



FOCAL POINT: CHINA EDITION

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BUILDING MATERIALS MARKET AND DISTRIBUTION MISSION

INTRODUCES US COMPANIES TO CHINA MARKET

In May, US-China Build led a group of eleven US building materials exporters on a one-week business development mission that resulted in over \$2 million in projected sales for the participating companies. The US delegation attended panel discussions with Chinese developers of single- and multi-family wood-frame and concrete residential projects, building material distributors, and home center representatives. The group also attended seminars about China's construction market and regulatory changes presented by the AF&PA and the US Foreign Commercial Service.



Mission members at Tecsun Homes' development of 107 wood frame homes.

US-China Build arranged pre-scheduled, one-on-one business meetings with developers, distributors, and wholesalers for the US companies based on their inter

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US-CHINA BUILD PROGRAM

The US-China Build Program (USCB) was developed by Evergreen Building Products Association and the American Forest & Paper Association, with federal support from the US Dept. of Commerce Market Development Cooperator Program and USDA Foreign Agricultural Service, to promote exports of US building products and services to China's residential and light commercial construction market. USCB offices in the Pacific Northwest and Shanghai are available to assist US companies. For more information about how your company can participate in USCB and opportunities available to US exporters in China's housing market, contact Rose Braden at (206) 543-0700 or rbraden@uschinabuild.org.



US PAVILION IN SHANGHAI INTERNATIONAL BUILDING & CONSTRUCTION TRADE FAIR

Eighteen US building materials manufacturers and exporters, state offices, and wood products associations participated in US-China Build's US Pavilion at the Shanghai International Building & Construction Trade Fair (IBCT) from May 19-21.

With six halls covering 540,000 square feet and over 1,200 exhibitors, IBCT is one of Shanghai's largest building materials trade fairs. Three halls were devoted to kitchen and bathroom fixtures. The remaining three halls featured a range of building materials, including windows, garage doors, interior and exterior doors, treated wood, and insulation.



Fifteen US companies exhibited products in the USCB/US Pavilion at the Shanghai IBCT

US participants rated the show highly and reported making a number of contacts that they expect to lead to near-term sales.

"The manager of our Shanghai office said that this (2004 International Building Materials Fair) was the best trade show that he has attended with regards to the quality of the leads," said Bill Mann, Vice President of Sales and Marketing for United Coatings, a paint and coatings manufacturer. "We were able to set up a couple of new distributors in China who are now in the process of finalizing their first orders. I also met potential customers from Singapore, Korea, Iraq and the Ukraine."

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Advice for Exporters: Due Diligence in China

Greg Kulander. Ph. D.

Doing business in China is just like anywhere else, only more so! Many US companies seemingly throw out their book of good business procedures when they touch down on the tarmac of their first Chinese airport. Befuddled by the enormous business activity surrounding them and intimidated by the indecipherable Chinese language and customs, they are easily led into believing that “China does things differently” and if they want to do business in China, they must do things “the Chinese way”. Many companies find out, too late, that the “Chinese way” usually amounts to financial losses for them and financial gains for their Chinese counterparts.

Reduce the “home court” advantage

Your Chinese counterpart has the home court advantage. However, careful due diligence can effectively reduce this advantage. Due diligence plays a much more important role in a commercial transaction with a Chinese counterpart than it normally does in a domestic transaction, and is much more likely to convey information that directly influences business decisions.

Due diligence is commonly defined as an investigation of the legal and financial condition of a target company to evaluate whether that company possesses the legal capacity and the financial wherewithal to perform as desired in the contracted agreement(s). It usually consists of an examination of the company’s official legal documents, as well as contracts with suppliers, customers, etc., and of its official financial records. The degree of due diligence performed varies with the type of cooperation and/or scale of investment envisioned. The greater the scale and the more complex the relationship, the more time and effort should be spent on due diligence.

Conduct more careful due diligence than you would in the U.S.

