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## Knowledge for the 21st Century

Speech on 28 April 2006 by

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Dear Friends,

Ladies and Gentlemen,

Good morning!

I am very honoured to attend the 5th Europe Asia Young Leaders Forum, and to be given the opportunity to share my experiences and understandings of enterprise operation and management. Today, the topic of my speech is “TCL – Learning and Growing in Transformation and Globalization”.

As we know, China has been witnessing dramatic economic growth for more than two decades. Many people are interested in and curious about how China has been able to achieve that. TCL probably can provide another angle to understand China's economic boom. Actually, TCL is just like a miniature of China's growing economy.

Twenty-five years ago (in 1981), TCL started its business with a loan of 600 USD. At that time, it was only a small factory with annual sales amounting to about 100 thousand US dollars. By 2005, TCL had become an international enterprise group with annual sales of 7 billion US dollars. During the past 25 years, TCL has witnessed an annual growth rate of over 40%. It owns 4 research and development centres and nearly 30 manufacturing bases worldwide, and also has set up marketing organizations in 45 countries and regions. After merging with Thomson colour TV, TCL produced more than 23 million colour TV sets in 2005, ranking first in the world. It manufactured more than 10 million mobile phones in 2005 after merging with the mobile phone business of Alcatel, becoming one of the top 10 global mobile phone manufacturers. In addition, TCL is also a leading player in China in a variety of industries such as IT digital products and home appliances. In 2005, TCL's overseas sales outnumbered its domestic sales for the first time, taking up 53% of total sales. This marks an important step of TCL in its efforts to establish an international enterprise.

Why has TCL been able to develop so rapidly?

An important reason is consistent system reformation and management innovation, by which TCL could effectively make use of the four advantages emerging in China's reform and opening-up.

First, the advantage of state-owned enterprise: In China, government support is one of the vital factors for enterprises, the favourable and preferential policies and resources are very crucial to the enterprises' development. No matter whether in domestic or overseas business, the background of "state-owned" has been playing an important role in the development of TCL. Though the state-owned share has been reduced from 100% to presently 15%, the government is still the second biggest shareholder of TCL Group.

Secondly, the advantage of private company: TCL Group now also has some characteristics of a private company through Management-Buy-Out which account for 25% of the total share. Thus, the key management team of TCL has also become the owners of TCL, so the management team naturally considers the development of the company in a more strategic way and maintains the passion of entrepreneurship, as company and personal interests are perfectly matched.

Thirdly, the advantage of foreign invested companies: TCL Group has introduced some well-known international enterprises as strategic investors, for instance consumer electronics giants such as Philips, Toshiba, Mitsubishi, etc. Among them, Philips Company has become the third leading single stockholder of TCL already, holding 7.5% of the shares of TCL Group. Through the cooperation of capital investment, the competition with these famous international counterparts has been advanced to a win-win situation. The strategic investment shareholders not only cooperate on technology and resources with TCL, but also contribute advanced systems and experiences of business management, turning TCL Group rapidly into a modern enterprise.

Fourthly, the advantage of the public company: TCL Group, as a whole, is a listed company on the Shenzhen stock exchange, and also, TCL multimedia division and TCL communication division are both listed on the Hong Kong stock market. This not only provides favourable financing channel for TCL's development; even more importantly, the supervision from public investors makes TCL a company with system transparency and reliability to the whole society.

Making use of and combining the four major advantages described above at the right time and in the right ways ultimately explains the marvellous growth of TCL.

Internationalization strategy and practice also strongly contribute to the speedy and healthy growth of TCL.

TCL pursues three approaches to internationalization:

1. Organic Growth Approach, namely the way of self-brand growth. We have used and developed the TCL brand business overseas since 1998 by establishing overseas production bases, overseas sales networks and service networks, covering more than 150 emerging markets.

Self-brand business has enjoyed an average growth rate of more than 50% for eight consecutive years and has carried a profit margin of more than 3% each year.

The TCL brand has gained a better market position: Subsidiaries set up 2 years ago normally rank among the top 7 in their markets; those set up 3 years ago, among the top 4; those started 3 to 5 years ago can obtain 18% market share on the average. Subsidiaries that have been set up over 5 years ago can be the top one or two in those markets.

