

# Chapter 9

## Experience with acquisitions of German *Mittelstand* companies – a case study

Xiling Zhu

### 1. Introduction

‘China’s global shopping tour has just begun.’ Felix Lee<sup>1</sup>

According to KPMG, China is expected to continue being the largest contributor to world GDP – in purchasing power parity terms – and is expected to account for nearly 20 per cent of world GDP by 2020, compared with 15.5 per cent for the European Union and 14.9 per cent for the United States (KPMG 2016).

Based on KPMG’s figures, Chinese companies conducted 502 overseas takeover deals in 2015, compared with 325 in 2014. The value of announced deals – USD 87.7 billion – rose by 40 per cent, year on year (KPMG 2016). Continuing this sharp growth, Chinese outbound mergers and acquisitions, including announced transactions, already hit the USD 100 billion mark in the first quarter of 2016, according to data provider Dialogic. This was one-third of the global cross-border mergers and acquisitions volume of USD 302.6 billion in the first three months of 2016 (Gätzner 2016).

Germany is one of the favoured target countries for Chinese outbound mergers and acquisitions investment. According to EY, China became the second biggest foreign investor in Germany from outside Europe, following the United States (EY 2016). In terms of number of deals, worldwide Germany ranked fourth as a target country for Chinese cross-border acquisitions in 2015 (KPMG 2016). In 2016 Chinese investors increased their takeovers in Germany even more dramatically.

This breath-taking development implies a significant economic and social impact on the receiving country.

This chapter is based on a study of a 2005 takeover of a listed German company with a global leadership position in the machine industry (company A) by a Chinese state-owned conglomerate (group B).

The goal of this case study is to throw light on the post-merger integration strategy and process with a focus on communications between the acquired company and the Chinese parent concerning the integration strategy. It explores the development of the target company before and after closing of the transaction for a period of ten years, asking the following questions:

---

1. China Correspondent of *Zeit Online*, TAZ and NZZ media group; keynote speech at the Bavaria-China Spring Festival, 3 March 2014.

- What are the motives for Chinese investors to acquire German *Mittelstand* companies?
- How do Chinese investors integrate their acquired German targets and what are the results?
- How does the Chinese acquirer manage communications and interaction, in particular with regard to decision-making structure, and how does the Chinese owner integrate employee relations?
- How are communications between Chinese acquirer and works council, as well with the target management?

The situation described in this investigation is presented from the point of view of a Chinese representative, a German manager and an employee representative and internet research. To ensure anonymity, all relevant information related to the names of both companies and persons is left out.

Although a single case study is not able to present the current situation of Chinese takeovers in Germany in general, it does provide an insight into the target company and its development after the closure of the takeover transaction. This gives an impression of the opportunities and risks characterising Chinese acquisitions in Germany.

The main motivation for selling the target company was to find a strong cooperation partner to access the Chinese market. For the Chinese investor, globalisation, market pressures from domestic and international competitors, upgrading to high-end manufacturing and brand were the main motives for acquiring the German target.

The target company has not been integrated into the parent group, and has kept its name and brand. Both acquirer and target have developed well from the standpoint of sales and operating results. However, no significant operating synergies from the merger can be identified.

The Chinese parent, together with works council representatives, makes strategic decisions. The local management team possesses considerable autonomy in operating decisions. Communications are limited between top managers from parent and target company. There have been no changes for employees since the transaction.

While communications between the Chinese owner, their representative and the works council are running smoothly, more challenges characterise cooperation between the local German manager and the top manager of the Chinese parent.

Section 2 presents the profiles of the acquirer and the target company. Section 3 describes the background, motives and process of acquisition. In Section 4 the integration strategy and its results are presented, while Section 5 depicts the decision-making structure, integration of employee relations and communications between the acquirer, works council and local management. Section 6 concludes.

## 2. Profile of acquirer and target

### 2.1 Profile of the acquirer<sup>2</sup>

The history of the Chinese acquirer company – ‘B’ – started in 1965 in Shanghai, the first group in that industrial area of China and wholly state-owned at that time. In 1993, the group was partially privatised by the state and brought to the Shanghai Stock Exchange as the first listed company from this industry. Control has remained in the hands of the Shanghai government, however.

During the 1990s B became number one in its industry. After China’s economic opening it faced increasing competition from private and foreign companies, especially from the beginning of the twenty-first century. It lost its position in the top 10 companies in China and faced a crisis. To cover its losses, it depended on selling land and premises to survive.

To turn this situation around, there were two solutions: either merge, a measure that would have resulted in the disappearance of the oldest Chinese brand in the sewing machine industry, or actively pursue China’s ‘Going Out’ strategy, changing the situation through internationalisation by acquiring companies abroad. The second solution was chosen.

After acquiring the German company A in 2005, B successfully completed restructuring by 2013. In that year, too, all its subsidiaries turned losses into profit. In the same year B completed two additional 100% acquisitions in Germany through its European investment subsidiary B Europe.

Today Group B has more than 30 branches and subsidiaries, including 15 overseas enterprises and is headquartered in Shanghai.

With its domestic and overseas subsidiaries, the conglomerate operates in a number of areas, especially in industrial and household sewing technology, foreign and domestic trade of sewing machines and parts, asset and investment management, office equipment and accessories, logistical services and management consulting.

