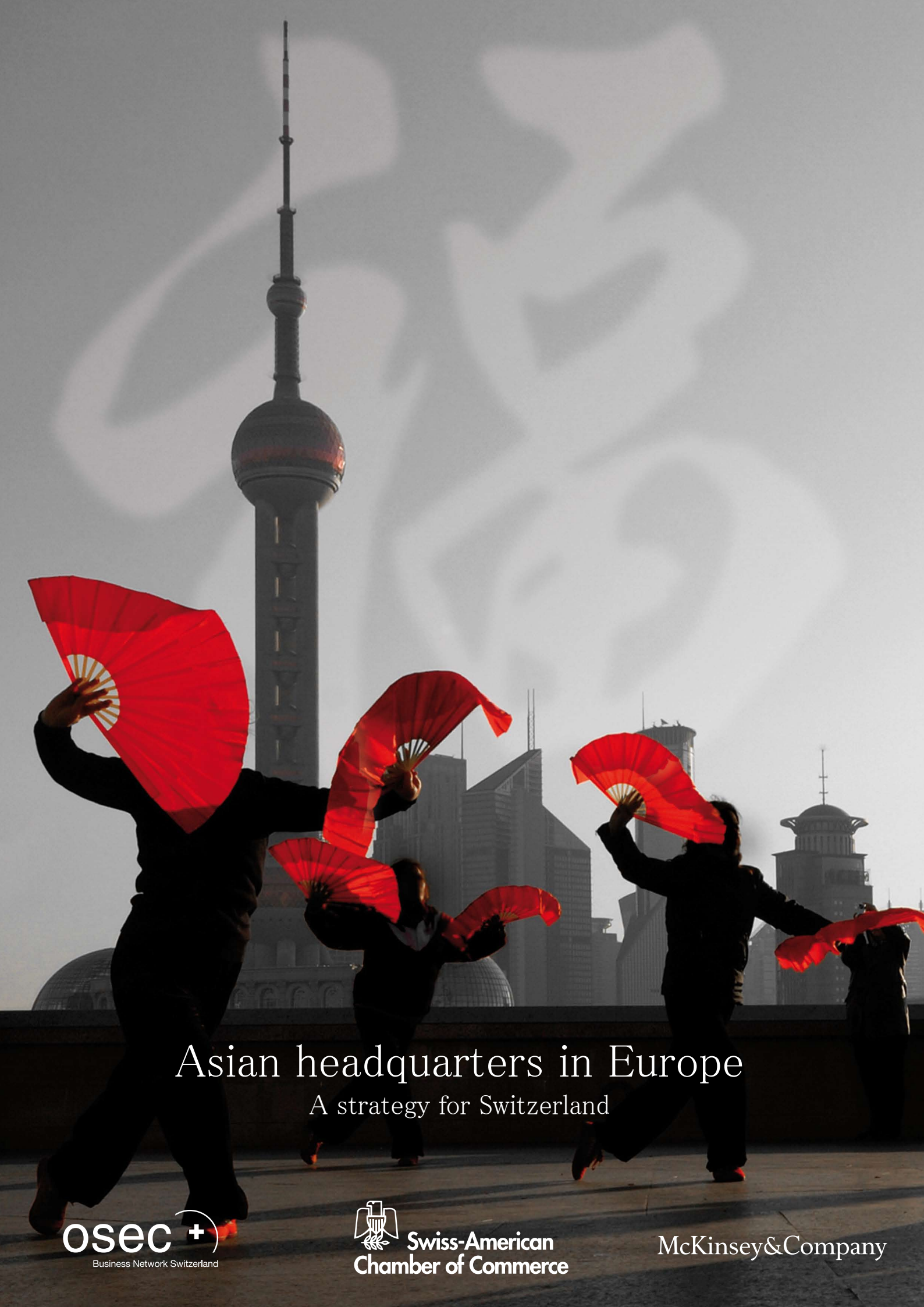

Asian headquarters in Europe

A strategy for Switzerland

osec
Business Network Switzerland

Swiss-American Chamber of Commerce

McKinsey&Company

Asian headquarters in Europe

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McKinsey&Company

November 2008

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FOREWORD

Over the last decade Switzerland has developed into a prime headquarters (HQ) location for multinational companies. Companies such as Procter & Gamble, IBM, Dow Chemicals, General Motors, Nissan, Google, Kraft Foods, and Amgen have chosen Switzerland as a location for important operations and regional HQs. With its high quality of life, central location and competitive taxes, among other advantages, it has attracted over 180 regional headquarters of large foreign companies in the past 10 years.

The international expansion of Asian companies may represent the next wave of foreign companies setting up operations and regional HQs in Switzerland. Asian economies are now outperforming North American and European countries and their leading companies are rapidly gaining significant positions in the world economy. So far, with the exception of multinationals from Korea and Japan, Asian companies have focused their expansion largely on their domestic and regional markets, but things are changing fast and Asian companies are increasingly looking to establish operations and HQs in Europe.

For Switzerland, this trend offers a significant opportunity as a location for these companies' regional HQs – with a potential to attract more than 120 regional HQs, to add 2–4 percent extra GDP, and to create 55,000–120,000 additional jobs over the next ten years. However, to capture this opportunity in the face of fierce competition from other European countries, Switzerland needs to take action so as to be able to offer to these companies what they are looking for.

In particular, the most pressing need is to ensure that Switzerland gets on decision-makers' shortlists, as Asian CEOs currently have very little awareness of Switzerland as a potential HQ location. Other areas that need to be addressed include facilitating the process for establishing an HQ in Switzerland, and maintaining and enhancing Switzerland's competitiveness as a business location in the years ahead.

This report identifies the scale of this opportunity for Switzerland, describes the decision-making process that Asian companies employ when setting up regional HQs, and develops recommendations for capturing the full potential of this next wave of companies expanding in Europe. In the context of the report, the term HQ may cover a range of set-ups, including the main headquarters, or the European or EMEA[1] headquarters; it may also include a significant presence of sales, research and development, or other functions.

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1 Europe, the Middle East and Africa

SWITZERLAND IS A PRIME LOCATION FOR INTERNATIONAL HQs

Overall, Switzerland is now regarded as one of the most attractive HQ locations in Europe and worldwide. A survey by Ernst & Young of 98 foreign companies that ran projects to set up or relocate HQs in Europe between 1999 and 2004 found that Switzerland had the best investment climate for European HQs, from both a cost and a benefit perspective.[2]

Switzerland also scores very well in surveys of global competitiveness, such as the WEF Global Competitiveness Index, where it ranked second out of the 134 countries surveyed in 2007.[3] And more than half of the companies that move to Europe or relocate in Europe select Switzerland as their location, as shown in a survey in 2002 of fifty Top-500 companies.[4]

Many foreign companies have already chosen Switzerland as their HQ location

Many foreign companies have already established their international or regional HQs in Switzerland. Our research shows that over the last ten years over 180 international companies have set up HQs or significant operations in Switzerland. Among them are 89 Forbes 2000 foreign companies, including firms such as IBM, General Motors, Kraft Foods, Phillip Morris, Procter & Gamble, Dow Chemicals, Amgen, Baxter, DuPont, Nissan and Google. Companies from the US in particular appreciate the many advantages offered by Switzerland as an HQ location. To date, over 150 US companies have a presence in Switzerland, primarily concentrated in the business agglomerations of Zurich–Zug and Geneva–Lausanne. The pioneers included Hewlett Packard and Dow Chemicals, both of which set up their European HQs in Switzerland before the 1980s, in the cantons of Geneva and Zurich respectively. US companies have since continued to set up regional HQs in Switzerland. Whereas Switzerland tends to attract the global headquarters of European companies, US companies typically establish regional (usually EMEA) headquarters. Asian companies, for the moment, are still in a minority, with fewer than 10 regional HQs currently established in Switzerland, most of which belonging to Japanese companies.

Switzerland's attractiveness has increased further in recent years

Several surveys have identified the reasons for Switzerland's attractiveness as a location for HQs.[5] Apart from its central location, they point to sociopolitical elements, such as its stable political environment, as well as to a competitive corporate tax rate and system. A liberal labor market and a very well educated workforce complement the country's robust infrastructure. In addition, Switzerland's academic institutions – with their world-class capabilities for research and innovation – support its well-established industry clusters, such as financial services, pharmaceuticals, chemicals and precision engineering.

An outstanding quality of life and a very safe environment further enhance these significant advantages. Mercer's 2008 quality of living survey ranked three Swiss cities in the top ten – Zurich at no. 1, Geneva at no. 2 and Berne at no. 9 – while all three cities are ranked second, equal (out of 215) for "personal safety".

2 Ernst & Young (2005)
3 World Economic Forum (2008)
4 Arthur D. Little. (2002)
5 See, for example, Swiss-American Chamber of Commerce & The Boston Consulting Group (2007); World Economic Forum (2008); Mercer (2008)

Moreover, the WEF Global Competitiveness Index indicates that Switzerland has become more competitive in recent years, both absolutely and relatively (See Figure 1).

Figure 1

Global Competitive Index ranking of top 15 countries

2002–2008

2002	2003	2004	2005	2006	2007	2008
1 Finland	1 Finland	1 Finland	1 Finland	1 Switzerland	1 US	1 US
2 US	2 US	2 US	2 US	2 Finland	2 Switzerland	2 Switzerland
3 Canada	3 Sweden	3 Sweden	3 Sweden	3 Sweden	3 Denmark	3 Denmark
4 Singapore	4 Denmark	4 Taiwan	4 Denmark	4 Denmark	4 Sweden	4 Sweden
5 Australia	5 Taiwan	5 Denmark	5 Taiwan	5 Singapore	5 Germany	5 Singapore
6 Norway	6 Singapore	6 Norway	6 Singapore	6 US	6 Finland	6 Finland
7 Taiwan	7 Switzerland	7 Singapore	7 Iceland	7 Japan	7 Singapore	7 Germany
8 Netherlands	8 Iceland	8 Switzerland	8 Switzerland	8 Germany	8 Japan	8 Netherlands
9 Sweden	9 Norway	9 Japan	9 Norway	9 Norway	9 UK	9 UK
10 NZ	10 Australia	10 Iceland	10 Australia	10 Australia	10 Netherlands	10 Canada
11 Ireland	11 Japan	11 UK	11 Netherlands	11 Japan	11 Korea	11 HK
12 UK	12 Netherlands	12 Netherlands	12 Japan	12 Netherlands	12 HK	12 UK
13 HK	13 Germany	13 Germany	13 UK	13 Germany	13 Canada	13 Korea
14 Denmark	14 NZ	14 Australia	14 Canada	14 NZ	14 Taiwan	14 Austria
15 Switzerland	15 UK	15 Canada	15 Germany	15 UK	15 Austria	15 Norway

Source: World Economic Forum Global Competitiveness reports 2002–2008

HOSTING INTERNATIONAL HQs BENEFITS SWITZERLAND

International and regional headquarters are beneficial for Switzerland. According to UNCTAD, the establishment of an HQ generates a range of tangible and intangible benefits. HQs provide opportunities for local employment in higher-level managerial positions and help bring international recognition as a prime investment location. Additionally, managerial expertise and other knowledge related to high-level decision-making functions may be transferred to the local workforce. Finally, local R&D is likely to receive a boost if a regional HQ also takes over some R&D responsibilities.[6]

HQs can also help generate new clusters, which can assist Switzerland in maintaining or improving its leading position as an HQ location. Foreign companies with an HQ in Switzerland also provide additional tax revenues (the amount depending largely on the taxation agreement reached with the companies concerned). Lastly, there is also a "pull" effect: in the long term, the establishment of an HQ will attract others of the company's activities to the same country, resulting in subsequent investments in the location.[7]

Macroeconomic impact of new HQs

To quantify the benefits of the establishment of an HQ in Switzerland, we have estimated the expected impact of one new HQ on Swiss GDP and employment, taking into consideration both the primary impact and multiplier effects. We have excluded effects that are more difficult to quantify (e.g., knowledge "spill-over") from our calculations.

