

The road to China: ten key lessons on doing business in China

As a result of the tremendous economic growth and liberalization of the past thirty years, China has become an attractive market for UK and other foreign companies, leading many to travel the road to China. This is culminating in a flurry of business arrangements between domestic Chinese companies and foreign entities. These arrangements have run the spectrum from complex joint ventures, investments and acquisitions to a variety of reseller, outsourcing and manufacturing arrangements.

Unfortunately, the road to China has often been characterized by friction, failure and the loss of millions of dollars. In short, it has been treacherous and fraught with economic peril. Many lessons on doing business in China have been learned, but most of them have been learned the hard way. Moreover, the majority of recent entrants into China have relearned those same lessons and suffered similar frustrations and financial losses as those who came before them.

This article is intended to summarize the key lessons learned by UK companies in the past thirty years and set forth factors that are critical for success in China. However, each industry has its own unique challenges and this article is not intended to address them. Instead, it is intended to summarize certain fundamental factors that must be addressed irrespective of the industry, size of company or success in the U.K. market. It should also be noted that many of the lessons learned overlap. Furthermore, one must keep in mind that China is rapidly evolving and the paradigms of today may not work tomorrow.

Don't Leave Common Sense at the Border.

In considering how to do business in China, the first place to start is to avoid leaving common sense at the border. Many of the same practices that work in the U.K and elsewhere also work in China. Fundamental business practices such as setting clear objectives and methods to measure success, thinking through the rationale for pursuing such objectives, establishing a tactical plan to achieve the objectives, finding the right people with whom to work, understanding the market and competition, and being prepared, work throughout the world. All too often U.K companies entering China abandon these fundamental practices. They become overwhelmed by the "need" to get into China and their fear of forever missing the opportunity. Accordingly, many companies rush into China, invest heavily, and proclaim that they will take the market by storm via superior products and services. In their haste and enthusiasm, they leave common sense at the border and forget everything they know about being successful.

Develop "Guanxi."

In every country, personal relationships are important for conducting business. However, because of China's long, tumultuous history, the country has a system of organized dependency. It is personal relationships that open opportunities and get things done. With many layers of bureaucracy and personal interests to deal with, China is not a place where individuals function alone. As a result, the whole pattern of business relationships in China is different than in the West.

Although the Chinese are generally polite, suspicion and distrust characterize all meetings with strangers. Moreover, China has a history of hostile relationships with foreigners. One will often hear reference to the "century of humiliation," a period during which foreign powers forced political, economic and territorial concessions from Qing Dynasty. As a result, trust is very difficult to earn, especially for outsiders. Yet almost no business relationship can be formed without it.

U.K. companies and others struggle with this dilemma that personal relationships are critical to business success in China, but are difficult to establish. In order to gain trust and be successful in this environment, the U.K. company must develop "guanxi." "Guanxi" is a Confucian concept of relationships that is at the heart of all business in China. It encompasses a complex set of values including hierarchy, respect, mutual benefit, obligation and "face." Developing "guanxi" takes substantial time and commitment.

In cultivating relationships with business, government and social leaders in China and developing "guanxi," there is no substitute for humility. A Brit coming to China to "show the locals how to do business" is bound to fail. China, like every international market, is different. Although developing "guanxi" is a long process, a U.K. company may still develop key relationships by leveraging the "guanxi" of others. To accomplish this, in addition to its own efforts, a company may consider using "zhongjian ren" or intermediaries which, for historical reasons, are very common in China. An intermediary can use his or her guanxi to bridge the trust gap. In essence, the intermediary is "vouching"

for his or her client. Accordingly, intermediaries can be helpful in making key connections and facilitating business transactions.

Understand the Role Government Plays in Day-to-Day Business.

The role the “government” plays in China is much different than the role it plays in the U.K. In China, the national, provincial or local government agencies and their respective officials are involved in almost every aspect of business. The license and permit requirements are numerous and complex.

As a result, U.K. companies should develop a strategy for dealing with key government constituencies. The foundation of this strategy is meeting and cultivating relationships with government officials at all levels. This group requires a lot of time and attention. The first step is for the U.K. company to bring something of value to China such as job opportunities, technology or investment. Government agencies will more likely take interest in the foreign entity if the company is bringing something of value to their country.

