

# **Cross-border M&A: A study of two Chinese cases**

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# Abstract

Since the 90's of the 20th century, driven by external factors such as the global industrial upgrading, restructuring and the tides of integration, the size and number of global M&A has been a rising trend, the volume of transactions reaching new heights. During this period, Chinese enterprises have become one part of the world economic market. Furthermore, under the influence of the last financial storm, lots of international companies skin into the financial crisis. This is a good opportunity for Chinese enterprises to executive Cross-border M&A to expand their international position and their competitive strength.

However Chinese enterprises just are the beginners on the Cross-border M&A, they have limit experience on Cross-border M&A. Cultural integration and corporate governance structure are the weakness of Chinese enterprises. It leads to the low success rate of Cross-border M&A of Chinese enterprises. This dissertation will study two cases in order to help the Chinese enterprises find out how to do cultural integrating work and adjust the corporate governance structure after Cross-border M&A.

Key Words and JEL classification: F23, Chinese enterprises, G34, Cross-border M&A, Cultural integration, corporate governance structure

# Sumário

Os anos 90 do século passado, factores diversos que se prendem com a globalização como sejam o desenvolvimento industrial, as reestruturações e integrações empresarias levaram a que o número de fusões e aquisições (mergers and acquisitions – M&A) globais atingisse novos altos nunca dantes vistos.

Foi também durante este período que as organizações chinesas iniciaram a sua senda como actor de economia global. Todavia com o surgimento da recente crise financeira, muitas empresas de grande porte passaram a estar financeiramente muito fragilizadas. E, esta situação de instabilidade corrente é uma grande oportunidade para as organizações chinesas avançarem para M&A para além das suas fronteiras, tendo como fito principal fortalecer a sua competitividade no mercado internacional.

Pode dizer-se que até o presente momento, as empresas chinesas são pouco experientes no que se trata de M&A internacionais.

As principais fraquezas das organizações chinesas são a integração cultural e a governabilidade empresarial. Estes são, efectivamente, os principais factores que têm levado ao insucesso esses empreendimentos transnacionais.

A presente dissertação tem como principal objectivo reflectir para ajudar as empresas chinesas a obter sucesso nos projectos de M&A transnacionais através da análise de dois casos e, estabelecer os passos que as empresas devem tomar tanto na vertente da integração cultural como na de *corporate governance* para uma efectiva fusão ou aquisição internacional.

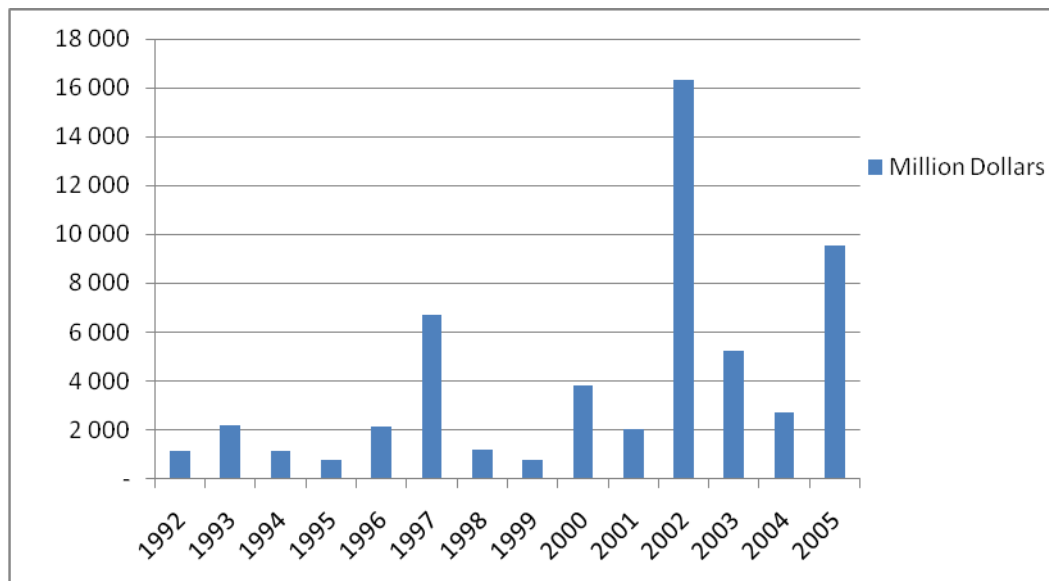
Palavras-chave e JEL Classification: F23, Chinese enterprises, G34, Cross-border M&A, Cultural integration, corporate governance structure

# 1. Introduction

Since the 90's of the 20th century, driven by external factors such as the global industrial upgrading, restructuring and the tides of integration, the size and number of global M&A has been in a rising trend, the volume of transactions reaching new heights. The World Investment Report of UNCTAD shows that in 2005 the world's foreign direct investment reached 916 billion U.S. dollars, of which the total amount of global cross-border M&A accounted for 761 billion U.S. dollars. That means 80% of total FDI were achieved through M&A. China has become the world's largest destination of foreign direct investment after UK and USA. FDI inflow increased to 72.4 billion U.S. dollars. In the strong absorption of foreign capital, the growing Chinese enterprise started to increase foreign investment. At the end of June 2006, Chinese accumulated direct investment reached 63.64 billion U.S. dollars. Cross-border M&A has become an important way in Chinese foreign direct investment.

The following data shows that Chinese enterprises have a rapid development on cross-border M&A. First of all, the cross-border M&A behavior of Chinese enterprises has significant growth both in frequency and amount (Chart1-1). During 1988-1997, Chinese enterprises only had a limited number of cross-border M&A, the annual amount of M & A is less than 600 million U.S. dollars. After 1997, the amount of cross-border M&A had rapid growth. The amount of M&A in 1998 is more than 1.1 billion U.S. dollars. In 2003 it is higher than the 5.2 billion U.S. dollars. In 2005, the amount reached to 9.5 billion U.S. dollars.

Chart1-1 1992-2005 the increasing of Cross-border M&A in Chinese enterprises<sup>1</sup>



Secondly, the percentage of the amount of cross-border M&A accounted for FDI had a large change (Chart 1-2). Before year 2000, the percentage of the amount of cross-border M&A accounted for FDI was no more than 20%, while in 2000 the percentage was as high as 50%. And in 2004 it was more than 60%, but fell back to 33% in 2005. Therefore, the cross-border M&A could not be said had an advantage in China's overall FDI, can only say that the growth was coming.

Chart 1-2 1990-2005 percentage of the amount of cross-border M&A accounted for FDI<sup>2</sup>

year	Amount of C-B M&A (hundred million dollars)	FDI (hundred million dollars)	C-B M&A / FDI %
1990	0.6	8	7.5
1995	2.5	20	12.5
2000	4.7	9.2	51.3
2001	4.5	68.9	6.5
2002	10.5	25.2	41.7

<sup>1</sup> UNCTAD.ORG, Key Data from WIR Annex Tables  
<http://www.unctad.org/Templates/Page.asp?intItemID=3277&lang=1>

<sup>2</sup> UNCTAD.ORG, Key Data from WIR Annex Tables  
<http://www.unctad.org/Templates/Page.asp?intItemID=3277&lang=1>



2003	16.5	-1.52	/
2004	11.5	18.1	62.6
2005	23	69.2	33.2

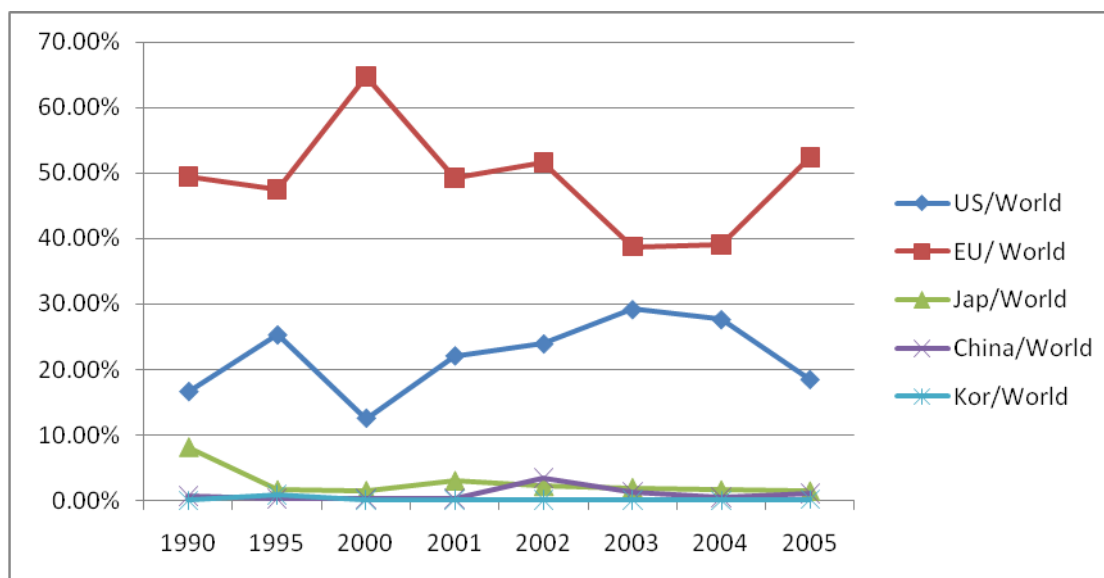
In horizontal way, the scale of cross-border M&A of Chinese enterprises is still insignificant comparing to some European and American countries (Chart 1-3 and Chart 1-4), but in 2001-2004, the amount of cross-border M&As of the Chinese enterprises was more than South Korea's. According to an incomplete statistics , in 2005, the amount of cross-border M&A of Chinese enterprises was just after Japan and South Korea in Asia, which means that the cross-border M&As of Chinese enterprises not only has a very high speed development, but also a big scale.

Chart 1-3 1990-2004 the amount of cross-border M&A of Chinese enterprises and other countries (million dollars)<sup>3</sup>

Country / region	World	Developed economies	Developing economies	United States	Japan	European Union	China	Korea
1990	200 389	175 360	9 975	33 292	16 294	99 195	1 340	46
1995	231 577	207 788	18 176	58 671	3 729	109 904	759	2 091
2000	1 349 777	1 209 787	120 746	168 965	20 264	874 258	3 787	1 442
2001	730 441	664 422	52 976	161 499	21 990	360 172	2 023	645
2002	483 238	423 909	42 195	115 708	10 492	249 534	16 332	217
2003	411 302	344 581	36 550	120 176	8 050	159 393	5 256	567
2004	565 871	471 033	45 894	156 593	8 992	221 273	2 725	206
2005	929 362	777 609	99 455	171 534	13 220	486 504	9 546	1 702

<sup>3</sup> UNCTAD.ORG, Key Data from WIR Annex Tables  
<http://www.unctad.org/Templates/Page.asp?intItemID=3277&lang=1>

Chart 1-4 1990-2004 percentage of the amount of cross-border M&A accounted for world (%)<sup>4</sup>



Statistics show that in the tenth Five-year plan period, China's enterprises which engaged in transnational business were more than 30,000. World Investment Report 2006 showed that Chinese multinational corporations took half in the world's 100 largest transnational corporations in developing countries.<sup>5</sup> From 2000 to 2004, the total amount of external acquisition raised from 1.8 billion U.S. dollars to 4.8 billion U.S. dollars. Even excluding China National Offshore Oil has withdrawn 18.5 billion U.S. dollars of the amount of the bid in 2005; the annualized transaction volume had reached 6.2 billion U.S. dollars. Studies show that high saving rate and the appreciation of the RMB will make the Chinese enterprises to maintain the Cross-border M&A. In the next decade Chinese enterprises will appear in the massive wave of Cross-border M&A.<sup>6</sup>

In the world economic market, Chinese enterprises are no longer the spectators; they have already been one part of the world economic market. However, on the Chinese management trend conference, Zhu Wei, the Chinese president of Roland Berger Strategy consultants- the biggest strategy consulting firm, said that "the M&A

<sup>4</sup> UNCTAD.ORG, Key Data from WIR Annex Tables  
<http://www.unctad.org/Templates/Page.asp?intItemID=3277&lang=1>

<sup>5</sup> World Investment Report 2006

<sup>6</sup> Xu Jing (2006), *Chinese biggest ten merger cases review in 2006*,

of Chinese enterprises are in the exploratory stage, most of the Chinese enterprises are lack of experience of M&A",<sup>7</sup> M&A agreement is just the beginning. For Chinese enterprises, the way how to integrate the business and the resource after cross-border M&A is the key to a successfully M&A<sup>8</sup>.

However the integration after merger is the weakness of the majority of Chinese enterprises. Those Chinese enterprises Cross-border M&A cases which have shocked the world should have basically completed the integrating task and achieved anticipated synergies and the financial returns. But so far their performance is not optimistic or even close the business altogether. Therefore, in order to enhance the integrating ability of Chinese enterprises, the success rate of integration and to achieve synergies of Cross-border M&A and financial returns, Chinese enterprises should learn and summing up experience from the case of the failure of the integration. Only in this way can provide the international status of Chinese enterprises and achieve the internationalization of Chinese enterprises.