Considering both direct and indirect effects, we expect one new HQ to have an overall impact of CHF 75–80 million annually on the GDP of Switzerland and to create 450–500 full-time jobs in the economy.[8]

The impact on tax income will vary depending on the type of company and the applicable tax rates in the canton concerned, as well as any specific tax incentives that the company is accorded. However, a rough estimate of the tax impact per new HQ is in the area of CHF 15 million p.a.[9].

6 UNCTAD (2003)

7 Ernst & Young (2005)

8 We estimate an average direct impact on employment of around 100 FTEs for each new HQ set up in Switzerland. Assuming that HQ productivity can be compared to that of financial institutions, we believe that each new HQ, once fully established, will generate added value of CHF 25–30 million p.a. Beside direct effects on employment and GDP, indirect (multiplier) effects in the range of 350–400 additional FTEs and about 50 CHF million could be generated by direct and indirect suppliers to these new HQs, as well as by the related increase in the income of private households.

9 Estimates based on total historical tax receipts as percentage of GDP (c. 20%)

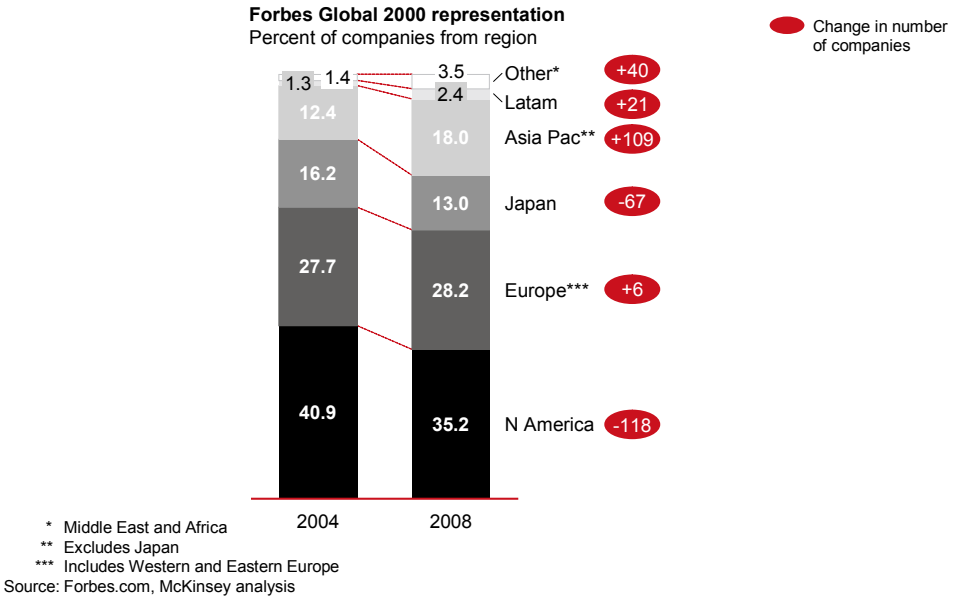
NEW WAVE OF HQs WILL COME FROM ASIAN COUNTRIES

Large multinational companies increasingly decide on the location of their international and regional headquarters on the basis of factors that open up the potential of more than just the home country. Additionally, the growing sophistication of information, communication and transportation technologies enables firms to slice up the value chain of their HQ activities. Companies are thus relocating more and more activities to regional HQs, as they try to optimize the geographic location of each value-adding business activity. The result is the establishment of more regional HQs and the relocation of more HQs.[10]

As growth in Asian economies outpaces that of North American and European countries, Asia's champions are steadily gaining prominence in global markets. Over the past four years, the proportion of Asian companies in the Forbes Global 2000 list has increased by over 40 percent, from 250 companies in 2004 to 359 in 2008. With 81 new entries between them, China, India, South Korea, and Taiwan account for almost 75 percent of this increase (see Figures 2 and 3).

Figure 2

Composition of Forbes Global 2000 list 2004 and 2008

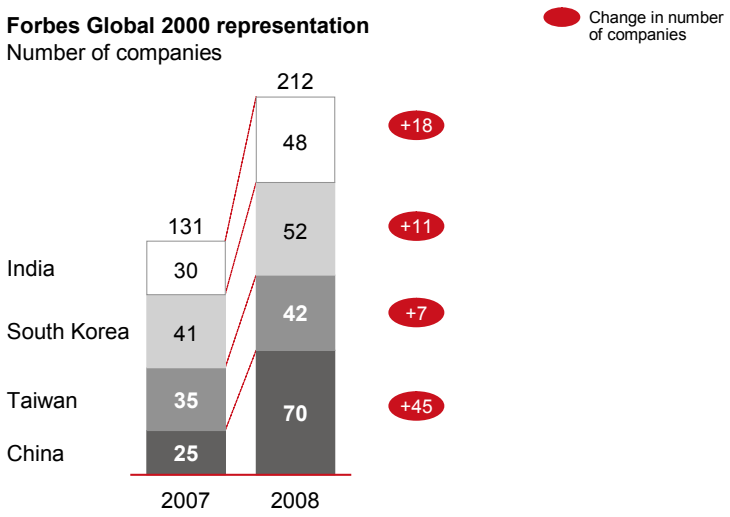


Compared to established multinational firms, international expansion by the top companies in the biggest emerging Asian economies is still relatively limited, with the exception of Taiwan. Taiwanese companies are only slightly behind the global average in terms of their global set-up. China's top 100 companies are the least internationally oriented among the Asian companies surveyed. While top Chinese companies generate only about 11 percent of their sales abroad, the corresponding figure for Taiwan is 48 percent – higher than the global average of 44 percent. Similarly, Taiwanese and South Korean firms have a relatively large proportion of their employees outside the home country, while the corresponding figure for China is close to zero. This reflects the fact that companies in countries with small domestic markets have to expand at an early stage into neighboring or international markets.

10 Holt, J., Purcell, W. R., Gray, S. J. & Pedersen, T. (2006); Birkinshaw, J., Braunerhjelm, P., Holm, U. & Terjesen, S. (2005)

Figure 3

Growth of companies from selected Asian countries

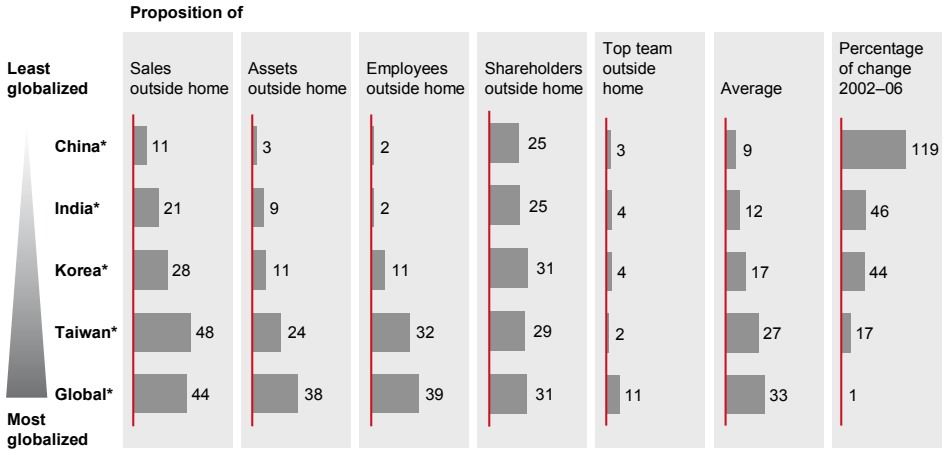


Source: Forbes.com, McKinsey analysis

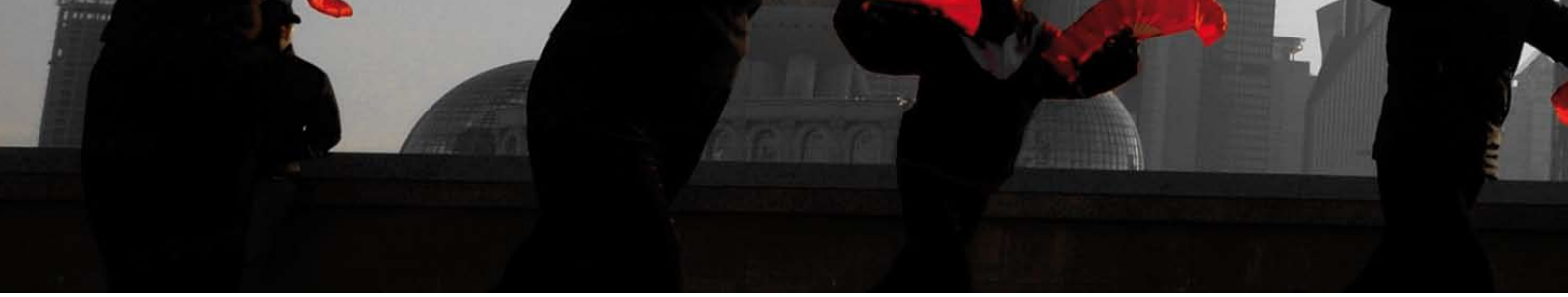
Figure 4

Internationalization of companies in selected Asian countries

Percent



* Top 100 companies based on market cap at year-end 2006
Source: McKinsey analysis



Less than 40 percent of the top 100 companies in China, India and South Korea combined have already established an HQ or a significant office in Europe. South Korea's presence in Europe is already fairly strong, with over two-thirds of its top 100 companies present in Europe. By contrast, fewer than one in five of the top 100 Chinese companies currently have a similar foothold in Europe.

Asian companies are becoming more international

The situation is changing, however; top companies especially in China, India, and South Korea may have started from a low base, but they are now catching up fast.