Group B, including its German subsidiaries, has increased sales and operating results in recent years. Figure 1 shows developments from 2010 to 2015.

B is a state-controlled stock corporation (Reisach 2016: 5; Ten Brink 2014: 691f.). This is a state-owned enterprise brought to the stock exchange by the government, with the State Asset Supervision and Administration Commission (SASAC) or its organisations at the provincial or municipal level as controlling shareholder.

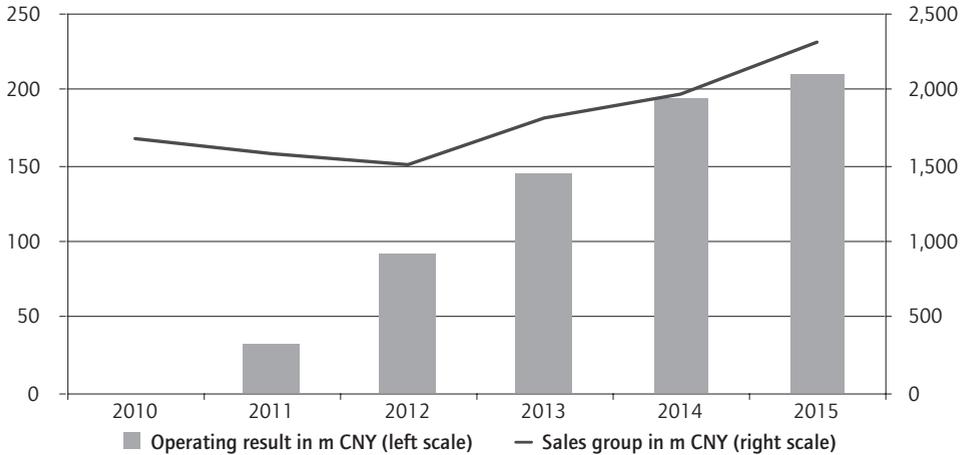
B’s controlling shareholder is the municipal State Capital Control and Administration Committee (SCCAC) with more than 16 per cent of total shares, followed by China Great

---

2. Group homepage and internet resources, anonymised.

Wall Asset Management Corporation with 4.05 per cent and Shanghai International Group Asset Management Corporation with 2 per cent.

Figure 1 Sales and operating results of group B 2010–2015



Source: Group annual financial report.

The State Capital Control and Administration Committee (SCCAC) is the SASAC in the municipality. China Great Wall Asset Management Corporation is a 100%-owned subsidiary of the Ministry of Finance of the People's Republic of China. Shanghai International Group Asset Management Corporation is financed by the Ministry of Shanghai and monitored by SASAC. These three state organisations together hold more than 25 per cent of the shares in Group B. No other shareholder holds more than 1 per cent.

According to JRJ Stock, a Chinese online stock news service, in February 2016 B applied for a one-month trading pause on B stock. The reason was that B had received notice from their controlling shareholder SCCAC that its equity will be significantly reorganised. To avoid price fluctuations, trading of the stocks should be paused for less than one month. The application was approved by Shanghai Stock Exchange. By the end of May 2016, however, trading had still not been resumed.

In April 2016, B published a resolution by its current board of directors which resulted in a continuation of the halt on trading. Moreover, millions of shares held by SCCAC were to be sold to an investor. The search for a potential investor was announced publicly in mid-April. This reorganisation of ownership and equity is another step towards reforming stated-owned capital in the company. The capital gained from selling the shares is planned to be reinvested in additional major overseas acquisitions.

The Shanghai Government hailed the internationalisation of Group B as a transformation 'from crow to phoenix through overseas acquisitions' on its homepage.

By 3 March 2016 Group B had 4,626 employees, 49 per cent of them overseas. Such a high degree of internationalisation is rare for Chinese state-owned enterprises.

In 2005, more than 90 per cent of A, a world renowned German brand, was acquired by B's 100% European subsidiary (BE) which was founded for this transaction. The purchasing price was almost 36 million euros, mainly debt financed.

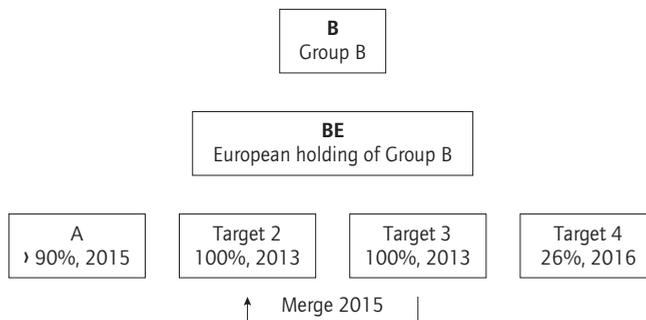
Having gained experience from the takeover of A, the acquisition of Group B in Germany was carried out at a rapid pace.

In March 2013 BE acquired Target 2, the largest rival of A for more than 150 years. Target 2, a worldwide leader in this industry, specialises in automation. The transaction saved Target 2 from its third insolvency, the previous one having occurred in 2009.

In July 2013, BE took over another automation specialist Target 3, established in 1964, which is an innovative leader in this industry worldwide with its 3D robot technology. The acquisition of Target 3 allows Group B to enter other industries, in particular aerospace which is expected to develop into a huge potential market in China. The Chinese manager, chair of the supervisory board enthused about the innovative advances of Target 3: 'It is totally beyond the imagination in terms of conventional technology. This is the future.'

