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Chinese Markets: How to enter into it under Brazilian enterprises´ perspectives

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Masters in International Management

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BUSINESS
SCHOOL

Department of Marketing, Strategy and Operations

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Abstract

The main objective of this dissertation is to analyze under Brazilian enterprises' perspectives the steps and main challenges to enter into the Chinese market. Doing business with the world´s second largest economy[1] has become increasingly important to Western companies of all shapes and sizes. Despite a difficult economic moment around the world, in part due to the COVID-19 pandemic, China's economy has continued to grow at near double-digit rates over the past two years (8.1% GDP growth in 2021)[2]. Nevertheless, to enter into the Chinese market is a complex task for foreign companies with little or no experience of doing business with this target market. In this context, the study identifies the recommended steps and the perspectives of Brazilian enterprises that a company should take before entering the Chinese market. It also addresses topics related to international market selection, competitive environment comprehensions, national competitiveness assessment, and overall business context analysis. Furthermore, it aims to identify the possibilities that a foreign company has to consolidate itself in the Chinese market, factors affecting entry mode decisions and business models, and the practical methods used by Brazilian enterprises to consolidate on this target market. Lastly, the study provides a specific knowledge on how to enter the Chinese market for Brazilian companies.

Keywords: China, International market, Intercultural management, Market entry modes

[1] BBC News (2023) Deflation: Why falling prices in China raise concerns. https://www.bbc.com/news/business-66435870

[2] Reuters Staff (2022) China revises 2021 GDP growth up to 8.4% from 8.1%.Reuters. https://www.reuters.com/article/china-economy-gdp-idUSKBN2TB03

Resumo

O objetivo principal desta dissertação é analisar sob a perspectiva das empresas brasileiras os passos e principais desafios para entrar no mercado chinês. Fazer negócios com a segunda maior economia do mundo[3] tornou-se cada vez mais importante para empresas ocidentais de todas as formas e tamanhos. Apesar de um momento económico difícil em todo o mundo, em parte devido à pandemia da COVID-19, a economia da China continuou a crescer a taxas próximas dos dois dígitos nos últimos dois anos (8,1% de crescimento do PIB em 2021)[4]. No entanto, entrar no mercado chinês é uma tarefa complexa para empresas estrangeiras com pouca ou nenhuma experiência em fazer negócios com este mercado alvo. Nesse contexto, este estudo identifica os passos recomendados e as perspectivas das empresas brasileiras que negociam e têm presença no mercado chinês. Abordando temas relacionados à seleção de mercados internacionais, compreensão do ambiente competitivo, avaliação da competitividade nacional e análise do contexto geral do negócio. Além disso, afim de identificar as possibilidades que uma empresa estrangeira tem de se consolidar no mercado chinês, foram analisados também os fatores que afetam as decisões do modo de entrada e modelo de negócio e as práticas utilizadas pelas empresas brasileiras para se consolidar no mercado chinês. Por fim, o estudo fornece conhecimento específico para empresas brasileiras sobre como entrar no mercado chinês.

Palavras-chave: China, Mercado internacional, Gestão intercultural, Modos de entrada no mercado

[3] BBC News (2023) Deflation: Why falling prices in China raise concerns. https://www.bbc.com/news/business-66435870

[4] Reuters Staff (2022) China revises 2021 GDP growth up to 8.4% from 8.1%.Reuters. https://www.reuters.com/article/china-economy-gdp-idUSKBN2TB03L

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Glossary

AMA - American Marketing Association

APEX - Brazilian Trade and Investment Promotion Agency

B2B - Business to business

B2C - Business to consumer

BERI - Business Environment Risk Index

C2B - Consumer to business

C2C - Consumer to consumer

CBBC - China-Brazil Business Council

CECC - China Economic Consulation Center

CEO - Chief Executive Officer

CJV - Cooperative Joint Venture

DFI - Direct Foreign Investments

EJV - Equity Joint Venture

GDP - Gross domestic product

HR - Human resources

IBM – International Business Machines Corporation

IMS - International market selection

IPR - International Property Rights

IT - Information technology

JV - Joint Venture

MOFCOM - China Ministry of Commerce

FDI - Foreign Direct Investment

FICE - Foreign-invested commercial enterprise

FIL - Foreign Investment Law

FTZ - Free Trade Zones

RCEP - Regional Comprehensive Economic Partnership

R&D - Research and development

RO - Representative Office

ROI - Return on investment

SMEs - Small and medium-sized enterprises

WTO - Work Trade Organization

WFOE - Wholly Foreign Owned Enterprise

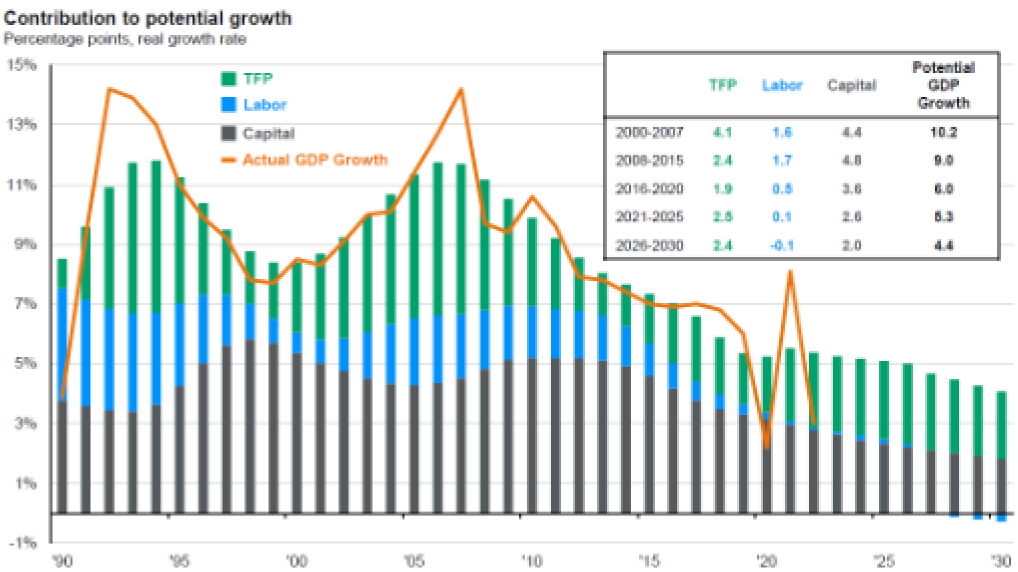
1. INTRODUTION

1.1. Contextualization

Located in East Asia, the People´s Republic of China (hereafter "China") has 9.6 million square miles of territory. The Asian country borders 14 nations and is adjacent to eight countries via sea. Although India surpassed China as the world's most populous country in April 2023, the Chinese nation has the mark of 1.4 billion residents[5].

Since the implementation of the Reform and Opening-up policies in 1978, Chinese economy has averaged over 9 percent a year, in terms of GDP[6] growth. According to JP Morgan, there are five main reasons to invest in China, namely: it is the second largest economy in the world, the second largest market in the world, it has potential to double the GDP per capita, it focuses on innovation, and it is an accessible market to global investors[7].

Figure 1: Long-term growth potential of China



Source: J.P.Morgan (2023)

[5] Felix Richter. (2023).Continental Shift: The world´s most populous countries. https://www.statista.com/chart/29853/the-worlds-most-populous-countries-since-1950/#:~:text=World%20Population&text=According%20to%20United%20Nations'%20latest,populous%20country%20in%20April%202023.

[6] The World Bank in China. (2023). China overview. The World Bank. https://www.worldbank.org/en/country/china/overview.

[7] Santos, Gabriela. (2023). Guide to China. J.P.Morgan. https://am.jpmorgan.com/br/en/asset-management/adv/insights/market-insights/guide-to-china/?utm_source=jpmam-sem-google&utm_medium=all-mixed&utm_campaign=br-en-guidetochina-acq&utm_content=economy&gclid=Cj0KCQjw4NujBhC5ARIsAF4Iv6ebekeQYeQQ9ZL-rgn_VZkPftkH2FSC4DGnLe_tPAY7E8Q96gwiIXYaAjeiEALw_wcB&gclsrc=aw.ds.

China was ranked 31st out of 190 economies in the World Bank's Ease of Doing Business 2020 report, with a score of 77.9. This was an improvement from its ranking of 78th in the previous year[8].

As the second largest economy of the world, China provides expressive economic numbers even facing a period after COVID-19. According to Santos (2023), “since the end of October 2022, Chinese equities are up nearly 40% and the Chinese Yuan is stronger by 4.5%”.

The economic results mentioned above are the consequence of political actions carried out by the government of China with the aim of boosting the county´s economy. As reported by Work Bank Group (2023), some of China´s reforms were:

- Protecting underrepresented group investors: it has strengthened the smaller number of investor protections by imposing liability on controlling shareholders for unfair related-party transactions and clarifying ownership and control structures.

- Paying taxes: China made paying taxes easier by implementing a preferential corporate income tax rate for small enterprises, reducing the value-added tax rate for certain industries, and enhancing the electronic filing and payment system.

- Trading across borders: China made exporting and importing easier by implementing advanced cargo declarations, upgrading port infrastructure, optimizing customs administration, and publishing fee schedules.

- Enforcing contracts: China made enforcing contracts easier by regulating the maximum number of adjournments that can be granted and limiting adjournments to unforeseen and exceptional circumstances.

Thus, understanding China is an opportunity for companies wishing to do business with that country. Inside this Asian giant, there are several possible opportunities for foreign investment. In order to take advantage of these opportunities, it is essential to develop a set of skills that go beyond the knowledge of processes and permeate other cultural aspects and the country's national strategy.

[8] The World Bank IBRD+IDA. (2020). Doing Business 2020: China’s Strong Reform Agenda Places it in the Top 10 Improver List for the Second Consecutive Year. https://www.worldbank.org/en/news/press-release/2019/10/24/doing-business-2020-chinas-strong-reform-agenda-places-it-in-the-top-10-improver-list-for-the-second-consecutive-year#:~:text=BEIJING%2C%20October%2024%2C%202019%20%E2%80%93,Doing%20Business%202020%20study%20says

According to Hollensen (2020, p. 33) *"Due to the high cost, going international must generate added value for the company beyond extra sales. In other words, the company needs to gain a competitive advantage by going international"*. Success in China necessarily depends on the multidisciplinary knowledge and excellent adaptability that Chinese dynamism requires; therefore, Western companies seek consulting companies specialized in this market with the aim of gaining this knowledge and establishing their businesses in China with more safety.

Given the above, the present work aims to contextualize the essential cultural aspects of doing business with China; a second objective is to analyze the business context in order to build up specific knowledge on how to enter into the Chinese market for Brazilian companies. This knowledge is intended to create sustainable competitive advantages in the Chinese marketplace specifically for Brazilian enterprises.

