

China is seeking cleaner and more efficient forms of energy as soaring oil and coal consumption poses an increasing threat to the environment and surging prices threaten to undermine economic growth. The world's second-largest oil consumer behind the U.S. is increasingly turning to European and U.S. companies to tap renewable sources of energy such as wind and solar power, and considering incentives for foreign investment. But natural gas and nuclear energy is likely to dominate the market for clean energy sources in China in the years to come because the alternatives are still too costly, the China Europe Business Meeting in Geneva heard.

Frank-Jürgen Richter, President, Horasis, Switzerland and Carlo Lamprecht, Minister of Economy, State of Geneva, Switzerland, opening the meeting.

Fu Chengyu, chairman and chief executive of China National Offshore Oil Company, or CNOOC, told a panel at the summit that economic incentives such as low-interest loans and clear regulation would be needed to attract foreign investors and technological know-how to reduce China's dependence on oil and coal.

"China can't afford its current energy mix in the long term…we need to promote wind and solar energy and for this we need technological partners from Europe," Fu said during a panel discussion at the China Europe Business Meeting, sponsored by Swiss-based Horasis. "We also need to increase our natural gas imports in the years to come." He added that CNOOC would increasingly widen its focus on oil to include other energy forms. Earlier this year the company failed in its attempt to take over U.S. competitor Unocal, faced with U.S. political resistance.

Fu said China's energy sector holds vast opportunities for European companies and there have been numerous examples of successful joint ventures in the oil industry, although he conceded that opaque government regulations are still discouraging some potential investors.

"Europeans like to stress the risk factors, but there are many mind-boggling opportunities in mainland China and in fact, no one can ignore them," said Vincent Lo, Chairman of Shui On Group. Lo, a property tycoon in Hong Kong, pointed to the company's joint venture with French cement maker Lafarge SA, saying such agreements are still a good way of tapping China's lucrative markets, especially those of western and northeastern China.

Networking

"For example, the cement market is extremely divided and is crying out for consolidation," Lo said, adding it is better to join forces than miss out on such opportunities - even though European companies can't fully control their

partners in China. Though calls for the privatization of government-owned Chinese companies have increased recently, joint ventures are likely to remain key to relationships between Chinese and foreign companies in the energy sector.

"Privatizations aren't on the agenda, because the energy sector is too much of a strategic asset for the state," said Nick Butler, general vice president of Strategy and Policy Development at BP. BP, which has around $4 billion in capital employed in China, is focused on ensuring that China's vast energy demands are met, and on the import and sales of oil and gas.

Butler said he expects China's energy consumption to come close to the U.S. in about 10 years' time, adding that efforts to curb pollution are on the rise. "There is much more interest in clean energy and a great focus on our technologies," Butler said. Though wind and solar energy technologies are increasingly attractive to China, also high on the agenda are improvements to coal refining facilities and increased use of nuclear energy, industry participants said at the summit.

As old nuclear power plants are decommissioned in Europe, China plans to invest in its own nuclear technology and is in the process of adding two new plants to its nine operating sites, panelists said. "Though wind and solar are being discussed, I think that these technologies are still 10 to 15 years away", said Dave Roberts, executive vice president of U.K.-based BG Group. The company has its eye on China but isn't active there yet. In the meantime, Roberts said, the use of natural gas will thrive, and distribution will be key to helping China keep costs low and calm energy consumption - currently at 7 million barrels of oil a day.

Discussion during a workshop

Financial Services

By Bruce VonCannon, Executive Director, UBS

Financial experts debated the opportunities of China's evolving financial sector at the Europe China Business Meeting held in Geneva on November 14-15. Moderator Bruce VonCannon, Executive Director of UBS AG Wealth Management, initiated comments for a panel that included Miquel Frasquilho, Member of Parliament of the Government of Portugal and Head of the research think-tank Grupo Banco Espirito Santo; Peter Burger, Regional Board Member, Commerzbank, Heinz Dollberg, Executive Vice President of Allianz Group of Germany; Marc Van Weede, Senior Vice President of Aegon Insurance Group of the Netherlands; and Zhang Yue, Chairman of Broad Air Conditioning Group of Changsha, China.

Bruce VonCannon opened the roundtable discussions with comment that traced the modern history of banking in China since the founding of the modern republic in 1911. He highlighted the government policy changes in the past 20 years that has shifted the economy from a "command style" economy to a "market driven" economy. "Among the most notable shifts in the past 10 years," he noted, "has been the lessening reliance on the top four state owned commercial banks Bank of China, Agricultural Bank of China, China Construction Bank, and International Bank of China." Recent figures show at least two-thirds of bank borrowings are still coming from these four banks, at least 50% of new borrowings in the past year have come from new privately held or joint venture banks. VonCannon noted, "The PRC government is on the right path in their reforms. Competition in the banking sector can only mean better service and better pricing to bank clients in China." VonCannon also highlighted the recent formation of the China Banking Regulatory Commission (CBRC) in 2003 which will now serve as bank regulator, replacing the Peoples Bank of China which will hereafter focus mainly on monetary stability and currency issues. He noted that the role of the CBRC will create a better culture of risk management in the banking sector.

Dr. Frasquilho offered the view that in many developing economies including China "we have seen historically time and time again that over involvement in the financial sector by governments has led to miss-allocation of resources and created economies too dependent on bank lending." Such over-involvement, he noted, "creates higher risk of more non-performing loans (NPL) not fewer," he noted.. Dr. Frasquilho also offered some suggestions for policy review in China that would address such issues as how can the local stock market to show greater transparency and greater appeal in the foreign investment community, how can a strong culture of risk management be developed in the banking sector, and how can lending practices be improved to bring about a win-win solution for both the banks and for clients in the private sector. " Failure to act in these areas," Dr. Frasquilho noted,

“ultimately results in a cost to the average citizen in any country in the form of unprofitable banks who must be rescued using taxpayer's money.”

Chairman Zhang Yue of Broad Air Conditioning Group noted to the panel and other roundtable participants that years ago “many private sector business managers avoided borrowing from the local banks in China because they did not offer attractive terms for their financial services.” He highlighted to the roundtable participants that “the WTO reforms which will result in opening up the China market to all banks, local and foreign, by the year 2007 will mean better banking services not only for large companies, but also for small companies and the average Chinese consumer as well.”

