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To Ride Chinese M&A Wave, Firms Need More Than An Office

By **Kelly Rizzetta**

Law360, New York (September 12, 2012, 8:00 PM ET) -- Against the backdrop of a worldwide recession and ongoing European debt crisis, China has upped its outbound mergers and acquisitions activity fivefold since 2005 to \$63.1 billion last year, according to new research from [Squire Sanders](#), signaling a long-term trend that will require law firms to field multifaceted, culturally savvy teams to cash in on the evolving deals market.

"It's all of the above. In addition to just having a physical office [in China], firms need people who understand [Chinese clients'] cultural background, really understand their perspective," Mao Tong, a Squire Sanders cross-border specialist based in Hong Kong, told Law360 in an interview.

For instance, Mao noted, Chinese investors tend to operate with a much longer-term horizon than their Western counterparts. In the 12-month period that ended in June, that attitude has helped Chinese companies notch a record 22 transactions worth \$1 billion or more at a time when risk-averse Western investors are tightening their purse strings, according to a report on China's outbound deals market that Squire Sanders published Tuesday as part of its global M&A series.

Previously confined to the energy and natural resources sector, cash-rich, government-backed Chinese companies are branching out and smartening up. Their shopping lists include consumer-focused businesses, industrial and infrastructure companies, private equity portfolio enterprises, auto parts makers, medical equipment manufacturers, and more — both for the value of the assets and, perhaps even more importantly, to get a leg up in terms of business know-how and technology, Squire Sanders global practice group leader William Downs told Law360 recently.

"We're just seeing more activity [by Chinese companies] in the west," Downs said. "Some of that is acquisition, but some of it is entering the market, buying something to be more engaged in the market, learning about how certain kinds of businesses operate in a more heavily regulated market."

The outbound deals market in China is a mix of the familiar and the novel, according to Squire

Sanders' report.

Chinese companies are still most interested in strategic acquisitions of raw materials to fuel their humming power and steel plants. Massive state-owned businesses — such as China Investment Corp., [PetroChina Co.](#) Ltd., China Petrochemical Corp. and their ilk — still dominate the M&A scene. And China is still paying close attention to emerging markets in Latin America, Central Asia and Africa.

But significant changes are taking place in the way Chinese companies broker deals, according to Squire Sanders.

Chinese companies are operating in more sophisticated markets lately, having increased the amount of business they do in North America and Western Europe from 50 percent of total deal value for the 2005-2010 period to 66 percent in the last two years, the global M&A report found.

Two of the biggest deals to come out of China this year are Bright Food Group Co. Ltd.'s £1.2 billion (\$1.9 billion) bid for a 60 percent stake in the popular British cereal company Weetabix Ltd. and Dalian Wanda Group Co. Ltd.'s \$2.6 billion acquisition of [AMC Entertainment Holdings Inc.](#) — both consumer businesses purchased from private equity owners, Squire Sanders noted.

Investment funds are making small but noteworthy inroads into a deals market previously exclusive to strategic acquirers, accounting for \$3.7 billion of last year's deal volume — up 16 percent from 2010. Hong Kong bidders, traditionally seen as more sophisticated than their mainland counterparts, lost ground to companies on the mainland in terms of number of outbound deals generated, Squire Sanders found.

At the same time, private companies facing stiff competition from the government-owned conglomerates on the mainland — which, in turn, enjoy teacher's pet status among state-owned banks — have learned to take their business to Hong Kong, where they can raise their own M&A financing on the stock exchange, Mao pointed out.

Chinese companies have been engaged in outbound trades for the last couple of decades, but the idea of Chinese companies truly "going global is still a very recent phenomenon," according to Mao. That said, lawyers have to act as both advisers and educators.

"There are huge cultural gaps in terms of due diligence," he told Law360. "[Chinese companies] are still on the learning curve to learn how to acquire Western companies ... how to handle integration, how to manage companies [in which the buyer does not have a] wholly owned interest. All of these require lawyers and professional advisers to close the gap and play the bridge role."

That role requires law firms to invest a good deal of capital in professionals who speak Mandarin and office space in Chinese financial centers, necessary steps for firms looking to get serious about Chinese outbound work, according to Downs.

"Being able to communicate [between lawyer and client, as well as between the parties] in a meaningful way is important, and to do that, one has to have an understanding of the culture of Chinese businesses and the way they work that I think does make [having] a Mandarin-speaking staff quite important, as well as a track record of working with companies in their home country," Downs told Law360.

Even if firms don't have room on the balance sheet for major investments like a brick-and-mortar office, they can begin to integrate themselves into the Chinese legal scene.

"Whether through a physical office in China or an alliance with a local law firm, there are ways to connect to this market," Elizabeth Fei Chen, a partner in [Pryor Cashman LLP's](#) corporate and China practice groups told Law360 via email.

Law firms looking to penetrate the market can "test the waters" by attending industry conferences in China, giving them boots on the ground, albeit temporary, that can be parlayed into partnerships with people who possess that key "understanding [of] or connection" to the deals market.

While it's impossible to predict the future, Downs of Squire Sanders estimates that such investments will pay off since the boom in outbound M&A does not appear to be a "flash in the pan."

"Chinese companies that we talk to are very proud of being the size that they are, [and they] want to make an impact not just in a trophy kind of way, but in a very serious way," Downs said.

Plus, they have the cash and human resources to back up their lofty talk.

Chinese companies are replete with haigui, or in English, "sea turtles," a slang term that refers to highly sought-after prospects who study at foreign universities, then bring their degrees and expertise home where they put them to work for Chinese companies, according to Fei Chen.

And of the more than \$3 trillion China holds in foreign exchange reserves, \$1.7 trillion is in U.S. Treasuries, Mao estimated.

"These are huge numbers," Mao said. "From a central government perspective, China is really trying to find ways to ... get a better return on their dollar.

"We're at the beginning of the trend," he said.

--Editing by John Quinn and Katherine Rautenberg.
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