Based on the integrating research after the Cross-border M&A from the predecessors, this dissertation will do an reflection based on the SAIC takeover Ssangyong case and the TCL takeover Thomson's European TV business case. Hopefully it can help the high level managers and the integrating managers to pay attention to the integrating work. Furthermore, from these two cases we can sum up some experiences which can be learnt by the Chinese enterprises and can play a guiding role for the Chinese enterprises in the Cross-border M&A area. This dissertation has a broad meaning for the enterprise management and the integrating managers.

Firstly it can make the main managers of the enterprises to understand the importance of the cultural integration and the corporate governance structural adjustment. Secondly, this study can provide some ideas for the integrating managers. Finally is to improve the success rate of Cross-border M&A and to ensure the

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<sup>7</sup> Pan Qingshan (2005), Chinese enterprises have to stride over four obstacles, *CNAUTONEWS*, 5.

<sup>8</sup> Wang Xiaobo (2007), *The integrating ability after Merger is the weakness of Chinese enterprises*, *China Youth News*.

efficiency of social resources can be maximized.

This dissertation has seven parts. The first part introduces the studying background of this dissertation and the object of writing this dissertation which is to study the cultural impact and the governance impact in the Cross-Border M&A and finally to increase the success rate of Cross-border M&A. The second part introduces the existent research result on the cultural integration and corporate governance structure. The third part gives the answer that why we have to study the SAIC and TCL case and the methodology to analyze the cases. In the fourth and the fifth parts, we have the description of these two cases by recurring secondary data. The sixth part proposes some recommendations which can help the Chinese enterprises to better execute the cultural integration and to improve Chinese corporate governance structures. The last part concludes this dissertation's research result and point out the limitation of this dissertation.

## 2. Literature review

Cross-border M&A is the extensive growth path to achieve rapid expansion for the enterprises. With the upgrading of Chinese industrial structure adjustment and increasing economic globalization, the M&A activities of Chinese multinational enterprises became increasingly active. However, whether in international or domestic, the overall results of M&A are not optimistic. The failure of a large number of cases led to many academic and business studies. Although the reasons for the failure are not all the same, but what is certain is that the cultural conflict after the M&A and the difference between corporate governance structures are the most important issues.

Hofstede (1984) considered that culture “is the collective programming of the mind which distinguishes the members of one group or category of people from another.”<sup>9</sup> Jemison, Sitkin (1986) and Buono *et al.* (1985) considered that “a big cultural difference probably may lead to “cultural ambiguity” and processing loss.” “A long cultural distance usually link to integrating conflict” (Jemison and Sitkin, 1986). Empirical result shows that a M&A activity with obvious cultural difference will lead to a negative attitude of the investors. “Buono, Bowditch and Lewis believe that the difference of the management style is probably the main reason of the failure of the M&A.” It will lead to the low commitment and the noncooperation of target company's staff. “Hambrick and Cannella (1993) believe that the difference of management style also will lead to high demission of target company's high level managers”.<sup>10</sup> Chatterjee (1992), Nahavandi and Malekzadel (1988) brought the cultural factor to the M&A research and built up a theory that a success mergers require cultural compatitablility.<sup>11</sup> The research discovered that the accordance of

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<sup>9</sup> Hofstede.G (1984), *Culture and Organizations of the Interculture Cooperation and its Importance for Survival*, London: McGrwa-Hill.

<sup>10</sup> Chatterjee,S., M.H.Lubatkin, D.M.Schweiger, and Yweber (1992), Cultural differences and shareholder value in related mergers: linking Equity and human capital, *Strategic Management Journal*.

<sup>11</sup> Nahavandi,A. and A.R. Malekzadeh (1988), Social capital, intellectual capital and the organizational advantage, *Academy of Management Review*, 2.

two different cultures is indispensable for a success merger.<sup>12</sup> After them, Cartwright and Cooper (1992, 1993) proposed the principle of cultural compatibility based on the cultural classification of Harrison (1975). Weber (1996) inspected the influence of the cultural distance in high level management. Philip Very (1997) inspected some advanced managers from English and French companies which have been merged by other companies. He pointed out that the target companies' performance after being merged has a direct link to the cultural attraction of the merging company. Olie (1990) has the same discovery. He considers that "the success integration of Cross-border M&A depends on the level of cultural influence, the level of integration and how much do they cherish their culture." Olie (1994) also inspected the company factors in Cross-border M&A. He discovered that the difference of management style, difference of organization structure and culture, the level of coordination after M&A and the relationship of the two companies have shown the difficulty of integration after Cross-border M&A.

Scholars in different areas have different definitions of corporate governance. "James McRitchie (1999) considers that corporate governance is most often viewed as both the structure and the relationships which determine corporate direction and performance. The board of directors is typically central to corporate governance. Its relationship to the other primary participants, typically shareholders and management, is critical. Additional participants include employees, customers, suppliers, and creditors. The corporate governance framework also depends on the legal, regulatory, institutional and ethical environment of the community. Monks and Minow (1996) consider "that corporate governance is the relationship among various participants, chief executive officer, management, shareholders, employees, in determining the direction and performance of corporations." There is a considerable variation in corporate governance structures around the world such as Korean model, Japanese model, Germany model and the Anglo-English model. "Therefore, the selection of corporate governance structure after Cross-border M&A becomes very complicated.

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<sup>12</sup> Weher, Y., O. Shenkar, and A. Ravel. (1996), National and Corporate Cultural Fit in Mergers & Acquisitions: An Exploratory Study. *Management Science*.

Because there are two sources of such difficulties: First, the different national or corporate cultures, and second, the different laws or constitutional conditions” (Reinhart Schmidt 1999). The OECD reflects this view in the preamble to its “Principles of Corporate Governance”, where it states: “There is no single model of good corporate governance.”<sup>13</sup> Monks and Minow (1996) said that “it is a mistake to attempt to impose one country's corporate governance system on another's”. And Sheridan/Kendall (1992) considered that “different countries have different ideas as to what constitutes good corporate governance.”

Currently Chinese academic circles mainly research the relationship between Cross-border M&A and corporate governance structure. Qu Tao and Li Shan-min (2004) consider “that absorbing Cross-border M&A will be favorable to the improvement of FDI quality and corporate governance”.<sup>14</sup>

According to the research, we consider that the cultural integration after the M&A and the corporate governance structure are the most important elements that will affect the success of the Cross-border M&A. But the fact is that the Chinese enterprisers pay little attention to the cultural integration and the corporate governance structure. In order to increase the success rate of the Cross-border M&A, the Chinese enterprises and the managers shall learn the importance of the cultural integration and the corporate governance structure and pay attention to them.

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<sup>13</sup> “OECD Principles of Corporate Governance”, Preamble, p2. (The Principles can be downloaded from: [www.oecd.org/daf/governance/principles.html](http://www.oecd.org/daf/governance/principles.html))

<sup>14</sup> Qu Tao, Li Shan-min (2004), Corporate governance structure and Cross-border M&A, *Journal of Guangdong University of Business Studies*, 3.

## **3. Methodology**

### **3.1 Study object**

Nowadays, more and more Chinese enterprises use Cross-border M&A to enlarge their business in the global market. From last part we know that the business culture and the corporate governance structure will affect the success of the M&A. In order to help people understand the importance of the cultural integration and the corporate governance structure I will analyze two cases in this dissertation. These two cases are SAIC takeover Ssangyong and TCL takeover Thomson's European TV business.

Choosing SAIC takeover Ssangyong as our study object is because this case is the first takeover case in Chinese automotives industry. It got lots of attention from both home and abroad. Furthermore, we can find that the cultural collision was very evident in the integrating process. The cultural collision brought many problems to both companies. After many years integration, the acquisition ultimately failed. But through this case we still can learn how to executive cultural integration after the M&A.

In the TCL case, we can find the importance of the corporate governance structure. A cross-border M&A may lead to the integration of two different corporate governance systems. But through the case we found that Chinese corporate governance structure is imperfect. The imperfect corporate governance structure effects the structural integration after the mergers. After studying this case, hopefully the Chinese enterprises will know how to design the corporate governance structure for the new company.

### **3.2 Study method**

In order to make the case more objective and comprehensive, I will use the secondary data to describe the cases. In this way, this dissertation is a new case analysis based on the secondary data.



In the SAIC case, the analysis will follow the step of cultural integrating process of Pan Ailing (2004). This model will separate the whole cultural integrating process into 4 stages which are the preparing stage, crashing stage, integrating stage and creating stage. I will analyze what have SAIC done in each stage and to find out what have SAIC done wrong and what can be a good example for other Chinese enterprise. For example, at the preparing stage, I will use Hofstede's five-factor model to analyze the Korean culture and Chinese culture. In addition, I will use the Culture Bridging Fundamental (CBF) model as the tool to analyze the business culture of SAIC and Ssangyong. CBF model is designed by Charles Gancel and Irene Rodgers (2004). It gives the manager an analysis of the business culture and helps the managers to solve the cultural integrating problems.

For the TCL case, The starting point is to compare the corporate governance structures of TCL and the corporate governance structure of Thomson. With the comparison we can find the difference of these two kinds of governance structures and the defects of the Chinese corporate governance structure.

### **3.3 Study subject**

In order to study these cases better, we also need to know the background of these companies. Here is a brief introduction of these companies.

#### **Shanghai Automotives Industry Corporation**

Shanghai Automotive Industry Corporation (Group) ("SAIC" for short) is one of the top 3 automotive corporations in China. SAIC and it is mainly engaged in manufacturing, sales, research and development, investment in passenger cars, commercial vehicles and components, as well as related services trade and financial business. Besides, SAIC holds 83.83% of the equity of SAIC Motor Co., Ltd. In 2007, SAIC once again topped the Chinese automotive groups for a sales volume of over 1.69 million units of vehicles, of which 1,137,000 are passenger cars and 553,000 commercial vehicles. In 2008, the company also entered the Fortune Global 500 list

for its consolidated revenue of \$22.6 billion (2007), ranking 373.<sup>15</sup>

#### Korean Ssangyong motor Group

The Korean Ssangyong Business Group was founded in 1939 and is now a large conglomerate with interests in cement, oil, paper and financial, information and leisure services. In 1986, Ssangyong bought the Ha Dong Hwan Motor Company, which had been making four wheel drives and trucks since 1954. In 1991, Ssangyong formed an alliance with Mercedes Benz, licensing light commercial diesel and petrol engines and other components. The Ssangyong Musso has been in production since 1993 and the smaller model of Korando since 1997. In 2002, new models have set to production like Rexton and Musso Sports Utility began being produced since late 2003. In January 1998, Korean carmaker, the Daewoo Motor, took a controlling interest in Ssangyong, but during the Asian financial crisis of 1999, the control of Ssangyong passed to Korean banks, with Mercedes Benz taking a minor shareholding.<sup>16</sup>

#### TCL Group

Established in 1981, TCL Corporation is a global leader and technology innovator in consumer electronics, mobile communications and home appliances. TCL employs more than 50,000 people in over 80 operations, including 18 R&D centers, 20 manufacturing bases, and more than 40 sales offices around the world. With 2008 global sales of USD 5.63 billion (including 14.36million TV sets and 13.7 million mobile handsets), and serving more than 100 million consumers worldwide, TCL Corporation is comprised of four business divisions -- Multimedia, Communications, Home Appliances and Techno Electronics. It also has two affiliated business areas: Real Estate & Investment and Logistics & Services. TCL is one of the world's leading producers of flat panel TVs, DVD players, air conditioners, and GSM, CDMA mobile phones. In 2004, TCL merged with some of the world's most admired and recognized brands and businesses, including the Thomson television business and

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<sup>15</sup> SAIC Group, Introduction of SAIC <http://www.saicgroup.com/English/sqjt/gsj/index.shtml>

<sup>16</sup> Ssangyong Moto, Ssangyong the company <http://www.ssangyong.co.za/news.asp>

Alcatel mobile phones.<sup>17</sup>

### Thomson Group

Thomson is the world leading provider of solutions for the creation, management, delivery and access of content for the communication, media and entertainment industries. Under the Technicolor brand, the Group offers its content creator and distributor customer base services related to the creation, preparation and distribution of premium video and film contents. Through its Thomson Connect activities, the Group supplies satellite, cable and telecom operators with access and home networking devices and software platforms. Thomson conducts extensive research and development activities to innovate and to support its solutions to the Communication, Media & Entertainment industries. The Group also licenses its intellectual property.<sup>18</sup>

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<sup>17</sup> TCL Group, Company profile about TCL  
[http://www.tcl.com/main\\_en/About%20TCL/Company%20Profile/index.shtml?catalogId=13046](http://www.tcl.com/main_en/About%20TCL/Company%20Profile/index.shtml?catalogId=13046)

<sup>18</sup> Thomson, About Thomson  
<http://www.thomson.net/GlobalEnglish/Corporate/About/Pages/default.aspx>