The benefits of developing these relationships will increase a company’s chance of success. For example, there are government agencies whose mandate is to protect foreign investors. These officials do not want foreign investors to lose money and will be helpful in many areas. Similarly, the government is very aware of China’s poor reputation with respect to intellectual property protection. Although this reputation has been earned over many years, part of the problem lies with foreign companies that fail to understand how the government can be helpful and to develop the relationships necessary to procure such help. The U.K. company should make it a priority to develop a relationship with the State Administration for Industry and Commerce (“SAIC”) representatives who can be very helpful in combating intellectual property infringements. The company should identify the people with influence within the SAIC. The General Manager or other top company officer in China should make a social call and introduce himself or herself. Thereafter, such officer should make frequent telephone calls and personal visits to discuss issues of mutual interest. Although it may take weeks or months to schedule a brief visit, the U.K. company should be persistent.

Learn to Thrive in the Local Business Environment.

The business environment in the industry or region in which the U.K. company intends to operate is critical. The company must learn to thrive in such environment. In order to understand the local business environment, the company must learn the local and regional political and business dynamics. In addition to developing relationships with the appropriate government officials, as previously discussed, the U.K. company must also meet and get to know the local business leaders. These individuals have significant influence in their respective business communities. Developing these relationships is not an easy task. Much time, patience and perseverance is required.

In addition, the U.K. company must learn the local business etiquette and norms. The correct protocol can actually be learned from the Chinese themselves. As previously stated, humility is a powerful tool in China. Accordingly, the U.K. company must be open to learning from the local Chinese.

It is worth noting that even western-educated Chinese, who have spent years in the U.K. working as engineers or managers, often struggle when they return to run operations in China. They often suffer from “reverse” culture shock. As a result of the tremendous change and growth, the China they left bears little resemblance to the China to which they have returned. Accordingly, a foreign company relying on such persons must be patient as such managers adjust to the new environment and learn the business etiquette and norms.

Know The Market and Your Customers.

Related to the need to learn the business environment is the requirement that the U.K. company must know the market it is entering. A basic knowledge of the competitive landscape is critical. The identities of the competitors, their strengths, weaknesses and strategies must be obtained. Avoid relying solely on research reports or the advice of marketing consultants.

The company should also do its own fieldwork and directly meet with people in the market. Although the Chinese economy has been rapidly growing for many years, the domestic market in China is brutally competitive. As discussed above, the U.K. company must determine which relationships are crucial for its prosperity. In addition, the company must “know” its Chinese customers. Whether the company sells to businesses or consumers, understanding attitudes, buying habits and other characteristics are crucial. To complicate matters, not only are the customer likes and dislikes based upon a different value system and vary from region to region, but they are rapidly changing as well. There is no substitute for

engaging in direct contact with potential customers. The company must also be flexible to adapt to these rapidly changing customer attitudes. A thorough knowledge of the market including the customer allows the U.K. company to identify the business opportunities and develop the strategy to be successful.

Select the Right Partners, Suppliers and Resellers.

Although this concept sounds obvious, many U.K. companies have failed to exercise the patience and persistence required to select the “right” partners, suppliers and resellers. All too often, the Chinese idiom “same bed, different dreams” describes the difficulties shared between the U.K. company and its partners in China. The U.K. company must work hard to understand the objectives and motivations of any party with whom they plan to do business. This is not an easy task in China. Brits tend to be straightforward and open. The Chinese are not. Learning and understanding the objectives and motivations of such parties is part of the relationship-building process. The U.K. company must be patient and persistent in this regard.

A thorough due diligence is required in choosing partners, suppliers and resellers with whom to work in China. Even though the sources of information and tools available in the U.K. make it much easier to investigate the backgrounds, histories and track record of potential partners, suppliers and resellers, finding the right relationships in the U.K. is still very difficult. Such a task is even more difficult in a foreign environment like China. Although these same due diligence tools are not available in China, certain sources of information are useful. For example, local government officials can be helpful in this regard, as can other organizations interested in protecting foreign investors. The U.K. State Department, Commerce Department and other U.K. government agencies located in China and elsewhere can provide valuable insight. Prior relationships with customers, academics, suppliers and others can be leveraged when investigating a potential partner or reseller. Information obtained should not be taken at face value but must be checked and rechecked for accuracy. Finally, the U.K. company should consider evaluating multiple partners. There is nothing like a competitive situation to illicit cooperation. In its desire to move forward, the U.K. company must be patient, do its homework and not rush into the wrong relationships, ensuring that thorough due diligence is conducted on any prospective partner, supplier or reseller.

Internalize Chinese Cultural Values and Ways of Thinking.

