02.03.2012 19:24

The Basics on Chinese Inbound Investment Deals

Despite the often prominent failures of Chinese companies to acquire U.S. companies, this past year saw even more interest in outbound investment

By Andrew Ross

An accelerating number of Chinese companies are engaging in acquisitions and joint ventures in the United States and while it's generally understood that a large number of other Chinese companies are also considering doing so, many still hesitate.

The first point to note is that the rate of deals is increasing, and is doing so dramatically. A second point is that as a percentage of the total number of deals, small to medium size deals make up the majority, although there are a few larger ones, and the buyers are generally not SOEs. Third, the industries of the acquired companies cover a broad range, from technology, apparel, consulting services, auto parts, hotels and many more.

In 2011, several Chinese companies announced their intentions to enter into deals in the U.S., including Shanghai Pharmaceuticals, with its publicly stated reasons being to seek new drugs to expand its product line and noting declining overseas prices and a strong Yuan, Bright Food Group, China National Materials Co. (Sinoma) and Fosun Group, which stated it is looking at consumer brands. Many Chinese companies are going global in the U.S., more and more will be doing so, and for those Chinese companies for which this makes sense and which proceed to do so, they will be in very good company.

So what are some of the strategies, procedures and lessons on pitfalls that can be garnered from recent deals?

Perhaps one of the most important points regarding engaging in transactions in the United States is to recall the reaction of many Chinese businesses when foreign companies came to China and sought to dictate that deals in China be done in the same manner as in those companies' respective homelands. This generated ill feelings and often did and can easily result in failure in a deal. The same is true in the United States. Companies from many different countries make acquisitions in the U.S. all the time, and one of the accepted norms is that the deal will be done in "U.S. style."

While not successful on occasion, the advisor for the U.S. company looking to be sold (especially a "hot" company) may seek to create an auction for the company, thus seeking to maximize the price and otherwise obtain the most favorable terms. Even if they do not succeed in doing this, they will generally seek to have the process move as rapidly as possible. Prospective buyers who are unwilling to follow an auction process when established or move too slowly are simply left behind. An important aspect in dealing with this is to be prepared. This means having done industry and market analysis in advance so as to be able to readily determine one's interest and willingness to devote the necessary resources to explore the deal, and have ready or be able to quickly assemble a team of qualified Chinese and U.S. advisors.

• 1

02.03.2012 19:24

The Basics on Chinese Inbound Investment Deals

Many U.S. businessmen object to the alleged slow deal pace of foreign businessmen (and not just Chinese), thus often giving U.S. buyers an advantage. Timing delays are, of course, a tactic to be considered; however they should only be used as deemed appropriate, such as to express reservations or concerns so as to try and enhance one's bargaining position. However, a buyer should not allow its perceived slowness to cost it a deal it otherwise wants.

While most people properly say "a deal is not done until it is done," in many U.S. negotiations the same often is not true of individual issues. Once an issue is resolved, it is generally not renegotiated absent special circumstances. A party which acts contrary to this undercuts its counter-party's trust in it.

There is great significance in the U.S. placed on the transaction contract, as each party seeks to maximize its benefits and protections. As a general rule, legal counsel for a U.S. party, will seek as much protection for its client and clarity in the terms of an agreement as possible. This can be especially important for a buyer or investor. This often means lengthy detailed contracts, and also emphasizes the need for the parties to make decisions relatively quickly with respect to the many points involved. In fact, one view is that many U.S. business persons and their lawyers will only encourage ambiguity in an agreement if they think that addressing the ambiguity in the negotiations would result in it being resolved contrary to their interests or if they think they will have greater negotiating leverage on the point once the agreement is signed or the deal is consummated.

By having a contract be as detailed and precise as possible, the likelihood of a dispute is reduced. This is augmented by the fact that in the U.S. there is a very substantial body of court rulings and laws which help determine what a particular contractual phrase will mean in a particular context, thus creating even greater potential certainty. Finally, it should be recognized that other than private arbitrators and mediators and the courts – all of which are objective but the last of which is slow – no governmental entity or person such as a governmental bureaucrat plays a meaningful role in resolving contractual disputes.

While concerns abound over the possible legal burdens that Chinese companies face in the U.S., there are many reasons for Chinese companies to go global, and in particular to do so in the United States.

This piece is an abridged version of a paper titled, "Acquisitions by Chinese Companies in the United States: The Case for Moving Forward Now."