## 4. Case 1: SAIC Takeover Ssangyong

### 4.1 Case description

At the end of 2003, Ssangyong's creditors decided to sell their Ssangyong's stake by global tendering. Shanghai Automotive Industry Corporation (SAIC) participated in this bidding, and by the end of October, SAIC hired third-party agencies such as Deutsche Bank and Swiss Bank to do the first phase responsible investigation, to study Korean law, regulations, customs and culture. July 27, 2004, SAIC had been identified as preferred bidder by Ssangyong creditors, and both of them signed a binding memorandum. SAIC began to start a 3 weeks comprehensive responsible investigation. After the final investigation, SAIC and Ssangyong entered the final negotiation.<sup>19</sup>

When negotiating with the Ssangyong's creditors, SAIC had a very tense negotiation with Ssangyong's labor union. July 22, 2004, Ssangyong's labor union held a strike and asked for a special agreement from SAIC. The special agreement included the establishment of overseas manage strategy committee, allow the labor union to participate the decision-making process, the protection of employment and the equipment will not be transferred. October 28, 2004, the special agreement was accomplished. At the same day, SAIC and Ssangyong Motor Company signed the M&A contract in Seoul, SAIC spent 500 million U.S. dollar to acquire a controlling 48.9 percent stake of Ssangyong Motor. South Korean Ssangyong Motor Co., Ltd. became a holding subsidiary of SAIC. Since then, SAIC purchased Ssangyong's shares through the stock market more than 10 times to have 51.33% Ssangyong's shares which achieve the absolute control of Ssangyong.<sup>20</sup>

### 4.2 Case discussion

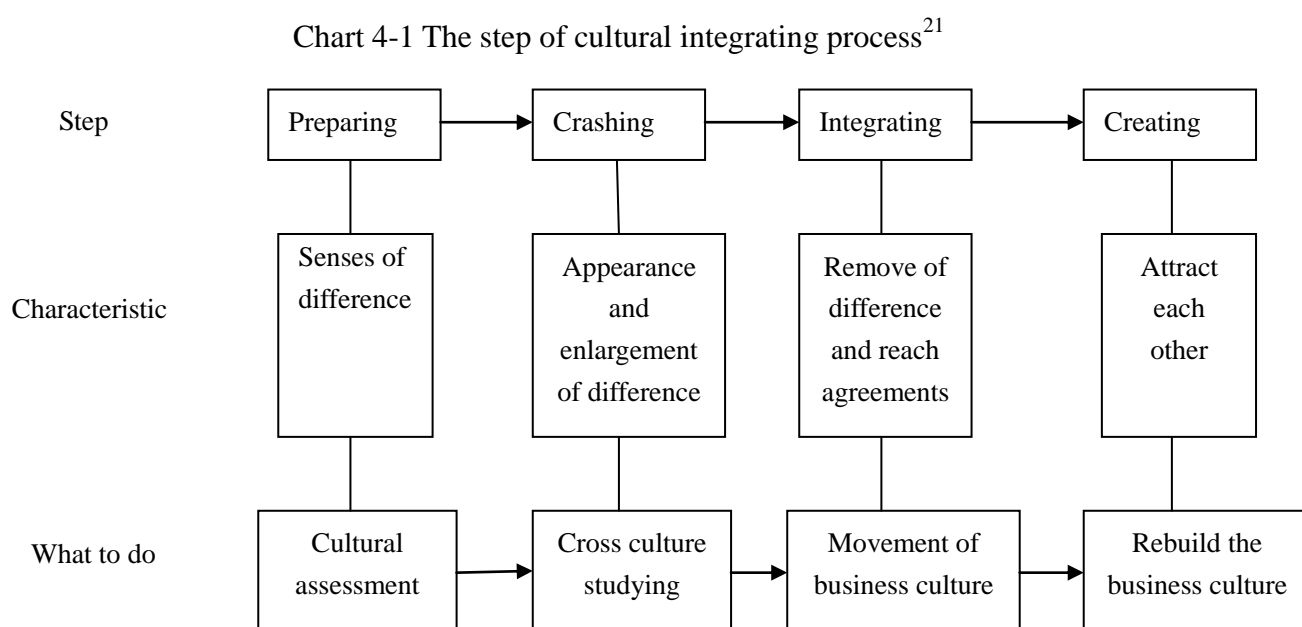
The analysis will follow the step of cultural integrating process. According to

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<sup>19</sup> Liao Yunfeng (2007), *Chinese enterprises Cross-Border M&A case analyze*, Enterprise Management Publishing House, P55.

<sup>20</sup> Liao Yunfeng (2007), *Chinese enterprises Cross-Border M&A case analyze*, Enterprise Management Publishing House, P56.

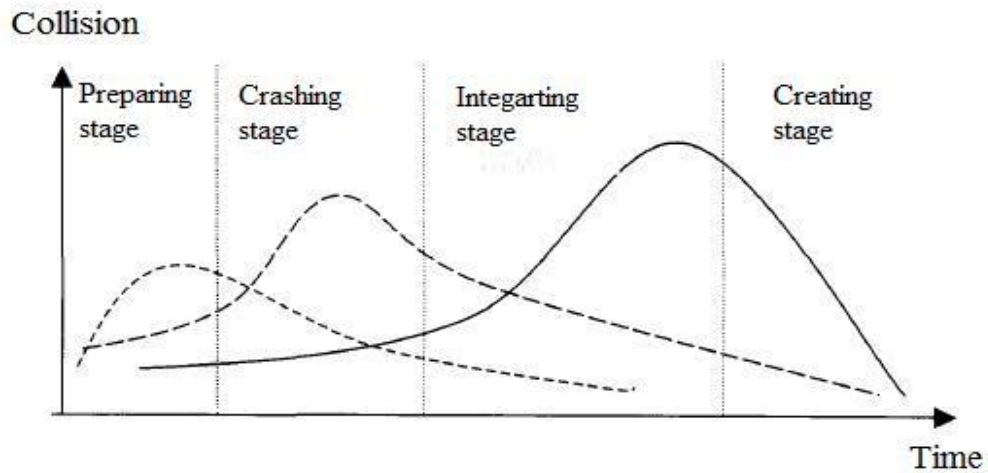
Pan Ailing (2004), the cultural integration of cross-border M&A can be divided into 4 stages which are preparing stage, crashing stage, integrating stage and creating stage. Each stage has different characteristics and focusing. In the preparing stage, the merger company has to do the cultural assessment and find the cultural difference between two companies. And in the crashing stage, the merger company has to study the cultural difference. In the integrating stage, the merger company has to remove the cultural difference. In the creating stage, the merger company will finally build up a new business culture. Now I will analysis this case accordance with the following chart. (Chart 4-1)



The integrating process is similar, but in the different cases, the possibility and the size of the cultural collision will be different. The following figure shows the main form of the possible three curves. SAIC used a secure integrating strategy. It means that SAIC will not do a drastic restructuring and personnel changes at once after the M&A. SAIC made a significant restructuring and personnel changes one year after the M&A. So the cultural collision occurs mainly in the integrating stage, just like Chart 4-2.

<sup>21</sup> Pan Ailing (2004), Process Designing and Pattern Choice of Cultural Integration during Cross-border Merger and Acquisition, *Naikai Business Review*, 6.

Chart4-2 Cultural collision curve<sup>22</sup>



#### 4.2.1 Preparing stage - Culture assessment

In the preparing stage of cultural integration, the main work is to make a comprehensive study and evaluation of cultural background of the enterprises, to analysis the cultural differences and the possibility of collision, and make a preliminary integrating program according to the study and the analysis. “Cultural assessment should be focused on the cultural strengths, weakness and type of the both of the companies. And cultural assessment should have the analysis of the both companies' business culture, the evaluation of the size of cultural difference, analysis of the cultural integrating points and opportunities.”(Pan Ailing, 2004) cultural assessment is the precondition to make a cultural integrating project, to select the integrated model and have an effective integration.

Because both of the cross-border M&A companies are from different countries, normally they will face the difference of the business culture and difference of national culture. As a result of differences in national culture, the members of the cross-border M&A companies have different values, beliefs and traditions, which determine their different behavior. Business culture is a "micro" culture which is born and running under the national culture. General speaking, the bigger differences in national culture, the bigger difference in business culture, It means that each national

<sup>22</sup> Pan Ailing (2004), Process Designing and Pattern Choice of Cultural Integration during Cross-border Merger and Acquisition, *Naikai Business Review*, 6.

culture has a strong relate with a range of business management, showing a special business culture which is decided by the national culture.

Chart 4-3 The relationship between cultural difference and M&A<sup>23</sup>

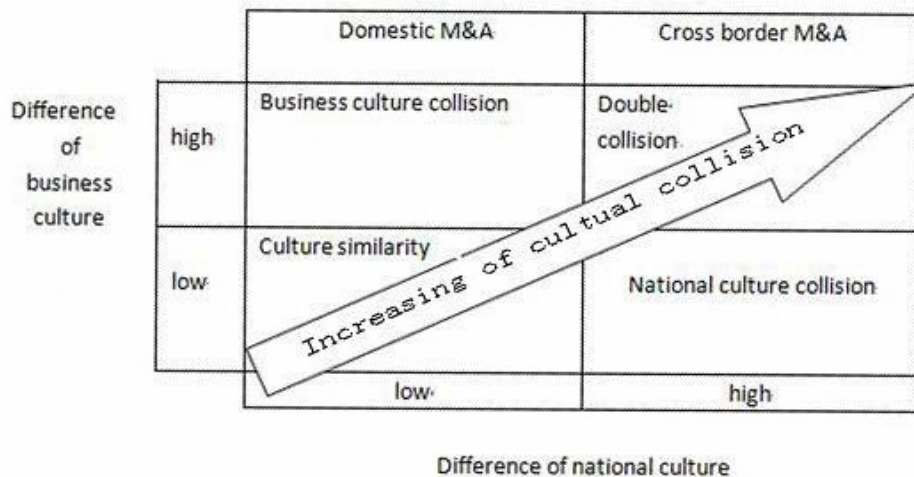


Chart 4-3 compares the cultural differences and collision of the domestic M&A and cross-border M&A. Domestic M&A majorly face the difference and collision of the business culture. The cross-border M&A face the difference and collision both of the business culture and national culture. Therefore, the cultural assessment of a cross-border M&A must contain the national cultural evaluation of two countries and the business cultural evaluation.

(I). Similarities and differences between China and South Korea's national culture

With Hofstede's five-factor model of cultural analysis (Annex I) we found that the national culture of China and South Korea has great similarity. But they still have some differences on power distance; the South Korea's score is higher than China, which means that in South Korea, there is great distance between the boss and the employees. On the uncertainty avoidance factor, China and South Korea are the high uncertainty avoiding society, but South Korea scored higher, most of Korean lack a sense of security, they have a strong contradiction on the uncertain and ambiguous

<sup>23</sup> Deng Hong (2007), Intercultural Integration in M&A in Chinese Enterprises, *Science & Technology Process and Policy*, 12.

things. Although China and South Korea are advocating collectivism, but nowadays the individualism is increasing in China while the Confucian culture in Korea has retained more complete. In the masculinity factor, South Korea is more like femininity. On the long-term orientation factor, the Chinese scored higher, it means that Chinese can give up their short-term gain in order to get a long-term gain. Compared with the Chinese, Korean people are short-term orientation. The long-term gain is full of risk, short-term gain is more reliable, so they do not believe that the long-term commitment. In addition to the five cultural differences, China and South Korea have some unique cultural characteristics of their own national culture:

#### (1) Chinese national culture

Chinese traditional culture has long history and is profound, is a multi-cultural composition. The doctrine of Confucianism and Taoism constitute Chinese traditional culture's main structure. The doctrine of Confucianism and Taoism contain numbers of philosophy and reason, they have tremendous impact on the mentality and character of the Chinese nation and imperceptible influence on people's life and ways of thinking. And its main features are the doctrine of the mean and the inclusive.<sup>24</sup>

- The doctrine of the mean

Chinese traditional culture of Confucian creates Chinese people's values-doctrine of the mean. The most basic meaning of the doctrine of the mean is "listen to both sides and choose the middle course", "going too far is as bad as not going far enough". It means pay attention to harmony, and insist on moderation. The doctrine of the mean is one of the basic spirits of the Chinese nation and making the Chinese people very focused on the achievement of harmony and maintain. Do no extremes, strive to safeguard the collective interests, seek common ground while reserving differences, and have become the universal principles of thinking. The doctrine of the mean maintains follow in proper sequence, saying that "More haste, less speed".

- Inclusive rather than lack of adaptability

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<sup>24</sup> Ma Juping, Chen Lizhen (2005), Unscramble the corporate culture of Korea, *Chinese & Foreign Corporate Culture*, 6.



Chinese culture has a strong sense of inclusiveness, and tolerance to allow the existence of various cultures. At the same time Chinese culture absorb the essence of other culture and constantly adjust and perfect its own culture. This kind of culture and the pride of the Chinese nation have been made the poor adaptability of Chinese culture. In 2004, Roland Berger did a research on the 50 biggest Chinese enterprises; the result showed that the Chinese enterprises are the groups that do not attach importance to cultural differences, although 90% of them have been in operating in overseas projects.