It is no surprise that the Chinese have a different value system than Brits. That value system dramatically affects how the Chinese think and filter information. In order to develop beneficial relationships and avoid problems and misunderstandings, an understanding of Chinese values is highly recommended. The difference between the Chinese and Brits value systems is dramatic. For example, Brits place great value on the individual. The Chinese place high value on the group or collective. The concerns of one individual are of little importance. Brits tend to be more egalitarian emphasizing equality under the law and equality in relationships. Relationships among business people in the U.K. tend to be on a “first name” basis. The Chinese place great value in the status of a person and strict hierarchical relationships. Even relationships among family members are not always on a “first name” basis.

Brits tend to be information oriented; the Chinese are relationship oriented. Brits usually break problems and issues down into pieces while the Chinese tend to look at problems and issues as a whole. Brits view themselves as problem solvers who are constantly seeking the right answer or solution. For the Chinese, the process of building the relationship is more important than solving the perceived problem. In China that process often involves exercising the correct amount of deference due to someone with a particular status. Finally, Brits usually take a “reason-based approach” to confronting problems or negotiations. The Chinese on the other hand, love to haggle. This process is not only important because of Chinese “jiejian” (thrift) and desire to always seek a bargain, but also as a process of compromise where each party can hold an equally valid position.

Furthermore, in order to tap into the Chinese way of thinking, knowledge of the national language is a must. Any U.K. company travelling the road to China must possess ample skill in Mandarin Chinese. Additionally, knowledge of the local dialectic is very helpful. For example, the ability to speak Mandarin Chinese will be helpful in Shanghai. However, the ability to speak “Shanghainese” while in Shanghai will increase the likelihood of success.

Appreciate the Chinese Negotiation Style.

As a result of the different value systems, the Chinese negotiate differently than Brits. A thorough understanding of that style, combined with the Chinese value system, will help the U.K. company to be successful in negotiating with the Chinese.

Such understanding will facilitate better agreements and allow the U.K. company to avoid the frustration and animosity that often characterizes U.K.-Chinese business negotiations.

Rarely will the Chinese offer a fair deal. It is up to the U.K. company to ensure that the deal is structured fairly and results in a win-win arrangement. Similar to Section 7, a comparison of fundamental U.K.-Chinese negotiation approaches is the easiest way to understand the Chinese style. Brits seem to be inherently restless and like short meetings. The Chinese require a long courting process characterized by lengthy meetings, banquets and social events. The Chinese are ready to take advantage of a U.K. company's over eagerness or impatience to get a deal done. Accordingly, the U.K. company must quickly demonstrate that it will not be taken as a fool. Once this is established, the second set of negotiations will be much easier. Brits, as a result of their historical development and egalitarian nature, are often informal. The Chinese, in their respect for hierarchy and status, are often formal. Brits are willing to make cold calls. The Chinese are not comfortable with this approach and, instead, draw on intermediaries in negotiations and other business dealings. The American negotiator tends to have substantial authority. The Chinese negotiator usually has limited authority. Top-level Chinese executives rarely bargain. It is not their role. Rather they will focus on evaluating the relationship and the sincerity of the Brits. As a result, the U.K. negotiation team must carefully evaluate the person with whom it is dealing.

Brits are direct and usually do not hesitate to discuss their interests and what they desire to achieve. The Chinese are the opposite. The Chinese approach is very indirect and cautious. American negotiators need to be very patient. They must also be attentive, looking for subtle clues and hints. Determining the Chinese interests and agenda can be likened to the process of putting a puzzle together. Similarly, the Chinese will often use misdirection or make outrageous demands just to see if the U.K. company will agree in its desire to get its foot in the door. In reality, the Chinese are using this tactic to test the American's resolve.

Also, Brits feel more comfortable working on a proposal such as a draft memorandum of understanding or term sheet. The Chinese prefer substantial dialogue. Often when Brits submit a proposal, the Chinese will ignore it or offer to "kan kan" or "yanjiu," i.e., study the proposal. Brits, in their "reasonbased" approach, argue the "pros" and "cons" aggressively. The Chinese use questions to elicit information and learn about the other party. Brits tend to seek to resolve each issue in a sequential fashion. The Chinese, on the other hand, jump from issue to issue and back again. In negotiating with the Chinese, Brits must also be prepared to discuss all issues simultaneously and in a haphazard order. Nothing is settled until everything is settled.