In 2016, B acquired a holding in another strategic company (target 4) in this industry with a minority share of 26%. A share increase is expected. Figure 2 provides an overview of BE's current investments.

Figure 2 Group B's acquisition activities in Germany



With these acquisitions group B has upgraded itself to become a world-leading high-end company in the fashion, automotive and aerospace industries and has completed its product portfolio. Its automation products are used for most European luxury brands and for 90 per cent of high-end cars worldwide. Since B entered aviation and space travel, almost all Chinese airplane manufacturers buy sewing machines from B, a market with the largest potential next to the automotive sector.

The high-end technology and automation solutions have led B to achieve 'Industry 4.0', the foundation of 'Made in China 2025', which the CEO of B calls 'AMS': automation, modulation and smart solutions.

B's goals are: to double its sales from 5 billion to 10 billion yuan;<sup>3</sup> to become number one in its industry worldwide; to accede to Industry 4.0 by developing the only robots in this sector; and to realise the 'Made in China 2025' strategy.

The strategy for achieving this plan is to continue growing through overseas acquisitions. Germany with its manufacturing processes and automated control systems meets expectations for a place of investment. There are many attractive targets in Germany for B.

The next major deals are expected in the near future. At the latest board of directors meeting, an increase in B's debt was announced. Additionally, the sale of shares by the controlling shareholder is planned to fund overseas acquisitions.

## 2.2 Profile of the acquired company A

Group A has a very different origin and background from its Chinese parent, although it has similar experiences in terms of mergers.

The history of A, a traditional German *Mittelstand* (SME) company, goes back to 1860. In 2005 A and its subsidiaries were sold to B.

During the world financial crisis in 2009, A suffered from a deep crisis and was facing insolvency. With financial support from Group B and selling its cash cow in the group, A has overcome the crisis successfully. Today, as a public company listed in Germany, A specialises in high-end technology, operating with seven direct subsidiaries worldwide and two joint ventures in services, distribution network and manufacturing. More than 90 per cent of its shares are in the hands of Group B; the rest are free-floating.

After acquisition, the company kept its legal form, name, brand and most locations in Germany.

## 3. Acquisition background, motives and process

### 3.1 Acquisition background and motives

In 2005, A was the first listed company acquired by a Chinese investor, one of the first mergers and acquisitions deals with Chinese strategic investors in Germany.

---

3. According to China Light Industry, 24 September 2015.

In 2002, the German managing director (2002–2006 and 2009–2011) started the restructuring of group A. The former owner had been taken over by an automotive group in 2001. As a private company, the automotive group did not want a listed public company in their portfolio due to the very strict publication regulations. Also, the business of group A, not the key business of the new parent, was making a loss. The new owner decided to sell A and its management had a chance to look for a new owner themselves. For the management team at that time, it was clear from the very beginning that the acquirer should be a Chinese company with existing structure and understanding of this industry because in their sector 80 per cent of the machines worldwide were sold in China at that time. With a Chinese partner, A would not only receive the cash needed to continue restructuring, but more importantly gain access to the Chinese and Asian markets. In addition, the Chinese partner could access high-end German technology and the European market. There were many possible candidates, but group B was ideal and met the expectations of both the management of A and its owner.

There were various motives for the acquisition of group B. The decision was not triggered solely by the government's call for internationalisation '*Zou chu qu*' (Going out), but mainly by economic pressures. For a typical state-owned company, overseas acquisition is the quickest and most efficient way of going global, reforming and restructuring the company to become future-oriented.

Second, B was driven by market pressure from national and international competition. National pressure came primarily from growing private companies in the provinces. The technology and products are easy to copy. Labour costs in the provinces are much lower than in Shanghai. The structure of these private enterprises is more efficient and flexible. International pressure came first of all from Japan. In 2005, the year of acquisition, B achieved annual sales of 141 million euros, but losses of 26 million euros. B was facing the most difficult time in its history: it had to sell plants and land in order to survive. With the acquisition of A, B expected to upgrade itself from a low-end sewing machine supplier to a high-end leading technology provider and thus to differentiate itself from its competitors and win back its leading position in the Chinese market.

Third, accessing A's worldwide distribution and service channel was another motive for this acquisition. Essential for this deal is Germany as an R&D centre and production location for high-end products.

Last but not least, to have an internationally-known German brand and its products with the favoured seal '*Made in Germany*' increases its competitiveness, according to group B's CEO, in an interview with a German institute.

### 3.2 Acquisition process and challenges

As the purchase price had to be financed by issuing new stocks and additional loans for A were requested, the negotiations took almost three years. The representative of group B, also the chairman of A's supervisory board, was appointed CEO of B just before the

signing of the contract. The negotiations were conducted by his precursor and the CEO of A, who remained CEO. According to A's German CEO, his precursor's approach to Chinese strategy was not continued by the new Chinese manager.

After the signing of the share purchase agreement, it took seven months to close the deal. It was a major challenge to fulfil one closing condition, a credit line of 9 million euros for working capital. Due to the loss-making situation of both companies, almost no banks – including affiliates of Chinese banks – were willing to provide this credit line. In the end, a Chinese bank issued a guarantee and the transaction could be closed.