From 2002 to 2006, the overall rate of change measured across various dimensions of internationalization was 119 percent for China, 46 percent for India, and 44 percent for South Korea (see Figure 4). More specifically, the percentage of world sales has more than doubled for China. Chinese companies have also shown increases on most of the other dimensions, with at least a doubling of the share of employees, shareholders, and top management teams located outside the home country.

Substantial potential from Asian HQs in Switzerland

The growing internationalization of Asian companies offers real potential for the establishment of new HQs in Europe during the coming years. Between 1997 and 2004, Asian companies represented only 5–10 percent of all foreign HQ projects in Europe. By 2004, however, Chinese companies had already taken second place, with 11 European HQ projects.[11] We expect this trend to continue.

Over the next 10-15 years, we believe that between 1,400 and 3,200 companies from China, Taiwan, South Korea, and India (according to the chosen scenario[12]) may consider moving to Europe (see Figure 5).

Most of these companies would come from South Korea and Taiwan, with China and India closely behind. The main industry sectors are likely to be high-tech, consumer goods, and diversified industrials. Taiwan is the leader in high-tech, while consumer goods and diversified industrials are more equally distributed, with South Korea taking the lead (see Figures 6 and 7).

Of all the companies considering moving to Europe, between 120 and 260 companies might establish HQs in Switzerland in this period. This would result in a rise in employment of roughly 55,000 to 120,000 FTEs, or around 1.5–3 percent of Switzerland's workforce as of 2007. And it would increase GDP by between CHF 9 billion and 20 billion, corresponding to 2–4 percent of the country's 2007 GDP (see Figure 8).

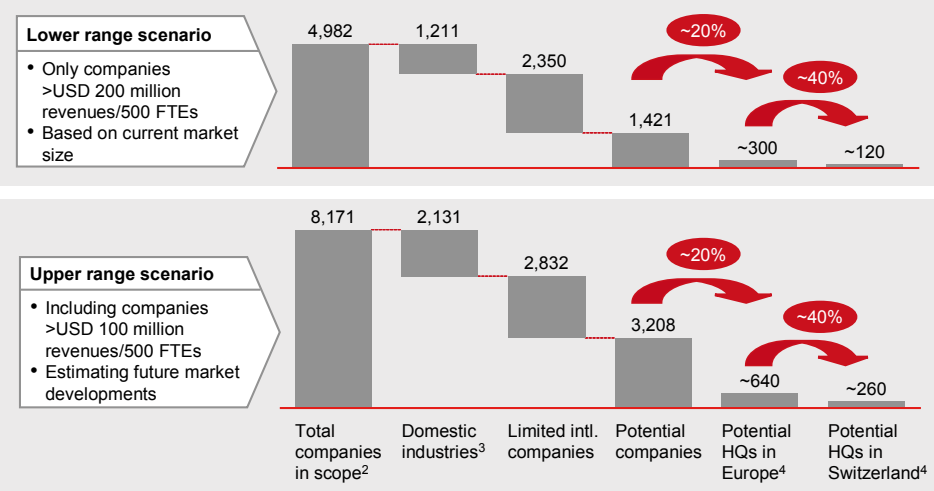
11 Ernst & Young (2005)

12 Lower-range scenario calculated on current size of Asian economies and companies, upper range scenario assuming 4–8% growth p.a. and increased rate of internationalization of companies

Figure 5

Potential Asian[1] company HQs in Switzerland over the next 10–15 years

Number of companies



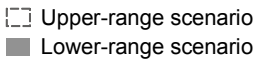
1 China, India, Korea, Taiwan
2 Excluding identified subsidiaries of foreign companies
3 Oil and gas/energy, basic materials, real estate
4 Including moves of HQs from within Europe
Source: One source, Prowess, Bloomberg, press search, McKinsey analysis

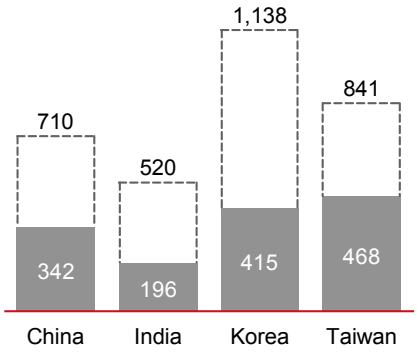
Figure 6

Potential companies by country

Number of companies

ESTIMATES





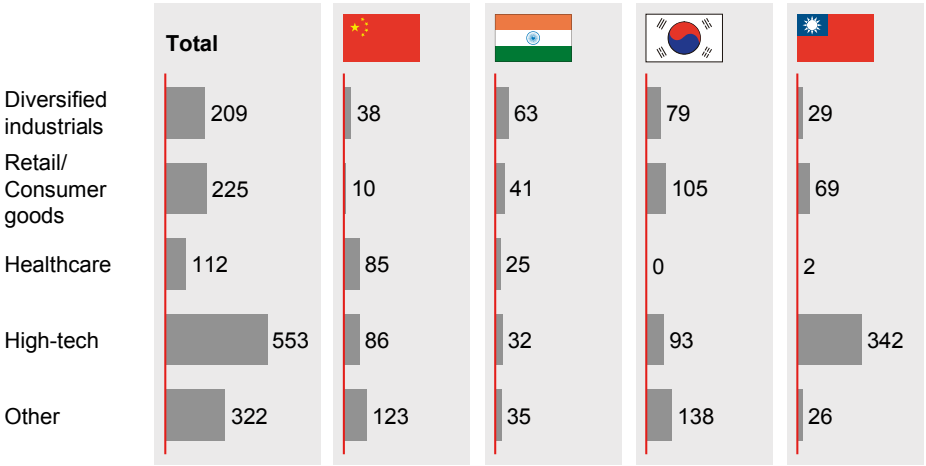
Source: One source, Prowess, Bloomberg, McKinsey analysis

Figure 7

Potential companies by industry

Number of companies

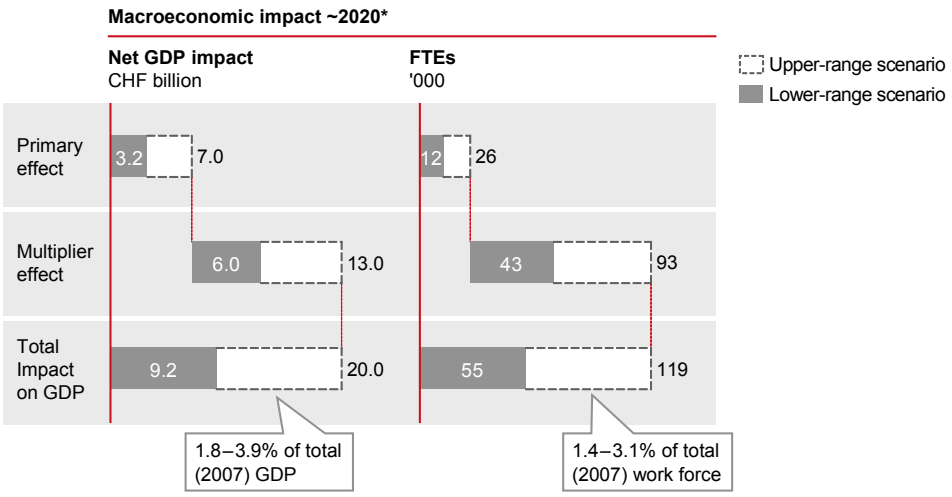
LOWER RANGE SCENARIO



Source: One source, Prowess, Bloomberg, McKinsey analysis

Figure 8

Macroeconomic impact of attracting HQs



* Calculation based on OECD tables for financial institutions
Source: McKinsey analysis based on OECD input-output tables for Switzerland from 2001

HOW DO ASIAN COMPANIES DECIDE ON HQ LOCATIONS?

To ensure that Asian companies find the business environment they need to establish their HQs, Switzerland needs to take account of how such companies decide on the location of their regional HQs. Asian companies sometimes do so differently from Western enterprises.

Chinese CEOs, for instance, conduct business in some markedly different ways from their Western counterparts. A different outlook and career experience shape Chinese CEOs' approach to decision-making. Firstly, reflecting the dynamic and rapidly evolving market environment that they operate in, Chinese CEOs often rely less on rigorous analysis and extensive research to come to a decision. Instead, their decision-making tends to be more spontaneous and flexible. They are more comfortable with responding to industry shifts rapidly and instinctively, but keep a strict focus on holding costs down to ensure competitiveness.

Differences are especially pronounced for CEOs of Chinese State-Owned Enterprises (SOEs), which also happen to be among China's largest and most internationally active companies. Often moving between political and corporate positions, these CEOs pay special attention to political developments and may link strategic decisions to national plans or political events. For instance, they may coordinate their strategic planning with plans outlined in the annual National People's Congress, or to political events such as visits to China by foreign political dignitaries.

Furthermore, given their position at the crux of the symbiotic relationship between state and enterprise, these CEOs characteristically focus strongly on corporate social and macroeconomic goals. With a view to boosting employment, they often emphasize aggressive top-line growth, market leadership and competitive advantage over bottom–line performance or financial objectives. This emphasis often leads them to operate across several different business areas and markets, sometimes leaving certain market niches underserved.

The example of Chinese CEOs shows the relevance of factors that may seem less relevant to a non-Asian decision-maker. For instance, for a Chinese CEO concerned about the political implications of his business strategies, a country's political stance and ties with China's government are likely to be key elements in any international HQ decision. Such a CEO may find it unnecessary to analyze different HQ locations in depth, if he routinely makes transformational decisions intuitively. To tailor our recommendations to the specific needs of Asian decision-makers, we have investigated both the key decision criteria and the decision-making process of Asian companies.

Decision criteria for locating Asian HQs

The main, generally applicable criteria used by companies to decide on an HQ location are fairly well known. The most important factors are proximity to clients, transport and accessibility, the quality and availability of labor, taxation, and the centrality of the location.[13]

However, our research, which also includes around 50 qualitative interviews with Asian CEOs, experts and opinion-shapers, indicates that the decision criteria for Asian companies differ in some respects.

As for Western companies, proximity to the market is a key criterion for Asian decision-makers; this applies both to distribution and main supplier markets. Besides geographical proximity, connectivity to the markets is a fundamental requirement, for Asian companies too. Thus a sound transportation infrastructure is seen almost as a prerequisite. In particular, the future location of an HQ has to have convenient access to a major airport.

Specific to Asian managers, however, is the weight they attach to personal "proof of concept". The presence of already established Asian companies is crucial, as this is seen as evidence that a location is likely to be suitable for their own HQ as well. In the same way, Asian decision–makers tend to rely heavily on recommendations by trusted advisors and personal contacts with local representatives, especially at an early stage. In this context, the existence of a first nucleus of activity, which might be an established distribution relationship with a local agent or representative, is a strong driver for decisions on preferred location.