As mentioned many times, Brits tend to have little patience; whereas "endurance" is an important part of the Chinese culture. The U.K. company should always be on guard for statements such as "trust me, this is how we do things in China." This type of statement is a negotiation tactic. Similarly, a U.K. company must be careful in making "goodwill" gestures or acquiescing for the purpose of generating goodwill. The Chinese rarely do this. From the Chinese viewpoint, such gestures are often seen as a sign of weakness and actually cause a loss of respect. Although the Chinese way of negotiating is different, the U.K. company hoping to be successful in China must be flexible and adaptable to the way the Chinese negotiate. It must also be patient and thorough in ensuring that bottom-line business objectives are met and the U.K. company truly understands the Chinese party's intentions.

Understand the Role of Contracts in Business Relationships.

The role of contracts is one of the big differences between Chinese and U.K. business cultures. In the U.K., contracts are a key component of any business relationship. Contracts memorialize the intent of the parties and serve as a tool to ensure that there is a meeting of the minds between the parties. As a result, contracts tend to be very detailed, long and provide solutions to almost every conceivable contingency. The execution of a binding contract tends to be a major milestone for Brits. The Chinese, on the other hand, are much more interested in the relationship than the contract. They often focus on the spirit of the agreement and not the actual language. Trust and harmony are more important to the Chinese than any piece of paper. As a result, for the Chinese, the negotiations often begin once the contract is signed. In addition, the "negotiations" may never end. This common practice has led to a tremendous amount of frustration for U.K. companies.

The Chinese response to lengthy U.K. contracts often take two dissimilar paths. The Chinese may review it, submit modest comments and sign it. They do not take this approach because they agree with the provisions of the contract. They take this approach because the negotiations have not yet begun. Alternatively, in their love to "haggle," they may aggressively negotiate each provision. In such case, the Chinese company may or may not care about the particular provision being negotiated but instead is establishing its power, saving face, adhering to the long process of developing the relationship or just testing the Brits. However, a common tactic used by the Chinese is to insist that the U.K. company's

obligations are very detailed to ensure that the Chinese can get what they want from the agreement, while leaving their own obligations vague and broad. This lack of mutuality in obligations does not trouble the Chinese. This approach gives the Chinese room to maneuver, claim a different interpretation and otherwise avoid performance. Notwithstanding the Chinese attempts to keep contractual provisions vague, the best practice is to clearly set forth in the contract anything that is important enough to affect bottom-line objectives of the U.K. company.

Develop a Comprehensive “China Strategy.”

The key step for a U.K. company is to thoroughly understand why it wants to do business in China. A clearly defined goal needs to be developed followed by a realistic and detailed plan for implementing it. Yet the plan must also be flexible permitting the company to adapt to the constantly changing market conditions. As previously mentioned, the road to China can be difficult. The conventional wisdom is that “in China nothing is impossible, but everything is hard.” Tremendous patience and perseverance are required.

Also worth consideration in the strategy is that China is not a homogenous market. There are significant cultural, language, legal and business differences from region to region within China. For example, business practices differ between Shanghai, Beijing and Shenzhen. Although most people will speak Mandarin Chinese, the local dialects are different. In addition, not only are Chinese suspicious of foreigners but Chinese from one geographic area tend to be suspicious of people from another geographic area. Accordingly, if a U.K. company intends to sell products throughout China, it must be mindful of “guo qing” or the “special circumstances” of each region.

Finally, a key element of the strategic plan for China must be the recruitment of strong local leadership in China to execute the plan. The managers in China should have access to the company’s top leadership in the U.K. The best practice is to initially select a great local team and keep it intact from the initial planning stages through the start-up of operations and growth phase. Given the importance of relationships in China and the benefits derived from the relationships with governmental and business leaders, having a senior leader who knows the history of the company and the relationships developed in China will help tremendously. Often the top management located in the U.K. does not appreciate the competitive nature of the Chinese markets and difficulty of doing business in China. When results do not meet expectations, the natural reaction is to quickly change the management team in China. However, it may be that the initial strategy (usually developed in the U.K.) was defective or expectations unrealistic. A quick change of management forfeits the lessons learned and relationships developed.

Conclusion

China’s evolution to a market economy has been breathtaking. Although tremendous opportunity exists, U.K. companies must be open to continuous learning and adaptability in order to manage the complex environment and the rapid pace of change. U.K. companies must appreciate the challenges waiting for them on the “road to China” and navigate the potholes, traps and other obstacles encountered along the way. Success in China can be especially difficult; it is a place where U.K. managers face exceptional language and culture differences and a constantly changing environment. In any competitive market, turning dreams into reality is challenging, and China’s complexities double that challenge. However, internalizing the lessons described above and exercising patience and perseverance, a U.K. company can achieve success in China.