## (2) South Korean national culture

South Korea and China belong to East Asia, they have many cultural similarities. In South Korean history, Confucianism has been the mainstream of South Korea as philosophy, and impact South Korea profoundly. However, the Japanese colonial rule during 1910 to 1945, years of the assistance from United States after World War II, development of export-oriented economic and prosperity of foreign trade have made the Korean culture affected by Japan and the United States in different level. In addition, Korean own history, tradition and experience formed a unique Korean culture.

South Korea's national cultural characteristics are mainly embodied in two aspects: the new Confucian ethics, multi-cultural integration and transformation.<sup>25</sup>

### ● The new Confucian ethics

The values of "virtue", "loyalty", "humility" are reinstated as part of the new Confucian ethics. However, due to the historical process and the special geopolitical background, Korean culture is mixed up with other foreign cultures such as Buddhism and Christianity and has transformed the core values of Confucianism. The new Confucian ethics, a political ethics with Korean characteristic, it stressed a sense of responsibility, patriotic loyalty, pay attention to family, stressed coordination and cooperation between members, pay attention to education and advocating talent. New

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<sup>25</sup>Feng Jinling (2004), On South Korea's National Cultural Characteristics and its Modernization, *Journal of University of International Relations*,4.

Confucian ethics has a profound impact on Korean socio-economic and family life.

South Korean business culture is full of features of new Confucian ethics which reflected in a highly centralized organizational structure and senior leadership of the power management system as well as acts of authority. Korean has strong personality, but when they are organized into groups together with a sense of belonging to the organizations, then a strong type of organizational culture is enacted. In the performance evaluation and reward system, seniority continues to dominate the Korean business.

- Multi-cultural integration and transformation

In the mid-20th century to 1980s, the number of Catholics and Protestants in South Korea has had a big increase. The fighting spirit of Christianity, the assertiveness of Protestants and the authority of Confucianism and Buddhism are integrated together and therefore, provided a reliable belief for South Korea's national spirit. This new spirit increased the concept of equality and independence, and provided a fresh air to the Korean traditional culture.

This kind of multi-cultural ambience pushes the Korean enterprises to “corporatism”. South Korean companies now have a common tendency which is stressing a “harmony” community-style business culture and a trust between employers and employees. Enterprises in South Korea stressed the harmony, especially in the different administrative levels; the leaders attach great attention to interpersonal relationships with their subordinates, and fully understand the needs and feelings of his subordinates. Before making major policy decisions, leader must ask for opinion from his subordinates. Especially in the development of decision-making, leader will do his best to determine and understand the views and feelings of his subordinates. However, many Korean employees are not good at expressing their opinion at a formal meeting, especially an opposition. Expressing a different opinion in public may embarrass the leaders or colleagues even breed emotional resistance. The essence of Korean culture does not encourage expressing personal views in public, unless the parties have a close personal relationship. However, Korean like to

express their views in an informal setting, sometimes is a negotiation with boss in an informal setting. In South Korea, the informal contacts between managers and subordinates are more frequently, contact in an informal setting is considered a very important way to build a superior-subordinate relationship.

## (II) Differences and similarities in the business culture

Culture itself is very abstract, unconscious and not obvious. And business culture, as compared with the national culture is more complex, more volatile. To integrate the two different business cultures, first of all, it is has to embody and simplify the corporate culture. Here I use Culture Bridging Fundamental (CBF) model as an analytical tool to analyze the business culture of SAIC and Ssangyong.

The CBF model is a specialized model designed by Charles Gancel and Irene Rodgers who are the managing partners of Inter Cultural Management Associates. The CBF model provides the manager an analysis of the business cultural integrating problem and helps the manager to solve the problem. If the enterprises want to integrate the business culture between two sides of the M&A, it must answer the following three questions.

- Forward-looking: How to communicate and exchange the company's goal in the organization and being generally agreed by the staff? <sup>26</sup>

In the forward-looking, the business culture have three orientation: some culture tend to focus on the organizational structure, they believe that if the organizational structure of enterprises is reasonable and everybody assume all their responsibilities, then the companies can be able to cope with the challenges from the market. Some culture tend to focus on the communication of the strategic objectives, they firmly believe that when employees know the direction of enterprise development - its strategy and objectives - especially when they know what should be done, the employees can feel a sense of security. Some culture stressed on the business tradition: they believe that whether the employees can find strong corporate values and

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<sup>26</sup> Xiong Yongqing, Hu Ming (2005), Cultural risk on M&A and its measure model, *Science & Technology Process and Policy*, 12.

traditions and use these strong corporate values and traditions to the development of the company, is the key point that the staff is able to really integrate into the enterprise or not.

Both SAIC and Ssangyong's business cultures are inclined to the communication of the strategic objectives they firmly believe that when employees know the direction of enterprise development - its strategy and objectives, the employees will feel a sense of security.<sup>27</sup> But they have a huge difference on the understanding of the strategic objectives. The strategic positioning from SAIC to Ssangyong Motor is the oversea technology platform, that is to say SAIC wants to use of Ssangyong's technology.<sup>28</sup>

It is clear that the Ssangyong is very worried about the strategic positioning.<sup>29</sup> In South Korean people's opinion, Chinese means cheap labor and backward technology, and they not only worry that the high technology will flow to China, but also worry that SAIC will move the factories to China, resulting in lost of their jobs. No matter what kind of culture, in the forward-looking challenges, communication is the most basic and most important point.<sup>30</sup> SAIC needs to make a continuous communication with Ssangyong's stakeholders in order to timely and clearly transmit the strategic positioning, the meaning and the benefits to the stakeholders. Make sure the Ssangyong's employees agree with this strategy positioning.

- Legitimacy: how will the staff regard credibility and authority of the managers and leaders in the organization?<sup>31</sup>

Different teams and organizations have different opinions on the legitimacy. In other words, it means that people have different preferences on what is their "reputation" and "authority". The standards that the employees choose to trust and the

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<sup>27</sup> Liao Yunfeng (2006), *Domestic enterprises' overseas M&A*, China Financial and Economic Publishing House, p247

<sup>28</sup> Liao Yunfeng (2006), *Domestic enterprises' overseas M&A*, China Financial and Economic Publishing House, p247

<sup>29</sup> Liu Tao (2006), Enlightenment of SAIC on Korea, *China Entrepreneur*, 12.

<sup>30</sup> Xiong Yongqing, Hu Ming (2005), Cultural risk on M&A and its measure model, *Science & Technology Process and Policy*, 12.

<sup>31</sup> Xiong Yongqing, Hu Ming (2005), Cultural risk on M&A and its measure model, *Science & Technology Process and Policy*, 12.

determination to follow a leader are held differently from different cultures. In legitimacy, there are three distinct cultural preferences: The first one is the preference of an intelligent leader which is well-educated, skilled with theoretical knowledge, academic qualifications and a variety of titles. The second preference is for a leader with good performance on the job and with lots of working experience. The third cultural preference lies in the "insiders" which have similar work experience and social background as the coworkers.

In the credibility and authority issue, Ssangyong belongs to the "insiders" type and "working performance" type. First of all, as a typical South Korean company, Ssangyong strongly emphasizes the seniority. Ssangyong's staff pays a lot of attention on leader's experience, background and social skills.<sup>32</sup> Most of the Korean managers have been working in Ssangyong for 20 to 30 years and most of them would have by almost all the internal departments like production, marketing and planning. This is also why managers could exert great influence on all strategic matters in Ssangyong'.

On the other side, according to article «Ssangyong event» from Xu Jiawang (2009), we can find that SAIC culture prefers a good working performance leader. All the managers that SAIC dispatches to Ssangyong are capable, such as director Jiang Zhiwei, the vice president of SAIC; vice president Zhang Haitao, general manager of one of SAIC subsidiary; Zhu Xian who is in charge of finance and Shen Jianping who is in charge of procurement. Unfortunately, all of these people lack of international management experience. That is because SAIC did not have enough managers who are good at cross-border management. And this is the same problem that most of Chinese enterprises will face which want to go out.

● Validity: which method should be used to resolve the contradiction, as well as how to deal with company's affairs?<sup>33</sup>

Different business culture has different preferences on the working method.

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<sup>32</sup> Ma Juping, Chen Lizhe (2005), Unscramble the corporate culture of Korea, *Chinese & Foreign Corporate Culture*, 6.

<sup>33</sup> Xiong Yongqing, Hu Ming (2005), Cultural risk on M&A and its measure model, *Science & Technology Process and Policy*, 12.

Some business culture prefers a programming operation; Some business prefers to act immediately; Some business culture prefers to start their work via their own relationship network.<sup>34</sup>

In the validity, SAIC and Ssangyong have a big difference. From the article «Unscramble the corporate culture of Korea» from Ma Juping and Chen Lizhe (2005), we found that Ssangyong is act-oriented. Ssangyong prefers to use various methods to achieve the goal as quickly as possible and gain as more resource as possible. This is also a reflection of Korean culture.

But SAIC is difficult to summarize in validity. On one hand they are action-oriented, good at self-management and act according to circumstances. On the other, the influence of Chinese culture makes SAIC to be “long-term oriented”, pay attention to a smooth business operations and risk prevention.

After the analysis of national culture between South Korea and China and the business culture between SAIC and Ssangyong, let's define the cultural integration model that SAIC used. SAIC and Ssangyong are highly relevant at the strategic level. The strategic intention of this acquisition can be achieved only after the realization of the technology sharing from Ssangyong. The inclusiveness of Chinese culture makes SAIC to be inclusive with different cultures.

Concerning cultural integration, it could have two choices: blended cultural integration and separate cultural integration. Ssangyong has a very strong sense of identity with the national culture, and Ssangyong's business culture is a strong business culture. Therefore, SAIC could only choose the blended cultural integration

#### **4.2.2 Crashing stage - initial contacts**

The integration after merger needs to combine two different operation systems, which is the most difficult and most important stage in the M&A management process. The failure of the cultural integration will lead to the failure of the M&A behavior. After the acquisition of Ssangyong, SAIC did not have a drastic

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<sup>34</sup> Ma Juping, Chen Lizhen (2005), Unscramble the corporate culture of Korea, *Chinese & Foreign Corporate Culture*, 6.

restructuring and personnel changes, but did some changes step by step. This activity is directly related to the Chinese culture. Chinese culture emphasize in front of an unfamiliar environment, step-by-step is the best way to minimize the risk. And we can learn and adjust as the case may change at any time.

In order to eliminate doubts from Ssangyong and win the trust, at the beginning of M&A, SAIC almost retained the whole management team of Ssangyong. But that is because SAIC didn't have enough international management talent and didn't have the ability to completely take over Ssangyong.<sup>35</sup> But objectively speaking, at that time, the market condition and the operation of Ssangyong were not bad. It's not necessary for SAIC to take over the Ssangyong completely. On the other hand, retaining the original management team can reduce the misgivings and achieve a smooth transition.

In order to achieve the integration and eliminate the differences between Ssangyong and SAIC as soon as possible, SAIC hired a multinational management consulting firm to make a “hundred days integration plan”.

One of the first measures were that the representatives of SAIC and Ssangyong to announce in press conference the new values of Ssangyong which are “ the new one mine”, “new starting point” and “new challenges”.<sup>36</sup> Ssangyong used the slogans such as "Let's start a new Ssangyong, you can do it" and "emphasize the principal and trust each other" to transfer these new values to the staff.

In the beginning of the M&A negotiation, SAIC's managers were very concern with how Ssangyong's employees understand the Chinese culture and SAIC's culture and to identity the future operating principle of SAIC.<sup>37</sup> After signing the formal M&A contract, in order to further appease Ssangyong which is known by the strong labor unions, and let the Ssangyong's labor unions to understand SAIC better, SAIC

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<sup>35</sup> Liao Yunfeng (2007), *Chinese enterprises Cross-Border M&A case analysis*, Enterprise Management Publishing House, P56.

<sup>36</sup> Liao Yunfeng (2007), *Chinese enterprises Cross-Border M&A case analysis*, Enterprise Management Publishing House, P60.

<sup>37</sup> Liao Yunfeng (2007), *Chinese enterprises Cross-Border M&A case analysis*, Enterprise Management Publishing House, P63.

invited the delegation of Ssangyong's labor unions to visit the SAIC, the Exhibition Hall of SAIC, production line of Shanghai Volkswagen and Shanghai General Motors factories.<sup>38</sup> So that the Ssangyong's labor unions could understand the development process of SAIC, as well as the level of vehicle manufacturing assembly line. Later, SAIC organized a visit to SAIC for the new employees who have the university degree or above for one day, so to make the new staff understand Chinese economic and cultural as well as the SAIC's future business environment.