Major challenges also existed on the Chinese side: At that time, overseas acquisitions were so new that the Chinese government had to decide how to process the approval. In particular, it was a case of 'a snake eating an elephant': in 2005, the target was, in terms of sales volume and international presence, bigger than the buyer group B. A was a world leader in this industry, B was unknown. Above all, B had no experience in overseas acquisitions. B's CEO was appointed in the late phase of the negotiations in 2004 and was not entirely confident about the acquisition decision. But he decided it was worth the risk. Five board of directors' meetings were called to make the final decision.

In this deal, group B engaged one of the so-called 'big four' accounting firms as their transaction advisor and a German law firm in Hamburg as their lawyer.

## **4. Integration strategy and results**

### **4.1 Integration strategies**

No integration into the Chinese mother group was planned: A enjoys a major degree of freedom. The German brand remains independent, in any case. The company is led mainly by a German management team.

The control exercised by group B takes the form of deeper involvement on the part of group B's CEO as chairman of the supervisory board and the appointment of Chinese managers in charge of finance/controlling, HR, legal and IT. Structures for reporting to Shanghai head office were set up.

Different locations of group A, also acquired by B in 2005, have taken over different tasks according to their different specialisations: Romania concentrates on the labour-intensive production of parts delivered to Europe and China; Czechia on parts and complete machines. In future, Czechia will produce more high-tech products, especially the new developments, which are high-class and well-priced. The German location continues the assembly of premium machines and is being developed into an R&D centre for the whole group B, not only for group A. Also, sales and services remain in Germany as A's main markets are Europe and the United States. These tasks can be carried out only by highly-qualified employees speaking more than one language.

For the most employees located in Germany there have been few apparent changes. Visible, however, is the Chinese flag hanging in front of the company – and A has an additional Chinese name.

This takeover can be seen as a successful and satisfying transaction by Chinese investors from financial point of view. Both acquiring and acquired company have benefited.

## 4.2 Integration results

### Target A

Table 1 documents the positive development of group A since acquisition: both sales and operating results increased until the financial crisis. After recovery from the crisis, the company's operating results increased to 20 per cent of total sales in 2015, compared with 1 per cent in 2005, the year of acquisition. Also the stock price in 2015 is almost six times the price in 2005.

Table 1 Sales, operating results and stock price development of group A, 2002–2015

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Group sales, million euros	155	146	133	129	146	151	135	82	76	90	97	103	119	142
Operating results, million euros	-1	-5	-2	1	6	7	1	-22	3	6	12	14	24	29
In %	-1%	-3%	-2%	1%	4%	5%	1%	-27%	4%	7%	12%	14%	21%	20%
Stock price high	5.1	4.0	3.7	3.9	4.8	8.1	6.0	5.6	6.9	7.4	6.1	10.0	14.6	25.0
Stock price low	3.1	2.2	2.4	2.3	2.9	4.4	2.0	3.3	3.4	4.6	3.8	5.9	8.1	13.6

Source: Company Business Report 2002–2015.

The positive results come, on one hand, from successful restructuring processes in 2002–2006 and the global economic recovery 2009–2010, and on the other hand from the confidence of the management team and employees in the cooperation with group B. From 1990, A's former owner replaced 18 leading managers. The continuity of the company is guaranteed by the current owner, however. This motivates the staff. In particular, the acquisition of A's competitors Target 2 and other two targets is a strong sign of long-term investment in Germany by group B. It provides management and employees of A with new prospects.

B was involved in both rounds of restructuring: in the first round as negotiating partner as negotiations started in 2002 and in the second round, B waived its shareholder loan to A, which was crucial for the success of the restructuring.

A's stock price increased from 3.91 euros in 2005 to 25 euros in 2015. In 2014, for the first time for eleven years, group A distributed dividends of 15 cents per share: a small amount, but a significant sign. In 2015, the dividend increased to 50 cents per share.

Looking into the figures more deeply, there have been some interesting developments during the past 10 years. In 2005 group B acquired over 90 per cent of A's shares. In 2010, during the world financial crisis, group A sold off its cash cow, a profitable subsidiary to an Austrian group to finance the restructuring of A, while, as already mentioned, group B waived its shareholder loan of 12 million euros; group B sold almost 30 per cent of its shares in A to a Chinese competitor C to enable group A to enter the Chinese market more easily. In 2014 group B bought back all the shares from C.

### Acquirer B

Group B, too, has benefited substantially from this deal. With the acquisitions of Target 2 and Target 3 in 2013, group B became number one in China again and in the top three worldwide.

Group B's restructuring of its domestic business took place in 2005–2013. It can be assumed that group B was inspired by the tough reorganisation of group A during 2002–2005 and 2009–2010.

Table 2 presents the development of the sales, operating results and stock price of group B from 2010 to 2015, including group A.

Table 2 Development of sales, operating results and stock price of group B, 2011–2015, including group A

Group B annual report incl. group A	2010	2011	2012	2013	2014	2015
Sales group in m€	204.0	192.0	183.1	220.6	239.7	281.4
Operating result in m€	n.a.	4.0	11.1	17.6	23.7	25.5
in %	-	2%	6%	8%	10%	9%
Stock price in CNY+A7 (1st working day 15:00)	12.2	15.5	6.8	6.8	10.2	13.1
Exchange rate Ø 2010–2015						8.2

Source: Group B's Business Reports; Group A's Business Reports.

