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I. INTRODUCTION

China was a late entrant in the competition for foreign investment. The nation faced enormous challenges in 1979 to become accepted as a credible investment partner. China had to create a basic investment framework for private businesses to operate within a socialist culture. Foreign and Chinese partners in the early joint ventures had to cope with many contradictions and delays. Neither side had experience to guide it. Nevertheless, investors were drawn from all over the world by China's immense domestic market, its low-wage rates, technical skills, natural resources, and an apparent commitment to reform.

After many setbacks and initial frustration experienced by some investors, foreign investment in China has grown rapidly in the past decade. Most investors are satisfied with the progress of their ventures, and feel they have accomplished their goals. Following a slow start, overall foreign investment in China (both utilized and contracted) more than doubled in 1984 and came close to doing so again in 1985. By the end of 1987, the Sino-foreign enterprises in China had earned over $6 billion in foreign investment. The growth trend continued throughout 1988, despite the economic retrenchment of domestic capital investment. A total of $4.03 billion in direct foreign investment was pledged and approved between January and November 1988, an increase of 45% over 1987. Utilized investment was $2.13 billion, a 60% increase over 1987.

About 11,000 foreign investment concerns, including equity joint ventures, contractual joint ventures and wholly-owned foreign ventures, have been established in China. United States investors now account for about 14% of the total. Over 400 projects involving direct investment, with a figure exceeding $3 billion, have been initiated by the United States, making it the second largest foreign investor in

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China, next only to the Hong Kong-Macao region.

The first foreign investors in China learned many lessons from which present and future investors can benefit. Some of them moved in too early and too eagerly, with too little preparation. Consequently, they soon became frustrated and disillusioned. Those who were committed to remaining in China for the long-term had more realistic goals, and moved more methodically and patiently to establish solid relationships for the future in China and the Pacific Basin.

II. THE SURVEY

I participated in the organization of a landmark study, in 1987, of foreign investors' experiences in China. The report was jointly published by the International Trade Research Institute of China and A.T. Kearney Management Consultants of the United States.[1] The study consisted of a comprehensive survey of a large number of manufacturing, equity joint ventures involving investors from the developed world who had a minimum of one year's operating experience in China. A further study was conducted in 1988 to check the improvement of the investment environment and the operations of these joint ventures.[2]

The focus of the studies was the investment objectives of both Chinese and foreign partners—their independent evaluations of the operating results of the joint ventures, the overall investment climate, and their major operating concerns. A comparison of the respondents' views on certain key subject areas would greatly help discern trends subsequent to the 1987 study, and aid those making future investment decisions.

A. *Operating Results*

When asked to compare operating performance to plan, the majority of the respondents said they were satisfied with their results in 1988. The respondents confirming satisfactory performance in 1988 increased to 91% from 60% the previous year. Those reporting serious difficulties fell from 15% to 9%, and the group which had responded "too soon to tell" in 1987 completely disappeared. The responses show that performances on both the Chinese and foreign sides of joint ventures are improving.

Fifty percent of all respondents in our 1987 survey reported they

1. A.T. KEARNEY MANAGEMENT CONSULTANTS & INT'L RESEARCH INST. OF THE PEOPLE'S REPUBLIC OF CHINA, MFG. EQUITY JOINT VENTURES IN CHINA: A PROGRESS REPORT AND EXPERIENCE GUIDE (1987).

2. A.T. KEARNEY MANAGEMENT CONSULTANTS & INT'L RESEARCH INST. OF THE PEOPLE'S REPUBLIC OF CHINA, MFG. JOINT VENTURES: AN UPDATE (1988).

exceeded target figures with respect to returns on investments, while 40% met their target, and 10% fell below target. In contrast, 64% reported improvement of returns in 1988, and 9% reported no change from the previous year; 27% were not willing to disclose this information. The obvious improvement in returns has resulted, at least partially, from the combined effects of the following factors:

1. Real increase in urban consumer income, in the range of 2% to 4% each year;
2. Emergence of an "upper income" group with larger disposable income;
3. 20% growth in the volume of expenditures by tourists;
4. Considerable protection for joint ventures against imports, introduced for key products in 1987; and
5. Substantially improved domestic marketing for established joint ventures, subject to their ability to deal with the foreign exchange balance problems.

B. *Foreign Exchange Balance*

The largest problem for joint ventures, aimed primarily at the domestic market, is meeting foreign exchange requirements. There have been some improvements in this area in the past year. The problem, however, still seriously retards the further growth of many joint ventures. In the 1988 survey, 52% of the respondents retained a deficit in foreign exchange, 18% reported a surplus, another 18% met their needs, and 12% had no foreign exchange revenue at all. Despite various remedial measures implemented by the government, it is still naive to enter China's market without a clear strategy for dealing with foreign exchange requirements. "Fire-fighting" in a shortage situation is expensive and can be highly disruptive.