Cultural integration should be bilateral, while promoting the knowledge from Ssangyong' staff to SAIC, therefore, Chinese managers were sent to Ssangyong for a cultural sensitivity training. From the Zhang Jinfang's article, SAIC didn't easily operate Ssangyong. The board of SAIC invited in-house staff of Ssangyong to train the Chinese managers and made them understand South Korea's customs, culture and traditions. After the acquisition the Ssangyong, SAIC gave everyone who works in South Korea a pamphlet, "Korean comic book". This book talks about the formation of Korean culture and the formation of the Korean strong sense of national pride. The highest manager Jiang Zhiwei had got a very friendly image in Ssangyong. He played a key role in the process of the acquisition of Ssangyong because he has a wealth of management experience, familiar with the automobile production and sales, participated in the whole process of the SAIC-Ssangyong M&A project.

During the "Integration Days", Ssangyong's management team and staff seemed to be coordinated. Ssangyong's high-level managers began to learn Chinese. More staff started to consider that, Ssangyong is now a Chinese enterprise, perhaps the future of themselves and their enterprises will be in China. In order to work well in China, you must learn Chinese. From January 2005, staffs in administrative and production sectors have also begun to learn Chinese.<sup>39</sup>

This good scene is reinforced due to the upgrading sales of Ssangyong: the first half of 2005, Ssangyong sales automobiles 60,908, of which exports 30,441, the total

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<sup>38</sup> Liao Yunfeng (2006), *Domestic enterprises' overseas M&A*, China Financial and Economic Publishing House, P250.

<sup>39</sup> Liao Yunfeng (2006), *Domestic enterprises' overseas M&A*, China Financial and Economic Publishing House, P255.



amount is almost 2 times of the same period last year, and created a highest record of export sales performance. And SAIC exports 389 million U.S. dollars, most of them is created by SAIC Ssangyong, the export growth of SAIC is 28.4% higher than the same period of previous year, was the NO.1 in the national automotive industry exports.<sup>40</sup>

#### **4.2.3 Collision stage - conflicts**

After the initial victory in the integration, SAIC began to gradually increase the control of Ssangyong. It sent more managers to Ssangyong and implemented the integration plan. At this time, the conflicts have come out and turned to be more and more severe. The integration went into the collision stage. This stage is often accompanied by bigger changes, such as the new organizational structure, the movement of the managers, the reducing of the employees and the start of the larger projects.

In this stage, SAIC has made some big personnel changes. SAIC replaced the chairman of Ssangyong and deployed five high-level Chinese managers to Ssangyong. SAIC replaced Ssangyong's general managers and two deputy general managers. These personnel changes made SAIC get the real control of Ssangyong. But these personnel changes led to the dissatisfaction with Ssangyong.

However, not everything went like SAIC expected. After 2002, the domestic demand of Korean automobile market shrank and fell to the valley in 2006. At that time, the price of the energy in the international market rocketed, and almost all the fuel of South Korea was dependent on import, the diesel price was also climbing. Korean automobile consumption tax rate slanted to small cars in recent years.<sup>41</sup> All of these things effected Ssangyong's sales. And because Ssangyong was debt-ridden in previous years, without a good credit to loan, Ssangyong had not enough money to develop new products. The new products were lack of new characteristics which made the sales of Ssangyong worse. For these reasons, the operational crisis of SAIC

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<sup>40</sup> Zu Jian (2007), Ssangyong's sales makes phenomenal progress, *China Auto Market*, 9.

<sup>41</sup> Xu Jiawang (2009), Ssangyong event, *Directors & Boards*, 3.

came out. According to Xu (2009), SAIC made a plan which would dismiss some staff and cancel some beneficial welfare in order to get out of the bad situation. When SAIC brought up this plan, the staff of Ssangyong struck to wreak their discontentment. The 49 days general strike not only made SAIC lost 300 million U.S. dollars, but also made SAIC's plan to profit in 2006 vanish into air.<sup>42</sup> However, on the issue of layoffs, SAIC became very tough. After the agreement with the labor union, SAIC still dismissed 544 employees, and completed the restructuring.

In our perspective, in the collision stage, it is very important to keep monitoring the “main obstacles”. These are the key factors which play a major obstructed role on the cultural integration. “Main obstacle” would be an individual, an interest group or an original system of the enterprise. With the process of the cultural integration, “main obstacles” will be a very active factor. Therefore, the key point to monitor the “main obstacles” is to handle the speed of cultural integration and the strength of cultural collision. In this case, I would consider that SAIC should have focused on the following “main obstacles”:

- Labor unions

Employees are the most important thing in a company. Their attitude toward M&A will directly affect the success or failure of M&A. In developed countries, labor unions, as the delegate of employees, can directly negotiate with the Board in order to secure the rights of employees. In order to integrate successfully, it must be accepted and supported by labor unions. Therefore, it is necessary to maintain a long-term monitoring on the labor unions so that managers can react timely when the labor unions have abnormal response. As it is obvious, the strong militant Ssangyong's labor union is the first main obstacle of SAIC.

Even before the SAIC taking over Ssangyong, Ssangyong's labor union had struck to oppose the M&A and that strike resulted a direct loss of more than 50 million U.S. dollars.<sup>43</sup> It can be said that in the early stage of the acquisition, SAIC

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<sup>42</sup> Xu Jiawang (2009), Ssangyong event, *Directors & Boards*, 3.

<sup>43</sup> QQ. Com, Ssangyong Strike investigation, 2009-01, <http://auto.qq.com/a/20090114/000179.htm>

should have paid more attention to this main obstacle. During the process of the acquisition, SAIC and Ssangyong's labor union had negotiated many times. Under the pressure of labor unions, SAIC signed a “special agreement”. With the signing of the agreement, on the one hand, it has lifted staff's main concern over the M&A, so that they can actively cooperate with the initial integration, but on the other hand, it does set a potential problem for future integration. Especially in adverse market conditions or bad business performance, once the company wants to dismiss the staff to relieve the bad situation, it will face a strong protest from employees and lose trustfulness.

When SAIC dismissed the original management of Ssangyong, the labor union lodged a strong protest. The dismissal let Ssangyong's labor union hold a big strike, which exposed the contradiction between SAIC and Ssangyong to the Chinese and Korean people. Although during the strike, the managers of SAIC Ssangyong negotiated with Ssangyong's staff many times and ultimately they could reach an agreement to terminate the strike, but the short-term exchanges didn't let SAIC win the trust of Ssangyong's employees. Even the strike came to an end, the labor unions of Ssangyong still doubt that in the future whether SAIC can fulfill the commitment.

- The delegate of the owners – Ssangyong's original director

The management team of the original company is another important interest group. Although they are far less than the number of employees, they are in the key positions in the company. Their attitude also comes from the original company as same as the employees, but they hold great difference from the staff. They are emotionally the same as the other employees holding deep feelings about the company. It is easily expected they will be more or less hostile to a strange new boss. On the other hand, in their day-to-day management, they deal with the employees as the delegate of employers, and strive to safeguard the interests of employers. The conflicting positions of the original management decides that their performance in the integration process will be more complex, requiring the merging side to pay a lot of attention.

Ssangyong's significant managerial changes were mostly due to the conflict in

business strategy from both sides.

The conflict was raised because of the cultural differences. As we know, cultural differences are in many cases the utmost concern on decision making about strategy, human resources. Additionally, cultural differences also lead to operational differences. When strategic conflict comes out, we should not only look at the surface conflict of the object but be focused on the integration issues and conduct an in-depth analysis of the potential cultural factors in order to identify the root causes of problems for further cultural integration.

#### **4.2.4 Creating stage - the gradual integration**

Creating stage is a new period under the cultural integration. In this period, the two companies will create or integrate a new culture. Compared with the first three stages, the beginning point of creating stage is a quite ambiguous. Because the process of cultural collision possibly is a cultural pioneering and innovating process. And the end of this stage is obviously not expected, it will carry on with company's continuous development.

According to the Xu Jiawang (2009), although the 49 days strike once made Ssangyong's production line stop, and lead to an enormous lost. The strike made SAIC to find out Ssangyong's labor union's bottom line. SAIC quenched the strike with a promise that no dismissal. But that is not absolute. Before the end of the strike, SAIC had dismissed 544 employees, the condition is a replacement for the 19-20 months of wages. In China, Hu Maoyuan, the director of SAIC, said that SAIC will not stop the dismissal; they do not only dismiss the workers, but also the person who do not work, including the management.

The SAIC's firm position in the strike and the compromise of the Ssangyong's labor union explained that the Korean workers began to truly understand the meaning of win-win solution they claimed. The successful settlement of the strike also means that SAIC has basically completed its restructure and personnel changes. The cultural integration has entered into a new stage: the creating stage. Furthermore, SAIC had found a person to solve Ssangyong's personnel problem, Philip Murtaugh, CEO of

GM China. Philip Murtaugh, has been named as "expert of structural adjustment" by Korean medias, who has proposed a plan that reduce 986 workers before he took office in Korea. He has also publicly stated that "if Ssangyong's labor union's strike activities hurt the company's long-term interests, SAIC will never make concessions".<sup>44</sup>

For the investment problem, Philip Murtaugh said that SAIC would not directly invest in Ssangyong, because the Korean company may get the necessary capital they need with floating bonds and borrowing from the banks. In Murtaugh's opinion, Ssangyong is an independent company even with the support from SAIC. This was the solution for the investment problem. It not only removed the concerns of Ssangyong's workers and greatly eased the contradictions, but also relieved SAIC's funding pressures.<sup>45</sup>

After the solution on the labor union and the investment problems, the situation of SAIC Ssangyong financial situation got improvements. The Financial Report of SAIC Ssangyong Motor Co., Ltd. of Korea in 2006 showed that in 2006 SAIC Ssangyong got a net loss of 196 billion Korean Won. Notwithstanding, the market did not pay much attention, though Ssangyong still provided big draw for the investors. Even well-known investment bank, the Goldman Sachs raised its rating of SAIC Ssangyong. In the year of 2007 the company did improve yet. In the first half of 2007, Ssangyong automobiles sales reached 69,755 units, meaning an increase of 13.2% higher than the same period of 2006. The figures include South Korea's domestic sales that grew by 4.7 percent. In overseas markets, export volume grew 20%. After the 3 years decline in profits, Ssangyong got profits in the first half of 2007. In the Chinese market, Ssangyong got a good performance too.<sup>46</sup>

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<sup>44</sup> Liao Yunfeng (2007), *Chinese enterprises Cross-Border M&A case analysis*, Enterprise Management Publishing House, P69.

<sup>45</sup> Liao Yunfeng (2007), *Chinese enterprises Cross-Border M&A case analysis*, Enterprise Management Publishing House, P70.

<sup>46</sup> Zu Jian (2007), Ssangyong's sales makes phenomenal progress, *China Auto Market*, 9.

## 5. Case 2: TCL takeover Thomson's European color TV business

### 5.1 Case description

Thomson Electronics Corporation is the largest electronics manufacturer in Europe. The sales on the field of consumer electronics in 2001 was 6.541 billion euros and in 2002, dropped to 5.444 billion euros. The financial report in 2003 showed that Thomson had a loss of 120 million euros in its color TV department. The competitive strength of Thomson's color TV and DVD has been progressively eroded. The United States and the European's TV market share were gradually shrinking. Therefore, Thomson wanted to change the business type as soon as possible. The best way to change the business type is to find a good partner and sell the TV and DVD department as package. So it could continue to get profit and change the business type.<sup>47</sup>

At the same time, TCL was looking for overseas markets because of high competition in the Chinese domestic market. The common needs of two companies made them go together. In July 2003, the two companies started to negotiate about the joint venture. In October 2003, the pre-negotiation came to an end and two companies agreed to go for a joint venture. The objective is building a new company TCL-Thomson Corporation (TTE).<sup>48</sup>

TTE headquartered in Shenzhen, and focused on TV's R&D, manufacturing, sales and services. TCL Group put all its color TV and DVD's factories, R&D and sales network into the joint venture company. Thomson did also put all its color TV's factories located in Mexico, Poland, Thailand and other countries, sales business and the R&D department into the new company. Thomson had 33% stake and holds the key management positions and 9000 staff joined the new company. TCL has a stake

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<sup>47</sup> He Bing (2005), TCL takeover Thomson, *China Entrepreneur*, 24.

<sup>48</sup> He Bing (2005), TCL takeover Thomson, *China Entrepreneur*, 24.

of 67%,. TCL and Thomson invested altogether 470 million euros, so that the capacity of color TV reached 18 million units, becoming the world's largest color TV enterprises. TTE had 6 global profit centers, 6 R&D centers, 10 production bases and more than 20,000 worldwide sales networks. The total number of staff reached 2.9 million people.<sup>49</sup>

### **5.1.1 After the acquisition the overall operations**

The acquisition activities provided a great increase in TCL Group's main business, reaching an increase of 42%. But the profits reduced by 57% compare with the previous year. The amount of cash flow from operating activities was minus 13 billion RMB. In 2005, the risk after acquisition showed up further. The main business income in the first three quarters has risen by 41.57% and reached to 36.53 billion RMB. However, the main business costs rocketed to a high level, the growth rate in the first three quarters was more than 50%.<sup>50</sup> And the income from the main operation increased slowly. At the end of the third quarter, TCL Group has lost 1.139 billion RMB.