The sales and operating results of group B show a similar trend to those of group A (Table 1).

As reflected in its stock price, the business development of group B seems still to be facing operating challenges. Only with the acquisition of Target 2 and Target 3 in 2013 and Target 4 in 2015 was it able to win the confidence of investors on the stock exchange. A Chinese financial analyst rated group B's stocks as a buy for the first time in 2015, indicating the risk of a further government reform, which could impact group B at the same time.

In Table 3, the sales and operating results of group B are presented excluding group A. Without group A, the results of group B would be negative. It is to be assumed that group B would not have come out of its business crisis without its overseas investments. It also helps us to understand the motives for the acquisitions from 2013 on.

Table 3 Sales, operating results and stock price development of group B excluding group A

Group B annual report excl. group A <sup>1) 2)</sup>	2010	2011	2012	2013	2014	2015
Sales group in m€	127.6	102.5	86.4	118.0	120.8	139.5
Operating result in m€	-	-1.9	-0.9	3.4	-0.7	-3.2
in %	n.a.	-2%	-1%	3%	-1%	-2%

1) The intercompany transaction is not considered as it is not significant

2) Including Target 2 and Target 3 with assumption that the effect is not significant

Source: Group B's Business Reports; Group A's Business Reports.

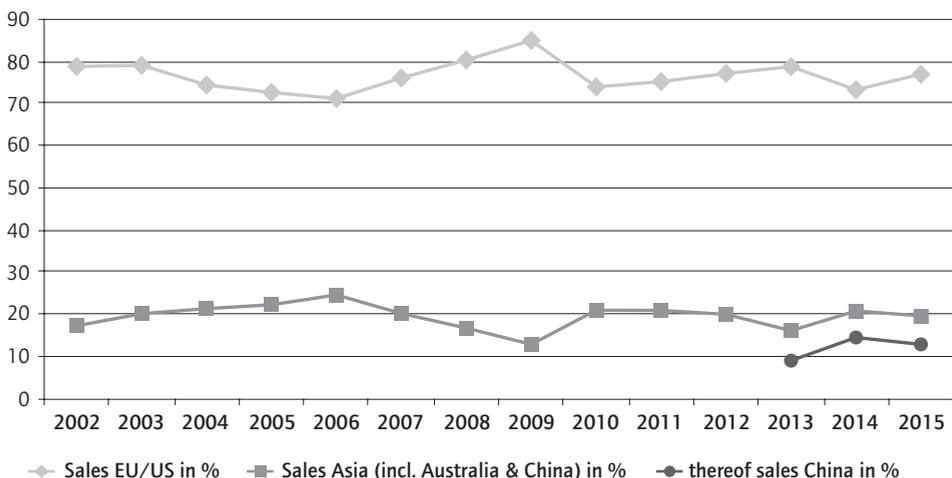
### Synergies from acquisition

No significant synergies from sharing purchasing or customer resources and no operating synergies in this acquisition can be observed.

From the purchasing point of view, it is very difficult to find suitable high quality Chinese suppliers for group A's products other than for large quantities for the Chinese market. If there were adequate suppliers, the purchase price might be higher than in Europe. Manufacturing in Romania and Czechia provides more price-competitive products with regard to price, logistics and quality, as one group A insider commented.

From a sales point of view, there have been no changes since acquisition.

Figure 3 Regional sales distribution of group A, 2002–2015



Source: Group B's Business Reports; group A's Business Reports.

Synergies from knowledge transfer are limited, based on the available data. With the involvement of group B's CEO in the supervisory board and a Chinese expat as managing director at group A, it can be assumed that managerial transfer has occurred. The restructuring of group B in mainland China from 2005 to 2013 can be interpreted as one result of the managerial knowledge transfer, inspired by group A's turnaround measures.

No further knowledge transfers and synergies can be determined from the research conducted.

The difficulties with regard to synergies can be seen as resulting from the difficulties experienced in the merger of two 'cultures', not only Chinese and German in general, but the different cultures and capabilities of the two organisations.

For entry into the Chinese market, knowledge of how to build up sales and a service channel is needed. Even in the aerospace industry, services and sales channels are indispensable. Moreover, past experience shows that the capabilities needed to set up these sales and service networks for high-end products does not exist in China. This is the major challenge faced by group B and its subsidiaries in Germany.

## **5. Communications in post-merger integration**

Communications are extremely important at the beginning of post-merger integration. A well-considered and appropriate organisational and decision-making structure is crucial for setting up harmonious and constructive communications.

### **5.1 Organisational and decision-making structure**

A was the first cross-border acquisition by group B. Experience of international cooperation were very limited within group B's management team and trust in Chinese investors was not generally high in Germany at that time. Therefore, group B handled the cooperation with the German organisation and management team very carefully. For the CEO of group B, one of the key factors in the successful takeover of A was to have a German management team leading a German company. They sent only two Chinese managers to Germany. Their task was not to control German management but to improve communications between the parent company and the local management team.

Accordingly, a two-in-the-box system was formed. Strategic decisions are made between the CEO of B as president of the supervisory board (*Aufsichtsrat*) and the German CEO, the spokesman of the board of executives (*Vorstandssprecher*) and his Chinese colleague. There are six members of the supervisory board: three from B, two from A's works council and one external member from a tax consultancy firm. The supervisory board meets four times a year and decides on major topics, such as business plans, high level management, major investments or mergers and acquisitions.