Heinz Dollberg of Alliance provided an update on the insurance industry and noted that since full opening of the insurance market in 2004, many positive developments had taken place. He emphasized that, “prior to 2004, the insurance sector had been one of the most highly regulated and restricted industries in China and the domain of only three big state owned insurance groups.” However, new competition in the market is taking effect and there are signs of improving services for Chinese citizens. Mr. Dollberg cautioned that “foreign insurance companies and joint ventures are still having some limitations on how quickly and where they can open offices in China” and hoped that the growing de-regulation in the industry would soon create more efficiency in approvals being granted. He gave an optimistic long term view of the chances for a successful venture in China in insurance services.

Marc Van Weede offered analysis on some of the examples of joint ventures that he had studied in China in both the insurance sector as well as in other industries as well. He highlighted the importance of joint venture partners setting mutually attainable goals and time horizons for achieving these joint goals. He said, “The old Chinese proverb, ‘one bed, two dreams’ can be avoided if joint venture partners set realistic goals and also set a vision and plan for ending a partnership if it is mutually the best plan of action after a certain period of cooperation. He also underlined the importance of putting together good management teams in joint ventures and seeking managers who have both the experience and the bi-cultural soft skills to make decisions and manage the growing number of company staff in China that increasing have culture diversity in their workforce. “Good examples abound in China in joint ventures,"noted Mr. Van Weede, "and we should learn from them.” He ended his remarks by noting that progress finally seems to be underway to alleviate the sensitive issues in the insurance sector that affect licensing agreements, limitations on foreign shareholdings, and myriad shareholding structures.

Session on energy.

Peter Burger of Commerzbank gave a brief overview of the financial markets and capital markets in China and cited his desire to see more local banks in China become well capitalized. He cited latest figures on Capital Adequacy Ratios (CAR) in China and noted that the market would be expecting that they would be brought up to levels in banks in other neighboring countries in Asia. He also noted the market was overdue for more retail products coming from banks in China. At present he noted, "large banks earn the majority of their income from bank loans. We will see one day in the not too distant future when the structure of profit streams from banks comes also from fee based services and structured products." He added, "this will mean fairer borrowing rates for businesses and consumers." Mr. Burger also cautioned that local and foreign analysts should be reasonable in their expectations as to the time horizon that China should have for setting changes in the future. He surmised a 5-10 year time horizon seems most plausible for setting in place many of the reforms that affect short term capital flows and the stability of the Chinese Yuan. "We must remember that de-regulation can also cause severe shocks. China can learn from the Australian and Japanese examples," he added, "as government financial officials in these two countries failed miserably a few years ago in implementing liberalization reforms too fast and caused severe asset inflation in their respective countries." Burger was optimistic about China and expected the new leadership to be aware of some of these potential risks.

Consumer Goods

By Jere Sullivan, Vice Chairman, Edelman

In the China Europe Business Meeting's panel discussion on the consumer goods issue, we were fortunate to secure the input from various professional communities including academia in the form of Sir Paul Judge, who runs the prestigious Wharton Business School program in the UK, the investment community through Mr. Phillip Comberg, managing partner for Alcosa Capital and from the Chinese business community, Mr. Zhang Guangming, who is Vice President of the Tasly Group, a manufacturer and marketer of traditional Chinese medicines. In addition, the panelists were joined by a diverse and multi-national group of participants which provided for interesting debate and dialogue on consumer products.

In order to fully appreciate the idea of producing, exporting and marketing consumer goods, one needs to first take a look at China's rich tradition in this area. In many ways they were the founders of modern day marketing centuries ago, through their export of brand commodities ranging from tea to silk to lacquer. While it is true that China had a relatively long hiatus from the west because of a closed political society, that has changed in the last decade with the explosion of Chinese exports – and imports for that matter – to and from the west. And that imitative has been jump started in the last five years through the government's "move out" strategy to expand their footprint overseas.

However, with opportunities come challenges and the issues of intellectual property, counterfeiting and copyright protection are on the front burner of many of China's trading partners. Dealing with such issues will require a delicate balancing act on the part of the Chinese companies that in many ways will need to serve as intermediaries between the Chinese government and its customers.

But a larger less tangible issue that was discussed in the group was the need for China to build its own global brands. While it is true that there are now major Chinese companies operating across various sectors and that they are indeed recognizable to consumers and business leaders in-country. They are veritably unknown beyond the Chinese shores.

The international growth strategy of many major Chinese companies has been to simply purchase well-known western brands. The results of this approach have been mixed. TCL Communication's acquisition of Alcatel's handset and telecom equipment assets was viewed by many industry experts as a win-win. Alcatel was able to divest a major loss-making operation from its books, and TCL was given instant access to distribution channels in coveted US and European markets. On the other hand, CNOOC's failed bid for Unocal was a lesson in "Politics 101" provided by Chevron-Texaco. CNOOC learned that simply offering the most competitive price for an asset was not enough.

There was a fair amount of politics that were played in this deal and a general mood of fear was created by some who suggested the U.S. would be held hostage to an energy thirsty China. Simply put, CNOOC was out maneuvered on the political and communications fronts.

The question remains, can China build its own brands? South Korean businesses like Samsung and their Japanese counterparts in Japan, Sony, have been able to do so. But the creation of these multi-national brands did not happen over night. Brand building is an evolutionary process and one that will need to be measured in China over the next 10-15 years not the next 18 months.

The discussion of branding of consumer goods remains somewhat foreign to China, and came to light in the group discussions. The hypothetical question posed by one Chinese businessman participating in the discussion was, "Rather than invest in building my brand, shouldn't I spend that same capital on improving my position as a major subcontractor to Sears?" The question was answered quite simply by the panel – that strategy is perfect if you want to remain a subcontractor to Sears, but if you want to become the next Sears in China, you need to invest in your brand.

Of course tied to the subject of investing in brand building is the operative term – investing. To invest, you need capital. And to obtain capital you need to convince foreign investors of your economic viability. This presents a chicken and egg quandary to Chinese businesses. Do I build my brand in order to secure capital? Or, do I secure capital to build my brand?