2. LITERATURE REVIEW

2.1. International Business

2.1.1. Theories & Models

The first literature of Internationalization Theories is based on marketing theories. The Penrosian tradition (Penrose, 1959; Prahalad and Hamel, 1990) reflects the traditional marketing focus on the firm's core competences combined with opportunities in the foreign environment. According to Johanson & Vahlne (2010), the Uppsala model and the Transactional Cost Analysis model assume that the price mechanism regulates the market. On the other hand, the Network Model proposes that the relationship of a company in its own country may be used as a bridge to leveraging its international activities in foreign countries (Hollensen, 2020). Subsequently, a table provides an overview of the tree theories mentioned before.

Table 1: An overview of the uppsala model, transactional cost analysis, and network model

Uppsala model	**The transactional cost analysis model**	**The network model**
Researchers at the University of Uppsala in Sweden identified in the 1970s that companies often follow specific patterns when operating in foreign markets, dubbed the "step-by-step process" (Johanson and Wiedersheim-Paul, 1975). This model presents four stages that businesses are thought to progress through when internationalizing, starting with no regular export activities, through export via independent representatives, establishing a foreign sales	In 1937, Coase proposed a model by which companies can outsource activities that are cheaper when performed by independent outsiders (Coase, 1937). Hollensen (2020, p. 243) points out that "*transaction costs emerge when markets fail to operate under the requirements of perfect competition ('friction free'); the cost of operating in such markets would be zero, and there would be little or no incentive to impose any impediments to free market exchanges*".	This model suggests that, for companies, the most important factor that keeps networks together is based on technical, economic, legal, and especially personal relationships (Morgan and Hunt, 1994). It is followed that an individual company's autonomy is connected to resources managed by other companies and that business networks form in areas where there is often regular coordination needed between different actors

subsidiary and ultimately foreign production and production/manufacturing units (Hollensen, 2020). In a recent article, Johanson and Vahlne (2009) updated their model and included more emphasis on network and opportunity recognition within the internationalization process (Hollensen, 2020).	For small- and medium-sized enterprises (SMEs), the lack of resources and knowledge is a major force for the externalization of activities. Additionally, the potential cost savings from outsourcing are not considered.	and with varying conditions. From this perspective, a company's relationships within its domestic network can be utilized to access networks in other countries, and for small- and medium-sized enterprises (SMEs), this could be a powerful motivator for internationalization. (Morgan and Hunt, 1994).

Source: Based on Hollensen (2020)

Although the theories mentioned above, in recent years, as the digital environment has taken place on the enterprises' business models, earlier research has identified an increasing number of firms that do not follow the traditional stages pattern in their internationalization process and design their business to aim at international markets since their birth.

Hollensen (2020, p. 253) explained that *"born globals represent an interesting case of firms operating under time and space compression conditions that have allowed them to assume a global geographic scope from the moment of their start-up"*.

Another concept that has been mentioned more recently is the *born-again global firms* that represents long-established firms that previously focused on their domestic markets but suddenly embrace rapid and dedicated internationalization (Bell et al., 2001).

The recent advances in communications technology, which has accelerated the speed of information flows, as an important trend in favour of *born globals*. With the internet, e-mail and other telecommunication aids such as smartphones, iPads and other computer-supported technologies managers of even small firms can manage operations efficiently across borders.

2.2. International Marketing

2.2.1. First steps into International Marketing

The American Marketing Association (AMA) defines International marketing as the *multinational process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organizational objectives*. The main difference between the domestic market and the international market is that in the latter case, marketing activities take place in more than one country. Consequently, the word multinational, from de concept, brings the importance of completely marketing activities to be coordinated across nations (Onkvisit & Shaw, 1988). As nowadays, the globalization of markets is a strong trend, managers have been paying more attention to the global environment and firms have attempted to expand their sales into foreign markets, which provides more profits and helps firms improve competitiveness for other reasons. In this context, it is necessary to be aware of all controllable (e.g., price, promotion, channel of distribution) and uncontrollable (legal, cultural, economic forces) elements that should be analysed in order to understand the variety from country to country (Cateora, Gilly, & Graham, 2011).

Hollensen (2020) points out some proactive motives (profit and growth goals, tech competence/unique product, foreign market opportunities, economies of scale, tax benefits) and reactive motives (competitive pressures, domestic market small and saturated, overproduction, unsolicited foreign orders, extended sales of seasonal products, proximity to international customers) which make the firms want to go abroad. To initiate the export process, it is necessary that some internal triggers (e.g., perceptive management, specific internal events, importing as inward internationalization) and/or external triggers (e.g., market demand, network partners, competing firms) support the process and carry it through to implementation. However, studies identify some factors that occur as barriers to export start. Hollensen (2020) split the barriers into three groups of risk: general market risks (e.g., market distance), commercial risks (e.g., export financing), and political risks (e.g. national export policy). Table 2 provides an overview of each risk group.

Table 2: Major Internationalization risks

General market risks	**Commercial risks**	**Political risks**
Competitive market distance.	Exchange rate fluctuations.	Foreign government restrictions.

Adaptation to foreign markets.	The failure of export customers to pay.	National export policy.
Competition from other firms in foreign markets.	Delays in export shipment.	Foreign exchange controls.
Adapting products and services to new local conditions.	Difficulties in obtaining financing.	The lack of governmental assistance.
Difficulties in finding the right distributor in the foreign market.	-	High value of the domestic currency.
Differences in product specifications.	-	High foreign tariffs on imported products.
The complexity of shipping.	-	Confusing foreign import regulations and procedures.

Source: Hollensen (2020)

Furthermore, Hollensen (2020, p. 154) defined *"global marketing* as a *firm's commitment to coordinate its marketing activities across national boundaries in order to find and satisfy global customer needs better than the competition does"*. To achieve this goal, firms should be able:

i) To develop a global marketing strategy that considers similarities and differences between markets.
ii) To exploit the knowledge of the headquarters (home organization) through worldwide diffusion (learning) and adaptations;
iii) To transfer knowledge and 'best practices' used from any of its markets and use them in other international markets.

To become competitive in the global market, firms must create sustainable competitive advantage. Hollensen (2020) introduced Porter's value chain as a framework model to identify the sequence of key generic activities that businesses perform to generate value for customers. However, the author draws attention that in most cases, it is not enough just to look at the internal value chain; it is also relevant to analyze the whole process, including how supply and distribution value chains are connected. Then, it provides an internationalization of value chain activities and decisions regarding configuration and coordination of a global value chain.

2.2.2. International market selection (IMS)

Most studies in global marketing segmented the world in groups of countries in order to gain advantage related to data, which is easily available on a nation - by-nation basis, and distribution management and media, which are also organized in groups of countries.

Hollensen (2020) presented an international market selection model composed of four main steps. First, in Steps 1 and 2, the author proposes the idea of selecting the relevant segmentation criteria and then developing appropriate segments. Based on internal (firm) and external (environment) analysis, the author proposed as criteria (i) measurability of the market in terms of size and purchasing power; (ii) accessibility; (iii) substantiality/profitability; and (iv) actionability in terms of resources to develop marketing programs. Therefore, in Step 3, a Screening of Markets/Countries should identify the most interesting region. However, regarding this step, the author divided it into two stages: a preliminary screening, which should be based only on external criteria using the BERI Index as a toll, for instance. Fine-grained screening, which is based on a firm's competitive power (internal criteria), was carried out using BCG's Market Attractiveness/Competitive Strength Matrix. Lastly, in Step 4, a micro segmentation is developed: sub-segments in each qualified country and across countries aim to use standard techniques and criteria (lifestyles, consumer motivations, geography, buyer behaviour, etc.) to segment markets.

After these analyses, firms must decide whether to concentrate resources on a limited number of similar markets or to diversify across several different markets (Keegan & Green, 2008). However, this decision should be made combined between country and customer levels. Hollensen (2020) proposed a market expansion matrix in which there are four possible strategies: (I) few customers in few countries, (II) many customers in few countries, (III) few customers in many countries, and (IV) many customers in many countries. In spite of this, companies should answer two underlying questions: (i) Will they enter markets incrementally (the waterfall approach) or simultaneously? (the shower approach), and (ii) Will entry be concentrated or diversified across international markets?

2.2.3. Market Entry Modes

Hollensen (2020, p. 705) defined entry mode as "*an institutional arrangement for the entry of company´s products and services into a new foreign market"*. The author also highlighted factors that influence a firm's choice regarding entry modes alternatives and splits these factors into four groups: (i) *Internal Factors*: firm size, international experience and product/service; (ii) *External Factors*: sociocultural distance between home country and host country, country risk/demand uncertainty, market size and growth, direct and indirect trade barriers, intensity of competition, small number of relevant intermediaries available; (iii) *Desired mode characteristics*: risk-averse, control, flexibility; and (iv) *Transaction-specific factors*: tacit nature of know-how, opportunistic behavior, transactional costs. All these factors support the choice for one of the three groups of market entry modes: (i) *Export Modes*: low control, low risk, high flexibility; (ii) *Intermediate modes* (contractual modes): shared control and risk, split ownership; (iii) *Hierarchical modes* (investment modes): high control, high risk, low flexibility. Table 4 provides more information regarding each entry mode and its advantages and disadvantages.

Table 3: Summary of the most relevant entry mode on foreign markets

Mode	Characteristics	Advantages (e.g.)	Disadvantages (e.g.)
A. Export Modes			
Indirect Export *e.g. export buying agent, broker, export management company, trading company, piggyback.*	A manufacturer uses independent export organizations located in its own country (or third country).	• limited commitment and investment required. • high degree of market diversification of an experienced exporter. • minimal risk (market and political). • no export experience required.	• no control over marketing mix elements of the product. • limited product experience.
Direct Export *e.g. distributor or agent.*	The manufactures sell directly to an importer agent or a distributor located in the foreign target market.	• access to local market experience and contacts with potential customers. • shorter distribution chain. • market knowledge acquired.	• little control over market price because of tariffs and lack of distribution control. • some investment in sales organization required.