Operational decisions are made by the German CEO and his Chinese colleague, while the German CEO is in charge of operations, sales and R & D and the Chinese CEO is responsible for commercial functions: finance, controlling, HR, legal affairs and IT. There is a monthly meeting between the CEOs with the involvement of the company lawyer and sometimes also the chief financial officer. The minutes are copied to the chairman of the supervisory board, the CEO of B.

In this way, the operational and strategic involvement of the mother company is guaranteed. Moreover, managerial knowledge could be transferred from A to B.

A kept the same decision-making structures after the takeover. Cooperation between the supervisory board and the board of executives has been intensified so that the CEO of B is more involved in strategic decision-making. It was clear from the beginning that the CEO of B would be the chairman of the supervisory board (*Aufsichtsratsvorsitzender*).

The responsibility of the supervisory board and the board of executives are defined by the law and the company statutes.

Decisions made by the board of executives alone are defined in the statutes and all other decisions need the approval of the supervisory board or its chairman. The decisions of the board of executives have to be approved by the supervisory board as they are laid down in the business plan which is to be approved each year.

As the majority of supervisory board members are from group B, final decision-making power is in the hands of B. On the other hand, all decision proposals come from the CEOs: local management in Germany has maintained its operational decision-making autonomy. The German CEO is usually able to reach agreement with the Chinese owner.

Proposals for strategic decisions are mainly prepared by the board of executives. Operational decisions – for example, investment, hiring within the business plan, changing suppliers – are made solely by the CEOs.

Until March 2016, B had three votes in the supervisory board, the chairman of the works council and his proxy as employee representatives two and an independent board member one. The independent member is a Chinese-German tax advisor, a senior female partner of a German tax and consulting firm.

From April 2016 on, the German CEO was proposed as a member in the supervisory board of A, while one member from B left. He gave up his position as CEO at group A to focus on his tasks in B's European holding BE to coordinate the acquired German targets and to expand BE through further acquisitions.

How BE is to be involved in A's decision-making structure is not clear based on the available data. According to an insider, most of A's managers have been appointed managers in BE as well to give them a bigger picture than A and thereby to obtain more synergies with the other acquired German targets.

## 5.2 Integration of employee relations

Today, group B (not including its German subsidiaries) has more than 2,000 employees in China. In 2013, B completed its restructuring and achieved an internal turnaround: 6,500 employees were laid off, more than 60 subsidiaries and branches shut down and manufacturing was relocated to low cost areas.

B has a group trade union organisation. The current president of the group trade union held several positions within the Communist Party of China in B's subsidiaries. The last position was vice president and secretary of the CPC committee in B's office equipment subsidiary. In December 2012, she became president of the trade union and also member of the CPC committee, director of the CPC office and employees' representative on the board of directors of group B. She is also a member of the general trade union of the commune. B's subsidiaries also have their own sub trade unions.

No information on the handling of labour relations and labour disputes are publicly available. No accessible information on collective bargaining exists either.

There have also been relocations of production from Germany to Romania and Czechia in recent years. This was an economic decision, also made by other German and Western European companies.

The fear of A's employees in Germany that the Chinese investor would transfer all knowledge and relocate production to China and lay off workers in Germany was not realised. In his first speech to German employees at a Town Hall meeting, B's CEO emphasised that the Chinese owner would keep the German location as a technology centre and keep investing in it. He repeated this statement at A's annual shareholder meetings during the following years. In 2009, when A was facing insolvency and urgently needed financial liquidity for restructuring, group B waived a part of its shareholder loan of 12 million euros to A. This, combined with other measures by the German CEO, saved A and its jobs. Since then, the works council members and employees have changed their opinion and have been won over by the Chinese owner. The acquisition of the other three German targets strengthened the confidence of group A's employees in group B's intention to keep German factories as important strategic locations. It is clear that the German location has become the R&D centre for both group A and group B.

No integration of labour relations and also no changes in the existing labour relations are intended by group B. A remains, as before, a member of trade union IG Metall and is integrated in IG Metall's collective agreement. B has agreed to all IG Metall's tariff increases. The company's bargaining agreements have not been changed.

Two employee representatives are members of the supervisory board, the president of the works council and his proxy, according to the legal regulations for listed companies in Germany.

Business trips were organised for works council representatives to visit the Chinese headquarters. Meetings with a trade union leader, also head of human resources, took place. No further contact between employee representative organisations took place.

The language barrier, the geographical distance, the cultural differences and the distinct systems and understandings of labour relations make it almost impossible for the two organisations to have much contact.

### 5.3 Communications between shareholder and works council

Although the distinction between the works council, employee representatives and the trade union seems unclear to the Chinese managers, both the Chinese CEO of A, responsible for HR and communications with the works council, and the chairman of the works council, describe their cooperation as friendly and constructive.

For the works council members, one of the biggest barriers in working with their Chinese managers and shareholders is language. They have a Chinese colleague who translates between German and Chinese at the supervisory board meetings and for communications between the works council and the Chinese managing director, who does not speak German. A translator is always present at the meetings and memos are in the two languages, but spontaneous discussion, as in the past with the former owner, is no longer possible. Discussions and contacts of a more informal character than official meetings are difficult.