C. *Operating Concerns*

The latest survey showed some changes in the order of relative significance of major operating concerns to foreign investors:

Rank 1987/88	*Operating Concern*	*Rank 1986/87*
1	Raw material/components	1
2	Joint venture/autonomy	3
3	Operating costs	6
4	Finance/borrowing	5
5	Implementation of laws	4
6	Foreign exchange balance	2
7	Management quality	7

The number one concern for joint ventures already in operation is domestic raw materials, which are in short and irregular supply, typically suffer quality deficiencies, and are subject to price escalation. To deal with this concern, the central and local governments have made substantial efforts to organize more integrated supplier networks for major joint ventures. They are providing foreign exchange to export-oriented ventures for imported raw materials and components, while investing heavily in upstream sectors.

Joint venture autonomy remains a major concern, indicating that joint venture management is becoming more entangled with outside interference while increasingly more day-to-day business decisions must be made. Nevertheless, the over-all management reform in the domestic economy will allow this issue to decline slowly in importance among investor concerns.

Operating cost is a rising concern due to three adverse trends in the cost of external services, as well as materials: (1) the shortage of power and transportation, producing downtime and delays; (2) the higher costs of imported commodities (such as steel and copper); and (3) the general upward pressure on all domestic costs associated with inflation and reduced infrastructure subsidies. According to joint venture managers, labor costs have also increased in nominal terms. The real cost of labor appears to have decreased, however, when gradually improving labor productivity is taken into account.

D. *General Environment*

While much remains to be accomplished, particularly in clarifying the practical implications of recent structural changes and economic retrenchment, our survey respondents believe the investment environment has improved considerably. The 1987 Provisions to Encourage Foreign Investment were perceived as effective by 90% of the respondents, while only 10% believed them ineffective. In addition, 64% of the respondents thought that trends in the investment environment were better, while 36% felt they remained the same as before. Most managers evidently perceive the problems pertaining to infrastructure to be a consequence of dynamic growth. Although annoying, the problems are considered by the managers to be short-term and increasingly manageable.

III. CHARACTERISTICS OF FOREIGN INVESTMENT IN 1988

The following characteristics can be detected from the foreign investment situation in 1988:

1. Expansion of the open economic regions in the coastal ar-

eas. Apart from the four Special Economic Zones and fourteen coastal cities, the counties included in the open regions have increased from 144 to 291; the newly added areas equal to the total size of the open areas approved in the previous nine years;
2. Further reduction of taxes and relaxation of the criteria for qualifying for these tax benefits;
3. Granting the most favorable policies to Hainan province to make it the largest special economic zone in the country;
4. Enlarging the approval authorities of various provinces, municipalities and localities to further simplify the approval process for investment projects. About sixteen provinces and municipalities are given authority to approve projects with total investment over $30 million instead of the previous $10 million limit; other localities now have authority to approve $10 million instead of $5 million;
5. Creation of more foreign exchange swap centers to amount to forty provincial level centers and fifty secondary local centers. The foreign exchange sold by joint ventures in the first half of 1988 exceeded those bought by about $130 million, showing a better foreign exchange situation for most joint ventures;
6. The approval in the past year of more wholly owned foreign ventures, partly owing to the credit squeeze for most domestic enterprises. Approval was given to 240 of these ventures in 1988, a six-fold increase over 1987 and 30% more than the combined preceding nine years. Total investment value involved was $290 million.

It is obvious that many obstacles still have to be removed before further investment, especially strategic investment, can occur in China. Concerns of foreign investors need to be addressed with continuing efforts. Chinese and foreign investors need to work together to improve their strategies, and their management and partner relationships, while the government will have to make further efforts to improve the investment environment.

IV. The Need For Realistic and Systematic Strategies

A recent study on United States manufacturing competitiveness indicated that companies with international operations generally enjoy a greater competitive advantage because of their international awareness and exposure to foreign competition abroad. These companies undertake more efforts to improve their competitiveness than do their domestic counterparts, and they are more optimistic about their prospects for future competitive advantage against foreign competition in the domestic market. Taking action now to develop options in China is one of the steps that can help a company become a greater competitor in all markets in the 1990s.

China's size, complexity and importance demand special attention in a company's long-term plans and strategies for entering that market. Lessons need to be learned from the early failures caused by the hasty, unprepared and unsystematic approaches taken by many investors. Blaming the external environment is not a remedy in itself. Given the same climate and condition, different investors could achieve significantly different results. The difference stems from the universal truth that the quality of people, the strategy adopted, and enterprising spirit and business sense are integral parts of business success.

Many investors tend to ignore these basic business principles. They have come to China with their own perceptions and beliefs, which are often untested and spontaneous, and result in many unwise decisions or hasty actions. In the end, they succeed in brewing only failures and frustrations.

Based on our extensive research on foreign investor activities in China and my personal experience in both studying and participating in joint venture processes, the following key factors could potentially benefit future investors in developing a strategy for China.

A. *Compatibility of Objectives*

Many foreign investors overlook the fact that the objectives of their potential Chinese partners may be different from their own. Typically, the Chinese partners are interested in joint ventures with the object of: (1) gaining export opportunities through their foreign partners' international marketing networks; (2) obtaining advanced foreign technology; (3) gaining more autonomy in decision-making because of the joint venture's relative independence from government controls; and (4) obtaining badly needed capital investment.