Obviously, there are no simple solutions to these questions. But what was made clear from participants and panelists, was China will remain attractive to the west for a number of reasons. Liberalization has allowed a middle class to emerge and it is a middle class willing to spend money. Chinese are great merchants, but they are equally great consumers. And with more expendable income in the burgeoning middle class, China presents opportunities for Western and Chinese brands alike.

In addition, geographically the targets for selling consumer goods are no longer restricted to the coastal region of China. With major cities popping up throughout the country, a marketer can no longer focus on the perimeter. Also, the land mass of China and its diverse population present challenges as well. A "one size fits all" approach will not fly. Investors and multi-nationals looking to set up shop in China need to do their homework. They need to comprehend the needs of the respective consumers as well as the government regulations of the sectors in which they are operating.

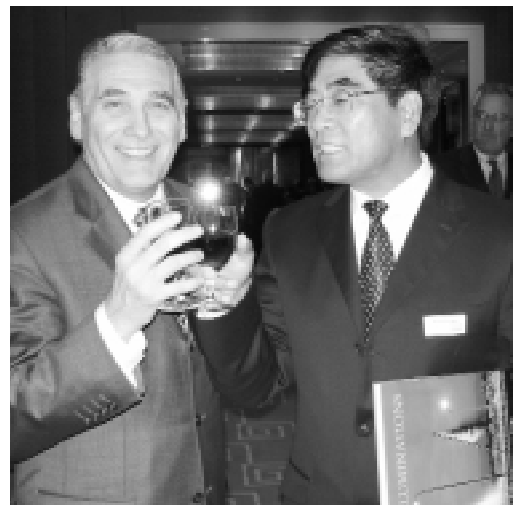
In conclusion, China is, and will remain, the market for both selling and buying consumer goods. But the building of brands by Chinese companies is paramount in order for them to compete to their maximum potential in the global market.

Information Technology

By Frank Blithe, Managing Director, Comparative Advantage

As the recent sales of IBM's PC business to Lenovo demonstrates, China is gradually becoming a player in the IT industry. At the China Europe Business Meeting, moderated by Yat Siu, CEO of Outblaze, experts from Asia, Europe, and North America—Philippe Doubre, Secretary General of World Trade Center Geneva, Frank Blithe, Managing Director of Comparative Advantage, Cyrill Eltschinger, CEO of IT United, Travis Kalanick, CEO of Redswoosh, and Guo Wei, CEO of Digital China—discussed the current status and future prospects of China in this industry.

Mr. Doubre believes that China has tremendous potential to become a driving force of the next IT revolution. Now, the attractive cost postion in labor is driving the production of IT equipments. As the whole economy grows and more Chinese companies become mature, there will be more and more demand for IT solutions. These factors will propel the Chinese to flourish in both hardware and software sectors.



Minister Carlo Lamprecht and Fu Chengyu

Coming from the outsourcing business, Mr. Eltschinger is bullish about China's recent developments. He foresees a rapid migration of IT offshoring from the West, especially Europe, to China. The present leader, India, will migrate to high-end services such as consulting, while the basic functions in the data center will go to China. Mr. Eltschinger also thinks that the large number of multinational production and sales organizations in China will provide the impetus and the tangible market for the rise and sophistication of Chinese IT providers.

As a founder of his own company, Mr. Kalanick appreciates the ever increasing entrepreneurism among the Chinese. While US is still leads the way in IT advancement, the number of Chinese graduates in the field is growing. Many of these graduates are being trained in Western firms, and many of them will one day be the founder of their own start-ups.

Mr. Guo is one such example. As the CEO of a major Chinese IT enterprise, he understands both the promise as well as the challenges. Most of Chinese IT companies are still focused on domestic demand. In some areas, the lack of uniform standards is a real hinderance to rapid progress. While intellectual property may still be a concern to many Western firms that want to invest in China, Mr. Guo cites the growing awareness among the Chinese leaders and the gathering of momentum to make concrete changes.

Since one of his portfolio companies is leveraging China to optimize its operations, Mr. Blithe can share his experience regarding the current Chinese capabilities. Mr. Blithe is highly confident in the hardware competencies of Chinese firms. Given the extensive activities in manufacturing of diverse products, including IT hardware, there is a tremendous level of skill among manifold Chinese companies to supply not just mass production but also product development to Western enterprises. On the software side, though, China still requires some time to gain sufficient experience, in order to produce internationally competitive solutions on a consistent basis.

The entire panel expresses optimism in China's trajectory. There are still a number of issues, like IP protection, universal standards, process rigor, and software experience, which must be resolved. Still, it is safe to say that the incipience of China's transformation from the factory of the world to a global technology wellspring has already passed; the evolution will increasingly accelerate.

Guo Wei, CEO, Digital China, in discussion

Mergers & Acquisitions

By Thomas Gilles, Partner, Baker & McKenzie

Since China's membership to the World Trade Organization in December 2001, China's importance to the global economy has grown rapidly. China is no longer just a destination for European corporations to invest in. China also grew Asia's new multinationals, which have the financial power to become a serious player in cross border M&A transactions. Following this development more and more Chinese corporations - mainly in branches of steel, electric products, automotive and textile - are starting to think seriously about investing in European corporate assets. The preferred way of starting business to Europe is through mergers and acquisitions, cooperative ventures and strategic alliances.

During the China Europe Business Meeting's workshop on Mergers & Acquisitions, the penalists Clare Cowan, CEO Cahill International Inc., Canada, Zhang Min, Chairman, Beiheng Copper, China, Frank Günther, Managing Partner, Günther & Partner, Germany, Winston Mok, Managing Partner and CEO, Invenite Capital, Singapore and Stanley Jia, Partner, Baker & McKenzie, China and focused on the reasons for the internationalizations of Chinese firms and the obstacles and pitfalls of the process of internationalization.

Clare Cowan stressed the cultural differences between Chinese and European or Northern American players in the M&A arena. While the conclusion of a written M&A agreement is from the point of view of European and North American parties the completion of a negotiation process, this point in time is, from the Chinese perspective, in many ways rather the commencement of a new dynamic of negotiations. Therefore, the management of expectations of the contractual parties and the bridging the cultural differences in the context of the negotiation process is one of the key success factors in a negotiation scenario involving European or North American and Chinese parties.