The brand influence of TCL has become better and bigger with TCL being considered tomorrow's star/rising star of CE products superior to Japan and Korean brands, though currently still inferior to them.

Simultaneously we have built a solid foundation and sustainable growth ability. For the time being, 18 subsidiaries have been built up in the important emerging markets, executing the production, marketing and service functions. Our overseas exploration and the establishment of these subsidiaries have provided a very good platform for the diversified business development overseas and carry major significance for the future.

2. Original Equipment Manufacturing (OEM) and (Original Design Manufacturing) ODM – the way of EMS (Electronic Manufacturing Services). In particular, we provide the global EMS service for some strategic partners such as Philips and Panasonic.
3. Mergers and Acquisitions, which is mainly deployed in Europe and North America, which helps us accelerate the establishment of operation structure and customer relationship in these markets.

Looking back at our eight years of internationalization, we find that the road ahead is tortuous and full of difficulties and challenges. What follows are four major challenges or obstacles that pioneering Chinese companies encounter when they start their overseas expansion:

1. The negative effects of China's image:  
We know that when we enter an international market to promote and set up the TCL brand, we must first change and establish the image of "China" brands, which is mostly negative due to former bad behaviour in bilateral trade and the misleading of some propaganda (such as the movies "Red Sorghum" or "The Story of Qiu Ju").

When TCL initially went out to the overseas market, it's easy to be recognized as a Korean or European brand by the consumers, because it's the only Chinese brand known by its English acronym. Later, after having become known as Chinese products, of course, the risks of returning goods often occurred. Fortunately, such phenomenon has declined a lot until now through our seven years of diligent work in the overseas market such as brand promotion, after-sale service, successful and appropriate communication with mainstream media propaganda. Therefore, we say "the pioneer enterprise

must bear the heavy responsibility of improving the image of the whole nation.”

2. The lack of internationalization theories and practical experiences

The internationalization of Chinese companies is an arduous business never done before. With no concrete theories for guidance and no existing practices for reference, we only have the courage and Chinese wisdom to conquer the difficulties, just like crossing the unknown ocean full of uncertainties.

Reviewing the existing management theories, they can be divided into two categories. One is western economics, which derived from the general case of European and the American enterprises, including a few principles of Asian enterprises' developments like Japan and Asia's Four Little Dragons (Singapore, Korea, Hong Kong, Taiwan), while the developing countries such as China and India are excluded. The other theory is eastern economics based on planned economy, not market economy. Therefore we go ahead lacking theories to guide us. Due to this lack of economic theories that can be used by us directly, we have to build our own theories through practicing, abstracting, and then summarizing and formulating.

3. Conflict between the importance of talents and the extreme shortage of them

In the early stage of internationalization, a company usually lacks a complete operation system to support its overseas business development. An example: With our headquarters based in Shenzhen and a production site based in a remote area of Brazil, it makes it extremely difficult to support an integrated workflow system. Hence what we rely on mostly will be overseas leaders' personal competency and their ability to break through, or the capabilities of a small team. But unfortunately, it is very difficult to find such individuals or such a small team. The reason is that the human resources market for international professionals in China is still in its early stage or not yet existing, while in European and American countries this market has been well developed. Now we are having two types of talents: One type are those returning from overseas educated with foreign economic theories, and TCL has recruited a lot of talents of this type. And the other types are those selected from domestic operation system. We should say that both types are not truly international professionals and both need further practices and study. This is also a big problem we are facing.

4. Compared to domestic business, international business is more affected by factors such as politics, society, and local environments, which actually gives us a full understanding of what plutonomy is. For instance, the location selection of a factory in Russia has to take into account the factor of Duma competition, and the strategy adoption in Indonesia has to watch out which political party is in power.

Despite such unfavourable factors such as relatively little brand awareness, lack of theoretical guidance for internalization, lack of high-calibre talents, and complexity of operational environment, TCL overseas staff, with great

adaptability and initiative, has achieved rapid business growth through a series of feasible and effective measures and through taking into consideration local conditions.

We have adapted four major strategies:

1. Attitude towards internationalization: strategically aggressive and tactically prudent

Internationalization is a double-edged sword, or even a game of “live or die”. It may result in new developments or end with loss and failure. Just as a line in the soap opera “A Native of Beijing in New York” says, international market may be “heaven” or “hell”. If you love the enterprise, send it to the international market, for it’s heaven; if you hate the enterprise, send it to the international market, for it’s hell. Any improper operation may result in great losses and even bankruptcy. Therefore, some people shrink from internationalization, while others take the risk. TCL does not ignore the ladder but puts great value on the importance of internationalization. So we shall be aggressive in strategies and prudent in tactics.