Another aspect frequently mentioned by managers of Asian companies is the possibility to acquire new skills and to attract "international" talent, which is often seen as a main barrier to Asian companies' ambitions to become multinational.

In terms of the political and business environment, a favorable tax regime is a very important deciding factor, as it is for non-Asian countries. But it is not the only factor. For example, Asian companies also look for a location offering political stability. Chinese companies, in particular, emphasize the importance of stable relations between the host country and the Chinese government, and of high-profile politico-economic exchanges and visits between the two countries. Also of very high importance is the ease of setting-up and conducting business out of a specific location; this involves availability of visas and work permits as well as the existence of a network of professional services – legal, accounting, financial – specialized in supporting Asian companies, such as the local branch of a Chinese bank, or a tax advisor specialized in dual taxation with Korea.

13 Ernst & Young (2005)

By contrast, Asian managers tend to rate the existence of Asian social communities or international schools quite low in their decision criteria. This may be because their families often stay in the home country or only come to Europe for a limited period – this is especially true for Chinese companies, less so for Indian executives.

Finally, a country's native language is perceived as less important, given that English is the common language of business; widespread fluency in English is therefore seen as a definitive advantage.

Decision-making processes in Asian companies

In addition to analyzing the decision-making criteria, we also investigated the processes used by Asian companies in deciding on the location of their HQs. As for any multinational company, the typical process for selecting a target location involves the assessment by a dedicated team of executives of a shortlist of potential locations, usually suggested by the company's CEO or owner. This evaluation is normally based on a series of pre-defined quantitative and qualitative criteria. The final decision, based on this detailed due-diligence process, is usually taken by the CEO or owner. This is particularly true for companies that have already been exposed to and adopted a Western management style.

Companies that follow a more traditional management style tend to give particular importance to "soft" factors such as proof of concept, personal experience or recommendations and peer practice. For these companies, the personal opinion of the CEO or owner plays an even more decisive role in the process, and may also be determined by factors that are not purely business-related.

The recent establishment of Dubai as a preferred location for MENA[14] HQs of Indian companies is a good example of decisions based on non-exclusively business criteria. In this case the positive image of Dubai as a tourist location and the positive experience many Indian managers have had when visiting the emirate have contributed to these decisions, in addition to the favorable business environment and taxation.

14 Middle East North Africa

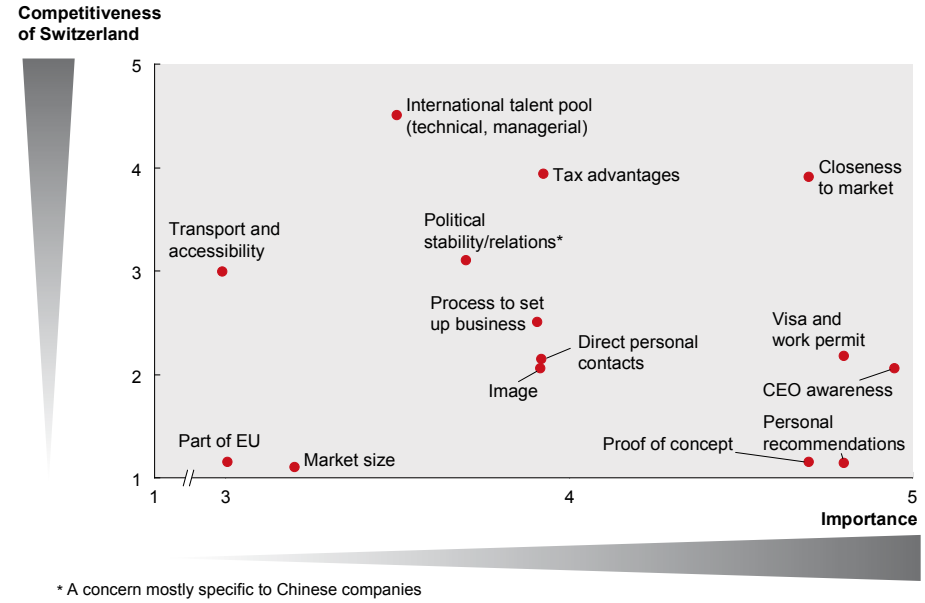
DOES SWITZERLAND MEET ASIAN NEEDS?

As we have seen, Switzerland is among the most attractive locations for international HQs on the basis of decision factors such as taxation level, infrastructure, quality of life and availability of international talent. While this is also true for Asian companies, two main weaknesses have been identified that significantly hinder Switzerland's competitive positioning towards Asian companies (See Figure 9). They are:

- The lack of a proper image as a business location
- Severe shortcomings concerning the entry process and the requirements for Asian companies.

Figure 9

Importance of decision criteria for Asian companies



* A concern mostly specific to Chinese companies
Source: Interviews, McKinsey analysis

These findings are substantially confirmed by previous studies such as the PresenceSuisse report. While in general the perception of Switzerland as a country is a definitely positive one, most Asian decision-makers do not perceive Switzerland as a prime business location. There are several reasons for this. A main one is Switzerland's traditional image in Asia, which is more related to tourism, political stability, high-quality education[15] and low taxation, but not that of a preferred HQ location. Another is that even when Switzerland is recognized as the home of some of the world's leading companies – especially financial services – the business environment and opportunities it can offer to foreign companies are not always apparent to Asian business leaders.

15 See also the study commissioned by the Nordic Council of Ministries in April 2008 assessing the perception of Chinese towards Switzerland, France and Nordic countries

This failure to perceive Switzerland as a business hub is reinforced by the fact that very few Asian company HQs have been established in Switzerland, so there is no "proof of concept". As we have seen, Asian CEOs tend to strongly rely on the experience of their peers, clients or suppliers when deciding on potential locations. Lack of already established Asian companies in Switzerland means that the country may not even be on decision-makers' shortlists when they consider locations for an HQ in Europe.

The second issue frequently mentioned by Asian managers and experts is the complexity and lack of transparency of the process for establishing a new organization in Switzerland. The need to deal with authorities at several levels and varying or intransparent requirements from different cantons are especially difficult to understand for Asian managers, and are seen as major limitations of the current Swiss system. Within this context, the particularly stringent requirements and long times for obtaining visas and work permits for Asian managers and employees have often been mentioned as a clear drawback.

Besides these two main issues, Switzerland also has other disadvantages relating to its competitive position.

First, Switzerland is a relatively small national market. As already mentioned, Asian companies often first establish sales organizations, before they set up a regional HQ. Large countries are more likely to be chosen as a location for a sales organization, and then often attract the regional HQ at a later stage. Similarly, an acquisition can serve as a magnet for a company's regional HQ to the same country. With a smaller domestic market to justify an acquisition and fewer target companies to feature in investment banks' pitches to Asian investors, Switzerland is at disadvantage relative to larger European economies.

Second, Switzerland is not a member of the European Union. Hence, Asian decision-makers perceive difficulties in managing other countries from Switzerland, due both to different legal structures (e.g. Societas Europeae) and limitations in movement to and from other European countries. The latter issue will be mitigated by the enactment of the Schengen Association Agreement later this year, at least with regard to those European countries that are members of Schengen.

WHAT IS AT STAKE?

If Switzerland does not successfully address the issues outlined above, it is unlikely to capture the full potential benefits from the wave of Asian HQs expected to be established in Europe. Recent developments indicate that competition between the top countries trying to attract foreign companies is increasing. This trend is reflected, for example, in the narrowing of the distribution of the WEF GCI ratings of the top ten countries.[16] European countries such as Denmark, Sweden, the United Kingdom, Ireland, Germany and the Netherlands are making great efforts to gain share in the international market for the location of multinational companies. Thus, the message to countries vying for international HQs, and for Switzerland in particular, is: "If you are not reforming, another country will overtake you."[17]

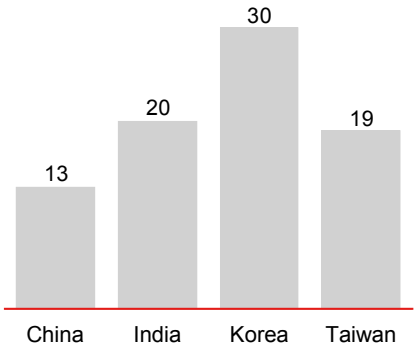
If we analyze the European presence of the 212 Asian companies listed in the Forbes 2000 ranking, we see that over 80 have already set up a significant presence in Europe (though only 7 have set up proper regional HQs), mostly in the United Kingdom and Germany but also in the Netherlands, Belgium and France (See Figure 10). As already mentioned, only a few have done so in Switzerland; this can be interpreted as a first sign that the country's competitive advantage might be less when dealing with Asian companies.

Sweden, for instance, opened an office of its "Invest in Sweden Agency" (ISA) in China in 2002. Today, ISA has three offices in China, offering local companies comprehensive information on business and investment opportunities in Sweden. Additionally, ISA provides Chinese companies with practical advice on how to proceed when setting up a business in Sweden.

Figure 10

Forbes 2000 companies with significant presence in Europe

Number of companies



Source: Forbes 2000, press search, McKinsey analysis

16 Swiss-American Chamber of Commerce & The Boston Consulting Group (2007)
17 World Bank (2008)

It also introduces decision-makers from Chinese companies to Swedish authorities and to professional service firms such as lawyers, accountants, relocation specialists and recruitment companies. ISA even supports companies in finding possible joint ventures or other forms of cooperation.

These activities have had impact: so far, ISA has facilitated entry into Sweden for over 100 Chinese companies, primarily in the retail, IT and telecommunications sectors. In 2008, a group of Chinese authorities and agencies, including the Chinese Ministry of Foreign Trade and the National Strategy Research Institution of China's Ministry of Commerce, named Sweden as the most attractive country for foreign direct investment.[18] Similarly, the Netherlands Foreign Investment Agency has established more than a dozen offices in Asia and "Invest in Germany" organizes high-visibility events and roadshows, and offers a comprehensive Chinese-language website.

In Germany, several cities are taking the lead. Hamburg, for example, has a long tradition of hosting Chinese firms, thanks to a city partnership with Shanghai established in 1986. Currently, over 400 Chinese firms are present in Hamburg, and every year brings a further 30–50 new companies (not all of these are HQs). In addition, around 700 China-related service firms are located in Hamburg, providing foreign companies with services such as translation, accounting and advertising. Research and academia have a strong focus on Asia too. For instance, the city's university offers a master's program on "Asian-European Business Transactions – Focus on China, ASEAN and the EU". Elsewhere in Germany, Cologne regularly organizes "business matching activities" that bring Chinese and German companies together.

Clearly, if Switzerland does not make serious efforts to improve its attractiveness to Asian HQs, the impact of the establishment of new HQs on employment and GDP is likely to be significantly lower.