Frank Günther made the point that Chinese firms tend to overpay companies, which they acquire in Europe. The reason for this tendency are that Chinese firms sometimes tend to be inexperienced with respect to the methodologies of valuating companies in a European context and that international acquisitions by Chinese firms are oftentimes financed by way of subsidized loans from Chinese banks. This analysis was confirmed by Winston Mok from an Asian perspective.

Winston Mok analyzed the probability of success of various internationalization strategies and concluded that very many of the successful projects of internationalizing firms were driven by internal organic growth. Within the group of companies which implemented an internationalization strategy on the basis of acquisitions, the growth scenarios which are based on the strategy to acquire new technologies are more likely to be successful than strategies which are merely based on the acquisition of a customer base.

According to Stanley Jia, the internationalization of Chinese firms is largely driven by the goals to develop new markets, get access to new technologies, to establish or acquire valuable brand names and to protect the long-term energy supply needs of China. As this process of internationalization evolves, the existing complexities of the political and economic system are going to be challenged. The main obstacles in the context of this process seem to be the political clashes of interests and the differences in the legal systems between China and Europe.

On the basis of the discussion of the above thesis and analyses, the panel concluded:

- Besides these promising opportunities of the internationalization of Chinese firms, there are various pitfalls, which have been experienced before by Western corporations entering the Chinese market, i.e.: missing information about the roles of government bodies and the target market and incorrect assessments of political and/or economic circumstances in the local marketplace, underestimation of local corporate law issues, licensing requirements, regulative issues (e.g. regarding environment and industrial relations), Different cultural backgrounds.

- In order to make the most of the opportunities available in the European marketplace, Chinese corporations need to better understand how that marketplace works and how the legal framework determines economic operations in Europe.

- Those Chinese companies thinking about doing business internationally can learn from the experiences of firms that have already become global champions. The TV manufacturer TLC, for example, took over the brands Schneider, Thomson and RCA in order to sell its TV sets in Europe and American under these brand names. Lenovo has taken over the PC business from IBM, thus creating the third-largest PC firm. Haier is the world's fourth largest producer of household appliances and the market leader in the US in small refrigerators and wine refrigerators. Huawai has a successful international profile as a network equipment manufacturer.

- Chinese corporations are oftentimes interested in financially distressed companies (e.g.: Shenyang Machine Tools bought Schiess AG from bankruptcy in 2004; Zhong Qiang Tools acquired Lutz Maschinen & Gerätebau from the insolvency in 2004; SGSB Shang Gong took over Dürkopp Adler in 2005 – a listed German company at the Stock Exchange - which was threatened by insolvency). While such distressed assets may sometimes be interesting in terms of purchase price and market access, Chinese players oftentimes seem to underestimate the operational and legal difficulties involved in the acquisition of distressed assets.

Financing Chinese firms' Overseas Expansion

By Max Burger-Calderon, Managing Director, APAX

During the last few years the Chinese Government has been encouraging Chinese state-owned enterprises and privately owned companies to venture abroad in order to secure international markets for Chinese brands, develop ties with global companies, secure key resource supplies such as oil and improve Management Know How through international tie-ups.

On the back of that a number of Chinese companies have successfully and unsuccessfully tried to acquire companies in Europe and the US. While doing this these acquirers were faced with issues they had not necessarily dealt before like

- how to finance these potential acquisitions
- what sort of advisors to sign up for the process
- take in a local partner or not when acquiring foreign companies
- how to integrate and manage the new subsidiary after the acquisition and many more

During the China Europe Business Meeting's workshop on 'Financing Chinese firms' Overseas Expansion' the panellists Fu Chengyu, President, China National Offshore Oil Company (CNOOC), China, Michael Kershaw, Global Head, China International Business Development, HSBC Group, United Kingdom and Li Lu, Founding General Partner, Himalaya Capital, USA and Max Burger-Calderon, Managing Director, APAX, Hong Kong SAR focused on the financing question when going abroad and the development of the Chinese Capital markets in general.

Having the chairman of one of the most acquisitive Chinese companies on our panel we started discussing CNOOC's foreign acquisition policies and also trying to compare them with what Lenovo had done when buying the IBM PC division.

Opening panel

Carlo Lamprecht, Xing Jun, Chairman, Shenyang Hope Industry

CNOOC is a very cash rich company and can finance its potential acquisitions through debt instruments and does not necessarily have to access equity markets while Lenovo was in need of additional equity when doing the IBM PC acquisition. But the panel was under the impression that Lenovo also took in third party private equity (TPG/Newbridge and General Atlantic) in order to have a partner with M&A expertise on board in order to guide them (Lenovo) around many of the pitfalls of such a transaction.

The panel came to the conclusion that apart from financing requirements it is actually good advice for all Chinese companies when going abroad to carefully study how successful companies such as Lenovo and CNOOC are handling their financing and study in particular detail to what degree bringing in a private equity partner can help avoid making mistakes in such transactions.

The panel then went on discussing the liquidity and accessibility of Chinese capital markets. We discussed the present inefficient allocation of capital in the Chinese economy due to not developed capital markets and the likelihood that this might change in the near future. The panel concluded that in a first step the RBM full floating has to be in effect before a serious capital market can develop. But the panel also concluded that the free float of the RBM could happen much faster than most people expect and on the back of that Chinese capital markets would then be restructured and debt and equity markets starting to grow very rapidly. Once we see this happening then a much more efficient allocation of capital will follow which will trigger a new growth phase of the Chinese economy.

Building Chinese Brands

By Stefan Fillip, Senior Partner, Lippincott Mercer

*Stefan Fillip,
Senior Partner, Lippincott Mercer,
Hong Kong SAR, makes a point
about building brands in China*

Chinese firms going global know that building strong brands is critical to their success. But a roundtable on 'building Chinese brands' at the first China Europe Business Meeting in Geneva revealed substantial barriers to building brands at the pace that Chinese firms plan to need them: barriers that could prove a serious obstacle to the successful globalization of Chinese firms if not resolved.