Cooperative export modes	Frequently found among SMEs attempting to enter export markets for the first time.	• shared costs and risks of internationalization. • provides a complete product line or system sales to the customer.	• risk of unbalanced relationship. • participating firms are reluctant to give up their complete independence.
	B. Intermediate Modes		
Contract manufacturing *(seen from the contractors viewpoint)*	Enables the firm to have foreign sourcing (production) without making a final commitment.	• permits low-risk market entry. • no local investment with no risk of nationalization or expropriation. • retention of control over R&D, marketing and sales/after-sales service. • avoids currency risks and financing problems.	• transfer of production know-how is difficult. • extensive technical training will often have to be given to the local manufacture's staff. • at the end of the contract, the subcontractor could become a formidable competitor.
Licensing *(seen from licensor's viewpoint)*	Sales abroad of rights covered by a patent or design or any intellectual property to be used for commercial purposes.	• increases the income on products already developed as a result of expensive research. • permits entry into markets that are otherwise closed on account of high rates of duty, import quotas and so on.	• the licensee may prove less competent than expected in marketing or other management activities. • danger of the licensee running short of funds. • The lack of control over licensee

		• a viable option where manufacture is near the customer base.	operations. • negotiations with the licensee and sometimes with local government are costly.
Franchising *(seen from franchisor's viewpoint)*	Sales of the rights by the domestic franchisor to conduct a commercial activity by a foreign franchisee.	• the greater degree of control compared with licensing. • low-risk, low-cost entry mode. • uses highly motivated business contacts with money and local market knowledge and experience.	• the search for competent franchisees can be expensive and time-consuming. • cost of creating and marketing a unique package of products and services recognized internationally.
Join venture *(seen from parent's viewpoint)*	An equity partnership typically involves two partners. It involves two 'parents' creating the 'child' (the joint venture acting in the market).	• access to expertize and contacts in local markets. • reduced market and political risk. • overcomes host government restrictions. • may avoid local tariffs and non-tariff barriers.	• objectives of the respective partners may be incompatible, resulting in conflicts. • contributions to joint venture can become disproportionate. • transfer pricing problems as goods pass between partners.
Management contracting *(seen from contractor viewpoint)*	Occurs in situations where one company seeks the management know-how of another company.	• relevant alternative when direct investment or export is considered too risky. • allows a company to maintain market involvement, and so	• training future competitors: the management transfer package may, in the end, create a competitor for the contractor • little control, which

		it puts it in a better position to exploit any opportunity that may arise.	also limits the ability of a contractor to develop the capacity of the venture.
C. Hierarchical Modes			
Domestic-based sales representatives	The sales representative resides in the home country of the manufacturer and travels abroad to perform the sales function.	• better control activities compared with independent intermediaries • close contact with large customers in foreign markets close to home country.	• high travel expenses • too expensive in foreign markets, far away from home country.
Foreign sale, branch/sales, and production subsidiary	**Foreign** branch is an extension of and a legal part of the manufacturer. **A subsidiary** is a local company owned and operated by a foreign company under the laws and taxation of the host country.	• full control of operation. • eliminates the possibility that a national partner gets a 'free ride'. • market access (sales subsidiary).	• high initial capital investment required (subsidiary). • loss of flexibility • high-risk (market, political and economic). • taxation problems.
Region centers/transnational organization	They usually play the role of coordinating and stimulating sales in the entire region.	• achieves potential synergies on a regional/global scale. • regional/global scale efficiency.	• possible increase in bureaucracy and limited national-level responsiveness and flexibility.
Acquisition	It is a rapid entry mode and often provides access to distribution channels.	• rapid entry to new markets to gaining quick access to distribution channels, a qualified	• usually an expensive option high-risk. • possible lack of integration with

		force, local knowledge, so on.	existing operations.
Greenfield investment	Occurs when firms prefer to establish operations from the ground up and where no appropriate acquisition targets are available.	• possible to build in an 'optimum' format. • possible to integrate state-of-the-art technology.	• high investment cost. • slow entry of new markets.

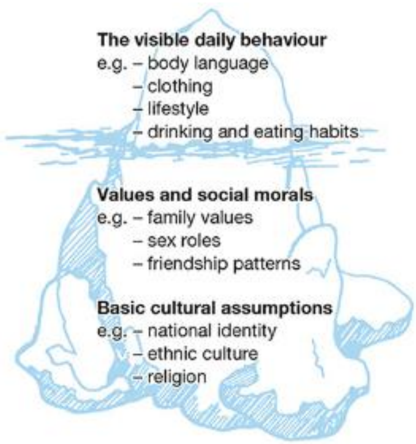
Source: Hollensen (2020)

2.3. Intercultural management

2.3.1. Managing cultural differences

Hollensen (2020, p. 550) defines culture as *"a pervasive influence which underlies all facets of social behavior and interaction"*. Aspects as religion, education and family influence the way that people live in a society. Furthermore, other aspects as legal, economic, political and technological forces also influences it (Hollensen, 2020). Based on Schein´s model, the author also points out that culture can be thought of as having three levels and the structure is drawn as the figure below. On the top of the iceberg, there are the tangible aspects of a culture regarding the things you can see, hear, smell, taste or touch. The aspects that are below the water are the values and assumptions. The first one helps people make short-term adjustments; these standards change over shorter periods (10 or 20 years). Whereas, the second one is probably formed over centuries.

Figure 2: Iceberg model



Source: Hollensen (2020)

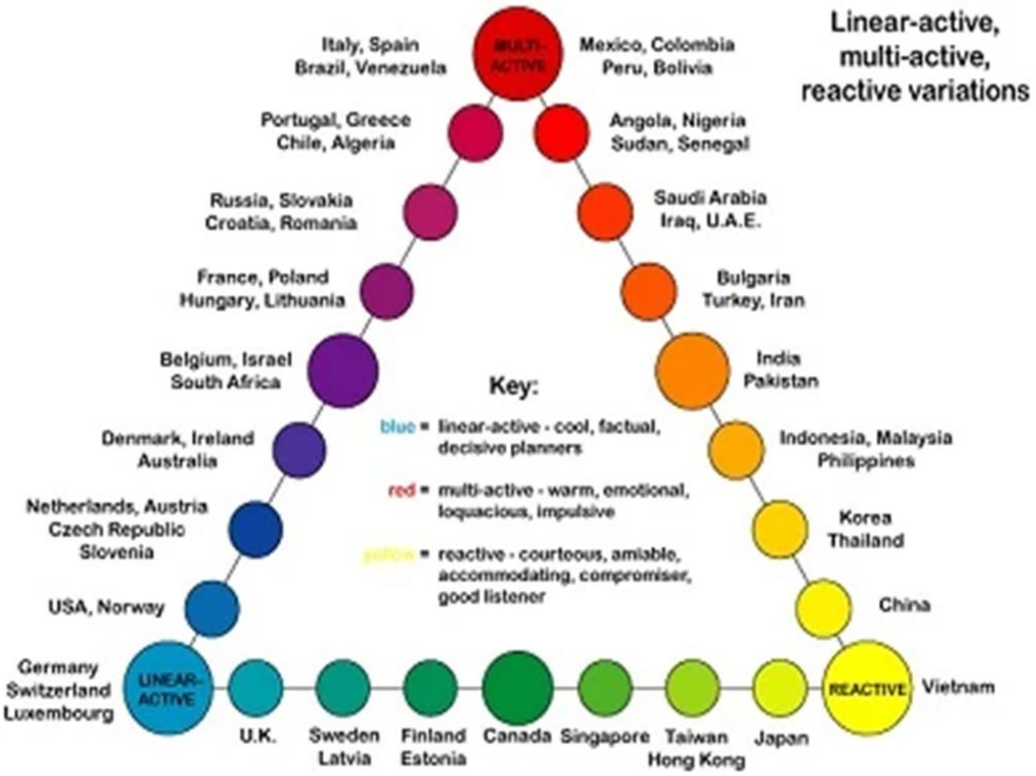
Dealing with cross-cultural difference is a relevant topic when a business is involved in several countries. Mcfarlin & Sweeney (2011) point out that one way to make things easier is to identify a core set of values that are shared by a specific set of countries. With this knowledge, it is possible to more effectively place international assignees, establish compatible regional units, and predict the results of policies and practices across national boundaries (Ronen & Kraut, 1977). Therefore, clusters aid the identification of variables that explain the variance in work goals and managerial attitudes such as language, religion, or level of industrialization.

Figure 3: Synthesis of country clusters

Source: Ronen, Simcha, and Oded Shenkar (1985)

In terms of intercultural communication, Richard D. Lewis developed a model that illustrates how each culture perceives a situation and communicates. This approach is very useful for leaders who have to manage a company/industry across countries with different cultural backgrounds. The cultures are divided into three main categories: (i) *Linear Active*: refers to societies where people focus on jobs. They separate their social and professional life. They work on one task at a time but have a detailed plan. They prefer polite and direct conversation with limited body language. (ii) *Multi Active*: refers to societies where people focus on building relationships. Their decisions are based on emotions. They work multi-task and plan their work and life only partially. They prefer to communicate emotionally and talk most of the time with unlimited body language. (iii) *Reactive*: refers to societies where people listen most of the time and react to others' actions. They prefer being polite and communicating indirectly. They never interrupt a conversation and take decisions as they are. They focus mainly on building close trusting relationships.

Figure 4: Cultural Types: The Lewis Model



Source: Based on Richard D. Lewis

2.3.2. Hofstede and Cultural Dimensions

Geert Hofstede, one of the 20 most influential business thinkers according to a Wall Street Journal ranking, conducted the most extensive research regarding cultural values.

Based on an extensive IBM study of 116,000 questionnaires in 72 countries and in 20 languages, Hofstede distinguishes six dimensions of national culture: power distance, individualism/collectivism, masculinity/femininity, uncertainty avoidance, long-term orientation, and indulgence/restraint.

Power Distance

This dimension observes the fact that individuals in societies are not identical. It represents the attitude of the culture concerning these differences among individuals. Power distance is defined as the extent to which the less powerful members of institutions and organizations within a country expect and accept that power is distributed unequally. Hollensen (2020) explains that in high power distance societies, power is concentrated among a few people at the top who make all the decision. People at the other end simply carry these decisions out. On the other hand, in low power distance societies power is widely dispersed and relations among people are more similar.

Individualism/Collectivism

This dimension concerns the degree to which societies are integrated into groups, in living arrangements, decision making processes, and values. In individualist societies, people look after themselves and their direct family only. In a collectivist society, people belong ‘in groups’. Individualism (versus collectivism) can also be explained as the extent to which the individual expects personal freedom versus the acceptance of responsibility to family, tribal, or national groups, i.e., collectivism (Hollensen, 2020).

Masculinity/Femininity

In masculine cultures, the dominant values are achievement and success. The dominant values in feminine cultures are caring for others and quality of life. In a masculine culture, performance and achievement are important. Status is important to show success. A feminine culture has a people orientation, small is beautiful and status is not so different between males and females, in feminine cultures there is a small role differentiation (Hollensen, 2020).

Uncertainty avoidance

This dimension explains the way that a society deals with the fact that the future can never be known: should we try to control the future or just let it happen? This ambiguity brings with it anxiety, and different cultures have learned to deal with this anxiety in different ways. The extent to which the members of a culture feel threatened by ambiguous or unknown situations and have created beliefs and institutions that try to avoid these is reflected in the score on Uncertainty Avoidance. It also expresses the extent to which society avoids risk and creates security by emphasizing technology and buildings, laws and rules, and religion. Weak uncertainty avoidance societies preserve a relaxed atmosphere in which practice counts more than principles and deviance is more easily tolerated (Hollensen, 2020).

Long-term orientation/Short-term orientation

According to Hollensen (2020, p. 577) time orientation is defined as "*the way members in an organization exhibit a pragmatic future-oriented perspective rather than a conventional history or short-term point of view*". Long-term orientation is focused on the future; it encourages thrift and efforts in modern education as a way to prepare for the future. However, the short-term orientation is focused on the present and the past, preferring to maintain time-honoured traditions and norms, and quick results are expected.