Why shall we be aggressive in strategies? Opportunities arising from global economic industry restructuring and ladder-like development may disappear soon. Once lost, these opportunities will not come up again. For example, we were at a critical point of whether or not to enter the Vietnam market in 1998. Fortunately, we chose to enter. Otherwise, we would not be able to enjoy the present favourable situation. We achieved great development by exploiting the opportunities and favourable government policies at that time, while others hesitated. When our competitors visited the market later, these opportunities were gone. We would have lost the opportunities if we had been afraid of the potential unfavourable results. That is why TCL has established more than 30 manufacturing bases and about 20 marketing organizations in emerging markets within a few years’ time.

Why should we be prudent in tactics? Because internationalized operation is a long process involving many elements and great risks; and the enterprise is at a relatively weak position, and negligence at any step may cause us to lose everything. Therefore, we should be very prudent and thoughtful when it comes to internationalized operation and should not take any unnecessary risks.

2. Control the tangible assets with the intangible ones, make full use of other forces and integrate the locate resources for our usage.

Overseas operation requires intensive support and normally needs massive hardware support, but actually we should refrain from investing heavily in tangible assets.

What we do is look for several strong partners and provide them with a complete set of investment plans, including workshop design, technical design, equipment purchase and installation on their behalf, establishment of quality assurance systems and manufacture management systems, technical training,

assignment of on-site representatives, and guarantee of the quantity of manufacturing orders. We do not engage ourselves in risky routine work like field management and warehouse management. In this way, we save lots of investment, accelerate capital circulation, highly increase our anti-risk capability; and we focus on “core work” such as developing customers, extending channels, establishing brands, training employees and establishing a friendly interaction with the environment. As a result, the strength of the enterprise is improved. That's the concept of controlling the tangible things with the intangible things and making full use of local resources instead of investing directly.

### 3. Pay attention to the “back side” of internationalization

A common misunderstanding is to only pay great attention to the front side while paying not enough attention to or even ignoring the back side; people think that internationalization is the job of the international business department and front-side salespeople, or at most, it is a business under the charge of a vice general manager.

In fact, doing international business means not only doing and running a business outside its homeland, but also a continuous and profound transformation of value, governance structure, management system, operation mode, and business activities of an enterprise, and an internationalization process involving the whole process and full elements of overseas operation. This is obviously the responsibility of the top leader of an enterprise. Besides, it is necessary to establish a powerful back side support and to enhance the specialization level. In this sense, the front office and the back office are equally important.

### 4. Cultivate adaptive core competition advantage.

At the initial stage of internationalization, compared to our Japanese and Korean competitors, we are usually not in a favourable situation: Our technology is not as advanced as theirs; our economic strength and scale are smaller than theirs; our brands are not as famous as theirs; our internationalization history is much shorter than theirs, our internationalization experience and skills are not as rich as theirs. Clients often ask: “What does TCL compete with?” It's a question of logic. It looks like that we are no good, not stronger nor cleverer than our competitors; it seems that we are hopeless.

In fact, in such cases, it is Darwin's theory of the survival of the fittest that points out a direction and gives us confidence. Yes, we are not the strongest, we are not the smartest, but we can be the group who best adapts to the environment. Furthermore, Chinese enterprises grown from Chinese culture have unique advantages for creating adaptability advantages. This is mainly apparent when it comes to products adaptability; service adaptability; brand promotion adaptability, price adaptability and work spirit adaptability.

These adaptability advantages exist in all regional markets, in all market segments, and in all operation aspects. Through continual creation and

accumulation, we will form powerful, unique and strategic adaptive advantages. We are not going to be the strongest or the most intelligent, but we will be the fittest.

Today, I am very happy to share with you some thoughts on TCL transformation and globalization. I would be glad to hear your opinions and comments as feedbacks. TCL, as well as many Chinese companies, has just taken the first step on the road to globalization. There is a long long way to go. We hope to learn a lot from internationally successful enterprises. Forums like the one today will be a great help to us.

Thank you all!