As set out by Stefan Fillip, Hong Kong-based senior partner at brand consulting firm Lippincott Mercer, Chinese firms have been building global brands in three ways: using their existing Chinese brands, like electronics giant Huawei; adopting a new name for international markets, as Legend Computers did with the name Lenovo; and acquiring foreign companies that have established brands, as Lenovo subsequently did with IBM's ThinkPad or Nanjing Automobile did with MG Rover.

*Xiang Bing,
Dean, Cheung Kong Graduate
School of Business, China,
discussing the nature of Chinese
brands*

The case for using existing Chinese brands was made by Xing Jun, chairman of Shenyang Hope Industry. "Giving foreign names is not correct. Brand names should be vitally connected to the local culture." This view was endorsed by Thomas Boegli, Director of UBS in Switzerland, who cited Toyota as a strong example of building a local brand whose growth reflects the transformation of its country's brand.

But the reality in China is not so simple. Joël Vauchel of ABB questioned the Chinese commitment to their local brands, asking the Chinese, "Are you proud? Can you build pride in your products? The Japanese and Germans had trust in their brands; do you?" As long as Chinese in their home market continue to pay a huge premium for German beer brands over Tsingtao, he argued, they should recognize that they don't really have local brands to start with. Then the real task is to build a brand from scratch from a low-cost producer model – not to globalize an existing brand. And that task must start at home.

Strong Chinese brands capable of globalization are the exception, not the norm. Huawei is one company that has the quality reputation and the margins in its domestic business to underpin brand-building abroad, but most have neither. Brand in China is still seen as a matter of buying ad hoc advertising for awareness-building. "There is not yet the perception that branding is something you have to work on every day," explained Serge Berthier, President of Hong Kong-based Asian Affairs. "And that it is based on something that is true."

Given the scale of the task, several participants questioned whether Chinese firms can afford the time it takes to build their brands. Xiang Bing, Dean of

the Cheung Kong Graduate School of Business in Beijing, emphasized the speed they need. Chinese firms are under intense pressure to go global quickly. With international trade at 40% of China's GDP, they are competing with global firms. But while these competitors have access to all of the world's resources, Chinese firms that do not globalize have access to only 4% of global GDP. If its firms are to compete effectively, China must achieve in 5-10 years the economic development that Europe achieved in 400 years and the U.S. 200 – and even Korea and Japan took 40 years to achieve. "This is a new setting, not encountered by any industrial power," argued Xiang. He cited Samsung as one of the best, and much-studied, examples of globalizing an existing brand, but was concerned at the "long build up of investment" that this entailed relative to the urgency China faces. "Over-attachment to Chinese brands could be dangerous. We should have a global mindset, not a Chinese mindset."

The tempting conclusion, then, is to acquire existing international brands. Cash is certainly available for acquisitions. But this route brings two big challenges that stop it from being the easy way out.

The first is the question of integration and fit. Recognising the fundamental relationship between business and brand, integration becomes critical, and an understanding of brand among top management is at least as important in an acquisition route. Without it, argues Berthier, you hit the attitude of, "We spent the money on buying the company; we have nothing more to spend on branding."

However good the integration and management, there is still the issue of availability. Are the brands you can buy the ones that you really want? Yes, in the case of Lenovo and Thinkpad. But Xiang gave the examples of TCL and its joint venture with Alcatel, launched in 2004, to build Alcatel-branded mobile phones. The attraction of an established brand to accelerate TCL's growth in the global mobile phone market is obvious, but with the Alcatel brand "the combination is still not in the first tier. It is therefore difficult even if you have great integration."

*Wang Zhaowen,
Secretary General, Shenzhen Federation of Industrial Economics, listens to a comment by a fellow panellist*

The truth is that for most companies there is no short cut, and there is no single right answer. The trade-offs of the different brand routes are summarized in the table below. Different routes will suit different sectors and individual companies, but none are without challenges. "The failure rate for Chinese companies abroad will be far higher than for western companies," predicts Xiang. But senior management attention to brand can help reduce that rate, whether it is through careful acquisition and integration or through the dedicated nurture of a true, deeply embedded brand for the Chinese business to promise and to live by.

The Challenge of Human Resources

By Madelaine Pfau, Managing Partner, Heidrick & Struggles

In a transformation worthy of an extreme makeover reality show, China is quickly becoming the ingénue of the superpower set. The country's stunning economic growth and newfound business empowerment after so many years of stagnation have thoroughly transfixed the global community.

Much has already been written about the fact that China is on track to overtake the United States as the world's largest economy in absolute terms by mid-century. At a more micro level, the real news is that the middle class in China is expected to grow by approximately 140 million people in the next five years. That means that a new group of people equal to about 40 percent of the entire U.S. population will soon have the disposable income to spend on everything from razor blades and sports drinks to cars and computers.

The speakers at the China Europe Business Meeting tried to look into the impact of China's rise on managing human resources in China. Speakers included Marjan Bolmeijer, Chief Executive Officer, Change-Leaders, USA, Chao Zhenjia, Governor, Shenyang German International Industrial Park, China, J.P. Huang, Chairman, JPI Group, China, Armin Meyer, Chairman, Ciba Speciality Chemicals, Switzerland, Michael Nobel, President, Nobel Family Foundation, Sweden, Zhang Ye, President, Industrial General Company, China, and moderator Kevin Kelly, Chairman, Heidrick & Struggles, Europe and Asia.

This promise of great domestic demand has made China the market of choice for MNCs looking for sustained revenue and profit growth opportunities over the next decade in order to generate attractive returns to investors. Indeed, the market capitalization of many companies—particularly multinational consumer and technology companies—assumes significant future revenue streams coming from China.

But there is more to the story that many companies have, to date, overlooked or ignored. An interesting confluence of demographic and historical events has created a major obstacle for companies looking to capitalize on China as a major source of new revenue: In a country of 1.3 billion people, there is nowhere near enough senior-level managerial and technical talent to satisfy the demands of all the foreign multinationals and large Chinese companies. The upshot: The problem is likely to get worse before it gets better.

