

## TRANSCRIPT

# How NOT to expand into China

### Michael Madsen:

Hi, I'm Michael Madsen, International Liaison Partner for BDO Canada. Welcome to Bored at the Airport with Mike. This show is about doing business globally. Whether your business has an international presence, is considering an international expansion, or if you're in the middle of revising your expansion plan, then this show is for you.

### Michael Madsen:

China is one of the hardest markets for U.S. and European companies to expand into. This is because the cultural differences are huge, and if you don't understand them, the results will be disastrous. Here's what happened when Mattel, Norwegian Cruise Line, and Home Depot attempted to expand into China without fully understanding the culture.

### Narrator:

Mattel opened a \$30 million Barbie theme store in Shanghai, in 2009.

### Clip:

China's giving in to pent up demand for a plastic icon. Barbie's making a flashy debut here with her first ever store. The House of Barbie in downtown Shanghai.

"I always wanted a Barbie," says this customer. "We didn't sleep last night."

The six-floor dream house features every Barbie ever made, including her new Shanghai friend, Lin, complete with multiple shopping bags. But the store's designers aimed to move beyond box sets, giving customers a full experience. Modeling copies of Barbie's clothes, visiting the Barbie spa, and even designing their own mini outfits.

### Narrator:

In America, Barbie established itself as an iconic symbol of femininity for young women. Over a period of 50 years, the brand has taken on a life of its own as Barbie assumed many roles of women. In China, Barbie is simply a doll. She's not associated with any cultural significance for Chinese girls or young women.

Many brands have found success in China. China makes up a big part of the customer base of luxury brands like Dior, Gucci, and Louis Vuitton. Beyond Meat, the largest alternative plant-based meat maker in the world launched in China in April 2021. How did such an iconic brand, like Barbie, fail in China? Partly, it was a failure of planning. The store was too big, too expensive, and too confusing in its mixture of adult pleasures: Barbie martinis, bust-firming treatments, and children's toys.

More fundamentally, Mattel misread the market. Instead of focusing on children's dolls, Mattel assumed that Chinese consumers would want a whole range of pricey, Barbie themed clothing, foods, and goods. Since Barbie is not a cultural icon in China, as she is in America, Chinese consumers couldn't care less about Barbie-branded products. By the time Mattel realized its mistake, the store was bleeding money. In 2011, the house of Barbie closed.

Norwegian Cruise Line is one of the world's three largest cruise brands, including Carnival and Royal Caribbean Cruises. In 2018, they launched its massive luxury liner, Joy, from its base in Shanghai with a performance by Mandopop crooner, Wang Leehom.

It all seems so simple. Build it, and they will come. The major cruise lines all did the math, that with many of the 1.4 billion population of China becoming more affluent and freer to travel, there would be an ever-growing demand for millions of potential customers from Asia for cruising. However, in a little over a year, the winds had shifted, and Norwegian announced it was relocating its luxury liner from China in favor of Alaska.

Norwegian Cruise Line made tremendous efforts to design and decorate their ship with culturally appropriate art, features, and entertainment. However, the Chinese consumer wanted a Western cruising experience. Something Royal Caribbean did and continues to do successfully in China today. And so ironically, Norwegian's efforts to localize their product actually backfired for them.

Home Depot's expansion into China was a cultural mismatch. In the 1990s, the Chinese government loosened regulations on its housing market, allowing its 1.2 billion citizens to own private homes for the first time since the communist revolution of 1949. Home improvement and furniture companies such as Sweden's Ikea, and the UK's B&Q, rushed in to meet the need.

In 2006, Home Depot bought the Chinese home improvement company Home Way and its 12 stores. With its booming economy and strong real estate market, China seemed like it would be an easy win for Home Depot. But by 2012, Home Depot closed the last seven of its 12 original stores. Home Depot failed to acknowledge that the do-it-yourself repairs are not a strong cultural match for China. Labor costs are relatively low, so rather than do the work themselves, many homeowners prefer to hire somebody else to do it. On the other side of the equation, the American brand failed to win over contractors doing the repairs and renovations.

Home Depot's product offerings were also left unchanged from America, making them a poor match for local tastes. In China, women are usually in charge of home decoration and styling over their male counterparts and undertake most of the furniture and home good shopping, controlling this aspect of the market. China's cultural traits overrode the globalization of the male-dominated consumerism of home repair products.

As a point of comparison, Ikea has had a presence in China since 1998 and continues to open new stores to this day. Ikea had what women wanted: modern European upscale furniture that could be easily assembled at home.

Technology and globalization have made global expansion far more accessible for businesses around the world over the past decade. However, just because a business has the resources to go global, whether or not they can stay global is a question that all brands should be asking themselves.

**Michael Madsen:**

Joining me in this episode is Jeanny Gu. Jeanny is a partner, and BDO Canada's country coordinator for China and Hong Kong. She helps businesses navigate the compliance and cultural issues they face when engaging in global business involving Canada and China. Jeanny, welcome to the program.

**Jeanny Gu:**

Thank you, Michael.

**Michael Madsen:**

China, such an enticing market for many businesses given the sheer size of its population and its economy, yet often one that's not well understood. If we look at the Home Depot story as an example, what would you advise Home Depot if they were to reenter the China market?