The full implications of what is at stake are partially masked by Switzerland's current economic situation. Although it appears that in recent years Swiss domestic companies have contributed more to stable GDP growth than multinationals, the combined contribution of foreign and Swiss MNCs has in fact been lowered by the negative contribution to GDP growth of Swiss MNCs. In line with trends towards greater HQ mobility, Swiss MNCs have been selectively relocating certain HQ functions outside Switzerland. On the other hand, foreign MNCs have contributed 0.5 percent p.a. to Swiss GDP growth.[19] So, without active efforts to continue to attract available foreign HQs, and particularly the next wave of these from Asia, Switzerland's sustained future GDP growth rates may be at risk.

18 Invest in Sweden Agency (2008)
19 Swiss-American Chamber of Commerce & The Boston Consulting Group (2007)

SWITZERLAND'S KEY CHALLENGES AND HOW TO ADDRESS THEM

Switzerland has already taken action to improve its competitive positioning. In 1995, the Swiss government officially declared the need for a national promotion campaign. This declaration was transformed into federal legislation in 2006, increasing the political commitment to the topic of promoting the location. In 2003, "Location:Switzerland" was established as a department within the Federal Department of Economic Affairs; "Location:Switzerland" was then privatized in 2008, by outsourcing it to a private company, OSEC. And now, in 2008/2009, the cantons, OSEC and SECO are jointly developing a new strategy for national locations.

However, to capture the potential of Asian HQs, Switzerland still needs to address three major challenges: 1) getting on the initial shortlist of Asian decision-makers; 2) facilitating entry for new HQs; and 3) maintaining and strengthening its competitive position over time. Although these challenges apply to attracting HQs of all nationalities, the first is particularly crucial in the case of Asian companies, especially in the short term.

Getting on the initial shortlist of Asian decision-makers

Our analysis of the different decision-making processes in Asian companies shows that the best point of entry into the selection process for a future HQ is the CEO's shortlist. Getting on the shortlist is the most important challenge Switzerland has to address in the coming years, since awareness of Switzerland as a business location is still limited in Asia. Furthermore, even where there is awareness of Switzerland's attractive business climate, it is not accompanied by knowledge of the business opportunities it offers Asian companies. The main levers to increase awareness are building success stories that create "proof of concept", enhancing Switzerland's image and increasing as well as targeting its promotion in Asia.

Creating "proof of concept" for Asian companies. Given the importance of "proof of concept" for Asian companies' decision-makers and the effect of clusters, Switzerland needs to attract and support the establishment of Asian showcase firms as its first priority. This can be done by setting up a project group within OSEC to identify and target a limited number of leading Asian companies, to attract them to Switzerland and support them in establishing a business in the country.

This project group would leverage the experience of Asian companies already present in Switzerland (e.g. the Chinese media company Alibaba). It could also approach these companies to explore possibilities of leveraging their contacts and inviting other companies to consider Switzerland as an HQ location. For example, the project group could propose a joint effort to attract these companies' Asian suppliers or partners with a benefit package for both companies. Swiss multinational companies already well established in Asia, like Nestle and ABB, could also be leveraged in this sense. This initiative would be a natural extension of the already ongoing "Friends of Switzerland" effort by OSEC.

The project group could also facilitate M&A activities involving Swiss and Asian companies, as both targets and investors, in order to create a first link with activities in Switzerland. To this end, it could discuss with leading investment banks the potential and requirements for greater Swiss involvement in M&A activity with Asian targets or investors. The project group could also organize a platform to bring together parties interested in such a transaction. Along similar lines, it could organize "matchmaking fairs" to promote selected Swiss companies (e.g. SMEs with succession issues or looking for a partner for entry in Asian markets) to Asian counterparties.

Enhancing Switzerland's image and increasing its promotion in Asia. Once the first success stories have been achieved, Switzerland needs to adequately communicate its value proposition to the broader Asian political and business community. We see two levers that need to be activated together to achieve the desired result:

- Consolidation and enhancement of the marketing budget
- Establishment and empowerment of a single promotion agency

Consolidation and enhancement of the marketing budget. To raise its visibility as a potential HQ location, Switzerland should initiate a coordinated marketing effort to improve the country's business image in the Asian business community. The initiative should empower a single national entity – such as OSEC – with clearly defined responsibility for the budget for promoting Switzerland's business image in Asia. This would entail pooling cantonal and federal marketing budgets.

An important first step in this direction was the agreement of the cantonal economic authorities in June 2008 to pool resources and conduct common marketing activities in nine countries through OSEC.

To ensure sufficient funding to market the country successfully, the overall marketing budget may need to be increased. As a first point of reference, the total marketing budget for the business promotion of Switzerland worldwide – at both national and cantonal level – currently amounts to less than CHF 45 million p.a., significantly less than that allocated for the promotion of tourism (c. CHF 170 million). (See Figure 11)

Figure 11

Switzerland's annual marketing budget (worldwide)

CHF million

ESTIMATES

	Tourism	Business
National level	**c. 70**	**3–5**
Cantonal level	**c. 100**	**c. 40**

Source: OSEC

Raising the marketing budget for business promotion at least to the level of the one for tourism may seem an aggressive proposal; it should, though, be considered against the potential benefits that such an investment would yield: the increase would represent less than the added value generated by the establishment of 2 new HQs.

Establishment and empowerment of a single promotion agency. Switzerland should replace the currently fragmented landscape of local promotional initiatives in target Asian countries with a single promotion agency. Given the relatively low awareness of Switzerland in Asian countries, competing promotional activities by different Swiss entities threaten to dilute the message and rob Switzerland of any chances of competing with larger European economies. Whereas cantonal, regional and other promotional bodies can continue to work on refining their competitive offerings at home, and can handle all enquiries once a company decides to opt for Switzerland, coordinating and executing local promotion efforts in Asia should be the responsibility of a single agency, ideally the one responsible for then supporting Asian companies' entry into Switzerland. Some progress has already been made in this direction with the consolidation of Location:Switzerland under the umbrella of OSEC as of January 2008.

The local offices of the consolidated promotion agency in Asia would aim to position Switzerland as a leading business location. They would provide companies with access to relevant, up-to-date information on Switzerland and serve as the first point of contact, handing over the responsibility for an interested party to a specific canton once the process of setting up there was under way. Another vital activity of the agency would be to set up and maintain target lists of CEOs, family owners of large enterprises and other key stakeholders to be systematically and proactively targeted. The agency would also launch PR programs with the participation of high-level Swiss business and diplomatic representatives, as well as business partners such as professional services firms (e.g. accounting, legal and consulting firms, investment banks) active in the target country. Similar public-private partnerships have resulted in highly effective promotional road shows in China for a number of countries such as Belgium and the US.

Given the size of the target markets and the sheer number of potential counterparties, it will be of paramount importance to target the PR effort accurately in order to maintain a sustainable cost/benefit ratio. Specifically, the following groups represent a first list of high-potential targets:

- Leading companies in "global" sectors such as China's emerging consumer and household electronics sectors, Taiwan and Korea's high-tech sectors and India's IT and pharmaceutical companies.

- Companies in sectors where Switzerland offers a clear competitive advantage, such as pharmaceuticals and chemicals, but also specialty machinery, precision engineering and, increasingly, commodity trading.

- Leading local professional firms and advisors, which have close ties to companies' decision-makers and are often involved in the very early stages of the decision process.

In Switzerland, the agency would also be responsible for organizing high-level business promotion activities targeted at CEOs, politicians and key decision-makers of Asian countries visiting Switzerland. International events, such as the World Economic Forum in Davos and World Trade Organization meetings in Geneva, could be leveraged for this; diplomatic visits by governmental officials or delegations from Asian countries also represent a good platform for initiating discussions on Switzerland as a business location.

Facilitating entry for new HQs

Secondly, Switzerland needs to facilitate the process of entry for new HQs. Companies have to interact with authorities at various levels, which results in a process perceived by decision-makers as opaque and inefficient. The main levers concern the process for entering Switzerland and for bringing foreign employees into the country, as well as the corresponding requirements.

Improving entry process and requirements. Switzerland needs to review the entry process and requirements for Asian companies. In our opinion, Switzerland needs to take action in two areas:

- The process for assisting Asian companies' entry into Switzerland
- The requirements for, and availability of visas and work permits

Process for assisting Asian companies' entry into Switzerland. Asian decision-makers regularly mention the need for Switzerland to make it easier to establish an HQ. The World Bank's "Doing Business" report for 2009 also highlights this; whereas Switzerland ranks no. 21 overall, it is only no. 52 when it comes to setting up a new business (See Figure 12).[20] To improve this situation, Switzerland needs to facilitate the entry process by improving coordination between the different bodies handling the process and by offering tailored assistance throughout the process.

Figure 12

Easiness of doing business

Country	Ease of Doing Business	Country	Starting a Business
Singapore	1	New Zealand	1
New Zealand	2	Canada	2
United States	3	Australia	3
Hong Kong, China	4	Georgia	4
Denmark	5	Ireland	5
United Kingdom	6	United States	6
Ireland	7	Mauritius	7
Canada	8	United Kingdom	8
Australia	9	Puerto Rico	9
Norway	10	Singapore	10
Iceland	11	Jamaica	11
Japan	12	Macedonia, FYR	12
Thailand	13	Azerbaijan	13
Finland	14	France	14
Georgia	15	Hong Kong, China	15
Switzerland	21	Switzerland	52

Source: WorldBank, 2008

20 World Bank (2008)

This requires the creation of a clear interface between the different entities handling an Asian company's entry process, from initial interest to completion of HQ set-up. Particularly for companies from distant Asian countries, a "no wrong door" approach should be taken in responding to their needs, so as to ensure that Asian companies looking to establish HQs in Switzerland have a first point of contact throughout the process and are not prematurely confused by competing offerings from different regions and agencies. Thus, a single coordination agency, which may also be responsible for promoting Switzerland in the target countries, should be the primary owner of all initial stages of contact and enquiry by Asian companies in Asia, and should remain available as a point of contact through the process. Moreover, the handover between this agency and local authorities should be handled transparently and professionally.

Furthermore, all agencies involved in the Asian companies' set-up process, both in the home country and in Switzerland, need to tailor their assistance to provide a comprehensive solution to the needs of these companies. This means not only being responsible for providing information to interested companies, but also helping with channeling paperwork to the relevant counterparties. Some local agencies could also expand their support by providing services such as tax, accounting, legal and real estate advice, or facilitate contacts with local providers of such services who have knowledge of Asian languages and regulatory systems. Ideally, all agencies involved in the process would employ a high share of personnel with Asian cultural and language skills to help bridge potential initial cultural gaps.

Requirements and availability of visas and work permits. A task force needs to be set up and empowered to focus the immigration authorities on the countries targeted with promotional activities, and to provide operational support for the process of allocating visas and work permits for skilled workers from these Asian countries.