For many years now, there has been considerable discussion about China's "one child policy" as a means to limit population growth. However, many have failed to consider the unintended impact of that policy. That is, that the growth in China's population of 35- to 44-year-olds—the prime cohort for management-level jobs—is projected to peak in the next two to three years

and then decline over the subsequent decade by nearly as much as it has grown in the previous one.

As a result, China now has the world's fastest aging population and faces another potential generation gap similar to the one created by the Cultural Revolution in the 1970s and the subsequent exodus of skilled professionals from China and Hong Kong in the 1980s and early 1990s. The country's adult population today has a dearth of senior-level talent with the international experience, Western commercial skills and education necessary to succeed in a managerial capacity, and the intimate knowledge of the Chinese culture multinationals need to effectively navigate the consumer market.

Further, much of China's current education system can still best be described as "passive"—one that does not foster creativity, risk-taking and entrepreneurialism—meaning that future generations of potential Chinese business leaders may well lack these critical skills. Mark Pearson, head of AXA Asia Pacific Holdings, said, "There's a generation of managers missing in China. When we and other companies go into China, we're trying to recruit and train up as fast as we can."

In fact, AXA has plans to expand its business in Asia and double its enterprise value to $8 billion by 2008. However, recruiting, developing and retaining high-quality local managers have presented a significant challenge to AXA's Asian strategy. AXA is not alone. Many other multinationals Heidrick & Struggles works with that are expanding or moving into China have also begun to feel the effects of the country's shifting demographics—in rapidly rising compensation expectations of top talent, an inability to fill positions with qualified talent, and rapidly rising turnover among top talent. In fact, while overall attrition rates across Asia rose to over 12% in 2004, some of our clients are indicating that turnover among managers in China may now be 20% per year or higher.

The typical corporate response so far has been to apply traditional approaches to ensure adequate management coverage in China. First, many companies tried staffing their China operations with Western expatriates, who proved to be very expensive and often met with limited success, as they lacked deep knowledge of local culture, tastes and customs. Then they tried expatriates from other Asian countries, who were still expensive and whose knowledge of the local China market was equally inadequate.

According to Mr. Pearson, "AXA's number one strategic imperative is to implement a human resources strategy in Asia," with an emphasis on China. "China is a journey, not a destination," he adds. Most recently, MNCs have begun to pursue more aggressively management talent with Western business skills as well as a strong understanding of local Chinese culture, traditions and preferences, to drive product development and sales, pricing, promotion and distribution decisions. In fact, many companies are tapping local mid-level

managers who they hope can step up to the task, or are trying to attract PRC-born Chinese who were educated or are currently working in North America, Europe or Australia.

Ghislain Lescuyer, Executive Vice President for Thomson, said, "The best solution is to identify good Chinese managers to run your Chinese operations, but the local talent market is thin and extremely unstable. We all know that a business entity must be managed well or it can offset any cost savings or revenue enhancement opportunities the market affords." Mr. Lescuyer also says Thomson is now recruiting more Chinese-speaking individuals from the United States and other countries than ever, as China is a key focus for Thomson—both as a location for low-cost manufacturing and R&D and as a market for consumer and professional electronics.

Despite their best efforts, demand for business leadership among foreign companies in China continues to outstrip supply. Says Carol Surface, Vice President of Human Resources for PepsiCo's China business, the shallow talent pool of individuals who possess the "MNC mindset" has sparked incredible competition between MNCs in China.

A few multinationals have also begun to augment recruiting efforts with broader talent management programs to increase the speed of career development and improve retention. "Chinese employees want to advance themselves," observes David Wang, President of Boeing-China. "If you provide an opportunity for them to advance, you'll get very 'sticky'."

The value of getting and keeping the right talent in China to establish and scale a business and its revenue can be measured in the billions of dollars. Unfortunately, most companies have proven to have a limited real understanding of "what good looks like" to executives in different industries, in different functions and at different career levels in China (and even in different regions of China).

So now what? Multinationals cannot just walk away from the incredible business opportunities in China. The good news is that several potential solution options are emerging on the horizon. Here are just a few examples:

- Identify what the target internal and external talent market segments—relevant to your particular business—really value when making decisions to join and/or stay with a company. Corporations need to understand that what attracts and helps retain mid-level engineering or R&D managers is likely to be different from those talent management elements and business practices that are especially appealing to senior marketing or general management executives in China. Likewise, managers in the same function and same level in different industries may also have different perspectives on what good looks like. We have found that cross-border transfers have greater influence in some of the industrial industries than, for example, in some consumer businesses, on executives in similar roles and at the same level in the organization.

Zhu Bangzao, Ambassador of China to Switzerland, making a point during the opening panel

- Take a hard objective look at the attractiveness of your organization's current position and likely future in China (versus other employers) from the perspectives of various key talent market segments. For many serious corporate players in China, overly optimistic assumptions about the relative appeal of their companies in the context of building and sustaining the best management teams across the organization could become increasingly painful and costly in the near term.

- Determine where you really need local market and cultural knowledge and skills within the organization. While this may seem intuitively obvious, we have repeatedly seen companies assume that local market savvy is required across the company when that is not necessarily the case. For example, local skills and knowledge are most critical in market-facing, product development and regulatory functions, but may not be vital in other areas such as cost accounting and manufacturing planning. Knowing what types of talent can fill which jobs can provide degrees of freedom in hiring and retention programs and communications. For example, with the sales function in particular, says Surface, PepsiCo is more selective today than it has ever been. The company seeks to ensure that current and future front-line sales managers have the Western education and creativity coupled with the personal style and experience to succeed in such a highly visible role in China.

- Adopt more sophisticated recruiting strategies to fit the more complex talent requirement. As most MNCs foresee the need for their management team to grow in parallel with the business in China in the years ahead, the number of executives hired from the outside will likely be significant. In order to achieve success, companies will have to take a more global view of talent acquisition. They should also create management bench and succession depth both inside and outside their own organizations. For example, by utilizing a dynamic gap analysis model that projects organization holes over three to five years, some leading-edge companies have begun to identify, contact and begin a longer-term recruitment effort with potential talent in the market today for actual hiring down the road.

- Consider leveraging non-core and/or non-market-facing functions in other countries in the region. Staff located in other countries where the talent situation is less competitive may best fill basic research and development, information technology and finance functions that require the advanced education and technical skills companies seek in China.