On the August 30<sup>th</sup> of 2006, TCL released its operating report on the first half of 2006. The report showed that TCL's main income in the first half of the year was 23.576 billion RMB, corresponding to a decreased of 3.4 percent. The net profit of the first half year was minus 738 million RMB and the lost has increased by 6.5% when compared with 2005.<sup>51</sup>

In October 2006, TCL Group and TCL Multimedia Technology Holdings Limited posted a “notice on restructuring the European TV business matters” and decided to give up its television business in Europe. TTE paid 45 million euros in restructuring, 20 million euros were paid by Thomson, 25 million euros were paid by TCL Group.<sup>52</sup> And the restructuring fee was mainly used to provide employees with severance or redundancy benefits.

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<sup>49</sup> He Bing (2005), TCL takeover Thomson, *China Entrepreneur*, 24.

<sup>50</sup> Lang lang (2006), Say goodbye to Thomson, *21<sup>st</sup> Century Business Herald*, 11.

<sup>51</sup> Lang lang (2006), Say goodbye to Thomson, *21<sup>st</sup> Century Business Herald*, 11.

<sup>52</sup> Lang lang (2006), Say goodbye to Thomson, *21<sup>st</sup> Century Business Herald*, 11.

## **5.2 Case discussion**

For the analysis of the case, we will divided it into two parts. The first part outlines the reasons that why TCL wanted to takeover Thomson's color TV business; the second part compares the corporate governance structure of TCL and Thomson and point out the defect of Chinese corporate governance structure.

### **5.2.1 Motive analysis of acquiring Thomson**

#### **(I) Increase the internationalization level**

After joint venture with Thomson, TCL became the world's biggest color television manufacturer. The joint venture brought TCL the advantage of economy of scale and it has also increased the brand awareness as well as expanded sales channels. Through the joint venture, TCL increased its acquisition in core technology, brand awareness and operational capacity. At the same time, the expansion in the international markets had also given an unprecedented opportunity to TCL. In November 2004, TCL's overseas color TV sales reached 1.46 million units more than the Chinese market 86 million units.

#### **(II) Acquisition of the core technology**

TCL is the leading manufacturer in the color TV industry, but some hidden factors speeded up the step of TCL's M&A. In the color TV market, the traditional CRT TV market had become saturated, the competition is very high. Beside this, in the new high-technologic television market such as LCD market and PDP TV market, TCL had not got the core technology.

As known to everybody, R&D costs lost of money and time. Facing other countries' new technology, R&D by TCL itself could not satisfy TCL's need, and obtaining the core technology through M&A can be a fast and effective way. Thomson Corporation has a large number of high-end intellectual property rights and core technologies. Joint venture with Thomson could combine TCL's low-cost advantage and Thomson's technological advantage, so that increase TCL's international competitiveness.



### (III) Developing the oversea sales channel

Thomson has well-known brands and broad distribution channels. Through M&A, TCL can effectively use the existing sales channels and reduce sales costs and increase their brand awareness.

### (IV) Decreasing the trade friction

Appliance manufacturing industry is a mature, highly competitive market. For the purpose of protecting the domestic market, in the international trade, trade barriers and anti-dumping sanctions are the mostly used. FDI is the only and effective way to avoid trade barriers and anti-dumping. Through joint venture with Thomson, TCL could bypass these barriers and fill the other domestic market gaps due to the enterprises' trade sanctions.

### (V) Integrating the global support chain

TCL not only has factories in China, but also has factories in Vietnam, Philippines, Indonesia and CIS countries. On the other hand, Thomson has factories in Mexico, Poland, Thailand and in France. The joint venture of TCL and Thomson would integrate the global supply chain then it will greatly reduce the logistics costs and provide complementary advantages.

### (VI) Ideal to become a global enterprise

The Merger of Schneider in Germany, Thomson and Alcatel in France showed that the future strategic positioning of TCL is the overseas M&A strategy. And such a strategy comes from the ideal that TCL wants to develop itself into a world-class enterprise.

### (VII) Thomson's wish to develop Chinese market

Thomson, as the Europe's largest consumer electronics manufacturer, has lost as much as 120 million euros in its TV department in 2002. Selling its whole television department to TCL may not only reduce the loss, but also can increase the visibility in Chinese television market and further penetrate into the Chinese market.

In regard of motivation, we can find that the internationalization process of TCL is a rational one. To cope with increasing competition in the Chinese domestic appliance market would be best dealt by developing the overseas market. But finally, TCL failed in the merger process with Thomson. In our opinion, the failure of the joint venture is not haphazard. There are many problems that have led to a failure of the joint venture, such as the strategic problems, competition problems and corporate governance structure problems. Again in our opinion, the corporate governance structure problem is the main one. It largely contributes to the failure of the joint venture as we will see in the following section.

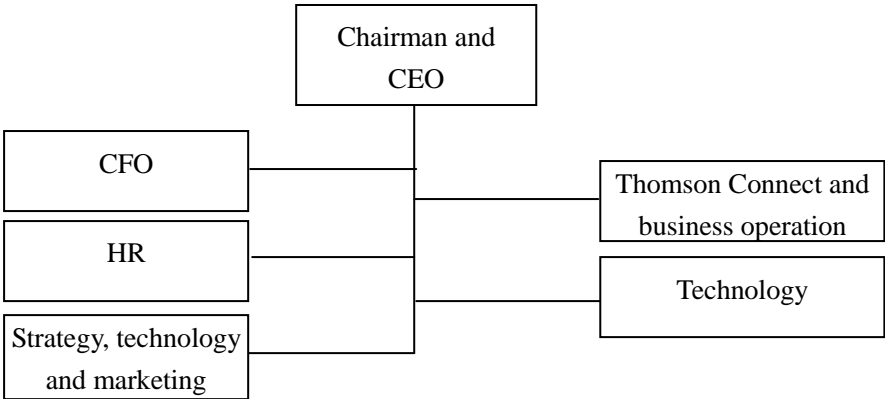
**5.2.2 The corporate governance structure analyses.**

As known to everybody, the main models of the corporate governance model are the Anglo-American model and the German model.

Anglo-American model's structure of corporate governance is composed by Shareholders Assembly and the Board of Directors (BoD). General meeting of shareholders is a non-permanent institution. The permanent governing institution is the Board of Directors which is directly elected by the shareholders.

Thomson's corporate governance structure is based on the Anglo-American model. The chart 5-1 shows the corporate governance structure of Thomson.

Chart 5-1 Corporate governance structure of Thomson



As the shown in chart 5-1, Thomson's corporate governance structure has not a Board of Supervisors. The BoD handles all the matters related to the operating of the company, and deliberates on the issues relevant to it with the invested power

explicitly granted by the shareholders in their ordinary meetings.<sup>53</sup> In addition, Thomson has an Executive Committee who is in charge of Group's performance and results.<sup>54</sup>

In this kind of corporate governance structure, the general meeting of shareholders is the highest institution. All the significant decisions and the management mobility are subject shareholders' discretionary reunited in the general assembly. It means that the shareholders can use their suffrage to achieve the supervisory to the company. The BoD elected by the shareholders is the institution to implement company's the decision.

But in China, the corporate governance structure is totally different. The company's high-level authority comprehends the general meeting of shareholders, the BoD, the Board of Supervisors and the managers. However, the core governance structure is the BoD.

The peculiar characteristic of Chinese corporate governance structure is the coexistence of the board of directors (BoD) and board of supervisors (BoS). There is no BoS in the Anglo-American model, but the Chinese model has one; in Germany, there is a two-tier board of directors while there is only one in China. Therefore, the coexistence of BoD and BoS is the main difference against the Anglo-American model and the German model.

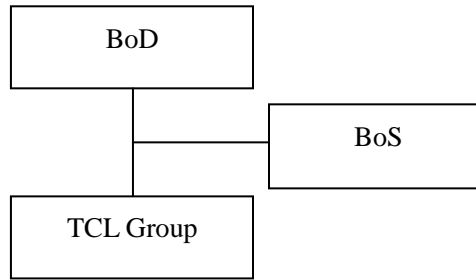
TCL's corporate governance structure is approximately the same as with other Chinese enterprises. The chart 5-2 shows TCL's corporate governance structure. In the chart 5-2, we can find that the coexistence of BOD and BOS.

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<sup>53</sup> Board of Directors' powers and missions <http://www.thomson.net/GlobalEnglish/Corporate/About/Organization-and-Management/Pages/board-of-directors.aspx>

<sup>54</sup> Executive Committee <http://www.thomson.net/GlobalEnglish/Corporate/About/Organization-and-Management/Pages/executive-committee.aspx>

Chart 5-2 TCL's corporate governance structure



This kind of governance structure seems to be perfect. Because in this structure, BoD' operating activities is under the monitoring of the BoS. The BOD can do the best commercial decision for the company. However, the Chinese corporate system is still imperfect. There are some problems in the Chinese corporate system:

(I) Dominance of the state-owned shares.

More than 90% of Chinese listed companies are set up by some or all of the assets from original state-owned enterprises, which results the dominance of the state-owned shares. The control from major shareholders not only weakened the check and balance function of BoD, but also easily lead to a related party transactions between the company and the major shareholders. These transactions may result in the loss of company resources and harm the interests of other shareholders. There are companies choose not to be listed in order to create profit for the primary purpose, but also to privately “enclose money”. This is clearly a departure from the economic rules, harming the interests of other shareholders.

(II) Managers are controlled by major shareholders.

So far, China has not established a normative manager market. The management of listed companies is generally appointed from internal selection. The major shareholders can assign the general manager. A number of listed companies also directly declare the chairman of the board as general manager. The decision-making power and executive power cannot be effectively separated. In this manner, the check-and-balance system cannot be effective. In addition, in China, there is no an effective motivational system. The price of the stock is not linked to the managers' performance, which is not good in terms of managerial motivation to add value to the

firm..

(III) BoS has not enough power.

Due to BoD and BoS are in the same level, BoD has no responsibility toward BoS. This arrangement weakens the BoS and cannot set up a truly and effective supervising mechanism. On the other hand, the salaries of BoS are established by the BoD, therefore, BoS has no economic independence which further harms the supervising function. Effectively, BoD has an excessive power in this setting.

(IV) The lag on the capital market development.

Chinese capital market has been developing since very recently. The relevant laws and regulation systems are imperfect. It results the single function of Chinese capital market and the irrational allocation of resources. In Chinese capital market, the amount of the institutional investors is small, the size of the capital is small, the operation of the capital is not normative, and the listed companies are not frankly supervision. Market imperfections had led to a distinct profit seeking behaviors. The price of the stock cannot reflect the actual situation of the listed companies.

(V) The setting of company's organizational structure and the configuration of company's senior management are still controlled by the government

"Company Law" stipulates that: "the setting up of the organizations' structure such as the board of directors and the board of supervisors as well their members must be decided by the meeting of shareholders. " However, in China, almost all the organizations' structure, members of BoD and BoS, CEO and general managers are appointed by the government. In China, the organizations' structure is very non-standard. Meeting of shareholders does not work and BoS has not enough power to monitor the company. The company is controlled by the chairman and the general manager.

(VI) Enterprise's decision-making power, supervising power and the operating power are not clearly separated; the decision-maker and the operator are the same person.

BoD and BoS work the same thing. The chairmen of most companies also act as the general managers. They are the decision-maker and the operator. Some companies' chairman, general manager plus the party secretary are the same person. He has all the powers of the company but without the basic control.

TCL Group's largest shareholder, Huizhou Investment Holdings Limited, which is controlled by Huizhou Government, held TCL 12.84% shares. Due to the change in ownership structure, there is an obvious centralization. Li Dongsheng held more share than other members of the BoD.<sup>55</sup> This is a modern form of corporate structure but without a modern corporate management system and a good manager-team structure. This kind of corporate governance structure has become the main culprit in the internal personnel disputes.

Li Dongsheng, who held TCL 4.72% shares, has almost the utmost powers. He is the Chairman of TCL Group, President of TCL, CEO, party secretary in the TCL Group, Chairman of Board of TCL Multimedia Technology Holdings Limited, Chairman of TTE, CEO and Executive Director. This is a significant imbalance of power.

From the motive analysis, we can see that TCL's internationalization has a certain degree of rationality.

But there are some questions which should be asked. For example: was Thomson the right M&A object and was the timing of the joint venture correct? Thomson is a mature company, but does TCL have enough capability to drag it into its circle? All these questions must be asked in a company with a better corporate governance structure and a better check-and-balance system. TCL's imbalance of power has a lot of hidden dangers from the perspective of risk aversion. I think this imbalance of power was the main reason of the failure of the M&A of Thomson.

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<sup>55</sup> Zhang Hao (2007), Europe nightmare: TCL lost in Europe, *Cai Jing Magazine*, 5.

