

## China – Law Firms

# How A Combination Of Diverse Cultures Makes For A Dynamic Team

*The Editor interviews Ying Li, Yuval Tal and James F. Chapman, corporate partners in the Hong Kong office of Proskauer Rose LLP. Mr. Li is a graduate of Peking University with an LL.M and LL.B as well as Harvard Law School with a J.D. degree; Mr. Tal holds degrees from Hebrew University where he was a member of the faculty and as a Fulbright Scholar received J.S.D. and LL.M degrees from the University of Chicago Law School. Mr. Chapman received an LL.B degree from the University of Aberdeen (Scotland).*

**Editor:** Please tell our readers about your plans to expand Proskauer's offices to Mainland China, part of your plan when we spoke last year.

**Chapman:** We hope that by the end of the year we'll have a license to open an office in Beijing. The waiting period is usually up to nine months.

**Editor:** Your office has been specializing in M&A work in the hospitality, lodging and gaming industry as well as other general corporate work. Have you expanded into any other areas of M&A work?

**Chapman:** The office is not entirely focused on the hospitality industry although hospitality is a strong practice for Proskauer globally. We've actually taken on some M&A work recently in the mining industry – one project in Africa, one project in Brazil – which are China-related projects. China has a big appetite for commodities. We are acting on behalf of the owners of the mining group. We are able to cover M&A transaction in any industry, not just the hospitality industry alone. We focus on all sectors for M&A work.

**Li:** We have recently been engaged by a Latin-American company that is a prospective seller of a mining business, while the purchaser is a China-based company that has operations in both Hong Kong and China. This is a huge deal in the mining industry, which is confidential at this stage. This is an excellent cross-border and cross-office effort with which I personally, and Proskauer as a firm, have had a lot of experience. We are also representing a U.S. general partner and fund manager in setting up an offshore China-focused private investment fund involving a major PRC state-owned enterprise which hopes to invest outside of China. We advised one of the major, top-tier PRC IT companies in setting up a Cayman buyout fund, which will invest back in China as well.

**Editor:** You also mentioned last year that you were helping Chinese clients go public, and you've mentioned the fund formation you're doing. With the economies of the world slowing, has this area been as active for you this year as it was last?

**Li:** Basically, there are two trends in our market – private financing and public financing. Because this firm's strengths are in private financing, we get more private equity deals, but we are hoping to do IPO deals in time in the U.S. and potentially in the Hong Kong market. Currently, we are representing some PRC companies listed outside of China in performing their compliance work.

**Editor:** Is the pace of M&A and IPO deals picking up again?

**Chapman:** Our impression is that deal flow

is picking up again, especially IPOs in Hong Kong, but M&A is still relatively slow.

**Li:** Earlier this year China opened a second board market in Shenzhen, similar to NASDAQ in New York or AIM in London.

**Editor:** According to Barclays Capital, emerging Asia is the only area in the world where output has regained its former level before the crisis, which is largely owing to China's industrial production growth of 11 percent in the 12 months to July. How has China been able to grow so rapidly in view of the diminished role of exports to the rest of the world?

**Chapman:** The Chinese government authorized a very big stimulus package last year, which probably ended up with funds flowing into the Hong Kong property market. We've seen our stock market and our property market grow rapidly in the last six months – probably 20 percent for the property market and nearly 100 percent for the Hang Seng Index. People in Mainland China seem to have a lot of cash, which seems counterintuitive since exports have declined. Local consumer demand in the PRC is high.

**Li:** China's internal consumption power is huge, which is its greatest advantage. Not only do domestic but also a lot of overseas investors look at China as a big potential market for consumer products, health, medical products, even recently real estate. The domestic market is very attractive to both domestic and international investors.

**Tal:** In the hospitality sector, people who are setting up resorts, even in the western part of China, may be charging US\$400 a night, and 80 percent of the clients are mainland Chinese – that's a big statement! It shows where China is headed.

**Editor:** What other effects has the stimulus package had?

**Tal:** It has clearly affected consumer spending as well as helped to create infrastructure projects. We hear that China is on a path of having more roads than the U.S. in a couple of years. On the transportation side there are 40 new airports. That stimulus has helped prop up manufacturing and give more employment to Chinese labor.

**Li:** We do note that the Chinese government is trying to encourage that money stays in China. That is why more foreign investors are exploring all possible vehicles to set up onshore investments. For example, our firm is very active in setting up RMB funds for our clients. This is a new vehicle for foreign investors to invest directly into Mainland China. Formerly, they would invest in an offshore Cayman fund outside of China or in Hong Kong, but now, because the government's policy encourages foreign investors to participate in onshore structures within China, we as lawyers try to develop a new skill set to help investors enter directly into China.