In China, it is necessary to conduct even more thorough due diligence than in the U.S., mainly because the quantity and quality of public information available about a Chinese commercial entity is limited. Moreover, Chinese legal and accounting standards sometimes differ significantly from Western standards, requiring considerable changes before lending themselves to comparison. Sometimes, a complete restatement of accounts has to be made in order to make an assessment according to Western accounting principles. Chinese accounting for accounts receivable/bad debt is much more lenient than in the U.S., allowing unrecoverable receivables to remain on the books for a long time. This makes a comprehensive evaluation of creditworthiness a critical part of the due diligence.

Engage a reputable **local** counsel (or foreign counsel with strong local capacity) to carry out legal due diligence. Legal due diligence in China begins with an investigation of the public documents of the commercial entity, i.e. its Business License, which will state the legal owner (is it the same as has been presented?), official address, approved scope of business, registered capital and the period for which the License is valid; its Land Ownership, including all registered mortgages; its Capital Verification Statement, which will substantiate that the registered capital has been paid up (an important consideration when considering liability thresholds) and is up to date; and other Permits or Certificates necessary for business operations, such as environmental permits, health certificates, etc. If the contemplated transaction involves investment of some kind by the American party, all of these documents need to be carefully reviewed for restrictions on transferability. Employ locally savvy legal counsel!

Visit the company’s factory in person

Financial due diligence likewise begins with a thorough examination of official public records such as the company’s Tax Report. Many companies will be quick to point out that these records are not accurate, but nonetheless they are an important starting point for the financial analysis as they are the only public records. Accountants are then called in to inspect the company’s books and to verify revenues, profits, receivables etc. A physical inspection of assets and even of sales turnover is also an important part of the financial due diligence. A personal visit by the U.S. side to the production facilities can provide a clear picture of actual working conditions and product quality. Finally, the company’s bank records and banking relationships need to be scrutinized. Company compliance for this will be necessary, and if it is not forthcoming, this should be a red flag.

Visit local government to understand the company’s standing in their community

More detailed due diligence proceedings include background checks on key personnel (and examination of employment contracts), interviews with customers and suppliers, discreet checks of actual physical movement of goods, relationships with local government representatives, etc. Watch for evidence of collusion between different parties. Hire a private investigator if the level of exposure is high. He can discretely ascertain if the company and its management have a good reputation, and whether the company is as it appears to be. A less expensive way is to ask the Chinese party for references, in particular foreign references that you can then check yourself. Pay a visit to the local government offices (on some other pretext) and do a little “sleuthing” about the company and its related parties.

Make contracts simple with incentives for both sides

It is important to remember that the Chinese are not used to working according to written legal documents and often the expected paper trail will not exist. This is also valuable

(Due Diligence, continued from page 2)

to remember when negotiating contracts with the Chinese. They generally do not put as much weight on the written word and often what the U.S. side considers to be the final definitive contract will be seen as the basis for “further negotiation” at a later time. Design contracts to be “win-win” with built-in incentives on both sides for fulfilling contractual obligations. Remember that your counterpart is unlikely to possess a Harvard MBA and complicated legal contracts may not be fully understood, easily leading to misunderstandings later on. Keep it simple! Use your own legal counsel for legal advice; do not rely on your Chinese counterpart to inform you about Chinese law.

Last words of advice

Don’t count on “guanxi” [relationships] with government officials to resolve commercial issues. Officials are notoriously fickle and subject to all sorts of pressures that are very difficult to understand and predict. Keep things simple, transparent and legal!

Minimize your risk exposure by securing payment in advance for products or services. Use letters of credit and other financial instruments to protect yourself. Chinese companies themselves rarely use terms that allow unsecured payments after delivery of goods.

Involve yourself personally in developing business relationships. Expression of true interest on your part in the livelihood of your Chinese counterpart is worth a thousand legal documents, and will increase the likelihood of establishing a robust and rewarding relationship many times.

Don’t let your Chinese counterpart convince you that due diligence is not part of the Chinese way of doing business and that it indicates mistrust. The Chinese themselves are moving towards this internationally accepted model of commercial transparency even in their domestic dealings as they expand into other provinces where they do not have strong personal relationships to protect their interests.

Finally, be open and flexible, but stick to your own business model and modus operandi. The Chinese want to work with you because you are a foreign company and do not expect you to behave like a Chinese entity.