Indulgence/Restraint

Indulgence stands for a tendency to allow relatively free gratification of basic and natural desires related to enjoying life. On the other hand, in restrained societies gratification needs to be curbed and regulated by strict social norms.

2.3.3. China´s cultural aspects

Each country has different cultural aspects, and it is critical to know them when a company has the intention to conduct business abroad. These intercultural differences become wider between western and eastern countries. Although the same aspects such as money, comfort, job satisfaction, security and others commonly motivate most people, every culture reaches these goals through a wide variety of routes.

Various authorities have identified the values underpinning Chinese culture that are relevant to management and organizational behavior (e.g., Shenkar and Ronen 1987, Lockett 1988, Redding 1990, 2002, Bond 1996). Redding's (2002, 234-5) list is one of the more comprehensive, namely:

Table 4: Redding´s list of the Chinese values

Value	**Description**
Societal order	This reflects the sense of Chinese civilization as based on learning and practice by individuals of clearly defined roles, all within a dominating state structure with a remit to preserve order, and all socialized into a belief in the need for appropriate conduct in the interests of harmony.
Hierarchy	This value legitimates paternalism at the levels of family and organization and patrimonialism at the state level. Furthermore, it provides a moral

	justification for hierarchy by stressing reciprocal vertical obligations.
Reciprocity and personalism	This is the currency of horizontal exchange and the guarantor of the limited but adequate trust that maintains the particular structure of transactions.
Control	In a society of competing families, under conditions of scarce resources, and in an interventionist state, control of one's fate becomes a core ideal for many, particularly business owners, and sensitivities to control become highly tuned.
Insecurity	It is associated with competitiveness and a work ethic. As China is a totalitarian state with weak property rights and building defenses and reserves, it has become a moral duty toward dependents as well as a practical necessity.
Knowledge	The Chinese respect for learning appears to have survived the ravages of the Cultural Revolution and the related persecution of intellectuals. The value of learning remains high nowadays.

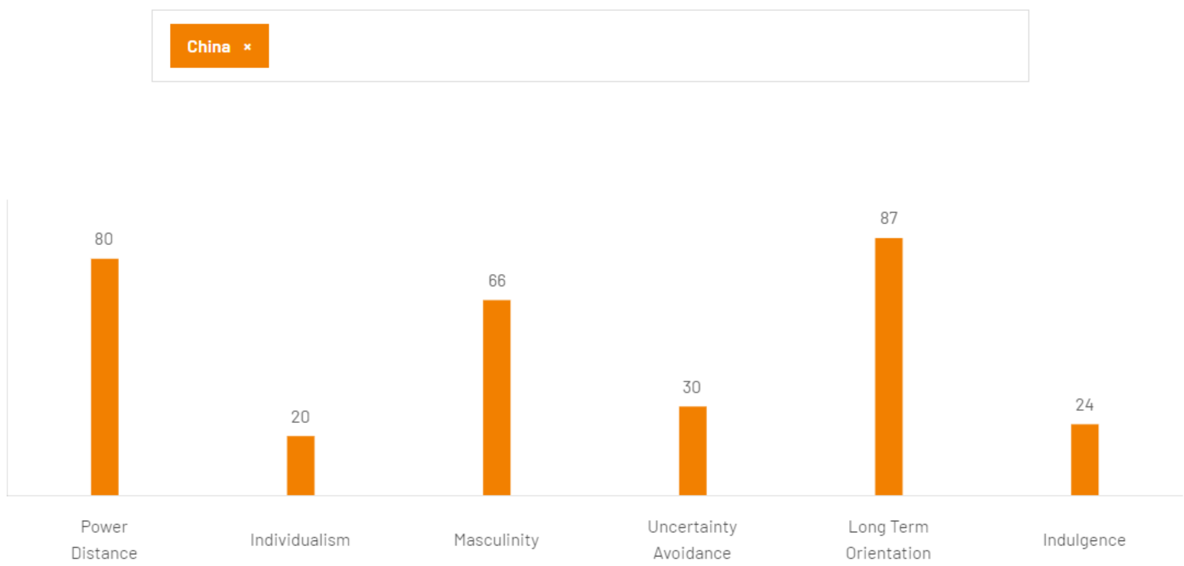
Source: Based on Malcolm Warner (2003). Culture and Management in Asia

The above values translate how a personal relationship leads to special importance to provide trust and maintain harmony. An example that Cannon (1990) highlights is *relational networking* based on interpersonal connection (known in Chinese as *guanxi*). Deeply, together with *guanxi* (relationship), *li* (rite), *mianzi* (face) and *renqing* (obligations) reinforce the social bonds that make the Chinese system function smoothly.

Hollensen (2020) also points out special cultural issues in China under Western executives and expatriates perspectives: (i) most westerners underestimate the role of the Chinese government — "*in most industries, it is impossible to do well in China without the government´s back-up"*, (ii) attracting and retaining people in China is not just about paying or providing opportunities for advancement — "*for many Chinese, the company is as much a social community as a place of work, and they want their boss to be more than a taskmaster or a distant professional*.

In order to have an overview of the deep drivers of Chinese culture and provide generalist statements, the Country Comparison Tool from Hofstede Insights scored the six cultural dimensions. China presents the following score to each dimension: (i) *power distance* (80): this higher score emphasizes that inequalities amongst people are acceptable, the subordinate-superior relationship tends to be polarized and there is no defense against power abuse by superiors; (ii) *individualism* (20): with this score China is a highly collectivist culture where people act in the interests of the group and not necessarily of themselves, employee commitment to the organization is low and personal relationships prevail over task and company; (iii) *masculinity* (66): China is a masculine society and success can be exemplified by the fact that many Chinese will sacrifice family and leisure priorities to work; (iv) *uncertainty avoidance* (30): the Chinese are comfortable with ambiguity, the Chinese language is full of ambiguous meanings that can be difficult for Western people to follow, Chinese are adaptable and entrepreneurial; (v) *long term orientation* (87): this score means that it is a very pragmatic culture, people believe that truth depends very much on situation, context and time; (vi) *indulgence* (24): China is a restrained society which means that it has a tendency to cynicism and pessimism, does not put emphasis on leisure time and controls the gratification of their desires.

Figure 5: Chinese culture through the six dimensions model



Source: Country Comparison Tool

3. METHODOLOGY

According to Burns (2000), research is a systematic investigation applied to illuminate specific problems. Secondary external data was hence approached through a literature review added to research on market information on websites of players that deal with the Chinese market and support the Internationalization process of Brazilian companies, contributing to a portraying of the situation faced to enter into the target market.

3.1. Research Approach

To develop a research approach, firstly it is important to determine the purpose of the study. Following this, the objectives of this study are to:

- Analyze the business context in order to build up specific knowledge on how to enter into the Chinese market for Brazilian companies; and
- Contextualize the essential cultural aspects of doing business with China.

Richey and Klein (2007) have identified three categories of research: exploratory, descriptive, and explanatory. Based on the mentioned objectives, the descriptive research method was used to construct this work. It provides a study of bibliographic analysis from government institutes such as the Brazilian Trade and Investment Promotion Agency - APEX and the Ministry of Commerce People´s Republic of China – MOFCOM. The study also consulted businesses, laws and consulting enterprises that deal with the Chinese market. Lastly, it also presents an analyzes of secondary data from interviews carried out by China-Brazil Business Council - CBBC with Brazilian companies with a presence in the Chinese market.

4. MODELS TO ENTER INTO THE CHINESE MARKET FOR BRAZILIAN COMPANIES

Successfully entering the Chinese market is a complex task for foreign companies with little or no experience of doing business in this market. Below are the main challenges and recommendations to Brazilian companies that intend to enter into the Chinese market.

4.1. Historical landmarks of Brazilian companies in China market

In China, the entrance of direct foreign investment was authorized in 1978 and it constitutes one of the main strategies of the economic reform policies of the Deng Xiaoping era. At that time, besides the huge scarcity of capital, the nation suffered from industrial inefficiency due to state-owned companies with technological deficits and limited production capacity[9].

According to Fleury (2021), *Embarco* was one of the first Brazilian enterprises to be present in China in 1995, with operations in Beijing as a joint venture.

During this period, multinational corporations that entered into the Chinese market had to operate as equity joint ventures with just one Chinese partner. Over time, this scenario changed and subsidiaries under the control of branch companies can perform activities too. These changes were happening due to industrial policies defining the economic sectors that would be open to foreign capital and what would be preserved from international competitors. The Chinese government´s concern was to guarantee technological improvements with a process that would induce learning for local businesses (Fleury, 2021).

Fleury (2021) also points out that, in the 2000s, several Brazilian enterprises settled in China, especially after 2004 when the Brazilian President, Luiz Inácio Lula da Silva, made an official travel to China; this opportunity was such that Brazil had understated the benefits of doing business with China. *Embraer* is a multinational aerospace manufacturer in Brazil that produces commercial, military, executive, and agricultural aircraft and provides aeronautical services. In the 2000s, this company began its activities in China with an office in Beijing and registered as a joint venture with two local companies, controlled by Aviation Industry Corporation, a Chinese company. *WEG*, which operates worldwide in the electric engineering, power and automation technology areas, started its activities in China with the

[9] Claudio Frischtak and André Soares (2012). Brazilian companies in China: presence and experience.China-Brazil Business Council - CBBC. https://www.cebc.org.br/sites/default/files/preview_relatorio_-_pesquisa_ingles.pdf

acquisition of a factory in Nantong, producing electric motors, and in 2019, it already launched its fourth unit, focused on the production of industrial automation equipment.

In 2005, *Vicunha*, a Brazilian multinational in jeans wear solutions, started its first subsidiary in Shanghai. *Vale*, a Brazilian multinational corporation engaged in metals and mining, established a joint venture with the Chinese company Zhuhai YPM in 2006 and announced another joint venture in 2020 with Ningbo Zhoushan Port. Furthermore, *Sabó*, an auto parts car producer, launched its first factory in Wuxi (Fleury, 2021).
The presence of Brazilian companies with operations in the Chinese territory has increased considerably in all sectors in the last decade, including agribusiness, natural resources, manufacturing, and services.

Table 5: Quantity of Brazilian companies in China

Sector	**Nº of companies**	**Nº of subsidiaries**
Agribusiness and natural resources	10	7
Manufacturing	16	28
Service	10	10

Source: Fleury (2021)

According to Frischtak and Soares (2012), *Suzano Papel e Celulose* bought FuturaGene in 2011, a pioneer in biotechnology and productivity for the forestry industry, based in the UK with laboratories in Israel, China and Brazil. *Suzano* was established in China with factory and commercial offices.

Randon is a Brazilian company dedicated to producing equipment, automotive systems, and services for transport. This company exported to China since 2001 and with the strategy of getting closer to stakeholders, decided to open its own factory for the production of tarpaulins and brake pads for heavy vehicles. Lastly, the company announces Nakata's purchase and with this, it doubles its production in China (Frischtak and Soares, 2012).

