Chinese Companies in the UK and US: Prospects and Concerns

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The past twenty years has witnessed the international expansion of Chinese multinational companies, especially in developed countries such as the UK and US. Most importantly, these Chinese multinational companies are not only from the traditional manufacturing industry, but also from industries such as technology, energy, entertainment and education. This growing presence of Chinese multinational companies brings new competition but also mutually beneficial commercial opportunities.

Chinese companies' overseas expansion

The well regulated UK and US markets offer significant opportunities for Chinese companies. There are four major methods for Chinese companies to expand their business overseas:

Investment through Mergers and Acquisitions: Because of international shipping costs and import tariffs, it may be cheaper for Chinese companies to directly build or buy a business in the UK and US. A common way is to use mergers and acquisitions. For example, Huawei, China's largest investor into the UK, opened its UK R&D centre in Ipswich after acquiring the Centre for Integrated Photonics (CIP), in 2011; Shuanghui International completed a $7.1 billion acquisition of pork producer Smithfield in the US last September, the largest Chinese acquisition in the US to date; Dalian Wanda Group acquired AMC Entertainment in a $2.6 billion deal in 2012.

Direct Overseas Investment: Some Chinese companies choose to build a business abroad from scratch. This option keeps the confidentiality and intellectual property (IP) of the original business and technology, avoids any acquisition premium and a long negotiation and legal process. For instance, during the international expansion process of Haier, the company built a production facility in the US at Camden, South Carolina which opened in 2000. Huawei opened its first office in the UK in 2001 and currently the company has 15 offices and 890 employees across the country. In April 2013, Huawei opened a new UK headquarters in Green Park, Reading.

After the 2008 global financial crisis, Chinese investors started pushing for a greater share in the UK and US property market. As a result, the transaction value has been much bigger than before. Fosun International made a $725 million purchase of Chase Manhattan Plaza in New York this October. Shanghai Greenland Group agreed to purchase a stake in the Metropolis site in downtown Los Angeles and the deal is currently pending government approval. Recently both the Chinese government and companies have been actively investing in U.K. property and infrastructure, such as the Zhongrong Group's £500 million investment to reinvent the historical Crystal Palace in south London and the Beijing Construction Engineering Group's investment in Manchester Airport.

Strategic Alliances: Some Chinese firms choose to form strategic alliances with UK and US local firms, if the acquisition target is not available or strict local government restrictions prevent them from acquiring certain local firms. A strategic alliance is an agreement between two or more parties to pursue a set of agreed upon objectives need while remaining independent organizations. The well-known example is when Lenovo Group and IBM formed a long-term strategic alliance relationship in PC sales, service and financing worldwide in 2004.

Initial Public Offering (IPO): IPO is a type of public offering where shares of stock in a company are sold to the general public on a securities exchange for the first time. The initial wave of Chinese firms' IPOs in the US started from early 2000. Since then more than 200 Chinese firms have successfully made their US debuts. In 2010, 40 Chinese companies had IPOs in US while the number of US firms' IPOs was only 11. In 2010, the London Stock Exchange (LSE) had its first ever Chinese member firm "Chinese International Capital Corporation" during LSE's 210 year history. By that time, 51 Chinese companies had listed on the LSE with a combined market capitalization of £30 billion.

Support from US and UK governments

There is no doubt that Chinese companies have gradually accelerated their activities internationally. Meanwhile US and UK governments have made their policies more flexible for Chinese firms' overseas investment. The US has already attracted the majority of Chinese overseas investments. US President Barack Obama made strong statements about overall U.S. policy toward Chinese investments in 2012. Most Chinese investments in the US do not require regulatory approval and some deals that do require regulatory approval by the Committee on Foreign Investment in the United States (CFIUS) have been successful in the initial thirty-day review period. Obama also suggested removing impediments of US Visa applications from China.

Recently, the UK Chancellor George Osborne, on his visit to China last October, said the changes will "streamline and simplify" the visa application process for Chinese visitors. George Osborne also signed a new memorandum of understanding on civil nuclear collaboration with Chinese energy firms. The memorandum shows the UK government's strong support for collaborations between UK and Chinese firms. This memorandum has deep political affects for Chinese companies' investment in the UK. UK nuclear plants have the highest national security level and now they are open for investment from China. Last but not least, Chinese investment banks will be allowed to set up branches in the UK, which greatly facilitates Chinese companies' investments in UK projects.

Concerns of Chinese overseas companies

Given the market expectation that Chinese RMB will appreciate against other main currencies, it is reasonable to predict the future growth of Chinese companies' presence in UK and US markets. While both markets are ripe with opportunities for Chinese companies, many challenges and concerns still warrant our attention. Three main concerns are as follows:

Chinese companies should learn from Japan, and be prepared to become more "localized" in the UK and US. In 1980s, Japanese investments were erroneously perceived as a threat to the US local economy. Today, Japanese investments are perceived positively and as integral to the U.S. economy. Car manufacturing firms like Toyota and Honda set very good examples. Chinese companies should foster relations with local communities and build strategic alliances with UK and US partners.

Product markets in the UK and US are very competitive. Brand recognition and customer services are critical. Sadly, some products made in China have been labelled as low-quality. It is a great opportunity for Chinese firms to rebuild a new image during the next round of expansion. Chinese companies, such as Haier, Lenovo, and Huawei, have been making consistent effort to build up their long-term brand reputation.

Chinese listed companies in the US and UK must improve their corporate governance and strengthen their internal accounting and auditing standards. Starting from the first half of 2010, US short-sellers and SEC exposed a series accounting scandals of Chinese companies listed in NYSE and NASDQE. From March to June 2011, more than 20 US listed Chinese firms suspended trading or were delisted on US exchanges for alleged financial fraud. Professional short sellers, like Citron Research, usually hunt for discrepancies between a Chinese company's US disclosure and its corporate annual filings maintained at the Chinese Administration of Industry and Commence (AIC); accumulate short positions on the target company's stocks; issue research reports based on their findings to the market; hammer the target firm's stock prices and finally profit from their initial short positions at last. In July 2012, New Oriental Education became the latest victim of short sellers and its stock price tanked more than 60% within the next two weeks. Financial market regulations and law enforcement are not well established in China. Chinese companies are used to operating business with "GUANXI" and taking advantage of grey areas in China. It is very important for Chinese companies to realize that they must adapt to the rules of local countries.

Because short selling is not allowed in Chinese stock markets, Chinese media and companies tend to believe that reports issued by short sellers like Citron Research are hostile and not based on factual market information. Short sellers can effectively detect public firms' misrepresentation in their financial statements before the misrepresentation is publicly revealed by the SEC. Indeed it can be shown that short sellers actually help to uncover firm misconduct and improve stock market efficiency. Although this research is not designed specifically for Chinese listed companies in the US, it does indicate that all Chinese overseas companies should take these short sellers' activities as a warning sign.

In conclusion, Chinese companies have already become global players in the US and UK. The prospect is bright for Chinese overseas companies especially in light of the positive reception and trust being shown by both governments towards inward Chinese investment. As we have highlighted, maintaining a quality brand both in terms of product and in terms of financial sustainability, will be imperative to continue this positive development.

(For interest of space and style, the original notes given by the author have not been included. They are available upon request.)