

## Yes, but how? Basic rules for investing overseas

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In the last decade, China's aspirations have grown in line with the country's economic strength. Political and business leaders are no longer content for the country to be the world's factory floor: they want Chinese corporations to rank amongst world greats. With government support – in the form of financing as well as policies – Chinese companies are increasingly looking overseas for assets. Mining companies, in particular, are being encouraged to meet demand by sourcing overseas. But although this process is natural, it is sometimes a rough road.

In the United States, political uproar over the notion of a potential rival nation controlling an oil company in California succeeded in quashing an acquisition attempt by a Chinese oil company. Mining companies have not been immune from controversy: a bid to acquire a Canadian mining property eventually collapsed for state-run Minmetals, but not before exposing public discomfort with the Chinese bid.

It is important for Chinese companies expanding overseas to learn from the experience of their forbears. It is also important for firms looking for Chinese partners to understand the potential. As an investment advisory firm, we have seen the flow of business both ways. The following is a summary of lessons we have learned, and advice we give our clients, after five years of helping these deals get signed.

### Advice for Chinese companies buying assets overseas

- Have a staffer who understands the Western approach to business. It is important that you delegate an experienced representative who will make sure to check back with management frequently throughout the process and who is not afraid to bring so-called bad news to management's attention. There is no use giving negotiating authority to someone who can't accept offers, or who is afraid to fully inform management of any problems. (We have seen cases where a foreign partner negotiated for months with a representative of the Chinese company, only to hear that "the boss" is not happy with the proposal at the last minute).

- Learn about the particular issues related to public companies. It is almost unheard of for a mining company to be private. So when a Chinese company is looking to develop a property overseas with a partner, it is almost certain that the partner will be a public company. This adds a few more challenges such as dealing with shareholders, public disclosure of information that they might not normally disclose, dealing with the exchange regulators, etc. Even if the Chinese company isn't public, the partner will likely have to deal with those issues. The Chinese company should not dismiss those concerns as "someone else's problem." (The upside

to working with a public company as a partner is that tradable shares can be part of the deal, and the Chinese firm may see some upside from the project in the form of capital gains long before the project itself becomes profitable.)

- Hire help! This includes hiring lawyers, financial advisors, public relations specialists and lobbyists. Many Chinese firms are reluctant to spend the money on hiring outside advisors when they decide to invest in an asset overseas. Spending the money on these advisors is an excellent investment: they will help you get the best deal possible, and make sure that all the elements are in place for the deal to go smoothly. For example, paying USD50,000 to USD100,000 (RMB400,000 to RMB800,000) for a company to complete a due diligence report on your potential partner may seem expensive, but it can potentially save you millions of dollars.

- Hire help early. It is important to hire support early on in the process. Saving money by delaying this expense may cost the whole deal in the end.

- Follow your advisors advice. The financial advisors, lawyers and public relations specialists that we have dealt with often stress the importance of their clients following through on the advice they are given. Although it is understandable if a particular client disagrees with the advice they are given, the usual step would



then be to ask for a second opinion, not to ignore the advice altogether.

- Keep advisors fully informed. Many Chinese firms are very secretive. But if you don't share important information with your advisors, it makes it impossible for them to do their job, and help you. This leads to the untenable situation where the outside experts are unable to offer sound or informed advice.

- Do not get lost in the details.

Inexperienced companies sometimes tend to pay too much attention to minor details of the deal, especially if they are unused to dealing with lawyers. Remember the big picture: you want to make a deal.

- Inform the foreign government.

This is particularly important when dealing with a sensitive asset. Let the right people know about your plans. In Canada, for example, this would mean meeting with a couple of federal and provincial ministers to ensure that they are informed of your intent. There is nothing politicians hate more than being caught off guard. Meeting with them early in the process gives them a chance to prepare their response to any negative reaction.

- But informing the government is not enough. You must pay attention to the other stakeholders as well (shareholders, the public in general, competitors, etc). Obtaining help to navigate the approval process is one argument for hiring a deft lobbying partner. But Chinese companies often make the mistake of presuming that lobbying at the government level is sufficient. After all, in China, it is important to have the support of government officials to guarantee success. But you must be yet aware of the powerful voices wielded by other stakeholders. It is important to make friends with these peripheral participants in your deal, to make sure they understand what is happening.

- Learn how the media work in other countries. In Western countries, the

government does not control the media, so you cannot lobby your government allies to change your coverage. This is why hiring a public relations firm that can address a variety of concerns is so important. They will help you make friends with the bodies mentioned in the previous item, and the media is an important partner in this process.

- Accept some bad press.

In this case "no news is bad news." It is better that the media have information directly from

you, so even if speaking to the media means you might sometimes get bad coverage, at least you are perceived as honest and open. If you never talk, you can never get your message across.

- Sometimes paying a high price is a good decision: Many Chinese firms hesitate to pay top dollar for the assets they are bidding on. Perhaps they believe that only a cheap deal is a good deal. But sometimes the importance of the asset is so high, that you want to make sure you acquire it. This may involve paying a high price if there are other competitors: that's OK. It doesn't mean you have made a bad decision. Sometimes, paying a premium may be in your interest if the acquisition meets your company goals.

- Be patient with your partner. Many foreign companies will be dealing with a Chinese partner for the first time. Just as "guanxi" is important when doing business in China, so Western partners first need to reach a comfort level before the business relationship can progress. Preconceptions need to be cleared away before the relationship can run smoothly. The Western partner will be hearing concerns from a variety of sources: employees might be wondering if they will need to learn mandarin; unions will wonder if there is pressure to change labour practises; shareholders will ask if disclosure will change; suppliers might be dubious that their products will still be in demand; environmental groups will ask if the potential Chinese partner will meet the same standards as the local ones, and so on. It takes a great deal of finesse to manage all these questions, and answers might not even be available. The point being, a Chinese partner can be a harder "sell" for in some Western companies.

**Suggestions for companies seeking Chinese investment**

As Chinese companies increasingly look overseas for assets, mining companies may find themselves with Chinese suitors. Here are a few basic guidelines for foreign firms to follow to help things run more smoothly.

- Let potential Chinese investors know about opportunities. Chinese companies may be unaware of the assets available to them overseas. It is your job to teach Chinese investors about the potential in your country, or company.

- Be patient with your potential partner. The relationship will begin slowly as you first establish a rapport. This is no different from any other deal: the partners have to learn to trust each other.

- Cast yourself in the role of advisor.

Once you have built a solid relationship, you can act as a helpful advisor in explaining some of the peculiarities of your country or market to your potential partner

- It is important to do your own due diligence. Perform due diligence as you would at home, from the accounting to the political. Have an international accounting firm review the books (especially with small companies, where there are sometimes irregularities in bookkeeping).

- Structure the deal to make it understandable and acceptable to Chinese partner. Some concepts are still very foreign to Chinese firms: debt guarantee, structured finance, convertibility, etc. Structure the deal in a clear way to make it more palatable to your partner.

- You may have to contribute to building consensus. To help the deal move along, you may need to contribute to helping your Chinese partner build support for the deal within his or her company. The best way to do this is to hire somebody who knows all the players and can moderate the process for you.

### And finally

Chinese mining companies will increasingly have the means and the ability to choose to expand overseas. In fact, growing domestic competition will mean they have no choice but to do so. There are no insurmountable barriers, just bumps along the road. In the end, successful deals will be signed by partners who make an effort to understand each other's position.

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