During the restructurings and relocations, it was very difficult for the chairman of the works council, who has been working at the company for more than 36 years, to accept the lay-off plan. After the important financial support of B in 2009 to save A from insolvency, however, he is convinced that the Chinese owner is serious about the German location and has thus supported decisions taken by management and shareholders. He could see that there is no other option: either A survives through reorganisation or it will disappear.

The Chinese managers have had to learn to deal with a strong trade union organisation. The unions in Germany are more powerful than in China, commented the CEO of group B. The Chinese CEO of A has learned that she has to convince colleagues by reasonable arguments. Reasonable means to show the trade union representatives that the decisions taken not only benefit the shareholder but also the company and the employees as well.

In 2006, the second year after the takeover, there was a change in the IG Metall tariff system. It was the first big challenge the Chinese manager faced in dealing with works councils. Communications to help the works council to understand the intention behind management proposals were crucial.

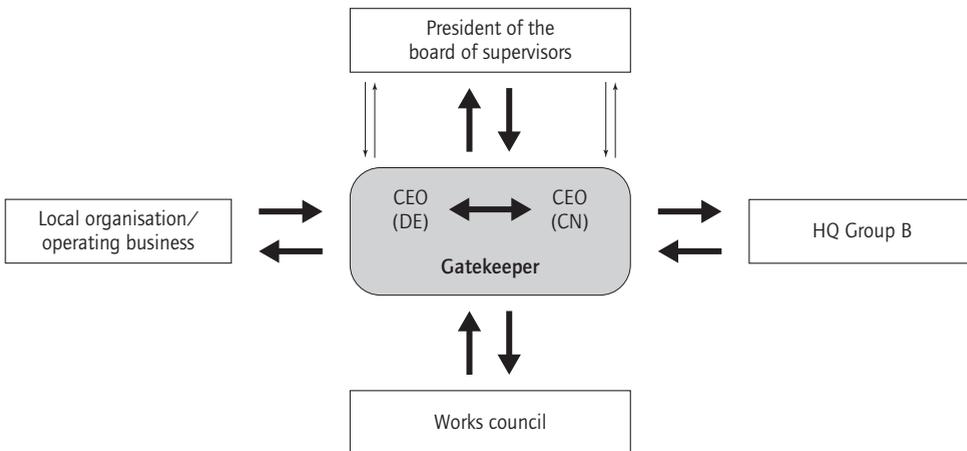
Another example: in the crisis, the works council and the Chinese shareholder were able to find a common solution: during the financial crisis of 2007–2009, IG Metall

demanded a 2.7 per cent wage increase for all its members, including A. At that time, B was working with the management team on cost reductions and restructuring in order to prevent insolvency. Therefore, this wage increase could not be agreed by B. After several discussions, they reached agreement on postponing the wage increase until A was back on a profit path. In 2010, A made a profit and paid the increase and interest on it.

#### 5.4 Communications between owner and local management

The engagement of a gatekeeper at the beginning of post-merger integration to enable smooth and constructive communications played a key role in its successful execution.

Figure 4 Gatekeeper at the beginning of post-merger integration



Source: own elaboration.

A key person in the initial communications after the deal was concluded is the Chinese CEO sent by B to A. Her most important function is to bridge the huge geographical and cultural gap between China and Germany, said her German counterpart (in 2005–2006 and 2009–2011). She has a good relationship with the CEO of group B who is both representative of group B and the president of A's supervisory board. He trusts her. That has made things much easier, especially at the beginning of the cooperation. If there was any misunderstanding or conflict – for example, increasing budgets or hiring – she cleared it up. She has been very helpful in setting up functional communications and collaboration. The Chinese CEO had experience in state owned and foreign invested companies in China for almost 20 years before she was sent to Germany by the CEO of group B with whom she had worked in another company.

From 2005 to 2016, B changed the CEO of A five times. The reason for the change in 2006 was the differing opinions between the German CEO and the management of B regarding China strategy. The German CEO did not agree with mass production by A in China. His intention was to utilise A's leading technological position to differentiate

it from its and B's Chinese low end competitors in China. The CEO of B insisted on expanding and quickly capturing the Chinese market by low end products with Chinese common quality.

According to B's understanding, the German manager insisted on focusing on European and American markets. That was not acceptable for the chairman of the supervisory board, the representative of group B.

The second CEO was a former CFO of A. There were no different directions in the China strategy, but they had differences on how to restructure during the financial crisis in 2007 and 2008.

When the economic crisis happened in 2006–2008, the total industrial market was reduced by 50 per cent. Group A faced the most difficult time in its history. CEO of B, chairman of supervisory board, asked the first German CEO to come back and replace the second CEO. After restructuring, operating results increased from –27 per cent of sales in 2009 to 4 per cent in 2010.

After successful restructuring, the difference regarding the China strategy became the point of conflict between the German CEO and the shareholder again. At the end of 2011, the German CEO left the company once more.

A Chinese insider sees this conflict as resulting from two strong personalities. In China, CEO is translated as '*zhi xing dong shi*', word for word 'implementing senior manager'. In China, the owner is the decision-maker and takes the liabilities. For a German listed company, the CEO is responsible and more or less independent of the shareholders (§76 AktG). He is also legally responsible for the company and has to bear the consequences of his or her actions.

A sales responsible was appointed CEO in 2011 until he was appointed a member of the supervisory board in 2016. The fifth CEO was assigned to replace him.