Foreign investors, in comparison, often have the following objectives in mind when considering China as an investment opportunity: (1) entry into the vast domestic market; (2) low-cost production base for regional expansion and market penetration; and (3) strategic positioning for long-term implications.

It is obvious that the primary goals of the two sides tend to be in conflict with each other and that these differences often affect the setting of priorities and the steady relationship between partners. Before committing themselves, foreign investors should seriously consider these conflicts, by carefully investigating the real motives and objectives of their Chinese counterparts, and by explicitly stating their own objectives so that no misconceptions or unrealistic anticipations could undermine the relationship. Foreign investors should also be prepared to adjust their own objectives and goals to match the realities in China, if the investment undertakings are of strategic significance to them.

B. *Research and Planning Before Action*

The common-sense business approach of researching and planning before taking action is often ignored by foreign executives when they deal with investments in China. Instead, they think that China should be treated as a special case.

Many foreign investors assume that their companies are household names worldwide and that their technological superiority would certainly make Chinese businessmen eager to join them. Necessary promotion and education are ignored. Surprisingly, some world-renowned corporate names and brands, such as AT&T and Xerox, are unheard of or mistaken by the Chinese consumers and business communities.

Some investors complain about the amount of effort and time they have to commit before discovering that their efforts have failed. This dissatisfaction is often caused by an investor's inability to obtain accurate and sufficient information prior to the search, a lack of understanding of the competitive situation, and hasty actions based on unfounded assumptions.

Many investors dealing with Chinese companies abandon normal business principles and procedures, believing them unnecessary in such an immature market. Chairmen and CEOs of corporations often personally take initial exploratory tours to China, dining and toasting in the glamorous Great Hall of People, and leave China with a handshake agreement on a joint venture. The puzzled operational men are then ordered to work out the details, starting where the often misinformed bosses have left off.

Very few foreign investors consider spending the time and money for a thorough investigation into the viabilities of a proposed project before committing extensive corporate resources in vain. Those who do investigate and come to China with a well-defined strategy create more successful joint ventures.

C. *Serious Presentation and Building of Trust*

Many foreign investors take for granted that they possess advanced technology, an important worldwide market share, and reputable business ethics. They often feel frustrated if their Chinese counterparts do not appreciate their superiority and have difficulty trusting the foreign investors. This is especially true for the negotiation of prices and technology fees.

The more thoughtful investors, however, are willing to spend the time to educate Chinese partners through a long process of serious presentations, first-hand exposure to their technological superiority, and a persistent effort to build good personal relations. Foreign investors should never take their superiority for granted. It is not just a question of ego; the lack of trust of foreigners is deeply rooted in the dark memories of modern Chinese history.

D. *Focus of Efforts and Flexibility*

Limited resources do not permit battling too many issues through the negotiation process. Therefore, investors should set priorities for their goals. No deals could be struck in China without compromise. The question remains, however, where should the compromises stop.

The experiences of some successful investors prove that focusing efforts on extremely important issues and being prepared to compromise other issues are sound negotiation tactics. These efforts need to be planned well in advance to achieve a systematic approach. The compromises help demonstrate flexibility and good will; in return, the primary goals of the partners are secured. Normally, issues such as export commitment, management control, and technology payment are the most difficult to negotiate. If an investor wants to get a better deal, he needs to determine where he is willing to concede points well in advance, not afterwards.

In order to achieve the goals already set, tactics such as team-building are essential in order to win the support and understanding of the partners. Some investors start involving their Chinese counterparts in the decision-making process by jointly test marketing their products in China, before a joint venture agreement is reached. Thus, the two parties already work as partners before a contractual relationship is cemented. This process provides an excellent opportunity to build mutual understandings, trust, appreciation of the technological and management merits of the partners, and the practical experience of working together. This "pre-marriage" relationship often helps remove obstacles for the settlement of major issues.

E. *Corporate Commitment*

Many joint ventures fail because of a lack of corporate commitment or a change of direction by corporate management. The initial long-term objectives of the top managers of a corporation often clash with the relatively short-term goals of the on-loan managers, due to the motivation and promotion mechanisms of the investing firms. Often, the original long-term objectives conflict with a spontaneous greed for short-term gains, thus affecting the management priorities of the joint venture business.

In terms of resources, a weak link between the Chinese joint venture and the foreign corporate headquarters is common; corporate support in terms of people, technical assistance and marketing help is often lacking. These deficiencies seriously undermine the long-term stability of the established ventures and the confidence of Chinese partners. It is worth noting that United States managers have the shortest average terms of service in joint ventures in China — only six months — compared to one year for West European managers and two years for Japanese managers. The constant change of people and a shortage of quality managers are already causing problems for some joint ventures.

V. Conclusion

A strategy is needed for China, tailored to suit the realities of this unique market. Naiveté, superficial thinking, and spontaneous action should give way to common sense, solid planning, and strategic approaches. Tomorrow's winners in China's investment scene will be those with greatest foresight, enterprise, and "can-do" spirit. An opportunity exists in China today for investors who are systematic, resourceful, patient, courageous, and willing to learn from the experience of others.