Fleury (2021) also brings data regarding the retail sector. With the intention of gaining competitive advantage, several companies associate themselves with local companies in order to adapt their strategies according to the needs and particularities of the Chinese consumer public.

Frischtak and Soares (2012) also point out that *Miolo*, a Brazilian wine´s brand, attended in 2011 on Wines from Brazil fair provided by APEX. On this event, *Miolo* initiated the approach with a Chinese importing company as an exclusive representative. The first store was launched in Shanghai; however, other units have been opened. As a result, China represents the fourth world market from *Miolo*. In the same year, *Arezzo*, a Brazilian footwear brand, also entered in China's market and faced some challenges such as adapting the product to local consumer´s desires and the pricing range. With its presence in the Chinese market, the company could reestablish its strategy and overcome these challenges.

The service sector is another that has gained relevance to Brazilian companies in the Chinese market. In 2010, Stefanini IT Solution entered the country with the acquisition of Tech Team Global, a North American enterprise, setting up facilities in Shanghai and Nanjing. Since then, the company has worked to provide a more extensive portfolio. In 2016, extensive products were developed in the business process outsourcing (BPO) area, automobilist industry solution, and automation industry 4.0.

Lastly, Brazilian companies that deal with the Chinese market observed a fast response from this market in view of the difficulties caused by Covid-19. Some companies from agribusiness such as *Marfrig* and *BRF* continued to export to China during this period. The experience of Brazilian companies operating in China has improved in terms of government policies, development of new businesses and products, and relationships. This exchange of knowledge has provided a gain of performance and an increase of competitiveness to these companies (Fleury, 2021).

4.2. Identifying China's potential market to Brazilian companies

Foreign companies of various sizes and segments may find difficulties to enter into a new market due to their lack of understanding of the target audience.

Although China is unified in terms of geopolitical aspects, its social and economic scenario is fragmented. It is possible to conclude that instead of representing a unified market, China is actually a collection of individual submarkets defined by demographic characteristics.

Hedley (2021) observed that companies in the B2C sector are focused on the traditional coastal provinces such as Zhejiang, Guangding, Jiangsu and Shanghai due to the concentration of population and higher incomes in these areas. On the other hand, B2B markets tend to be more geographically dispersed, as China has industrial clusters in specific cities and regions.

Below, the figure 6 shows a map of the 33 provinces and administrative regions of China. In red, the cities with industrial orientation.

Figure 6: Map of China´33 provinces and administrative regions

Source: Hedley (2021)

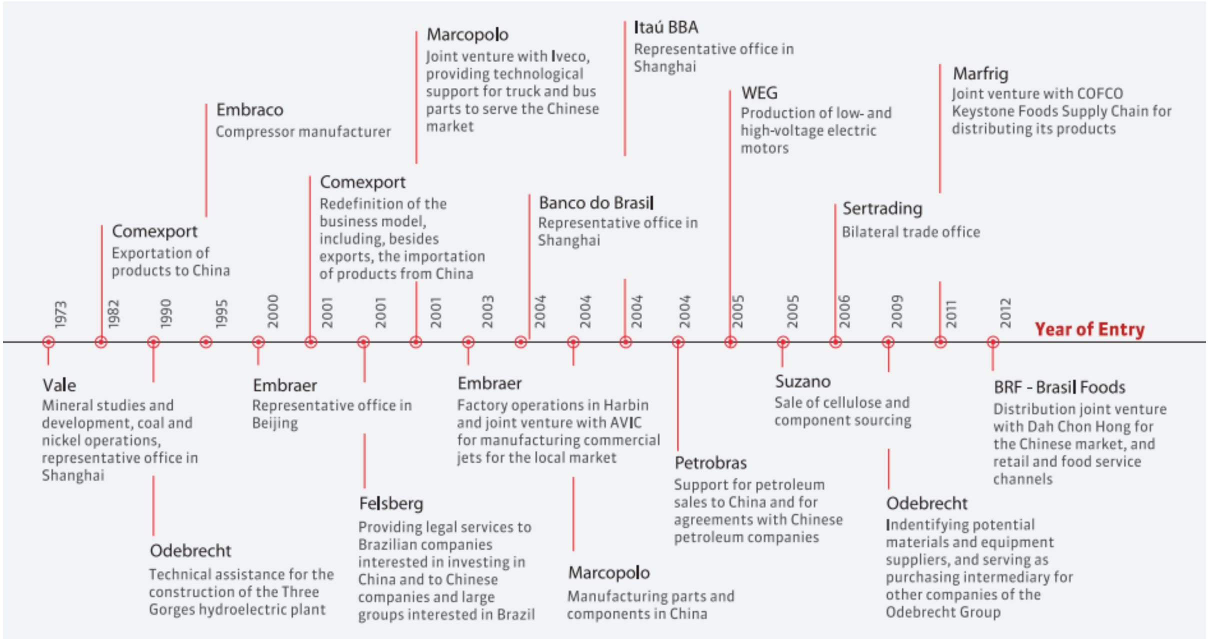
Table 6: Selected cities according to industrial orientation

Province	**Industry**
Shanghai	Petrochemicals, chemicals, pharmaceuticals, automobiles, electronic apparatus, financial
Beijing	IT, communications, electronics
Guangzhou	Automobiles, electronic appliances, textiles, apparel, toys, petrochemicals and chemicals
Jiangsu	Chemicals, textiles, communications, petrochemicals, steel, foods, auto parts, biomedicine
Shenzhen	IT, semiconductors, biomedicine, communications, electronics information
Zhejiang	Light industry, plastics, textiles, apparel, toys, metallurgy, household electrical, furniture, kitchenware
Shandong	Agricultural, oil & food supplies, pharmaceutical

Source: Hedley (2021).

Frischtak and Soares (2012) mentioned on the report that 80% of Brazilian companies with presence in China are concentrated in 12 provinces and municipalities of the East Coast. The main provinces are Jiangsu, Zhejiang, Shandong, Heilongjiang, Shanghai and Beijing. Furthermore, it was also identified that 90% of Brazilian investments in China are in joint ventures with local partners.

Figure 7: The main Brazilian companies' entrance per year in China



Source: Frischtak and Soares (2012)

4.3. Choosing a location

The choice regarding the local structure of the company depends on various factors, and the final decision is based on deep market landscape research.

In general, China´s cities are classified into Tiers, which include cities with similar market and economic characteristics.

Table 7: China´s tier areas

Tier	Cities
1st Tier	Shanghai, Beijing, Shenzhen, Guangzhou
2nd Tier	Hangzhou, Chengdu, Chongqing, Tianjin, Wuhan
3rd Tier	Ningbo, Suzhou, Xi'an

Source: Hedley (2021).

Referring to Hedley (2021), China´s Tier 1 represents a highly populated area with a majority, middle-class representation, and income levels well above the national average. Furthermore, Tier 1 concentrates the most mature market in terms of consumer behavior and is typically the most acceptable testing ground for foreign companies with lower experience in China. Although being based on a Tier 1 city can represent the lowest risk point of market entry, it also means that the company faces higher operational costs and more competition.

On the other hand, China´s Tier 2 includes cities that face economic growth and rising incomes. Based on these results, foreign suppliers entering these markets are much more attractive than they were in the past, especially due to strong commercial opportunities for foreign companies across a range of sectors.

Lastly, including Tier 2 and Tier 3 cities on the entry strategy can enable foreign companies to gain a first-mover advantage in these cities and lead to greater long-term market success.

Beyond that, certain locations extend more attractive policies to foreign investment in accordance with their local economic objectives. These locations are called Free Trade Zones. Dezan Shira & Associates (2022) point out that China has established 21 FTZs, which constitute part of China's efforts to transform into a more innovative, service, and consumption-driven economy and the creation of sustainable and high-end manufacturing capacity to attract international businesses.

Furthermore, some of the benefits of cross-border sales through an FTZ are [10]:

- Simpler records;
- Possibility of using bonded warehouses;
- Faster customs clearance;
- The possibility of goods being moved between FTZs and abroad without the need to pay taxes and fees.

[10] Domenico and Antunes. Investment Guide in China. InvestSP &BDCo. http://bdco.com.br/wp-content/uploads/2021/09/BDCo-Guia-de-Investimento_link.pdf

5. BRAZILIAN COMPANY´S EXPERIENCE IN HAVING PRESENCE IN CHINA'S MARKET

Frischtak and Soares (2012) interviewed a significant number of Brazilian companies with presence in China and members from the Ministry of Commerce People´s Republic of China – MOFCOM. Below, the main piece of information shared by the companies regarding the entry process into the Chinese market.

5.1. The main objectives to enter into China market

The main objective of Brazilian companies in being physically in the Chinese market is to take advantage of the growth opportunities offered by the country, gaining access to a vast consumer base and an expanding market. In addition, Brazilian companies seek to take advantage of opportunities to expand their international operations by establishing partnerships with local companies and establishing commercial contacts with other foreign companies. Another objective is to take advantage of the competitive advantages offered by China, such as tax incentives and access to qualified workforce and low operating costs. Below is the testimony of some Brazilian companies interviewed by Frischtak and Soares.

Banco do Brasil

With reference to China, we noticed a tendency for growth, which might not be 10%, but that will come to 7% or 8%, which is still a strong growth rate. For some years now, China has seen people transfer from rural areas to urban centers. In this context, there is an increasing demand for food supplies, while local production has dropped. To a certain extent, this benefits the Brazilian situation, which will probably continue to focus on natural resources and agribusiness. Another important point is the growing need for Brazilian iron ore because of the rebuilding of China—with steep growth rates and increasing dependency. China is Brazil's largest trade partner, and this degree of dependency will tend to climb. The U.S. will gradually lose its relevance and China will become more prominent.

Admilson Monteiro Garcia – Executive director of the Banco do Brasil

Comexport

Our history in China is much older than that of most Brazilian companies. At the beginning of the 1980s, our mission was to export large volumes of textile raw materials that were produced by several multinational companies installed in Brazil. The Brazilian market is still relatively immature for the consumption of these fibers, resulting in a significant amount of material left over during offseason consumer periods. We noticed that we could not sell the *product to just any country, on the spot market, that is, during a short period of the year and in large volumes, except to countries with very significant consumption levels. It was at that time that China arose as an alternative for these exports.*

Roberto Milani – Vice President Comexport

Petrobras

Petrobras set up its office in China in May 2004. This was the result of the company "discovering" China during that year. We noticed that the country was a huge consumer of energy, especially petroleum. At the time, China was the third largest petroleum buyer in the world. Today, it is the second, after the U.S. So, we saw that we couldn't ignore it. We launched the office in Beijing with the presence of President Lula.

Marcelo Castilho – General manager of the Petrobras office in China

Suzano

The Chinese market for cellulose is number one in the world, and it is our trade policy to not sell through trading companies.

…

The tendency in China is toward growth. The country, which is one of our target markets, is the one that most invests in producing paper, and has very ambitious growth projects—approximately five million tons of paper to be produced over the next 20 months.