At the highest policy level, the task force should initiate and support a review to align the high-level immigration strategies of various government authorities. The different strategies pursued by the BRIC and the Duale Zulassungssystem models illustrate the need for such coordination. Furthermore, it should initiate policy discussions to refine the visa and work permit policies toward skilled workers from target countries where appropriate. Even if in some cantons, such as Zurich, there is evidence of a trend toward increased issuance of work permits to qualified workers from outside the EU/EFTA[21], and limited trainee-exchange programs, at the moment there are few explicit initiatives to smooth the process for these workers.

Approaches that should be explored include the creation of an expedited process supported by company-guarantee schemes, simplified requirements, "fast-track" processes or skilled-worker quotas. Where wide-ranging policies covering broad segments of the skilled foreign workforce might prove politically difficult, specific initiatives targeted at defined segments from the target Asian countries could be considered. Such schemes would simplify the work permit process for top Asian graduates of selected Swiss and Asian universities, the top management of larger Asian companies, or highly skilled foreign professionals in specific functions. Similarly, a pre-approved quota of work permits dedicated to the initial effort of attracting a shortlist of Asian companies could serve as a near-term solution.

21 Based on statistics from Zurich's Amt für Wirtschaft und Arbeit

Operationally, the task force would be responsible for aiding the implementation of policies to facilitate the entry of skilled Asian employees. Once specific initiatives or work permit quotas were granted, together with the coordination agency, it would apply its intimate knowledge of the business and skilled-worker communities in Asian countries to allocate them efficiently.

As a first step, the task force should build up clear and comprehensible documentation in Asian languages of the Swiss visa and work permit processes.

Maintaining and strengthening competitive position over time

Thirdly, Switzerland needs to maintain and improve its overall competitive position. An evaluation of current competitiveness rankings shows that Switzerland is well positioned as an HQ location within Europe, so this is not the focus of attention here. However, Switzerland does need to ensure that it remains competitive if it is to sustain its leading position in the future, especially considering that other countries such as Sweden, the Netherlands and Germany are investing significantly to fill the gap. The main levers here are taxes, transport infrastructure, the availability of skilled workers, and the fostering of Asian communities (the importance of which varies depending on the country of provenance of Asian HQ managers, so that it is less relevant for Chinese managers, for example).

Maintaining Switzerland's competitive positioning requires, in addition to competitive taxation, the application of three key levers:

- Constantly upgrade the transport infrastructure
- Enhance the talent pool
- Build Asian communities

Constantly upgrade the transport infrastructure. Another component of Switzerland's longer-term competitive positioning is the constant enhancement and monitoring of its transport infrastructure, and particularly its links with Asia and the main European markets.

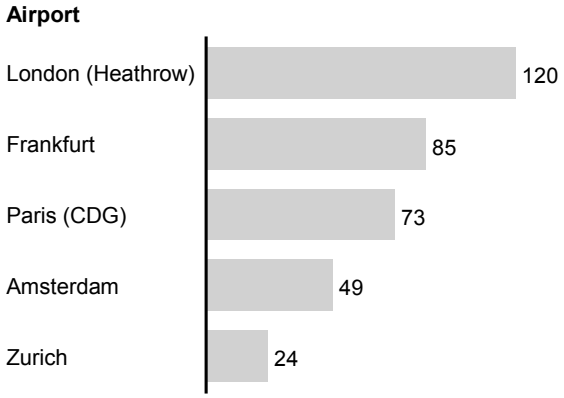
Such an initiative would encompass general improvements that enhance Switzerland's position as a transport hub at the heart of Europe, for instance by ensuring adequate future capacity at national airports, across the country and at a "system-wide" level, as well as increasing connectivity among national airports with those of neighboring countries.

Furthermore, the initiative could target Switzerland's links with Asia for further improvement. Despite the recent reintroduction of non-stop flights to Shanghai, twice-daily flights to Hong Kong and frequent flights to Mumbai and Seoul, the need for such improvement is illustrated by the lack of a direct flight between Beijing and Zurich (at least until 2009).This need is even more evident inasmuch as cities such as London, Frankfurt, Paris and even Amsterdam have more than daily connections with all the main Asian business cities (See Figure 13). Attracting a leading Asian airline to establish its European hub in Switzerland could pave the way for improved links with Asian destinations, as could an increase in the connections to Asia offered by Swiss and other leading international airlines.

Figure 13

Direct flight connections to main Asian destinations*

Weekly direct flights, September 2008



* Mumbai, New Delhi, Seoul, Beijing, Shanghai
Source: OAG; McKinsey analysis

Enhance the talent pool. Another potential pull factor for Asian HQs could be created by an initiative to enhance the talent pool available to Asian companies in Switzerland. In the first place, given Asian companies' frequently-cited hunger for international managerial talent, Switzerland could work to constantly improve its value proposition as an international managerial training ground of choice. To better tailor Switzerland's offering in this respect, Swiss institutions could launch more specialized management and international relations courses with an emphasis on Asia. In this respect, the University of St. Gallen already has a dedicated Asia Research Centre focusing on business and management in Asia, offers an Asia Management curriculum, and promotes exchanges and links with Asian management universities through its Asia Campus Network.

Additionally, the talent pool with Asian language and cultural capabilities could be enhanced. Currently, in addition to dedicated institutes of sinology offering degree programs at the Universities of Zurich and Geneva, numerous other universities and universities of applied sciences, as well as over a dozen Swiss secondary schools, offer Chinese language instruction. Government-supported student exchange programs open to all universities already bring dozens of Swiss students to China and vice-versa. However, further emphasis could be put on bringing more Asian students to Switzerland through actively promoting Swiss universities in Asia, establishing more targeted scholarship programs, and offering more assistance to Asian students in Switzerland in overcoming language difficulties and differences in educational requirements. Similarly, programs between leading Swiss and Asian institutions could be increased. For instance, the Sino-Swiss Science and Technology Cooperation (SSSTC) program has promoted significant scientific exchanges between the Swiss Federal Institute of Technology and Chinese institutions. Its activities include annual symposia, research fellowships and scientific workshops.

Graduates from top Asian institutions could also be targeted through career fairs with leading Swiss employers and through incentives such as support in the visa process for successful candidates.

Build Asian communities. To further tailor its value proposition towards Asian companies, Switzerland could foster Asian communities. Professional communities consisting of accountants, banks, consultants and other services with links to Asia are often cited by Asian decision-makers as being important in making a location attractive for their HQs. The formation of a network of such services could be encouraged by investing in talent with Asian skills, as previously mentioned, but also by actively seeking to encourage the opening of branches of Asian professional service firms. In this perspective, an active role of the bilateral Chambers of Commerce[22] is a fundamental enabler.

Secondly, Asian social communities could be fostered in the country in order to enhance the quality of life for Asian immigrants. Pockets of sizeable Asian communities already exist in Switzerland, for instance those working in international institutions based in the Geneva area, or the various communities of Chinese entrepreneurs and students who have settled in Switzerland in successive waves. Although this is a secondary factor for most Asian executives, it can, nevertheless, play an important role in some cases. Along similar lines, associations such as the Swiss-Chinese Association, the Swiss-Indian Association Zurich, as well as programs by institutions such as the Museum Rietberg, already provide a focal point for Asian communities and foster intercultural exchanges, as do sister-city relationships such as those between Zurich and Kun Ming. Further intercultural exchange could be encouraged through more partnerships between Swiss and Asian cities and cultural institutions, as well as through the promotion of Asian-themed cultural events in Switzerland.

CONCLUSION

Asian companies are becoming increasingly multinational. The expected establishment of regional HQs represents a sizeable opportunity for European countries. This is the case for Switzerland, which is very well positioned today. However, the current situation cannot be taken for granted. Global competition among countries trying to attract HQs is increasing.

Switzerland needs to focus on actively promoting itself as a prime location for HQs in Asia, while steadily improving the entry process for companies interested in setting up an HQ in Europe. If Switzerland overcomes these challenges and successfully attracts a significant share of Asian companies moving their HQs to Europe, the benefits for the country will be substantial in terms of both GDP and employment growth.

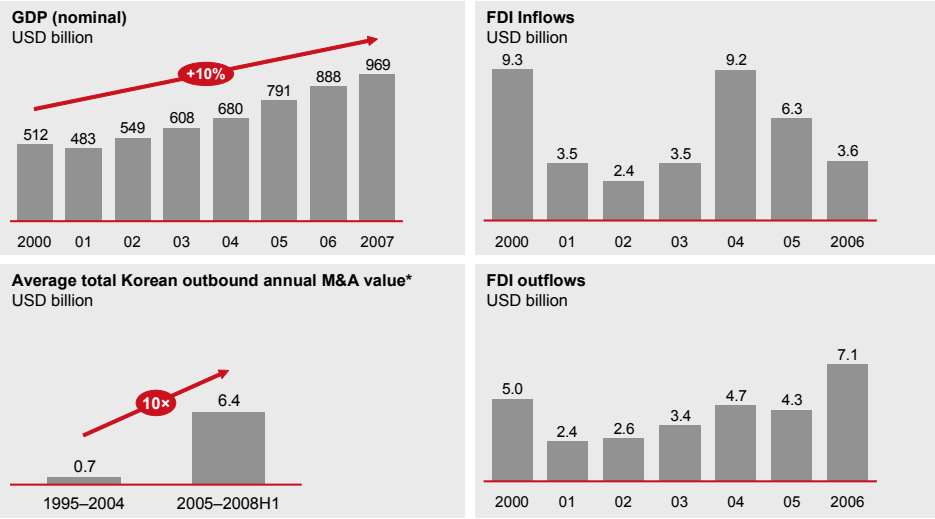
22 E.g. the Swiss-Asian Chamber of Commerce, the Swiss-Chinese Chamber of Commerce, the Swiss-Indian Chamber of Commerce

COUNTRY PROFILES

Korea

With its GDP reaching nearly USD 970 billion in 2007, Korea's economy is the 14th largest worldwide and ranks fourth in Asia, behind Japan, China and India. Korea's GDP has been growing at 10 percent per year since 2000 (5 percent in real terms), continuing a stunning growth story. The country has evolved from exports of low-value-added goods to an economy based on modern technologies and large-scale production, as well as, increasingly, technological innovation. As of 2007, nearly half of Korea's total exports was machinery and high-tech goods.[23] Policies such as directed credit and import substitution historically played an important role in Korea's emergence, and today Korea ranks 13th out of 134 countries on the WEF's most recent Global Competitiveness Index, outstripping all other Asian economies but Singapore, Japan and Hong Kong. In terms of business regulations, the World Bank's ranking of countries on ease of doing business places Korea at 23rd of 181 ranked countries, just behind Switzerland's 21st place.

