China goes shopping

By Dexter Roberts, in Beijing, with Frederik Balfour, in Hong Kong; Pete Engardio, in New York and Joseph Weber, in Chicago

Lenovo-IBM is only the highest-profile deal yet in a wave of Western acquisitions that is certain to build

Got a tired brand that needs a shot of adrenalin? The answer to your troubles may reside in China. Billions of dollars, euros, and yen have been invested to build up companies on the mainland in the last decade. Now Chinese companies, flush with cash and in command of the world's lowest-cost manufacturing plants, are doing some foreign investing of their own. First it was Huizhou-based TCL Corp. merging its television business with France's Thomson to create the world's biggest TV manufacturer -- one of whose brands is venerable RCA.

In September, Shanghai Automotive Industry Corp. announced it was buying a 48.9% stake in Korean truckmaker Ssangyong for close to $500 million, and there are rumors that SAIC's next target is Britain's troubled MG Rover Group Ltd. Then, on Dec. 7, Beijing-based Lenovo Group Ltd., China's biggest computer maker, agreed to buy a controlling stake in IBM's PC operations for $1.75 billion. "We saw a unique opportunity in front of us," says Mary Ma, Lenovo's chief financial officer. "It is an opportunity to differentiate our products and our technology."

GOVERNMENT PUSH

Plenty of other Chinese execs will be looking for similar opportunities. China's Commerce Ministry figures the country's corporations spent $2.85 billion buying foreign companies and other assets in 2003. Straszheim Global Advisors, a Los Angeles-based research outfit that specializes in Chinese equities, says total outlays by Chinese companies on foreign deals may total as much as $7 billion in 2004 and could reach $14 billion in 2005.

Don't expect a bid for Exxon Mobil Corp. or Dell Inc. anytime soon, though -- and don't expect the process to be easy. The Chinese have plenty of issues to sort out before they completely master the art of the deal, from smoothing over cultural differences to building up brands to running global supply networks.

But the momentum that's driving China's acquisitive streak is bound to grow. For starters, Beijing wants to create global champions, such as Lenovo in computers or TCL in TVs and mobile phones. "Go global" has become a catchphrase in China's official media. Beijing has just loosened the rules for companies investing abroad. "This is part of the more developed stage of China's opening to the world," says Gu Kejian, a professor in the Business School at People's University in Beijing.

What's more, though the amounts involved are small now, allowing further overseas investment could eventually help relieve pressure on China's overvalued currency. Investing yuan outside the mainland will balance the inward flow of money lured by a possible revaluation. And when China lets the yuan appreciate, the buying power of Chinese companies will increase.

Finally, the Chinese need to go abroad for resources to feed their industrial machine and to scare up the talent and research they can't find at home. China National Petroleum Corp., parent of New York Stock Exchange-listed PetroChina; Sinopec, an oil-and-gas company; and CNOOC, an offshore driller, have each invested billions in oil-and-gas projects in Africa, Southeast Asia, and Latin America. More recently talk has been rife that Beijing-based China Minmetals Corp. will spend up to $5.5 billion to buy Canada's biggest mining company, Noranda Inc.

The next big wave of Chinese overseas investment will come from manufacturers such as Lenovo. China will buy into the industries in which it already competes heavily, particularly electronics, auto parts, appliances, textiles, and apparel. These are industries where acquiring global supply chains can confer big advantages, even for low-cost players like the Chinese. "The Chinese understand that global scale gives them lower-cost components, and that R&D and branding are now done globally," says Paul DiPaola, a managing partner at Bain & Co. China. "Chinese companies in industries where the economics are global will have no choice but to make these deals."

COMMUNICATION GLITCHES

Global scale has motivated Hangzhou-based auto-parts maker Wanxiang Group to buy 10 overseas companies in the last few years, including NASDAQ-listed Universal Automotive Industries Inc. "We combine international and domestic resources to speed up development," says Chairman Lu Guanqiu. The Chinese certainly have to do something. Their cell-phone, washing-machine, and electronics makers face overcapacity and razor-thin margins in their home market, where they already often compete with the world's best brands. Lenovo, for example, is No. 1 in desktop computers in China, but it has been under pressure from Dell and other non-Chinese brands. And as they enter foreign markets, Chinese execs realize they lack essential skills. "China needs brand names, reach, logos, marketing, distribution -- and the management that attends to all of those," says Donald Straszheim, head of Straszheim Global Advisors.

The pressing question is whether the Chinese can get what they're looking for. Asians have a long history of overpaying for foreign assets: Remember the Japanese, with their ill-fated U.S. real estate and entertainment-industry deals? Analysts say China's oil companies have already spent too much on overseas reserves.

The Chinese have internal problems as well. Too many of their best-known companies, such as appliance maker Haier Group Co., rely on the vision of a charismatic founder and have little management depth. A merger can struggle with cultural differences, including management styles and big pay gaps between Chinese and Western executives.

Thomson and TCL, for example, have a lot to thrash out. In China, says one TCL official, "if the leader says something is right, even if he is wrong, employees will agree with him. But in foreign companies, they will not agree with him. We have two different cultures." Alar E. Arras, president of TCL-Thomson Electronics, says the venture is working through pay issues and other problems, but he concedes the hurdles: Try solving a technical glitch through translators, for example. "The communication challenge is one of the unique items we face," he says.

Given the problems, the Chinese may try various tactics in their forays abroad. Edward King, executive director for mergers and acquisitions at Morgan Stanley in Hong Kong, figures they will use joint ventures more than outright acquisitions to spread responsibility for making a deal work. But one way or another, more of those deals are on the way.

China Abroad

Big Chinese companies have recently made or are considering lots of foreign acquisitions. Some deals:

TCL-THOMSON The Huizhou electronics company merged its TV unit with that of France's Thomson, acquiring the RCA brand in the U.S. Revenues this year: $4 billion.

SHANGHAI AUTOMOTIVE-SSANGYONG The Chinese auto maker paid $500 million for almost 50% of the Korean truckmaker. It may also buy control of Britain's Rover.

WANXIANG-UNIVERSAL AUTOMOTIVE The auto-parts company has bought 10 U.S. companies, including a stake in Nasdaq-listed Universal Automotive Industries.

UTSTARCOM-AUDIOVOX The U.S. gearmaker, which has most of its sales and workers in China, bought the cell-phone business of Long Island-based Audiovox for $165 million.

CHINA MINMETALS-NORANDA China's mining giant is considering offering as much as $5.5 billion for the Canadian nickel-and-copper miner.

Data: Company reports

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