Alexandre Yambanis – Director of the Cellulose Business Unit of Suzano

WEG

WEG needed a local plant because the services provided from Brazil involved very high logistic costs and transfer time.

Siegfried Kreutzfeld – Director-superintendent of WEG Motors

5.2. The main challenges faced

Frischtak and Soares (2012) highlight the main difficulties, solutions, and perspectives found by Brazilian companies in China. The summarized points are the following:

a. Cultural Differences: China and Brazil have different business cultures, which can make it difficult for Brazilian companies to adjust to the cultural norms of doing business in China.

b. Market Access: Accessing the Chinese market can be difficult for foreign companies because the Chinese government has certain regulations and policies in place that restrict the ability of foreign companies to do business in the country.

c. Government Policies: The Chinese government has certain economic policies in place that can make it difficult for foreign companies to operate in the country. For example, China has a complex tax system and certain restrictions on foreign investment.

d. Intellectual property: Chinese competitors seek to upgrade themselves technologically and consequently disrespect ownership rights. Furthermore, they transfer the government incentives to incoming foreign companies; however, it is required that technology be transferred to Chinese partners.

e. Distribution Channels: Finding appropriate distribution channels in China can be difficult for Brazilian companies. To be successful in the Chinese market, companies need to identify a reliable distribution network.

Below, the testimony of some Brazilian companies interviewed by CBBC regarding this theme:

Banco do Brasil

We took nearly five years to understand how we could do business in China. It was not an easy learning process, especially for a Latin American bank, since western culture is completely different from eastern culture. Besides the cultural factor, at that time, there was not such a profusion of Brazilian companies in China.

We will begin with the relations with Chinese banks. One of the first difficulties was the fact that the Chinese banks do not engage without having a signed memorandum of understanding in place. Usually, we only sign memoranda of understanding when we already have a specific project. In China, however, this had to be the first step.
Since this was the rule of the game, the BB signed memoranda with the greatest possible number of Chinese banks and, thus, business began to flow much better. We learned, with some difficulty, that in China it is not so important what the bank has to offer, but rather, the "guanxi".

Admilson Monteiro Garcia – Executive Director of the Banco do Brasil

WEG

"Guanxi" is a pure relationship based on the ethics and principles of mutual trust between people. There is nothing unethical about this. It is merely based on trust. It is a relationship where directors and clients talk sincerely and openly about strategies, growth, and opportunities. If the client, who is on the other side of the table, feels that the company communicates trust, the deal will go forward; and the opposite can also happen. There's nothing more than that. It is earning trust at the highest levels.

In business meetings, there is little dealing with trade subjects, but the main things are generalities and personal subjects. It is a very interesting ritual. There are protocols: a way of talking and of celebrating. "Ganbei" (gift) is essential to the Chinese, as a means of showing gratitude. It is a sign of trust.

If we had not established a good relationship, difficulties would most certainly arise. Fortunately, "guanxi" helps us in this respect, like speedily obtaining certain licenses. It is essential that there be "guanxi". This trust relationship is built over a period of time.

Siegfried Kreutzfeld – Director-superintendent of WEG Motors

5.2.1. Perspectives and suggestions for investments in China

As mentioned before, there is an asymmetrical relationship between Chinese investments in Brazil and Brazilian investments in China. In this context, it is relevantly amplifies Brazil's participation in the Chinese market. As the biggest population in the world, even with the first population decrease in the last sixty years (National Bureau of Statistic of China, 2023), ApexBrasil (2023) points out some opportunities for Brazilian companies to export to China, namely: soy, corn, iron, steel, cotton, coffee, wood, pork, peanuts, cellulose and crude oil.

In terms of policies, ApexBrasil also mentions that Brazilian exporters should pay attention to non-tariff measures to enter into this market. Brazil does not have a Free Trade Agreement with China. Currently, the main Chinese agreement is the RCEP, which came into force in January 2022. Furthermore, the last travel of the current president of Brazil to China resulted in 15 cooperation agreements (EBC, 2023).

Below, the testimony of some Brazilian companies interviewed by CBBC regarding this theme:

Felsberg Associados

It is not viable to negotiate with Chinese companies in the same way we negotiate with companies from other countries, that is, in a market-driven fashion. It is necessary to establish a strategy, have clear objectives, and negotiate them.

Thomas Felsberg - Founding Partner of Felsberg e Associados

Suzano

In our China office, we work with Chinese professionals because we believe that a local executive who is fluent in Mandarin is of great importance in contact with clients. We also arrange executive interchanges between China and Brazil, by bringing Chinese executives to train in our country and taking Brazilians to be enabled in China. In this way, we pursue a deepening of our trade relations and a greater understanding of the Chinese market.

Alexandre Yambanis – Director of the Cellulose Business Unit of Suzano

National Industry Conferation (Confederação Nacional da Insdústria - CNI)

Today, any company that wants to develop a survival strategy should consider China in its analyses, diagnose the existing chains, and pursue ways of being distinctively different in this scenario. For example, if the company chooses specialized automation, its chances of success increase. If the decision is to produce a generic system, then, losses to the Chinese are certain. Competing with Chinese products as equals is aggravated by all of the cost issues in Brazil, which do not exist in China, such as labor costs, taxes, and exchange rate.

José Augusto Coelho Fernandes – Director of Policies and Strategy of CNI

6. OPPORTUNITIES AND CHALLENGES TO BRAZILIAN COMPANIES IN CHINA

Despite the benefits of being located in China, Brazilian multinationals still have conservative investments in this market compared to investments made by China in the Brazilian market. In 2021, Brazil was the 7º biggest supplier to China; on the other hand, China was the main supplier to Brazil.

Table 8: Bilateral trade - 2021

Brazil supplying China	China supplying Brazil
7º biggest supplier	1º biggest supplier
4,2% of market share	21,7% of market share

Source: ApexBrasil (2023)

In this context, it is important to expand Brazil's participation in the Chinese market and diversify Brazilian exports, which are mainly concentrated in commodities, almost 75% of sales — soybeans (35,5%), iron ore (20,3%) and oil (18,7%).

Apex-Brasil provides the *China Opportunities Map* with the aim of helping entrepreneurs interested in exploring Brazil's largest trading partner (Apex-Brasil, 2023). Bellow, the main segments to be explored by Brazilian companies.

Table 9: The main Brazilian products with opportunities in the Chinese market

Segment	**Regions**	**Commercial Data**
Footwear.	Hainan, Zhejiang and Chongqing.	• Brazilian exports in 2022 US$ 3 Mi; • Main competitor: Italy
Articles, paper, pulp.	Shandong, Jiangsu, Guangdong, Zhejiang, Fujian, Chongqing, Jiangxi, Beijing, Guangxi Zhuang, Shanghai, Anhui, Sichuan, Hebei, Henan, Hunan.	• Brazilian exports in 2022 US$ 6 Mi; • Main competitors: Canada, Indonesia, United States, Russia, Chile, Laos, Thailand.
Vegetable fats, oils.	Zhejiang, Guangdong, Shanghai, Tianjin, Shandong, Hainan, Jiangxi.	• Brazilian exports in 2022 US$ 4 Mi; • Main competitors: Indonesia, Malaysia.
Metallurgical machinery.	Guangdong.	• Brazilian exports in 2022 US$

		6 Mi; • Main competitor: Taiwan.
Manufacture of wood and of products of wood and cork, except furniture.	Zhejiang, Beijing, Tianjin, Liaoning, Anhui.	• Brazilian exports in 2022 US$ 62 Mi; • Main competitors: Russia, Thailand and Germany.
Electric machinery.	Tianjin.	• Brazilian exports in 2022 US$ 139 Mi; • Main competitor: Japan.
Tanning or dyeing extracts; tannins and their derivatives.	Guangdong, Fujian, Zhejiang, Shandong, Hebei, Henan, Liaoning, Beijing, Sichuan, Heilongjiang.	• Brazilian exports in 2022 US$ 9 Mi; • Main competitors: Italy, Turkey, South Africa, Australia, India.
Animal fats and oil..	Guangdong, Shandong, Jiangsu, Fujian, Shanghai, Anhui, Henan, Tianjin, Chongqing, Beijing, Liaoning, Hubei.	• Brazilian exports in 2022 US$ 27 Mi; • Main competitors: Australia, Peru, Chile, Belgium, Vietnam.
Essential oils and resinoids/ perfumery or toiletry.	Shanghai, Guangdong, Jiangsu, Zhejiang, Yunnan, Hunan.	• Brazilian exports in 2022 US$ 27 Mi; • Main competitors: United States, Taiwan, Vietnam and India.
Non-monetary gold.	Beijing, Shanghai, Fujian, Zhejiang, Shandong, Yunnan.	• Brazilian exports in 2022 US$ 4 Mi; • Main competitors: Sweden and Russia.
Plastic in primary form.	Shanghai, Shandong, Fujian, Hunan, Mongolia Interior.	• Brazilian exports in 2022 US$ 24 Mi; • Main competitors: Iran, South Korea, Saudi Arabia, United Arab Emirates, Germany.
Medicines and	Chongqing, Hubei.	• Brazilian exports in 2022

Pharmaceutical products.		US$ 16 Mi; • Main competitors: South Korea and Italy.

Source: Apex-Brasil (2023)

However, Brazilian exporters need to pay special attention to non-tariff measures when entering into this market. Brazil does not have a Free Trade Agreement with China. The Regional Comprehensive Economic Partnership (RCEP) Agreement is the main Chinese agreement currently, which came into force in January 2022, with a 20-year unlocking window (Apex, 2023). RCEP is a free trade agreement among the Asia-Pacific nations.

Furthermore, it is relevant to know that the reasons for the direct investments in China by Brazilian companies can be classified as efficiency-seeking, resource-seeking, market-seeking, and strategic asset-seeking (Frischtak and Soares, 2012).

Recently, another reason has motivated the companies to invest in China: the need to reduce costs in order to face off with China in the dispute for Brazil´s own domestic market. Frischtak and Soares (2012), point out as an example the textile companies that import their winter collections directly from China, since the production cost in the country is about 80% lower than the production in Brazil. For other collections, the advantages are around 30% to 40%.

7. PRESENTATION OF FINDINGS

7.1. Brazilian business with China

China is an attractive and strategic market for Brazilian products. This market is among the main destination of Brazilian exports. In 2021, Brazil was the 7º biggest China supplier, with a 4,2% of share (Apex-Brasil, 2023).

According to Wittenberg, Leal and Welgacz (2017), 80,7% of the responders of the research regarding Internationalization of Brazilian companies said to be export companies and only 38% have branch companies abroad.

Furthermore, 10% of the companies point out China is a country where they plan to open a new unit or have a partnership in the next 3 years, and 15% have chosen China to expand exports.

7.2. China government's policies and regulations

As the Chinese economy continues to advance, industry-specific rules and standards have been steadily increasing, presenting challenges that domestic and foreign companies must meet in order to remain compliant (CECC, 2020).