## 6. Suggestions

TCL case and SAIC case are the epitome of the most of Chinese enterprises. These two cases show the shortages of Chinese enterprise in doing the integration. First is the weak in cultural integration. Second is the weak in corporate governance structure. But the cultural integration and the corporate governance structure are the most important factors that can affect the success of a cross-board M&A. If the Chinese enterprises want to increase the success ratio in cross-board M&A, they must pay attention on those two factors.

What should the Chinese enterprises do after signing the M&A agreement? Which problems have they to pay attention when they doing the integration between the two companies? How to achieve the synergistic effect?

### 6.1 For the Cultural integration

#### 6.1.1. Making a good cultural assessment

All the people who participate in M&A know that the responsible investigation is an indispensable process for the M&A. The main objective of responsible investigation is to discover and analyze the factors which may affect the M&A in the target company and all the problems about the merger cost. The result of the responsible investigation is very important to evaluate the value of target company and the feasibility of the merge.

In M&A, responsible investigation comprehends four factors: strategy, finance, law and operation. Cultural responsible investigation is behind the legal investigation and the operating investigation. Time pressure and the particular properties of the organizational culture will make the underlying cultural conflicts become a most likely neglected problem in evaluating the potential feasibility of a merge.

Furthermore, in the M&A process, the parties involved have normally their main focus on financial, legal and operating issues. So they spend very few time and energy to handle the cultural problems.

However, all the merger cases have problems in the cultural integration. The outcome of the cultural integration will affect the whole post-acquisition behavior. The failure of an M&A is mainly due to an unintegrated business culture between the involved companies. Contrarily, if we can do an exhaustive cultural responsible investigation and evaluate the business culture between the two companies before the M&A, some failures could probably be avoided. If the cultural difference between the merger company and the target company is very clear as well as the possibility of the integration is very low, the merger company should think about the merger decision one more time. According to the cultural match theory, there are some business cultures that are impossible to get integrated. It is better to give up as soon as possible rather than forced integration. If the result of the evaluation indicates possibility of integration, then with the evaluation, we can foresee the problems which will probably come out in the M&A process. And then we can draft a plan in advance to solve the problems at once.

It is because of this reason, although it is very difficult to know the target company's business culture before a M&A, the merger company still needs to make efforts on this. Normally, the cultural surveys are completed by the internal investigating group and the external consultants. Hiring of external consultants allows the merger company to get to know the target company cultural profile in a comprehensive approach. Therefore, the merger company could discover the cultural differences earlier. When doing cultural surveys, it is required to fully use some potential information such as: the employees of the target company, other industry participants, customers, the target company data released over the years, reports on mass media. In fact, this potential information includes all the original or processed information which is helpful to make decision.

SAIC's experience on responsible investigation is worth for the Chinese enterprises to study. SAIC hired Shanghai Llinks Law Offices to do a legal and cultural evaluation of Ssangyong. After the evaluation, SAIC recognized that the labor unions have a very important position in South Korean enterprises. And SAIC also fully used the results of the cultural evaluation; it expressed its respect to



Ssangyong's labor union in many public occasions. This successfully won the goodwill of Ssangyong's labor union. SAIC did a lot on stabilizing and appeasing the mood of Ssangyong's staff.

SAIC's experience also shows that doing a cultural assessment and survey before the merger integration can make an overview of the integration and foresee the main conflict or negative impact which will come out after merger. Understanding of these negative conditions will enable the work more targeted and thus help the integrating project team to make decisions faster. It can increase the possibility of successful integration. Due to the lack of cross-border M&A experience, Chinese enterprises should complete the responsible investigation with the help of an external force such as the consulting company. With the help of a professional consulting firm, the company can solve the cultural, legal, financial and other problems which will come out in the merger. Although this need a large sum of money, these professional consulting firm could help the companies to foresee some detail problems which may occur in the actual condition.

#### **6.1.2. Constituting a integrating plan**

Evidently, the cultural assessment by itself is not enough, the more important thing is to use the result of the cultural assessment and establish an integrating plan. Integrating plan is the most important part to evaluate the target company's value. Without the integrating plan, the merger company will have not an accurate evaluation on the synergy and the M&A transaction. So the merger company needs to make a good integrating decision in advance and constitute a thorough plan for the coming integrating stage and then to reinforce the control of the target company.

About constituting the integrating plan need to pay attention on the following points:

First, the integrating plan should be broken down into several specific resolutions - which can be effectively controlled to ensure their success.

The merger company has to decide which resolution needs to be implemented

immediately after the merger and which resolution will be followed. The merger company has to ensure that every resolution can be completed before the deadline. Merger company have to quantify the risks associate with each resolution and separate into two parts: avoidable risk and un-avoidable risk. Merger company have to forecast the problems which may occur in implementing the resolution and constitute the solution project.

Second, the integrating plan should clarify the key issues and the need for resources, and to ensure that these resources can be used.

On the capital investment issue, SAIC did not do well enough. It gives people an impression that SAIC had no plan on this issue. For a long time, SAIC's funding chain is tight. All the business plan of SAIC such as the new automotive R&D, new product plan and automotive financial services, required a large amount of funds. Facing the bigger requirements on the capital, SAIC has to expand the source of the capital. At that time, SAIC's asset-liability ratio had been close to 50%. Under the tightening national macro-control, the redistribution on loans from the bank and internal cash flow was very difficult. Because of the lack of the capital, SAIC had a big problem on implementing the promise of investing in Ssangyong. After many times rush up from the Ssangyong labor union, SAIC still has not enough capital until the arrival of Philip Murtaugh. He helped SAIC to solve the investment problem, by recommending the issuance of float bonds and getting loans from banks. SAIC did not pay any capital; it just used Ssangyong's good assets condition to eliminate the concerns of Chinese and Korean banks. If SAIC could constitute this plan "using Ssangyong's good assets condition to float bonds and loan from the bank" before merger and use this plan immediately after merger, then SAIC would not have such a big problem with Ssangyong's labor union. The contradiction between SAIC and Ssangyong's labor union would be relieved for a large extent.

At last, it is appropriate to prepare a contingency plan for emergencies that may arise.

In the global market, everything is variable and risky. Every company should

constitute some contingency plans for the changes that may arise. But SAIC seemed to forget this point, it did not take the possibility of shrinking market into account. During the M&A negotiation, SAIC made a promise to Ssanyong that she would not cut down the staff according to the market condition and capacity on that time. This promise forbid SAIC to cut down the staff even the market is bad. SAIC has not established any contingency plan to react to a market in crisis or to overcome the effect of bad policies. On the contrary, SAIC cut down the staff when the economic crisis arisen. It made SAIC losing the trust from the Ssangyong's staff. This trustfulness is the most important foundation in the M&A integration

### **6.1.3. Implementing the integrating plan as soon as possible**

Once the M&A transactions completed, the integrating plan should be implemented as soon as possible. Research shows that in the 8-hour work system, the effective working time of the normal day is 5 ~ 7 hours. And in the condition that the management of company has changed, the effective working time will reduce to less than 1 hour. Because under this condition, everybody will worried about themselves. They felt worried about how to adjust to a new working environment just like some Ssangyong's staff.

Another reason for why the integrating plan should be implemented as soon as possible is that at the beginning of M&A, the staff of the target company has already made a psychological preparation for the change. To a certain extent, the staffs expect change. It's very normal to have change after M&A. And an acquired company is more or less having some problems. Under this kind of psychological condition, the opposition from employees would be smaller than a normal circumstance. In the same way, the cost of restructure at once would be smaller than the cost of restructure after a long time of M&A.

Therefore, a smart merger operator is always trying to reduce the time interval between signing the M&A agreement and fully completion of the M&A. In an ideal situation, the merger company only needs 100 day to build up a effective control to the target company. They clearly understand that only to complete the M&A as soon

as possible, clarify the truth and destroy every unrealistic rumors, then they can have a better chance to make clear to the staff of the target company and the customers that the M&A behavior will not affect their benefit. Merger company should demonstrate the results to the stakeholders as soon as possible. Merger company can overcome all the problems that may occur in the integrating stage, but speed is the most important thing.

SAIC's integrating plan has a very obvious Chinese characteristic. It shows the integrating idea of most of Chinese enterprises. SAIC clearly understood the importance of the first 100 days after the M&A. So SAIC made a 100days integrating plan especially for Ssangyong. And in these 100 days, the behavior of both side shows that the 100days integrating plan was successful. However, did the success of 100days integrating plan mean that Ssangyong has approved SAIC's culture and the culture of two companies have integrated? In my opinion, the answer is no! During the integrating period, SAIC painstakingly blurred the difference of two companies. She has not done any structural adjustment or personal changes. The continuation of Ssangyong's original management and the promise that SAIC will not cut the staff gave a feeling to Ssangyong's employees that the M&A have not any effect to them. It successfully implemented the smooth transition after the merger. It is an expected result of SAIC. One year later SAIC started the real integration. When the real change came, Ssangyong's staff and management have no mental preparation at all. They felt that they had been cheated. It made them very anger and had a fiercer boycott behavior to the change.

SAIC' integrating experience has shown to all the Chinese enterprises that if the structural adjustment and personnel changes are inevitable, then just do it as soon as possible. A step-by-step integrating plan is not a good choice.

#### **6.1.4. Keeping a continuous and open communication with the labor union and staff**

During the whole integrating process, an open and sincere communication is always necessary and the most important.

First of all, the merger company should pay attention to the communication before the M&A agreement.

When the merger company shows its willing to the target company, its behavior and word will be attached great attention to the staff of target company. The staff will use these behavior and word to deduce that what will that merger company do when it successfully takeover the target company. Previous analysis has pointed out that South Korea is a country with very strong nationalism. The Korean is skeptical about the foreign capital. Due to the complex history between China and South Korea and the subtle psychological and cultural confrontation, Korean has more vigilance to the Chinese enterprises. Therefore, when Chinese enterprises want to do M&A in countries such as South Korea, especially in important and sensitive area such as resources and high-tech area, they must keep a low profile and not to promote the M&A. They should guide the public opinions advisably and prepensely. Merger company can't make the staff of target company feeling being betray and annex.

All the Chinese enterprises must keep this principle in mind that never make a promise easily, especially never make a promise that never changes the current situation. Normally after M&A, the company will have a set of change and adjustment in management and personal change. For the things that can not be guaranteed, it is better to remain silent. If you can not make your promise come true, it just shows your levity and breach of duty. It greatly reduces the authority of the project management. As well it makes the merger company lost its trust to the target company and then increases the difficulty of merger.

I think the wrong thing that SAIC did in integrating Ssangyong is the the hiring promise to the staff and the retaining promise to the management. Because of these promises, SAIC fall into a situation that it can't achieve the merger target if SAIC implement the promise or it will lose the trust of Ssangyong's staff if SAIC didn't keep the promise. And SAIC selected to break the promise. The result of SAIC's selection was the loss of the trust from Ssangyong's staff and break out the strike crisis, increase the operating loss and result in investment loss. It will destroy SAIC's

image in Korea. I think SAIC's experience teach other Chinese enterprises that implementing the promise is very important to keep the image of the merger company's leader and integrating team. Once the merger company makes a promise, it has to try its best to implement this promise.

Secondly, a continuous communication in the beginning of the integration is essential.

When employees face a new enterprise, the uncertainty of the future makes them feeling anxiety, insecurity. At this time, they urgently need the information about the merger company and about their future. So the speed of communication is the most important. If the staff can not get any positive official information, then they will be very worried and try to get the information in private. At this time, the rumors will be full of the company. Once the employee trust these rumors, it is very difficult to change their mind.

In order to avoid a situation that being full of rumors, merger manager should clearly tell the staff the actual situation of enterprises, which program will be implemented, as well as the future works. Perhaps at the beginning of the acquisition, middle managers did not have sufficient information or did not permit to give the certain information to the staff. But it can still communicate with the employees. Managers must wake up to the fact that not only the stuff of communication can transfer the information, but also the communication itself contains some information. Even if you can not give any answer to the staff, you should keep the channels of communication open. If you can't tell something to the staff, you need to tell them the reason and tell them when you can say. As long as you keep the promise, you can win a long-term trust and support from the staff. And it's good for the integration.

Finally, the communication must run through the whole integration.

Both sides of two companies need to maintain a continuous communication until the disappearance of the difference of the two companies and they could transform into a new company. M&A experts believe that this period will last for three years, at minimum.. In cross-border M&A, as there is huge cultural difference between the

two parties, something is normal or merited for the merger company. But it may be hard to be understood or mysterious for the target company. Therefore the merger company should explain the new management system, new policy to the staff many times. Merger company can not just promulgate the new system to the staff and expect they can understand and follow the new system. Because Chinese enterprises lack of experience, they are very careful at the beginning of M&A and followed M&A expert's advice to keep in touch with each benefit group. But when they get some small results in the merger business, they became blindly optimistic and consider that the integration has been completed and stop or reduce to communicate with the staff. Integration process is a management process with lots of changes. The problems and conflicts can be occurred at anytime and anywhere. The only way to find out the problems and solve the problems is to keep communicating with the target company.