**Editor:** Why are the economic fundamentals so much better in China than in the rest of the world? Has foreign capital played a big role in China's robust growth?

**Tal:** In terms of the fundamentals, China is a growing economy. Consumer spending is on the rise and that is what has propped up the

U.S. for years. The economy is not suffering from an overlay of tremendous amounts of debt at the national or individual levels, which is what is crippling both the U.S. and Europe. In the U.S. and Europe corporations have difficulty borrowing for transactional work, whereas in China and in Asia generally the banks have money and leverage has been kept low.

**Chapman:** The planned economy has a major impact on debt levels as well.

**Li:** Foreign capital is key to economic growth. Without foreign capital China would not be able to achieve its target numbers. You have to look at this from both historical and current perspectives. Foreign capital has aided the early stage of China's development and has provided a lot of financial resources. Even with domestic consumption being quite substantial, foreign capital supports much of Chinese investment.

**Editor:** Isn't the government looking inward toward developing the remoter interior areas that have been neglected for so long?

**Li:** Cities such as Xian and Chongqing are starting to accelerate in growth. In the international public media they are called second-tier or third-tier cities. Both domestic and international hotel groups look at the second-tier or third-tier cities as the new frontier. We are representing a major European-based energy company, which is providing energy services through a joint venture in Chongqing. To stimulate the economy the government elevated the level of that city to that of province, just like Beijing, Tianjin and Shanghai. However, when I arrived there, right away I saw that it was not very well developed and the living conditions were poor, but it attracts a lot of foreign investment because labor is cheaper and the infrastructure is easier to maintain. The biggest problem in developing the interior of the country is transportation. For example, between Hong Kong and Chongqing there is only one flight every day, whereas there are 14 flights between Beijing and Hong Kong. Because along the coastal area the first-tier cities are already occupied by the major players and business costs are very high, investors are looking at the interior of China as a new frontier.

**Editor:** What trends are you seeing in foreign investment in China, especially on the private equity side? You mentioned hospitality and mining and health-related products.

**Chapman:** The big change is the consumer market where a significant part of the population has money to spend. For example, some people are spending their discretionary income on nutritional supplements and healthcare products. The big attraction of China has always been its massive population. There are 1.3 billion potential consumers.

**Li:** A lot of major players in the U.S. such as GE and other major medical care or food industries come to China because the current medical system in China is definitely more primitive than in the West and the government tries to solve this problem by privatizing these industries. Manufacturing, healthcare and consumer products are of great interest.

**Tal:** If you could guess what would be the product that the upper middle class Chinese person would want and you were the first to market with it, you would instantly be a lot more than a millionaire.

**Editor:** What areas would be off limits for inbound investors?

**Li:** Telecom can be divided into two major categories. One is basic telecom – existing overhead lines and mobile services, where foreign investors are not allowed to control. The other is the value-added business, i.e., Internet business, where the policy is more liberal. You will see more investors participating in the PRC ICPs or ISPs of Internet business, but not in basic telecom.

The real estate market is very, very attractive to foreign investors, but that market has not been completely opened to foreigners yet.

The Shanghai Pudong government has recently tried to liberalize its private equity investment policy by approving six or seven foreign fund managers who would invest in and manage purely domestic funds. Foreign fund managers are allowed to manage domestic investment but without foreign limited partners' participation, which is the newest trend in introducing foreign investment in the private equity area.

**Editor:** What challenges do Chinese investors face in investing overseas? Often Chinese firms, such as CNOOC, have been rebuffed by the U.S.

**Chapman:** One of the challenges is that some of the large Chinese state-owned enterprises tend to invest in particular industry sectors so already they will be very large players in one particular sector. When they attempt to invest in America or Europe, naturally they choose to invest in the same sector as it is the sector which they are familiar with. Consequently, they run into problems with the competition authorities.

**Li:** The biggest problem is that so many businesses in the Chinese economy are all or partly owned by a sovereign state or government interest, which may be a serious problem or concern to the U.S. or other Western governments. Also, cultural differences are very important, not only at the M&A stage but also at the stage of post-merger integration.

**Editor:** How are U.S. law firms able to assist their clients around the world in taking advantage of Chinese business opportunities?

**Tal:** We have rich experience in Asia. Jim Chapman has been in Hong Kong for 24 years. Ying Li has been in Asia for over 15 years. Our local team is very strong. For foreign investors who want to invest in China, our team is able to give them the know-how, the legal background in Chinese legal matters that Ying provides as well as Jim's experience in Hong Kong and Asia generally. My legal background provides a bridge between East and West because I received my early legal education in Israel before going to the United States, where I received additional legal education and practice experience. As a team we bring knowledge of two or three legal systems, two or three languages, and at least two, if not three or more, cultures – all of which is crucial in terms of doing deals on this new frontier known as China.

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