According to Hedley (2021), the choice of company formalization in the Chinese market is one of the most important decisions to be made. Choosing this entry mode depends on many factors, including: industry landscape, geographic size, market scope, overhead costs of creating the legal entity, and hiring local employees.

Foreign enterprises may entry in China's market by some register forms. Below are the concept and main characteristics of some them:

7.2.1. Representative Office (RO)

Based on Dezan Shira & Associates (2022) "*an RO is an attractive way for foreign investors to get a feel for the Chinese market as it is the easiest type of foreign investment structure to set up*". An RO is an extension of a foreign company, but does not possess any legal standing, and cannot independently assume civil liability. When an RO enters into a contract, the responsibility and obligations of the agreement are hold by the foreign company[11].

[11] Dezan Shira & Associates (2022). An introduction to Doing Business in China 2023. Dezan Shira & Associates. https://www.china-briefing.com/news/an-introduction-to-doing-business-in-china-2023/

Furthermore, an RO can only engage in non-profit activities and can perform the following functions[12]:

- Conduct research and surveys for its parent enterprise in the local market;
- Liaise with local and foreign contacts in China on behalf of the parent enterprise;
- Conduct research and provide data and promotional materials to potential clients or trading partners;
- Act as a coordinator for the parent enterprise's activities in China;
- Make travel arrangements for parent enterprise representatives and potential Chinese clients.

The representative office is a non-legal entity representing its parent company overseas. Its name should be in the form of "Name of the Enterprise + Name of the City + Representative Office". Lastly, the business address must be located in commercial buildings or apartments that the government provides. It also needs to register employees with the local social security authority within 30 days of the employee receiving their work permit (Hedley, 2021).

7.2.2. Wholly foreign-owned enterprise (WFOE)

A Wholly Foreign Owned Enterprise (WFOE) is a "*limited liability company incorporated in China by foreign investors, allowing 100% foreign-owned operations, with a separate legal entity status, registered capital, and independent accounts in China. This setup also provides owners with the ability to open a Chinese bank account, hire staff, and apply for local business licenses"*[13].

In comparison to an RO, a WFOE can generate profits, issue invoices in RMB to suppliers, hire staff directly and even create subsidiary businesses in China.

Originally, WFOEs were designed to facilitate the manufacturing of goods for export or the implementation of cutting-edge technology. However, following China's accession to the World Trade Organization (WTO), these conditions were gradually abolished, and service providers such as consulting firms, management services, software developers, and traders have been increasingly utilizing this corporate structure. Thus, any business in China that is

[12] Hedley, Mark. China Market Entry Strategy: How to enter the Chinese market. https://www.b2binternational.com/publications/china-market-entry/

[13] Worldwide Incorporations. (2020). Wholly foreign-owned enterprise (WFOE) in China. https://www.worldwideincorporations.com/wholly-foreign-owned-enterprise-in-china/

composed of 100% foreign capital may be considered a WFOE. As WFOEs have wide ranging potential with regards to new markets, they operate on the basis that the capital subscribed and contributed to the company is exclusively held by overseas investors, thus excluding any branches established in China by foreign companies or other foreign economic organizations[14].

Dezan Shira & Associates (2022), points out the three distinct WFOE setups available in China: (i) *service (or consulting) WFOE*; (ii) *trading WFOE;* and (iii) *manufacturing WFOE*. All three corporate structures possess the same legal status, but vary widely in terms of their setup procedures, costs and the range of commercial activities they are authorized to undertake. For example, Trading WFOEs and Manufacturing WFOEs must generate most of their income from their core business, yet can offer associated services. Furthermore, Service WFOEs are qualified to engage in trading activities related to their service offering (Dezan Shira & Associates, 2022).

Lastly, Table 10 highlights the main differences between WFOE and Representative office.

Table 10: Main differences between WFOE and Representative Office

WFOE	**Representative Office**
Primarily used for operations that generate profit in China	Primarily used for nonprofit or research operations in China
Can hire employees	Cannot hire employees
Can generate profit	Cannot generate profit
Needs to file taxes	Needs to file taxes (on expenses)
2-3 months set up time	2-3 months set up time

Source: FDI China. (2021). China business solution guide 2021.

7.2.3. Joint Venture (JV)

A JV is defined as "*formed by one or more foreign investor(s), along with one or more Chinese parties"* (Dezan Shira & Associates, 2022). Dezan Shira & Associates (2022), explain that prior to the Foreign Investment Law (FIL) taking effect on January 1, 2020, Chinese individuals were largely ruled out as potential shareholders in a joint venture, apart from a select few circumstances. However, the FIL now permits Chinese individuals to co-invest with foreign partners, providing investors with increased flexibility in selecting their business associates.

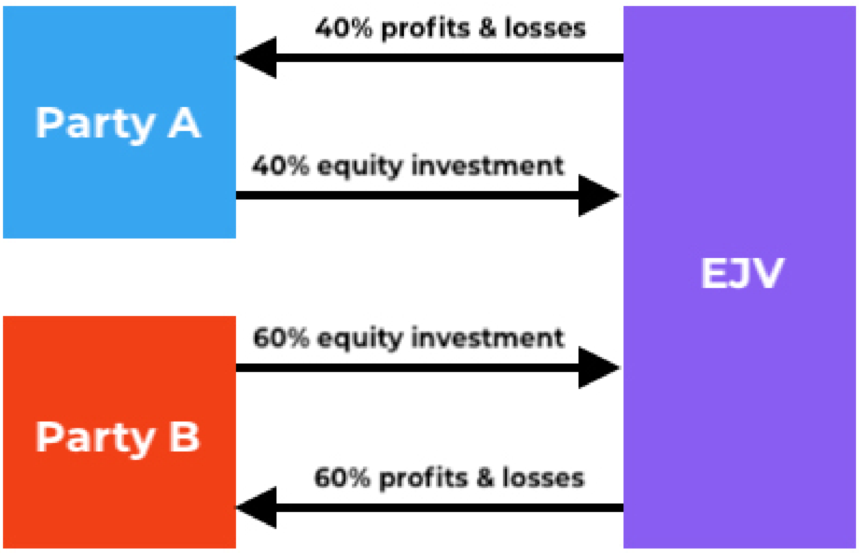
[14] Path to China. (2021). Wholly foreign-owned enterprise (WFOE) in China. https://www.pathtochina.com/reg_wfoe.htm

Dezan Shira & Associates (2022) highlight mainly two reasons for foreign investors to choose a JV structure. Firstly, the foreign investor wants to invest in a restricted industry sector, where the law permits foreign investment only via a JV with a Chinese partner. Secondly, the foreign investor wants to make use of the sales channels and network of a Chinese partner who has local market knowledge and established contacts.

Furthermore, there are two types of Jvs in China, namely:

a) Equity Joint Venture (EJV): (i) the distribution of profits and losses between the parties of the EJV will be proportionate to their respective equity interests; (ii) generally, the foreign partner should hold at least 25 percent of the registered capital of the EJV; and (iii) an EJV should be a limited liability company.

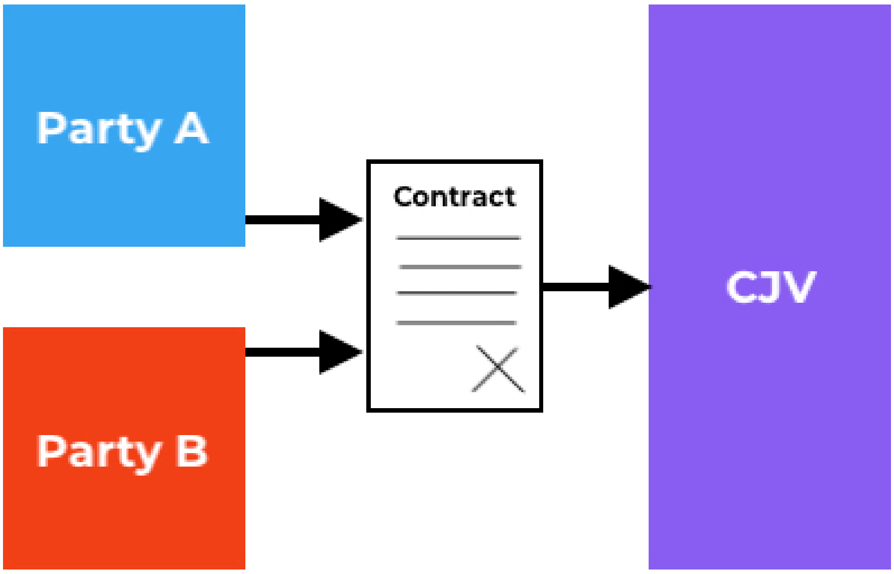
Figure 8: EJV model



Source: FDI China (2023). https://www.fdichina.com/china-company-registration/china-jv-registration/

b) Cooperative Joint Venture (CJV): (i) the distribution of profits and losses between the parties of the CJV will be according to the provision laid out in the joint venture contract; (ii) a CJV can be operated either as a limited liability company or as a non-legal person.

Figure 9: CJV model



Source: FDI China (2023). https://www.fdichina.com/china-company-registration/china-jv-registration/

7.2.4. Foreign invested commercial enterprise (FICE)

According to Dezan Shira & Associates (2022) a FICE can either take the form of a WFOE or a JV, and is commonly used for retail, franchising or distribution purposes. Depending on the needs of the establishment, FICEs can combine various activities such as manufacturing and services with their sourcing and quality control operations, providing more control and agility compared to solely sourcing from an overseas headquarters.

Furthermore, FICEs offer an efficient solution for foreign companies that resell goods in the domestic Chinese market as they can purchase items in China without being subject to extra costs associated with imports (e.g. logistical expenses, customs duties, value-added tax) or having to ship the items outside China before reselling (Dezan Shira & Associates, 2022).

7.2.5. Advantages and disadvantages

When deciding on an entry mode in China, various components should be taken into consideration such as the industry landscape, the scope and size of the desired market, the planned approach to manufacturing or importing products, and the level of local sales and technical support customers require. Conducting a cost-benefit analysis of the processes involved in creating a local entity and hiring local employees can help to determine the ideal approach. Below, Table 4.4 exposes the main advantages and disadvantages of each entry mode.

Table 11: Foreign entry forms: Advantages & Disadvantages

Form	**Advantages**	**Disadvantages**
WFOE	• High level of managerial control; • Can employ own people without restrictions; • Greater flexibility; • Can convert RMB profits into US dollars; • Greater level of IPR protection.	• Initial set-up costs high; • Long incubation period; • No access of JV partner resources; • Higher start-up and operating costs (registered capital); • Some industry limitations; • Minimum number of staff required; • Challeging tax and repatriation of profits.
Joint Venture (JV)	• Mandatory for some industries; • Opportunity to use existing sales networks and customers bases; • Access to partner´s existing resources; • Production facility; • Lower cost base (local management).	• Less managerial control; • Finding a trustworthy partner is critical; • Challenging to agree terms of partnership; • May be a long negotiation period; • Potential risk to IPR; • Success may depend on having staff on-the-ground to oversee operations; • Partner likely to negotiate terms in their favor.
Representative Office	• Quick to set up; • Low cost (low overheads); • No registered capital requirement; • Good for marketing and partner auditing.	• Unable to trade; • Staff employed via third party; • Limits on number of staff.