Korea: macroeconomic overview



* All deals with deal value >USD 10 million
Source: Global insight WMM, National Statistics office, Dealogic, McKinsey analysis

Korea's corporate landscape has traditionally been dominated by *chaebols*, large and complex corporations or groups with roots as family-owned businesses and with close ties to the government. Although family stakes in all but one of the top 10 *chaebols* have fallen below 4 percent[24], even without significant ownership the original families still have considerable say in how these centralized organizations are run.

23 Global Insights, United Nations Industrial Development Organization
24 Korean Fair Trade Commission

Korean companies have made a global name for themselves in industries such as consumer electronics electronics (e.g. LG electronics), high-tech (e.g. Hynix Semiconductor), shipbuilding (e.g. Hyundai) and automotive (e.g. KIA), with a particular strength in unrivalled speed-to-market strategies. Korea's high-tech sectors have been less Original Equipment Manufacturing (OEM)-oriented than some of their other Asian rivals and have also put more emphasis on international branding and marketing. A combination of these capabilities has produced some truly global champions, such as Samsung Electronics, which generates two-thirds of its revenues internationally. This is also reflected in the latest trends in Korean companies' M&A activity. The average annual outbound M&A conducted by Korean companies has grown significantly in recent years, and in 2007 outbound M&A value exceeded inbound M&A by over one-third. The high-tech sector has led the way with the highest outbound M&A deal volume.

For those Korean companies that have already attained world-class status in their own industries but lack geographic diversification, or contend with saturated domestic markets, access to new markets drives international expansion. While numerous world-class Korean companies continue go abroad to seek new markets, many of Korea's companies are already looking ahead: as they aim to boost their original innovation capabilities they also see going global as a means of tapping into international talent.

An example is the Doosan *chaebol* (heavy equipment manufacturer), which recently completed the biggest foreign acquisition by a Korean company, with its takeover of Bobcat (construction machinery), thus acquiring strong in-house technology and product development. According to Mr. Yongmaan Park, CEO of Doosan, among the key challenges Korean companies face in going global are understanding value-creating levers for acquisitions, and effectively instilling shared corporate values and processes across global operations.[25]

25 Transforming a South Korean *chaebol*: An interview with Doosan's Yongmaan Park. *The McKinsey Quarterly* September 2008.

China

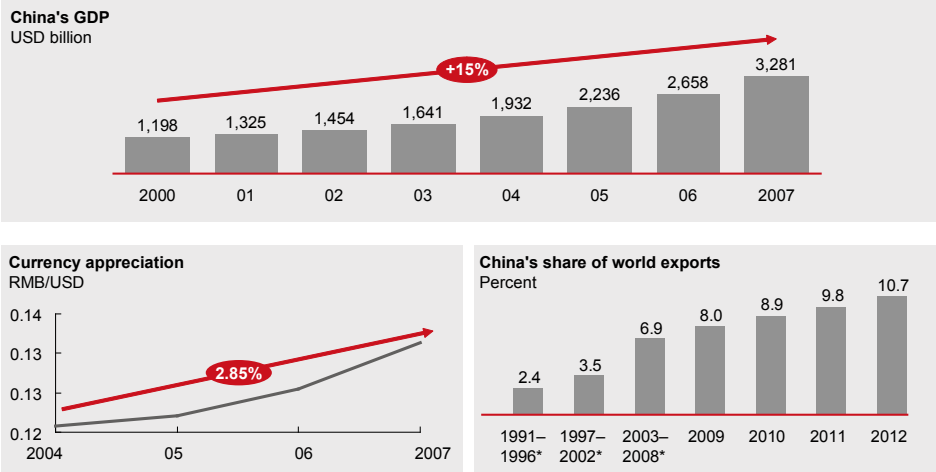
With GDP of nearly USD 3.3 trillion in 2007, China is already the world's fourth-largest economy. Since 2000, its GDP has been growing at a breathtaking pace of nearly 15 percent (10 percent in real terms). With a labor force of nearly 800 million and competitive costs, China's relentless export growth continues to uphold GDP growth even as the Renminbi has started to appreciate over the last few years.

Although its competitiveness has traditionally derived from labor cost advantages, China's manufacturing capabilities are increasingly moving up the value chain. It has rapidly increased its investment in innovation - according to the OECD, China is now second only to the US in R&D spending and the number of the researchers it employs. Annual growth rates of approximately 40 percent in the production of medical and measuring equipment and 30 percent in electronic and communication equipment highlight this expansion into higher value-added capabilities, as does the fact that high-tech goods now account for 33 percent of China's goods exports.[26]

26 China Statistics Yearbook on High-Technology Industry; Global Insights

This rapid growth has been enabled by China's implementation of its "reform and opening-up" policy since 1978. However, despite the fast-paced economic reforms China has pursued since then, it still ranks 30th out of 134 countries, and 10th among Asian countries on the WEF's 2008 Global Competitiveness Index. In terms of ease of doing business, the World Bank ranks China 83rd of 181.

China: macroeconomic overview



* Average of 5 years
Source: Global Insights, EIU world data

China's path to reform has created a unique symbiosis of the public and private spheres in business. Many of the largest Chinese companies (e.g. China Petroleum and Chemical Corporation, China Industrial and Commercial Bank, China Mobile Communications Corporation) are State-Owned Enterprises (SOEs), with strong connections to the ruling Communist Party. The definition of SOEs is somewhat ambiguous, but they constitute an important part of China's economic landscape. Around 150[27] large corporations report directly to the central government, but the number of their subsidiaries and other companies at least partially owned by the central or local governments runs into the thousands. Traditionally associated with government favoritism and cumbersome management, China's SOEs are today blurring the line dividing them from private companies.

A policy of separating politics from business has gradually weaned them off much government backing, while at the same time many have embraced leaner operations and a more transparent management style. By comparison, some family-owned firms in China's private sector can seem more impervious to transparency, open governance or external ideas and management. Moreover, far from living up to the stereotype of inward-facing, monolithic organizations, SOEs account for by far the most international expansion in recent years. This has resulted in a unique acquirer profile for outbound Chinese M&A.

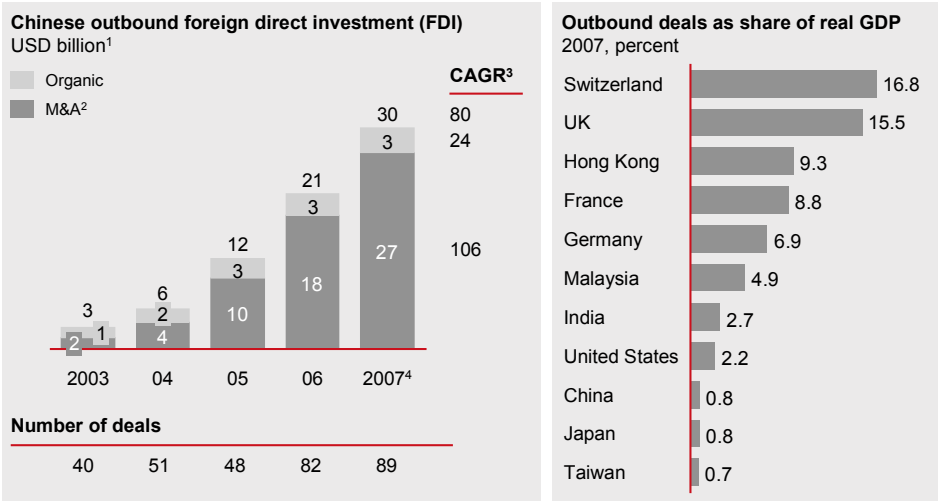
27 *The McKinsey Quarterly, 2008 Number 3.* pp. 59–66

China's track record in M&A

International M&A activity by Chinese companies is a relatively new phenomenon. Long considered overdue, it has recently been experiencing a boom. With Chinese companies enjoying abundant cash balances, they are increasingly undertaking outbound deals, with a total deal value growing at an average of 106 percent yearly since 2003. Deals such as the Lenovo acquisition of IBM's personal computer business or the USD 4 billion acquisition of PetroKazakstan by China National Petroleum are clear examples of this trend.

Outbound Chinese M&A has not always boosted shareholder value. A number of strategic goals other than the maximization of shareholder value underlie most acquisitions of foreign assets by Chinese companies. The top five of these are access to natural resources, access to new markets, financial investment, access to capabilities, and gaining scale. As most recent deals are the first of their kind for the acquiring company, they have predominantly been small and focused on one specific strategic goal. For instance, many manufacturing companies have ventured into cross-border M&A to gain access to new markets or lower costs by globalizing supply chains, whereas financial institutions have aimed at gaining access to foreign risk management, credit rating and other expertise.

China: outbound M&A



1 USD 1 = 7 renminbi
2 For 2003–06 includes deals with final stake of >10%.
3 Compound annual growth rate
4 Estimate based on M&A deal value (USD 26.8bn) from Dealogic, plus organic outbound investments (USD 3.3 bn), assuming 10% growth in organic investments over previous year; 2006 and 2007 data include financial investments
Source: Dealogic, McKinsey analysis

Interviews with the CEOs of two of China's most global companies illustrate the accelerating M&A trend and the strategic rationales at individual company level. Mai Boliang, President of China International Marine Containers (CIMC) recalls the first partnership with a German company, aimed at gaining access to technological capabilities, followed by increasingly active foreign acquisitions in recent years. Yin Tongyao, CEO of carmaker Chery, lists the four goals of an international strategy that began as an accident, but has recently turned his company into a multinational firm: "technical cooperation with overseas enterprises, car exports, overseas assembly plants, and equity joint ventures".

Both CEOs anticipate further international expansion. However, both also highlight finding and fostering talent with international capabilities as a key challenge to their further global aspirations. This is in line with their peers at other Chinese companies, 44 percent of whom say that finding managerial talent is the greatest barrier when conducting activities abroad, above barriers such as lack of capital, which only a quarter of executives surveyed saw as a concern. As Chinese companies continue to venture abroad, they will increasingly do so not only in search of acquisition targets, but also in search of talent – 62 percent of the Chinese executives surveyed expect their foreign contingent to increase in the next three years.

Both China's state-owned and private sectors increasingly face the same challenges as they become international. According to a survey of Chinese executives[28] a lack of sufficient managerial talent, insufficient capital and inadequate understanding of legal and reputation risks in other countries are the top three barriers to undertaking activities outside China. Another challenge, identified by 22 percent of respondents, is the development of effective cross-cultural management. On this front, overcoming the shortage of talent with sufficient English-language skills and international exposure and redesigning Chinese companies' top-down organizational models are significant challenges. Similarly, due to the relatively low proportion of foreign or foreign-educated senior management in Chinese enterprises, awareness and intimate knowledge of foreign markets and opportunities can be more of a challenge than for companies from India, Taiwan or Korea.

28 *The McKinsey Quarterly, 2008 Number 3.* pp. 18–21.