- Rethink classic organization structure models, recognizing that even the best recruitment and retention or development programs may not fill the talent gaps for your company. Combining functions and/or business units in fresh ways may result in new kinds of roles, responsibilities and organization structures that might be applied elsewhere geographically in the company while also providing exceptional personal development opportunities that competitors may not be able to replicate. We have already begun to see some companies experiment with novel non-traditional structures in China to help alleviate pressure on the business.

- Be willing to innovate and take risks as never before in the management of human capital in China. Traditional approaches that have proven successful elsewhere may not result in your company achieving sustainable competitive advantage in the China talent market. Those companies that innovate and try programs, tactics and communications that have not been utilized elsewhere are more likely to emerge as winners.

The emerging China market is truly vast and incredibly seductive for multinationals of all stripes. Those companies that can achieve revenue and profit scale in the market over the next decade can handsomely reward all stakeholders. Nevertheless, the magnitude of the war for talent in China cannot be overstated. Serious introspection, investment, innovation and risk-taking in human capital and talent management will take on new meaning and become the hallmarks of those companies that truly succeed in China.

Establishing Headquarters in Europe

By Stefan Schmid, Partner, PricewaterhouseCoopers

Chinese groups have started to set-up own distribution channels in important markets like Europe to ensure better market control and to increase market share. For this purpose, Chinese groups either acquire existing European companies or incorporate own entities. The topic of establishing regional headquarters in Europe has been discussed by Michael Meyer, Director General, Seco, Switzerland, Joachim Erwin, Lord Mayor, City of Düsseldorf, Germany, Wang Fang, Managing Director, China Hub Geneva, Switzerland, and Wang Zetian, Secretary General, Beijing Council for the Promotion of Industrial Foreign Trade and Economy, China. Daniel Gremaud, Partner, PricewaterhouseCoopers, Switzerland, moderated the session.

In some circumstances, it has even proven beneficial to have own European assembly/manufacturing sites as well as own European research and developments centers to ensure closer relationship to the customers, to get a better grip of the market trends, to overcome import restrictions and to resolve customs issues. These benefits may well exceed the disadvantages of Europe's generally higher production/labor costs.

The main drivers for Chinese groups to build up or to acquire own operations in overseas markets may be summarized as follows:

- Improving market access
- Buying European technology and design
- Providing quicker services
- Conducting R&D locally to capture trends
- Acquiring business know-how
- Getting access to resources
- Diversifying currency risks

Chinese groups investing in own European distribution channels, assembly/manufacturing capacities and R&D centers find themselves confronted with an increasing need to co-ordinate the different European activities.

Chinese groups have therefore started to set up regional headquarters in Europe (ie COSCO established its European headquarter in Hamburg and moved to new premises in the harbour city of Hamburg in June 2005).

The main reasons for this trend are:

- Having management capacities that are closer to the market, i.e. being located in the same time zone, speaking the "language" of the client
- Getting a better understanding of the customer's needs to ensure that the products meet the market's demand with respect to desired design and

quality and to ensure a responsive first class customer service
- Implementation of an efficient value chain (so-called "best practice business models") eliminating a multiplication of functions in all European countries that host distribution and/or production companies
- Ensuring that the best practice business model is operated tax-efficiently

There are many factors that drive the decision where a regional headquarter should be located. Some of them are strictly operational (e.g. central location, good infrastructure, closeness to airports and/or harbours, attractive tax environment, multilingual workforce) and some might be called soft factors (e.g. size of Chinese community, educational facilities close to the regional headquarter etc.). In any case, a Chinese group should decide according to its needs and therefore choice a location which suits it's needs best.

Traditionally, Chinese groups have started their own European activities in major harbour cities of large European countries. While a group looking for capital market access might have been interested to start with own operations in a city like London, a manufacturing group might have been interested to have its first distribution entities close to a harbour city like Hamburg or Amsterdam.

With the extension of a Chinese group's presence in Europe, the establishment of a regional headquarter becomes increasingly important.

Such regional headquarters are coordinating the European value chain and hence the European distribution and service network, but are typically not directly involved in the physical flow of the goods or the provision of services to end-customer. A regional headquarter is therefore often located at a central location of Europe that suits the respective co-ordination needs best.

reception dinner

During the opening reception

Düsseldorf has just opened a second China Center financed by the Chinese community to extend the business opportunities, while Geneva has just opened a China Hub in the world trade facilities of Geneva to facilitate the establishment of such regional headquarter.

It is further understood that an existing Chinese community and Chinese schools are important factors when choosing a location in Europe, which explains why a sizable number of Chinese groups have started their European operations in cities that already have a well-established Chinese community, like London.

Many European countries and cities have therefore started initiatives with the aim to assist Chinese groups in setting-up regional operations and to facilitate settlement of Chinese management and their families at the very location.

While Chinese groups have historically been less focused on smaller, but centrally located countries like Austria, Luxemburg and Switzerland as location to start with their European presence due to the comparably small size of the domestic market and the missing access to a sea harbour, such countries become now of increasing interest to Chinese groups as location for the regional headquarter coordinating the European operations.

This goes along with the changing focus of leading Chinese groups to truly international players. While for smaller Chinese groups, establishing regional headquarters in Europe might not yet be a main focus, a number of large Chinese groups are seeking or will be seeking to conquer the world market in the near future and will therefore have the need for regional headquarters.

Having a regional headquarter in Switzerland does not only allow Chinese groups to benefit from the stable economical and political environment, the effective banking institutions, the well-established infrastructure, the state of the art legal framework and the multilingual workforce, but also from the exceptionally competitive tax environment combined with a long lasting experience to host regional headquarters of global groups.

The Chinese Approach to Corporate Citizenship

John Elkington, Chair, SustainAbility

Whatever else it has been, 2005 has been the Year of China. The giant country has loomed every larger on our radar screen as the year wound by, not least because of my first visit to the country in May. In addition to speaking at the Fortune 500 Global Forum in Beijing, I had wonderful opportunities to meet people from the Chinese government, business and NGO sectors courtesy of people like CGA, the China Business Council on Sustainable Development, Shell and WWF. Then, on 15 November, I took part in the first China Europe Business Summit, held in Geneva by Horasis - The Global Visions Community, which helped me to pull many of the loose threads together—although not all the conclusions were comfortable ones.

