Energy

Going global: The challenges of international expansion

An interview with Zhang Kehui, Chief Financial Officer, China Shenhua Energy Company

Outlook Q&A: Over the past few years, many Chinese enterprises have embarked on global expansion strategies. China Shenhua, for example, has increased its M&A activity overseas. What kinds of strategic goals guide your plans as you look to expand your international presence?

Zhang Kehui: Our efforts have been focused on acquiring companies that augment or supplement our existing capabilities and markets in important ways. For example, China is rich in coal but coking coal is scarce and the existing reserves have been carved out. So the desire to obtain high-quality coking coal overseas is one driver of our acquisitions in the international market and is something that can increase our market share overall.

Another advantage we can see is in acquisitions that reduce our transportation costs. Of course, China is a very large country—more than 5,000 kilometers from east to west. China’s coal reserves are concentrated in the central and western regions, while the areas where demand is growing the most are in the southeast coastal areas. So if we have a presence in Indonesia, Australia and other countries to supply the southeast region, we will be able to reduce our transportation costs to move our products to market.

What factors and issues go into a decision to make an overseas acquisition?

A business never goes global just in the pursuit of pure profit—there has to be a long-term fit with the overall business development strategy: How might new markets help grow our business? How could an overseas operation effectively augment our domestic operations? How might we acquire new world-class technology and management skills through an acquisition? We, as well as many Chinese enterprises, are becoming more disciplined and rational in our overseas development strategies.

What specific challenges have you encountered in executing your global expansion strategy?

At times, I think companies can be a bit too risk-averse. This is often rooted in an inability to gather the right kind of knowledge to make faster and more informed decisions. We sometimes find that we lack specific instruments to judge overseas projects. The decision is often too subjective and qualitative,
and often based on verbal discussions that are not sufficiently rooted in quantitative analysis. We need a set of stringent and standard criteria, according to which relevant data can be collected, which then, in turn, enables us to consider different possible scenarios and thereby make a more-informed decision.

Do you operate according to different management models in your domestic and overseas enterprises?
One can be tempted to try to apply a domestic management approach to global operations, but that is often not successful for a number of reasons. One has to do with financing implications. Overseas project financing involves many processes, calling for joint participation of the operator, the constructor and the suppliers, with the risk shared by each of the participants. With our first acquisitions, we acted concurrently as the operator, constructor and material supplier. That approach caused funding challenges because the parent company was reluctant to bear all the risks due to political and regulatory uncertainties.

The various legal environments in different regions also need to be carefully considered. Relevant legal systems are well-established in some countries but immature in others, with a lot of provisions and regulations that are not adequately defined in the legal documents. In some cases, you are forced to learn as you go.

Finally, there is the challenge of developing more effective leadership talent in the overseas locations. If you simply move executives from China to a different country, they may have excellent reputations domestically but, in fact, might have little overseas experience. They need to be trained before they can be truly effective.

Can overseas acquisitions be a way to gain management expertise and experience to support development of the whole group?
To date, we have not yet acquired any business that has highly mature management, or management that exceeds our own current capabilities in our domestic business. Our overseas companies have basically copied China Shenhua’s domestic management model and corporate culture. We are certainly interested in merging with or acquiring a company with executive expertise as a way of improving our overall management capability. However, in some cases, overseas M&As focus too much on the quick financial payoff and not enough on the longer-term benefits in areas such as talent and management expertise. As we move forward, we need to examine these longer-term benefits more carefully.

What about the issue of controls? Does the risk management model for overseas operations differ from your domestic emphases?
In fact, we have specialized personnel in charge of overseas operations because the financial systems and requirements differ from one country to another. We have studied the financial systems in almost 50 countries that we either do business in currently or may be interested in for the future. We looked at issues such as exchange rates, profit distribution and funding allocation, and then conducted in-depth research into the financial systems of these countries. Based on the research results, we are developing financial management regulations and standards that are appropriate for the context of the target country.

How do you balance the need for local autonomy with global consistency?
Our overseas operations give local management considerable autonomy. Other specific initiatives such as technology projects, however, are managed at the group level because we want to maintain a standardized, unified approach to our systems and technologies.

From a management perspective, we work to take a coordinated and integrated approach. China Shenhua has set up an overseas management company, which we intend to use as a means to manage our overseas investments in an integrated way. I noted earlier the need to become more quantitative, and this approach is a way to do that. We can use statistical analyses of data to perform more objective assessments in a standardized way—to evaluate projects before we invest in them, and then to monitor their progress in a timely manner.

We also know that there are different aspects of projects and acquisitions that need to be managed based on specialized skills in certain areas. For example, if we invest in a coal project, the safety aspects of production need to be managed by a professional company with skills and credentials in that area.

We take an integrated management perspective for critical functions and processes such as regulations, standards or performance appraisal systems. At the same time, some flexibility is essential when it comes to the practical application of processes in different environments. For example, recruitment of non-national employees needs to be carried out while taking into account local labor costs.

Finally, are there particular keys to success that are on your mind as you move forward on your global expansion and acquisition strategy?
I have alluded to this in my previous comments, but the talent issue is very important. We have many top-notch Chinese nationals working in our overseas operations—people with excellent educational backgrounds and extensive experience—but we need to attract more non-nationals to our overseas companies. For any company, that means improving your international image.

We need to be aware of the fact that when we speak of our brand, that concept is important not only to our customers but also to the experienced managers out there who might be interested in working for China Shenhua. We need to be aware of the image we are projecting about our culture and the opportunities available to those who work for us.