South China Morning Post 南華早報

Is the golden age over for multinationals in China?

PUBLISHED : Thursday, 28 August, 2014, 5:30pm
UPDATED : Friday, 29 August, 2014, 4:42am
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Edward Tse and Paul Pan say multinationals' experience in China varies, depending on the sector and the company's ability to adapt. Some are thriving, notwithstanding the antitrust crackdown

Multinational corporations are in the spotlight these days. Recently, the Chinese government has accused a number of foreign companies of violating the antitrust law. Mercedes-Benz, Audi, Microsoft, and some Japanese car parts companies have been among those charged.

In fact, this is nothing new. Last year, Beijing also charged a number of foreign milk powder producers with alleged "abnormal price fixing", while pharmaceutical companies - including, most notably, GlaxoSmithKline - were caught in bribery and corruption scandals.

According to the results of a business confidence survey by the European Union Chamber of Commerce in China, conditions in China are getting tougher. There's an entrenched sense of pessimism within the European business community, as persistent market challenges show little sign of abating.

In turn, according to the chamber, many companies are setting more modest expectations for revenue and profitability growth and are scaling back their investment plans for the Chinese marketplace. Is the "golden age" for foreign companies in China over?

Multinational corporations started making significant investments in China in the early 1990s, especially after Deng Xiaoping took the now famous "southern tour" in 1992. After more than 20 years of investing in China, these companies' attitudes have changed dramatically.

Broadly speaking, there are three groups of companies distinguishable by their market views. The first includes multinational corporations that have come to China, made investments and, being unsuccessful, decided that China is not their cup of tea.

They have found it difficult to earn a profit and some have withdrawn from the Chinese market. Examples include Home Depot, Best Buy, Media Markt and Mattel. PepsiCo, for instance, sold its bottling business in China to Taiwanese company Tingyi Holding, which has a broad distribution network across China.

The second group are those in sectors that exhibit overcapacity in China, such as cement, steel, solar panels and the like. These companies are typically in a wait-and-see mode - waiting to see if and when the overcapacity can be managed away.

The final group of companies are those that have found China to be a major, and often highly profitable, market. For them, China is one of the largest markets in the world, if not the largest. Prime examples are the carmakers Audi/Volkswagen Group, BMW, Daimler and General Motors. It also includes others like Yum Brands, Starbucks and Apple.

For these companies, the golden age in China is here and will probably continue in the near future. At a recent meeting, the China head of a leading premium-car maker told me that his company sees huge opportunities in China and one of their biggest challenges is how to build the production capacity fast enough to capture the upcoming market demand.

In short, multinational corporations' views of China depend on their relative market position, and there isn't a single uniform view.

Nonetheless, as China evolves, there are a number of recognisable patterns. On the one hand, Beijing continues to open more sectors to non-state capital (recent examples include commercial banking and telecom operations); on the other, it is also visibly applying more stringent laws and policies such as antitrust and anti-corruption measures.

In the open sectors, competition is intense, often the most intense in the world. In addition to their usual global competitors, multinational corporations will also have to deal with local competitors, some state-owned, some privately owned. While multinationals are fairly used to how other multinationals compete, the ways Chinese companies compete is often quite different, and therefore surprising. On top of all this is the rapidly changing, complicated and ambiguous operating environment in China that can catch multinationals off guard. Increasingly, many realise that they cannot apply their cookie-cutter ways of working to China and that they need to adapt.

As China evolves into a market economy, it has been trying to learn from other countries, benchmarking and adapting other practices into the Chinese context. A notable example was how the Chinese recognised - from US politicians - the application of national security to businesses, after a bid by China National Offshore Oil Corporation to buy the US energy company Unocal was rebuffed in 2005.

China's antitrust legislation, largely modelled on EU law, came into force in 2008. The Chinese have insisted that the law applies equally to foreign companies and Chinese ones. In fact, last year, two state-owned liquor companies, Kweichow Moutai and Wuliangye, were fined 247 million yuan (HK$310 million) and 202 million yuan respectively after being found guilty of price fixing.

Foreign companies have registered concern over the recent antitrust crackdown, especially the use of "intimidation tactics". It is unfortunate that, quite often, when the Chinese authorities begin to implement certain new practices or laws, their execution can be quite unpolished. Over time, things are likely to improve.

But it's ironic that many of these same multinational corporations which are now raising concerns are the same ones that have complained about the lack of law and order in China.

Though economic growth in China has slowed, the growth of some sectors continues to be very strong. The internet sector, for example, is growing by leaps and bounds. Companies such as Alibaba, Tencent, Xiaomi and JD.com [1] are commanding huge valuations.

The health care and environmental sectors, for instance, are also growing fast. According to Liang Xinjun, chief executive of the Fosun group, a large Chinese conglomerate, in several years, the size of the "big health" sector, which includes all businesses along the health value chain, will exceed that of the property sector that has been the engine of growth in China for the past decade.

In a complicated and fast-changing environment, there are tremendous opportunities and challenges for everyone, multinational corporations included. They need to know how to strategically anticipate and capture these opportunities and handle the challenges.

Foreign companies which can see the opportunities in China will stay and continue to invest, whether or not there's an antitrust crackdown. And if they manage to build the right capabilities on the ground, enabling them to compete effectively, then the answer to the question of whether the golden age is over will be a resounding "no".

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[1] http://JD.com