Source: Hedley (2021)

7.3. Due Diligence

According to Howson (2017), due diligence is the most important but least well-understood aspect of the acquisition process.

Structuring a due diligence program is a balance between cost and estimated risk as it is not possible to measure all possible risks. On the other hand, those programs highlight areas of uncertainty in which warranties, indemnities, or other forms can provide protection to the business (Howson, 2017). Below are the main objectives that each due diligence aspect should pursue by Howson (2017):

Table 12: Due diligence aspects and main objectives

Due diligence aspect	**Main objectives**
Financial due diligence	• Interviews with key people in the business to perform a detailed analysis of business support. • Presenting how the process works in the target company and how effective it is. • The underlying profit that the target company is capable of earning. In addition, cash flow.
Legal due diligence	• Reporting any litigation or disputes affecting the target company. • Identify what needs to be done so that consent and releases do not delay the transaction. • Conducting a search on the target and its subsidiaries and searching the seller to check whether it has the power to sell the target company.
Commercial due diligence	• Providing a wider range of estimates of market size and future growth rates.
Human Resources due diligence	• The due diligence process begins with an information request followed by management interviews. • Reviewing the targets compliance with the legislation and, if possible, health and safety. • Furthermore, specialists should inspect the site.

Management due diligence	• Evaluating management both as individuals and as a team using disciplined methods. • Management appraisals provide an objective assessment of senior managers' capability both individually and collectively. • Reports should provide insight into individual managers and the capabilities of the senior management team as a team. • Reports are confidential, but feedback to managers can usually be arranged.
Pension due diligence	• Actuarial valuation attempts to assess the value of the pension scheme's assets and the value of future pension payments. • Detailed due diligence is required if the purchaser is acquiring the pension schemes as part of the transaction.
Tax due diligence	• Investigation should cover most of the taxes. • Anglo-Saxon practice calls for a tax indemnity, often referred to as the tax deed.
Environmental due diligence	• Highlights matters that require a seller or a buyer to notify insurers of liabilities to which policies attach. • Reporting the environmental problems in which the company is involved.
IT & production technology due diligence	• IT due diligence is as about people as about technology and systems. • An acquisition is a prime opportunity to make the changes necessary to elevate IT to where it belongs, as a strategic tool for creating competitive advantage.
Technology due diligence	• This aspect deals with the product technology, the technology associated with the product itself.

	• Approaching customers and personnel issues as well as examining the technical merits of the product. • Analyzing the decision-making behind new product releases. • Covering customer and personnel issues; and examining the technical merits of the product.
Intellectual property (IP) due diligence	• This aspect is about patents, trademarks, and other rights to designs and inventions. • Ensuring that the IP that has being bought really exist, can be fully exploited and will give the competitive advantages assumed. • Warranty that if the target company is being sold out of a group, the IP may have to be assigned or licensed as part of the deal.
Insurance and risk management due diligence	• Reducing the costs of risk. • Highlighting the areas where insurance is appropriate and providing options based on variable levels of self-insured risk retention combined with practical steps to reduce exposures.

Source: Howson (2017)

7.4. Hiring staff

According to Dezan Shira & Associates (2022), the enterprise can hire employees in China in the following three ways:

- Direct hiring;
- Dispatching; and
- Outsourcing.

Direct hiring

Employers in China are required to have a written contract with their employees before the end of the first month of employment. If an employer fails to do so, they must provide double salary for every month without a contract and must also provide an agreement for non-fixed term work after one year. The only exception is part-time work, where an oral agreement is accepted as sufficient (Dezan Shira & Associates, 2022).

Dispatching

Labor dispatching is a common form of supplementary employment in China. A host company hires workers from a dispatching agency in a triangular employment relationship. The dispatching agency is the legal entity responsible for the administrative management of such employees, as they typically have more experience and knowledge about hiring in the locality (Dezan Shira & Associates, 2022).

Outsourcing

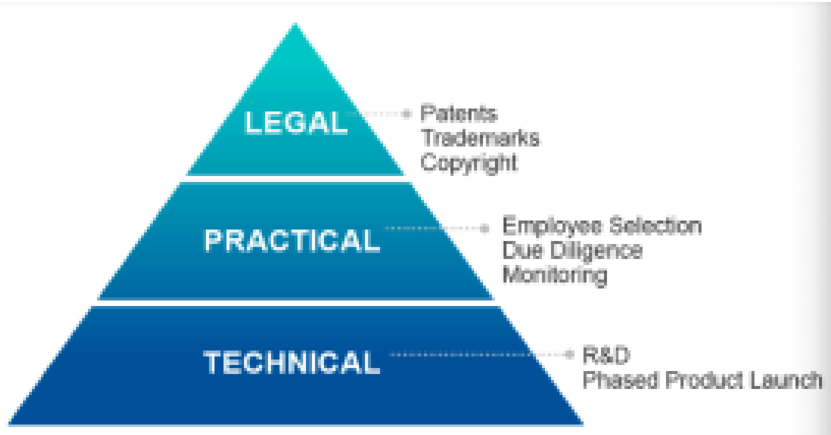
This other form of supplementary employment in China is traditionally applied to tasks that require specialist skills, a high degree of confidentiality, or those that have a clear scope but incur in major consequences if incorrectly implemented, such as IT development, accounting, tax filing, HR administration, and payroll processing (Dezan Shira & Associates, 2022).

7.5. Developing international property rights (IPR) strategy

Developing an international property rights (IPS) strategy is an important step to observe before building a strategy to enter the Chinese market, as IPR infringement is common in China.

According to Hedley (2021), an effective IPR strategy includes legal, practical, and technical measures to prevent infringement and ensure legal rights in case of some event of infringement.

Figure 10: China IPR strategy



Source: Hedley (2021).

Hedley (2021) also clarifies that China has a “first-to-file” patent system, which is defined as the possibility for local Chinese companies to register another company’s patents even though it is not the original inventor of a technology. Regarding the time, it relevantly points out that there is a time limitation to register patents in China, so firms that have patents registered abroad for more than 12 months previously, usually are unable to register their patents in China.

Furthermore, China also has a “first-to-file” trademark system, which is defined as *a foreign company’s legitimate brand and logo that cannot be used if these trademarks have already been registered by a local Chinese company* (Hedley, 2021).

7.6. Summary of presentation findings

From the analysis of the descriptive research approach, this study sought to understand the main advantages and disadvantages of the process of entry into the Chinese market. Based on these findings, below are the main steps to be followed by Brazilian companies to build a consistent proposal in order to have success in expanding their business in this market.

The follow steps are proposed for companies that already have made a first analysis and identified China as the market to be focused on for the expansion of their business.

Some assumptions guided the development of the recommendations set out below:

a) “*Guanxi*” and “*Ganbei*”: as trust sustains relationships and the act of giving confirms this trust and shows gratitude, these two values must be present when doing business in China.

b) Physical presence: even nowadays that it is possible to do business in a virtual environment, the way to do business in China requires constant contact and face-to-face.

Due to the above assumptions, the following steps are recommended:

Step 1: **Target market segment analysis, company strategic analysis, and international expansion plan**

In order to gain knowledge regarding the target market and to provide a plan which translates a valuable proposal to the business and support a strategy to expand the business, it is recommended: (i) environmental analyses based on PEST approach (political/legal; economic; social/cultural; technological); (ii) strategic analyses as SWOT, Porter’s forces; (iii) scanning China’s map in order to identify the regional that contribute to the business of the enterprise; (iv) providing a Business Model Canvas as a strategic management to be follow; (v) based on the previews data, proposing a detailed Business Plan in which a valuable proposal will be used on the target market, a price matrix with the competitors of the market comparing price charged and product/service offered; (vi) risk analyses; (vii) defining the strategy of the internationalization.

Step 2: **Define the entry model and Corporate Governance**

Based on the Business Plan, provide a study with the entry model, approaching: (i) the register's forms which contribute to the strategy of the internationalization process; (ii) the steps to conclude the register's forms; (iii) a comparative location proposal, to define the physical installation, labor and survey of the estimated costs involved in opening and maintaining the structure and point out the tax incentives of each location in order to base the best option for this structure.

Step 3: **Action Plan (5W2H)**

Provide an Action Plan detailing the arrangement to be developed in order to achieve the goal using 5W2H methodology (what, why, where, when, who, how and how much).

Step 4: **Hiring a law firm**

In order to support with legal aspects defined on the business model and: (i) to register firm and brands in local regulators, under the laws of foreign investment in the country according to the model defined ; (ii) depending on the strategy, to provide support on the due diligence process of the companies and staff involved; (iii) to draw up contract drafts with local companies, partners and employees; (iv) to advice on supplementary operating documents such as business rules, shared management and conditions for initiating the business.

Step 5: **Communication and promotion**

For this step, it is possible that more deeply and specific data are necessary; then, the company can consider hiring local research firms to collect various materials to build a consistent Communication and Promotion Plan for the insertion and consolidation of the company in the target market.

Step 6: **Policy for evaluating and reviewing actions**

As a way of controlling and identifying possible failures, it is recommended to draw up an evaluation plan that should be carried out at the end of a period of time determined by the company. As a suggestion, this plan should contain the following analyses: (i) planned action to be executed in the cycle; (ii) actions performed in the cycle; (iii) comparison of the planned budget with the executed budget by activity; (iv) ROI evaluation; (v) development of improvement plan; (vi) review of upcoming activities to compare with the company's current internationalization strategy.

8. CONCLUSION

In conclusion, based on this study, it is possible to have a comprehensive overview providing the main aspects regarding doing business in China. Through an analysis of the Chinese business context and an exploration of the essential cultural aspects, this study provides the specific knowledge required to prepare companies that intent to do business with this market with a sustainable competitive advantage specifically for Brazilian companies. Firstly, in order to build the specific knowledge this study is composed by a bibliographic analysis from government institutes such as the Brazilian Trade and Investment Promotion Agency - APEX and the Ministry of Commerce People´s Republic of China – MOFCOM, and from businesses and law consulting enterprises that deal with the Chinese market. Secondly, the analysis of secondary data from interviews carried out by the China-Brazil Business Council - CBBC with Brazilian companies with a presence in the Chinese market bring the specific topics to be observed by this target public, which intends to deal with a complex market as China. Thirdly, there is an overview regarding exports' opportunities to Brazilian companies to explore in China by segments of products, regions with potential to absorb more demands and the main competitors. In addition, it also points out the main China government's policies and regulations addressing the main forms of formalizing a foreign company in the Chinese territory. Lastly, the study suggests six main steps to be followed by Brazilian companies to build a consistent proposal to have success in expanding their business in this market.

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