The China Europe Business Meeting—now set to become an annual series—is the brain-child of Dr Frank-Jürgen Richter, who I had first met when he was the World Economic Forum's Director of Asian Affairs. Now President of Horasis, he had asked me to chair a session on 'The Chinese Approach to Corporate Citizenship', which sounded intriguing. In welcoming delegates to Geneva, he stressed that "China's rise to global eminence is providing formidable opportunities for European firms." True, but the event also underscored the uncomfortable fact that European—and North American—firms are facing increasingly formidable competitive challenges from the same direction.

In the wake of CNOOC's recent attempt to take over the US oil company Unocal, one panellist wondered aloud how long it would be before a Chinese company had a go at taking over Wal-Mart? Tongue-in-cheek, perhaps, but today's lightly dismissed improbabilities have an uncomfortable way of becoming tomorrow's probabilities and realities. And the same, inevitably, is going to be true for the Chinese. Issues that would have once have seemed impossibly remote to them, alien even, are now racing up the business agenda for Chinese companies with international aspirations.

CNOOC President Fu Chengyu was one of the top Chinese business leaders who made frequent reference to issues like climate change during the Geneva meeting. But perhaps the most interesting voice for the future of Chinese capitalism was the extraordinary Zhang Yue, who Forbes magazine listed—with his brother—as No. 25 in its 2001 survey of China's 100 Richest Business People. Given that he was once a public school teacher, Zhang's rise to success is even more striking. In 1988, he founded Broad Air Conditioning, where he is now CEO, and which has boasted an 80% share of the energy-efficient air-conditioning market in China. His personal quest, he says, is "to make society a better place to live."

Zhang was also one of the panellists in the session I chaired. And while several speakers—including Serge Berthier who founded the quarterly Asian Affairs and chairs Oriental International Strategies and the Asia-Europe-Forum—questioned whether China could afford to adopt foreign standards of corporate citizenship any time soon, Zhang repeatedly stressed the stunning nature and scale of the environmental challenges his country faces. Like a number of the companies represented at the Geneva summit, he noted that Broad Air Conditioning's ambition is to go global. In the process, he noted, the aim will not be to become a "big company, but a great one." And for that to be sustainable, the international corporate citizenship agenda will become increasingly important.

Several other speakers discussed the rising expectations and standards that all high-brand businesses are now expected to meet. Perhaps most strikingly, we had Eva Biaudet, a member of Finland's Parliament and a former Minister of Health and Social Services. Modestly introducing herself as "a typical Nordic woman politician", with an interest in such areas as human rights and climate change, she accepted that it might seem strange that a country of 5 million could have something to offer to a country of 1.3 billion. But she noted that Finnish companies are increasingly active in China, with over 200 firms now employing some 24,000 local Chinese.

That was the positive side. More challengingly, she explained how she is Teaching her children to choose between products offered by different companies on the basis of their environmental performance—and, she warned, the behaviour of such companies will increasingly be vetted by western consumers for their performance in relation to such issues as environment, working conditions and human rights.

Xiang Bing and ZhangYue sharing a light moment

In headlines, we discussed three main areas of the citizenship agenda: international companies moving into and operating in China; national Chinese countries operating in the domestic market; and, the big long term trend, the growing number of Chinese companies operating abroad.

From the presentations of people like Nick Butler, BP's Group Vice President for Strategy & Policy Development, it was clear that the best of overseas investors in China are doing their best to ensure that their operations in the country are state-of-the-art. But several speakers underscored the political challenges that will surface as China moves onto the international stage.

Tom Spencer, Executive Director of the European Centre for Public Affairs at Surrey University, and a former Member of the European Parliament, recalled this year's 'Bra War'. This resulted in over 80 million items of clothing - including sweaters, trousers and bras - piling up in warehouses at European ports. Spencer accepted that Zhang Yue was highly unlikely to face a consumer boycott against air-conditioners any time soon, but continued to say that the range of contentious issues is growing rapidly. Among others, he spotlighted the continuing problems international companies trading into China face in terms of intellectual property and counterfeiting. In fact this issue surfaced repeatedly through the summit, with some participants arguing that this has been one of the features of Chinese business practice (or, more accurately, malpractice) that has been preventing more EU companies from getting involved.

Carlo Lamprecht, Xing Jun, Chairman, Shenyang Hope Industry

Interestingly, Spencer also raised the distinct possibility that the early twenty-first century vision—in the West, at least—of 'turbo-capitalism' evolving along Anglo-Saxon lines will prove illusory. Instead, our session concluded, the future is likely to be one of multi-polar politics and multiple capitalisms, with huge implications for the types of 'corporate citizenship' that will take root (or fail to do so) in the various world regions.

Our last speaker—but one of the most interesting—was Zhao Min, the Harvard-trained President of Sinotrust Management Consulting. When he and two colleagues resigned from China's former Ministry of Foreign Trade and Economic Cooperation in 1992, Zhao scarcely dared tell his parents that he was venturing into the private sector—and met with sarcastic comments when he went to register the new company with the Beijing Industry and Commerce Bureau. Now Sinotrust employs over 600 people at its offices in Beijing, Shanghai, Guangzhou and Hong Kong.

Zhao joked that in the old order, the smartest Chinese became government officials, the next level down went into education, and (by implication) the bottom of the barrel went into business. Although he commented that there are very few companies anything like Broad Air Conditioning, he reported that business is becoming increasingly popular as a career path for bright Chinese youngsters—and, in a parallel trend, many business leaders are beginning to acknowledge the need not just to pursue raw profitability but also to manage against a "balanced scoreboard".

The relatively low turn-out for our corporate citizenship session—which faced competition from parallel events on such themes as intellectual property, intangibles, corporate governance and innovation—led some of us to conclude that the title should have been more along the lines of 'How To Make Billions From Corporate Citizenship'. But it will be fascinating to track the evolution of the emerging Chinese scoreboards as Frank-Jürgen Richter and his colleagues continue to build their series of summits.

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