As analysed in Section 4.2, entry into the Chinese market has failed to date. The main increase of sales in recent years, especially in 2015, came from Europe and the United States. The new German CEO of A has long experiences with China and comes from manufacturing and R&D. It is expected that he will bring new impetus to the China strategy.

For the CEO of B, managing the German managers has been a major challenge since closing the deal: The big challenge for the Chinese owner is to have a senior manager who can understand their intentions and be able to implement them.

Both the German and the Chinese managers see the cultural difference as a barrier, but one not to be overemphasised. The Chinese CEO and her boss are well aware they are operating in a foreign environment. They respect the rules of the country and the company and fit into them. Also the German CEO's past experiences allow him to understand and work with different cultures. The problems are not insuperable.

Another challenge is language, as the Chinese manager does not speak German and the German managers do not speak Chinese. They communicate in English. The fact that the two parties cannot use their mother tongue does not make communications easier. Having learned from her own experiences, the Chinese manager communicates very directly. If the two sides fail to express their opinions or decisions straightforwardly, there is no way to achieve understanding in a foreign language.

## **6. Conclusion**

In the case presented here, the acquirer B was aware of its lack of experience with regard to cross-border mergers and acquisitions and the significant differences between the two cultures. Consequently, they consciously decided to limit their control over the acquired company. On the other hand, this meant that the knowledge transfer that was one of B's acquisition goals was limited.

Although the target management team is not completely intact, with the Chinese CEO sharing decision-making power with her German counterpart, the local management can still make decisions in cooperation with the Chinese partner with considerable freedom. The fact that the Chinese CEO sees herself as part of the local team is a crucial factor in preserving the identity of the acquired company, which makes this transaction successful.

German managers are also involved in strategic decisions. This is due to the Chinese owner's need to learn. It enables the transfer of managerial knowledge to the Chinese managers, who can subsequently disseminate it within the parent organisation.

The acquiring company not only provides strategic advice to the target company, but is also deeply involved in decision-making. Using its position in the supervisory board and the power to hire or fire the CEO, the Chinese owner has the final say in strategic decision-making. However, the Chinese acquirer is highly dependent on the competence and support of the German management to implement decisions made. This dependence forces the Chinese owner to hold back somewhat in terms of control and interaction.

The major question is how to realise the planned synergies at operational level. They have not been observed during the ten years since the deal was concluded.

The cultural differences between Germany and China have been a hurdle, but should not be overemphasised. The crucial factor is whether the persons involved possess the adaptiveness or the cultural intelligence to deal with this difference. This adaptiveness or cultural intelligence is very individual and depends strongly on attitude but also experiences with diverse cultures, as is the case for both gatekeepers.

It is similar with language. It is a hurdle, but once it is accepted and an openness to change is there, a solution can be found.

Not to be ignored is the Chinese CEO who acts as a bridge between the two worlds to minimise the cultural and geographic distance and to improve communications between the two units.

Conflict between the Chinese owner and the German managers can be assumed to arise from the organisational and cultural differences identified by Sarala's research (Sarala 2010). However, understanding the conflict requires deeper investigation.

With two seats on the supervisory board based on German law on listed companies, employee representatives are involved in the decision-making process. The existing employee agreements and regulations have been accepted and respected by the acquiring company; to date, employee relations remain intact.

The commitment of the Chinese parent to maintain Germany as a strategic location has been conserved for the past 10 years. Job cuts in recent years has resulted from economic necessity rather than ownership by a Chinese investor.

Language is a barrier in communications between the works council and the Chinese managers.

The main challenges identified in this case study are (i) bridging the different interests and aligning business strategies, including bridging the different understandings and approaches to accessing the Chinese market, which is one of the key aims of the takeover; (ii) finding a suitable match between the German and the Chinese managers, characterised by difficulties in recruiting and retaining the right candidates; and (iii) setting up a bridge by means of the right candidate.

The number of Chinese mergers and acquisitions in Germany has increased rapidly in the past two years. The impact of such acquisitions on Germany is growing. However, the integration performance, cultural considerations and communications characterising such transactions remain relatively unstudied. This case, investigating the ten-year development after the acquisition of A by B, gives us deep insight into the integration approach and results, opportunities and challenges in a cross-border acquisition by a Chinese investor in Germany. The main standout features of this case are the type of acquirer (a state-owned enterprise), the nature of the target (a German *Mittelstand* company with global leading technology), the particular sector and the acquisition motives of the two parties.

## References

- EY (2016) Chinesische Unternehmenskäufe in Europa. Eine Analyse von M & A-Deals 2005-2015. [http://www.ey.com/Publication/vwLUAssets/EY-MA-China-Deutschland-2016/\\$FILE/EY-MA-China-Deutschland-2016.pdf](http://www.ey.com/Publication/vwLUAssets/EY-MA-China-Deutschland-2016/$FILE/EY-MA-China-Deutschland-2016.pdf)
- Gätzner S. (2016) Chinas Outbound-M & A auf Rekordkurs, 25 March 2016. <http://www.ma-dialogue.de/maerkte/chinas-outbound-ma-auf-rekordkurs/>
- KPMG (2016) China Outlook 2016. <https://home.kpmg.com/cn/en/home/insights/2016/03/china-outlook-2016.html>

All links were checked on 21.04.2017.