**Jeanny Gu:**

You know, Michael, I think for Home Depot, the key thing was recognizing that the consumer preferences are quite different in China compared to the West is really key in this circumstance. The concept of DIY projects, it's developed over time as a hobby in Canada and the US, but it's not recognized as such in China.

I live in Toronto and if I walk my dog around the neighborhood over the weekends, I see people working on their cars, doing gardening, building something in their garage. But in China, to the contrast, most people live in apartment buildings. There is no garage. The typical working adult in China endures a very long day at work compared to what we have in Canada and the US coupled with demanding child caring priorities.

There's actually very little leisure time for them to focus on DIY projects. And the population in general are not handy to begin with. So, it's something that they're not used to being brought up with culturally. And that's one area that I would say Home Depot missed when they were considering whether a DIY approach would work in China.

**Michael Madsen:**

How do you know if China is a good fit for your expansion plans, and what are the things that you might need to consider?

**Jeanny Gu:**

Businesses in the consumer goods and services sector is obviously a very important industry to consider China from an expansion perspective. But I would say it's not limited to just that. I mean, if your business is something that is looking at any sort of global expansion, it's very hard to ignore China. Businesses need to consider the pros and cons of how to enter the market as the legal and regulatory environment there is vastly different from what we see in the West. China is on a civil law system versus a common law system, which we see in Canada, which means getting properly advised is very critical to the success of the company. The regulatory environment is also very different with restrictions on ownership in certain industries, which adds to the complexities of deciding how you would do business.

**Michael Madsen:**

A lot of complexities, obviously, in working in China. The benefits of social media and the internet have significantly increased everyone's understanding of global and cultural norms and have brought these into our living rooms, as it were. Are there certain cultural etiquettes you should be aware of when looking to do business in China?

**Jeanny Gu:**

It's funny you ask, Michael. There're tons of materials on etiquette on the internet, and it goes through how you should conduct yourself during business meetings, how meals should be conducted, best practices for things such as site visits and so on. Which I find to be sometimes a bit dated, just because it more closely mirrors observations around etiquette for the 1990s or the early 2000s.

But these days, we're seeing a new generation of business leaders, many of whom have received education overseas or have had a lot of experience working with foreign businesses already

over the past 20 years. Many Chinese businesses do continue to operate in a hierarchically sensitive manner, so being mindful of that when having meetings in groups and having dialogue is critical.

**Jeanny Gu:**

Focusing on a win-win business deal that benefits both sides and articulating that clearly, as a mutually agreed upon objective outcome, is the true backbone for a successful collaboration in China. One of the areas of caution is on the use of translators in business dialogue, as the risk of miscommunication is significant here. Many entities underestimate what gets lost in translation and the impact of something like that on the success of a business deal and the bucketing failures in dealings arising from these sorts of things as cultural mishaps. But really, it's just a bad choice in terms of who you bring to the table with respect to negotiations.

**Jeanny Gu:**

The importance of having a bilingual individual with strong business acumen is critical to the success of the win-win negotiations, as there's lots more to the role than purely translating what's said by the parties word for word. Appreciating and being strategic about addressing the language differences is critical to the success of the business dealing.

**Michael Madsen:**

Jeanny, are you able to share some stories as to how you helped your clients with their expansion into China?

**Jeanny Gu:**

Yes, definitely, Michael. As you're aware, our firm in China is a very reputable firm with lots of history and experience serving the local market in China. We've had them evolved as boots on the ground for clients looking to expand, helping them with outsourced accounting and tax services, and really navigating the regulatory environment in China. It's a potentially temporary or short-term solution to what may be a more expanded role on a goal four basis. When considering how to do a China expansion, including whether it should be through a wholly owned foreign subsidiary, a joint venture with a local partner, or a rep office.

It would involve experts from both the client's home country in China to collaboratively advise. So understanding the cost and benefits of operating under the different arrangements from both the perspectives of the home country advisor and the China advisor helps to ensure that the arrangement put in place is best suited, considering the future growth plans in China. And lastly, we've also assisted clients with M&A expansion needs in China. So in those circumstances, we bring together our firm's China Desk expertise in combination with our in depth M&A subject matter expertise, to provide the client with the best combination of language, cultural and business knowledge, along with the technical knowhow.

**Michael Madsen:**

Thank you for coming on the program today, Jeanny. I need to consider as to how China can play into global business expansion. Your comments were very insightful and useful for our listeners. Thank you.

**Jeanny Gu:**

Thank you, Michael.

**Michael Madsen:**

Jeanny Gu. Jeanny is a partner and BDO Canada's country coordinator for China. Thanks for being part of Bored at the Airport with Mike. I'm Mike Madsen. If you like this episode, subscribe to our podcast and connect with us on our LinkedIn group page Bored at the Airport.

**Narrator:**

On our next episode.

**Clip:**

My life depends on me working from home these days. It really is a matter of life and death.

**Narrator:**

We'll explore how the global pandemic has made workers reevaluate, what they're really getting out of their jobs and what they aren't. How to hire the right people when expanding internationally.

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**Clip:**

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