Taiwan

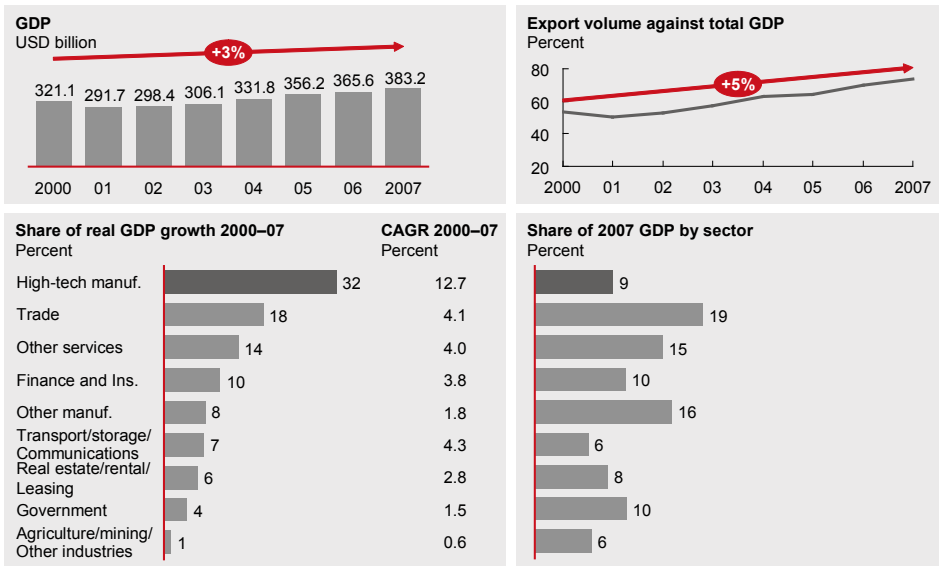
Taiwan is the world's 24th largest economy, with GDP of over USD 380 billion in 2007. Only the much more populous Japan, China, Korea, India and Indonesia outrank it in Asia. After decades of high growth that supported the speedy emergence of Taiwan's economy, the country's GDP growth has moderated to around 3 percent per year (4 percent in real terms). As has historically been the case for this "Asian tiger", growth continues to be export-driven, with almost half of GDP growth over the past ten years due to exports and the most significant portion of it coming from the high-tech manufacturing sector.

Several phases of government-directed development have underpinned the emergence of Taiwan's export-led economy.[29] Through investments by the National Development Fund, the government has successively channeled resources to high-priority sectors. Emphasis was first put on semiconductor and petrochemical manufacturing in the 1970s; then, in the following years ten key industries were encouraged, including IT, communications and aerospace. Since 2000, the focus has been on biotechnology and digital content. Furthermore, government institutions have complemented the investment in R&D and engineering knowledge-building by Taiwan's academic institutions. Reflecting the fruits of such active policies, Taiwan ranks 17th of 134 countries and 5th in Asia on WEF's Global Competitiveness Index, though a somewhat less impressive 61st of 181 in the World Bank 2008 ease of doing business rankings.

29 National Development Fund Annual report (2006)

Taiwan's export-driven economy has been led by the high-tech sector. Its leading companies include major foundry, memory and IC design companies in the area of semiconductors, such as Taiwan Semiconductor Manufacturing Company (TSMC) as well as Original Design Manufacturers (ODMs), Original Equipment Manufacturers (OEMs), and Electronic Manufacturing Services (EMS) in ICT hardware, such as Hon Hai. These have flourished in a country that has successfully developed technological clusters with supplier presence all along the value chain, and they have also benefited from government-supported investment in R&D at the national level, and growing local technical and engineering talent pools.

Taiwan: macroeconomic overview



Source: Taiwan DGBAS; WMM, McKinsey analysis

With outbound FDI flows increasing at over 11 percent per year since 2000, Taiwanese companies are also increasingly growing more than just their exports abroad.

India

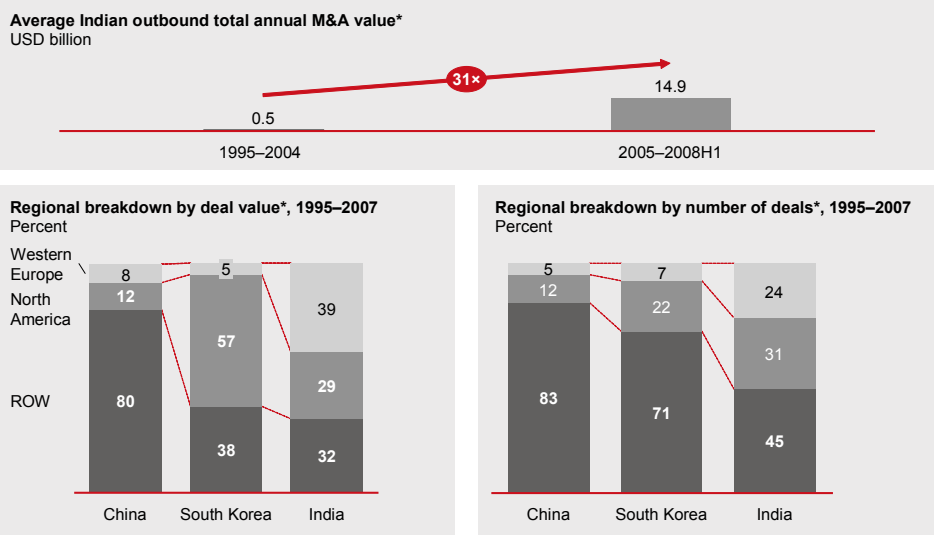
At over USD 1.1 billion, India's GDP in 2007 places it 12th in the world and 3rd in Asia. Following decades of sluggish growth after independence, India's economy has been growing at a steady rate of 14 percent per year (8 percent in real terms) since 2000. This growth trajectory followed reforms towards greater openness initiated in 1991, including a gradual easing of restrictions on FDI and the opening of successive sectors to private participation. Since 1991, India's exports have grown at 14 percent per year in real terms, and annual FDI has grown at 23 percent per year an average, since 2000.[30] One of the India's biggest assets is its 0.5 billion-strong, young and growing labor force; however, its full potential is yet to be unlocked – productivity is relatively low compared to China's, and most of the goods India produces for export are still raw materials or low value-added goods. In addition to gradual human

capital formation over time, India's economic growth has also been supported by rising capital intensity and the rapid emergence of service industries.

Despite continuing reforms, India is still only in 50th place on the WEF's 2008 Global Competitiveness Index, behind 16 other Asian countries, and the World Bank ranks it 122nd of 181 on ease of doing business. For instance, the infrastructure is still relatively poor compared to countries such as China, and although reforms have reached many sectors, heavy regulation still stunts India's retailing, defense, media and banking sectors.

On the other hand, India is home to world-class companies in the automotive, IT, business process outsourcing, steel, telecommunications and pharmaceutical sectors. Ranbaxy Laboratories' prominence in generics pharmaceuticals and Tata's breakthrough "one-lakh" car are some of the more visible examples of leading companies' success, which has provided a solid springboard for further internationalization. As a testament to Indian companies' growing success, 48 of them made it to the latest Forbes 2000 list, compared to just 30 in 2004.

India: outbound M&A



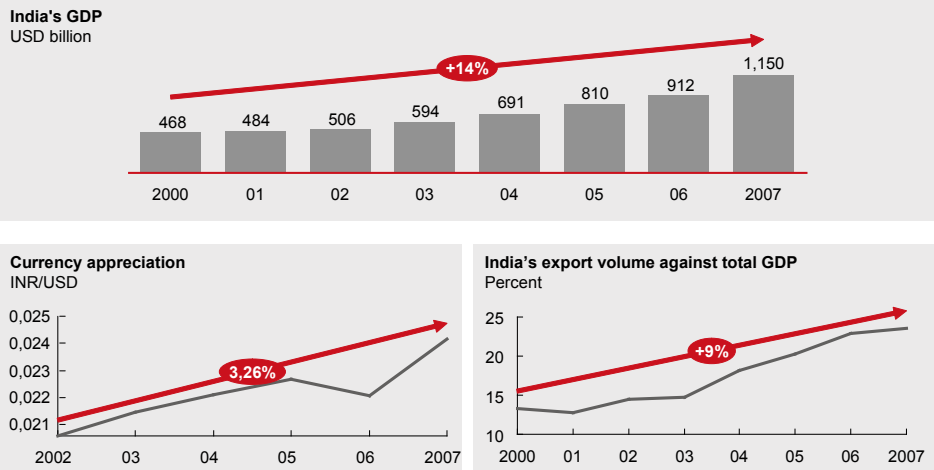
* All deals with deal value >USD 10 million
Source: Dealogic; McKinsey analysis

With deals such as Mittal's USD 37 billion acquisition of Arcelor and Tata Steel's USD 11 billion takeover of Anglo-Dutch Corus Global in 2006, the global ambitions of India's corporate champions have been making headlines, and this has been a broad trend. Outbound M&A deal value by Indian companies has reached 31 times the annual pre-2004 average, with the most active sector in terms of deal value being metal and steel, representing nearly 40 percent of Indian companies' total outbound deal value. In terms of M&A volume, the running has been made by India's pharma and IT sectors, due to opportunities to take advantage of expiring patents and IT's inherent appeal for off-shoring.

30 Ministry of Commerce and Industry of India

Strikingly, compared to China and South Korea, Indian companies have been conducting significantly more acquisitions in the developed world, and particularly in Europe. This in part reflects India's more extensive cultural and historical ties to Europe, and also its greater proximity, both of which often contribute to a higher level of awareness of European markets and opportunities among its business community.

India: macroeconomic overview



Source: Global Insights; EIU world data

Not surprisingly in view of this trend, surveys indicate that Indian executives tend to be more positive than others about expanding internationally. Moreover, more Indian executives indicate that it is their aspiration to become truly global MNCs, compared to their other emerging-market peers[31]. Indeed, some Indian companies already appear to be well on their way to attaining this aspiration. Unlike companies from China and Korea, most of which have only conducted 1–2 significant acquisitions abroad, a few serial international acquirers such as the already mentioned Tata Group, and Ranbaxy Laboratories (pharma) as well as Wipro (IT services) have already emerged amongst India's top 100 companies. Indian companies have also tended to extract more value from their foreign acquisitions than Asian peers.

Nevertheless, Indian executives still see domestic obstacles on the way to greater international expansion, and are also concerned about talent shortages. Despite India's large, young labor force, and broader English-speaking talent base, lack of global HR policies also makes retention of talent difficult. Unsurprisingly, this concern is especially important among executives in the IT and business services sectors.[32] Another series of challenges are those that still encumber Indian companies' growth at home, and distract them from devoting more of their energies to expansion abroad. These include fiercely competitive markets and inadequate infrastructure, as well as lack of access to capital, poor legal protection and extensive regulation.

31 McKinsey Globalization survey 2007
32 *The McKinsey Quarterly 2005 Special Edition*: Fulfilling India's Promise

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