#### **6.1.5. Keeping paying attention to the cultural integration**

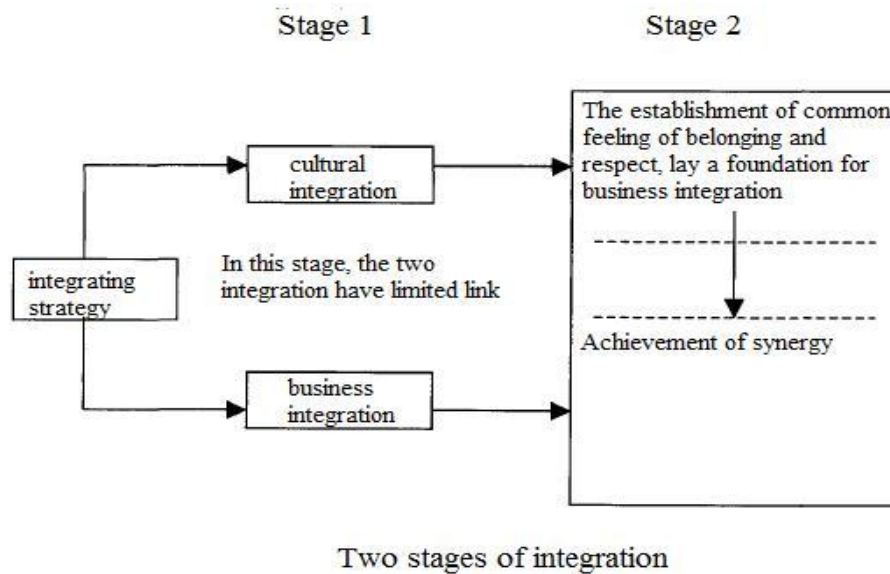
Business culture is evolving over a long time development. It has historical continuity and relative stability. It can not and will not be changed in a short time. That's why the cultural integrating manager not only need to pay attention to the cultural difference between the two companies and try his best to avoid the cultural conflict, but also need to make a preparation for the long-term integration.

The whole integrating strategy can be divided into two parts: cultural integration and business integration.<sup>56</sup> They are closely linked. According to the different progressing speed of two parts, the whole integrating process can be divided into two stages, as chart 6-1.

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<sup>56</sup> Pan Ailing (2004), Process Designing and Pattern Choice of Cultural Integration during Cross-border Merger and Acquisition, *Nankai Business Review*, 7.

Chart 6-1 two stages of integration



The first three months of the M&A agreement is the first stage of the integration. At this time, cultural integration has a high speed development. Then integrating manager need to integrate the enterprise's name, management system, strategic objectives and so on. He also need to reduce the negative impact of cultural difference, try to create a atmosphere with respect and trust between the two companies, to increase the satisfaction of the staff, to bring up a positive attitude to the staff. Cultural integration is the foundation of the operating integration. A good cultural integration can help to achieve a smooth operating integration. But a bad cultural integration will lead to big conflicts between people and people, organization and organization. These conflicts will severely obstruct the operating integration.

Once the basic cultural integration of first stage has completed, and having laid a good interpersonal relation foundation for the business integration, then the second integration-business integration can be speed up and more efficiency, more placid. At this time, integrating managers don't need to promote the object of new company as well as the bylaw system. The cultural integration is more reflected on the daily management details. But it does not mean that the cultural integration has been stopped. The integrating managers still need to pay enough attention to the cultural difference and try to assist a further cultural integration until that the staff in two companies can work together without any problems or conflict and having a new



business culture.

#### **6.1.6. Monitoring the high level management's behavior**

Any type of acquisition will have an impact on management. It should be the first concern on the agenda. The first difficult question after the merger is how to handle the high level management. A double president system ostensibly temporarily evaded the sensitive personnel issues, but it can't be a long-term solution.

Senior managers of target company are the key resources. Retaining them is beneficial for the smooth transition of integration. The central task of integration is to retain or appropriate adjustments to build up a competitive high-level management team. The loss of a high-level manager means the loss of developing plan on the organization. The new senior managers has to face high initial cost, for example, the new manager need to know well the organization and job requirement, establish his own prestige, be recognized by other staff, establish a new communication network and interpersonal network. These are the necessary requirements for effective leadership. Compared with the original managers, the new senior managers have to spend a lot of extra time or even to pay the cost of mistakes. Unless the new leader have had a good operating performance before, he can give a positive impact to the target company, otherwise using the external people are more likely to cause instability than using the internal people. Only the stable and innovative management team can create the best performance. Therefore, according to McKinsey's survey we can find that nearly 85% merger companies will retain the original managers. Retaining the original managers has two benefits. One reason is the original managers know well the business and problems of the company; it's good for the integrating work and keeping the normal operation. The second reason is the original managers can keep the staff stable and avoid the occurrence of accidents.

However, according to statistics only 10% of the top executives still remain in their positions after the merger. For this reason, Peter F. Drucker has the following commentary: "Merger company must have ability to provide high-level manager for the target company. The buyer must have preparation for the loss of the original

senior managers. These senior managers used to be a boss. They didn't want to be a 'department manager'".

Most of Chinese enterprises are facing the lack of international management talent. That's why the Chinese enterprises must train their own international management talent. When the company can't provide the top managers for the target company, they must be very careful in doing the cross-board merger decision.

#### **6.1.7. Establishing full-time integrating managers.**

An expensive lesson in the M&A history is that the merger company has to regard the integration as a separate process with company's business. Integration after merger is a complex process to integrate two companies' organization and business. It requires a professional integrating project manager to handle the process.

Normally the merger company will set up a merger investigating team to investigate the target company. However, although the merger investigating team has the most in-depth understanding of the target company and the most comprehensive understanding of how to integrate the two company after the merger, they will be disbanded and go back to their original position or to the next business when the merger agreement was completed. Therefore the merger needs to set up a full-time integrating manager to in charge the integrating management. What he undertakes is a specialty function just like the administration, marketing and financing department. It will run through the whole merger process instead of one stage of the business deal. The integrating manager not only can avoid the missing position during the integrating process, then solve the problems occurred in the merger process without delay, but also can reduce the possibility of a random decision during the integration.

For such a focused and highly professional job, which kinds of people are fitted? The answer from GM and other companies with lots of experiences in cross-board is the persons who had a very good performance in merger integrating team. They have a very strong ability on handling interpersonal relationship and have a strong insight with the cultural difference. The integrating manager has responsibility for the target company's performance, but he doesn't represent any part in the integration. He is the

link to integrate two companies and makes the information and resource can be transferred among the organizations.

For the integrating managers, the way to get the ability in handling interpersonal relationship and unique insight in cultural difference is not only the innate factor but also the training from the company. Cultural sensitivity training is obligatory not only for the integrating managers but also every manager who are sent to other country. They don't participate a specific cultural integrating plan, but they have to have a cross-cultural cooperation with target company's staff no matter in R&D, marketing, financing or purchasing. The cultural sensitivity training not only can make the staff to understand the cultural origin and the cultural historical background of both sides, but also can make them to pay attention to the cultural difference. Furthermore, the cultural sensitivity training can help the staff to absorb the good parts of the other cultural and make their own culture completed. In this way, they can create a new business culture.

## **6.2 For the corporate governance structure**

From the TCL case, we discover that a good corporate governance structure is very important to the Cross-border M&A. However, currently Chinese policy about the corporate governance is not perfect. It makes that Chinese corporate governance structure has lots of problems. Qu Tao (2004) believes that a perfect corporate governance structure is very important to create a win-win situation in the Cross-border M&A.<sup>57</sup> Nowadays, Chinese academic circles have already put forward some recommendation to complete Chinese corporate governance structure.

### **6.2.1. Reduce the ratio of the state-owned shares**

The excessive proportion of state-owned shares makes power of different shareholders in state-controlled listed to be seriously inequality. Some listed companies' BOD and BOS are controlled by the major state-owned shareholders. The incentive function, restricting function and informational function of the modern

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<sup>57</sup> Qu Tao, *Corporate Governance Improvement And International M&A*, Journal of Guangdong Institute of Public Administration, 2004 (6)

governance structure can't be really embodied. Reducing the state-owned shares can further improve the equity structure of the state-controlled listed companies, increase other stakeholders' status and effect and push forward the standardization of corporate governance structure. Reducing the state-owned shares is the requirement to complete the corporate governance structure. If we can't solve "dominance of state-owned shares" this problem, completing the corporate governance can't be come true.

#### **6.2.2. Reform the appointment of company's executives**

In China, the executives of State-owned enterprises and listed companies are generally appointed by the government. However, according to "Company Law", the members of BoD and BoS are elected by the general meeting of shareholders. This is the main reason why the enterprises and government department can't be separated in China. First of all, we need to change the way how to select the high-level managers. Nowadays, the high-level managers of State-owned enterprises and listed companies are appointed by the government. But the high-level managers should be selected from the managers with lots of operating experience or the success professional managers. In view of the small ranks of professional managers in China, the high-managers can be recommended by organizational departments, the State Assets Administration Committee (SASAC), the majority of enterprises and shareholders. The managers selected from this way are more scientific and accurate than appointed by the government. Secondly, we should change the way how to examine the top managers. Normally the high-level managers are examined by the organizational department. And now the managers should be examined by the organizational departments, the SASAC, the enterprise employees and shareholders. The Organizational departments main assess that whether the managers follow the policy of the government. The SASAC main assess that whether the manager maintain value of national asset or increase the value. The staff and shareholders main assess that whether the manager can guarantee the benefit of employees and shareholders, whether the manager can increase the income and treatment to the employees. And then we synthesize the assessment of these four parts. The assessment result from method is more comprehensive, objective and fair. Thirdly, we can hire the

international professional managers. There are a flourishing personnel market and more professional managers in the western developed countries. For the Chinese enterprises to hire the high-level managers from the international personal market is one of the important choices.

In my opinion, these recommendations are completing the corporate governance structure from exterior. I consider that we also need to adjust the governance structure from interior. Due to the defect of Chinese corporate governance structure and relate to the TCL case, I think we can adjust the governance structure with the following ways.

#### **6.2.3. Bring in an external Director.**

Bring in external directors can avoid a highly superposition of directors and managers, and achieve the separation of the right of decision-making and executing right. It guarantees that the BoD can make independent judgments and choices. The significance of bringing in external directors is to guarantee the normal operation effective and ensure the maximization of the investors' benefits.

#### **6.2.4. Combining the strict supervision and effective excitation**

The first is to increase the power of supervisors. The increase of supervisors' power is good to control the major shareholders, is beneficial to supervise the major state-owned shareholders. The second is to retain the financial independence of the supervisors. Economic dependence is impossible to have a truly and independent supervise. How can we keep the financial independence of the supervisors? First we need to change the way to pay the allowance. The allowance should be paid by a third party in stand of company. And then we should change the appointment. The supervisors should be appointed by the SASAC or the stock supervisory committee (SSC). So the independent director can really use his right of supervise. The third is to increase the excitation mechanism. We can link the high-level managers' performance with the motivation. For example, we can use the stock option as a long-term motivation to link the managers and the company together. We also need to establish and improve the incentive mechanism to the independent directors and

external directors. The fourth is to increase the punishment. We should increase the punishment to the dereliction of duty of the managers, supervisors and independent directors in order to increase their sense of responsibility.

## 7. Conclusion

Cross-border M&A has been an inevitable trend for China to attract foreign investment as well as the Chinese enterprises to be internationalization. And the present financial storm makes lots of well-known companies sink into the economic crisis. This is a perfect opportunity for the Chinese enterprises to executive Cross-border M&A to expand their power. However Chinese enterprises' immaturity of cultural integration and completion of corporate governance structure make the success rate of Cross-border M&A of Chinese enterprises maintain in a low level. Via the study of these two cases, this dissertation makes a conclusion that Chinese enterprises want to increase the success rate of Cross-border M&A, they have to pay close attention on the cultural problems, make a good cultural assessment and manager the cultural integrating work in the cultural integrating process. Also they have to complete Chinese corporate governance environment, decrease the intervention of government as well as complete the corporate governance structure, increase the power of the shareholder meeting and BOS, and complete the balance of power.

SAIC case and TCL case were end with failure. But what have they done in the integrating process still provides the experience for Chinese enterprises which are going to have Cross-border M&A.

Hopefully the study result of this dissertation can help the senior managers to executive the cultural integration and corporate governance restructure. Finally it can increase the success rate of Cross-border M&A and the international position of Chinese enterprises.

# Annex I

## Geert Hofstede™ Cultural Dimensions

	Power distance	Individualism	Masculinity	Uncertainty avoidance	Long-term orientation
Countries	score	score	score	score	score
USA	40	91	62	46	29
CHINA	80	20	66	30	118
SOUTH KOREA	60	18	39	49	81
JAPAN	54	46	95	92	80
HONG KONG	68	25	57	29	96
GERMANY	35	67	66	65	31

SOURCE: Hofstede.G.(1995), *The business of international business in cultures, Cross-cultural management*, Butterworth-Heinemann Ltd.

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