Greg Kulander, is a Beijing based consultant with 8 years of on-the-ground experience in China. He holds a Ph.D. in Modern Chinese studies from the University of Aarhus in Denmark. He can be reached at greg_kulander@yahoo.com

Thanks are due to Patrick Powers, China Director for the U.S.-China Business Council, Lester Ross, Counsel in the Beijing office of Wilmer Cutler & Pickering and William Baker, Chief Representative of Mahon China for allowing me to learn from their substantial experience in the area of due diligence in China.

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ests. As a group, the mission participants reported making over 40 new contacts that are expected to lead to new sales for their companies. One company expects a meeting with OBI, a major retail home center, to lead to distribution for his product through OBI’s China stores. Other mission participants reported meeting potential agents and distributors, identifying potential projects,



Mission members talk to a developer during visit to Yi Shing Garden, a concrete single-family home development.

Mission Participants

Company	Product
Louisiana Pacific	OSG & Panels
Demilec	Spray-in Insulation
CGI Silvercote	Insulation
Metals USA	Structural Insulated Panels
Nemiroff Group	Porcelainized Wall Panels
North American Wholesale Lumber Association	Association
Light Concrete LLC	Concrete
Associated Materials	Vinyl Windows & Siding
Globex/Platt Electric	Electrical Equipment
Almond Brothers Lumber	Southern Pine Lumber
Pacific Modern Homes Inc.	Panelized Homes

and making progress towards getting government recognition for their products from China’s Ministry of Construction.

All participants commented on the importance of visiting China to understand the market and the business culture. One participant said “learning about the business culture from the panelists and other meetings was the most valuable part of the mission”, adding that first-hand experience beat any text book or publication available.

US-China Build will lead a sales mission to Shanghai, Ningbo and Beijing—China from September 13—17. The sales mission will be organized around seminars promoting the benefits of using US building materials using the theme of energy efficiency. Featured technical presentations and individual company presentations will address energy efficiency to audiences of developers, architects, interior finish companies, and other construction professionals. For more information about the sales mission, please contact Rose Braden, US-China Build Program Manager.

(Trade Fair continued from page 1)

During the fair, APA-The Engineered Wood Products Association, American Forest & Paper Association, and the Southern Pine Council held a seminar about timber bridges and the use of treated wood for structures and landscaping. According to Ed Elias, APA International Marketing Director, the show provided an excellent venue for US companies to hold follow-up discussions with seminar participants about project ideas and US products. As a result, APA and its member companies are in the planning stages for construction of a wooden bridge project at a Shanghai-area golf course.

US Pavilion Participants

Company	Product
Boise Building Materials	Southern pine lumber
Calvert Company, Inc.	Glue-laminated members
Almond Brothers Lumber	Southern Pine Lumber
American Forest & Paper Assoc.	Trade Association
APA-The Engineered Wood Assoc.	Trade Association
Demilec	Spray-in Insulation
Hurd Windows	Windows
Pacific Modern Homes Inc.	Prefabricated wood homes
Regal Ware	Water purification systems
State of Idaho	Promotion office
State of Missouri	Promotion office
State of Oregon	Promotion office
Southern Forest Products Assoc.	Southern Pine Association
United Coatings	Paint & waterproof coatings
Weather Shield Windows	Windows
Western Wood Structures	Engineering
Yasuda	Plumbing Fixtures
Zurn Plumbing	Plumbing Supplies

SOFTWOOD EXPORT COUNCIL'S "CHINA PROMOTION WEEK" JUNE 7-11

China's furniture industry was the focus of the Softwood Export Council's (SEC) "China Promotion Week", a program of seminars, trade shows, and factory tours in June. US softwood lumber producers and wholesalers joined the SEC, the American Hardwood Export Council (AHEC), and AF&PA to generate sales of US softwood lumber to China's furniture industry.

The SEC joined the mayor of Dalian to open the 9th Annual Dalian International Furniture Show, where SEC, AHEC, and AF&PA staffed a US wood products booth and gave a presentation about American softwoods used for furniture manufacturing.

The group also traveled to Qingdao to attend AHEC's 9th Southeast Asia and Greater China Convention. Qingdao, the northern capital of Shandong Province, is a quickly growing commercial and trading hub for Northern China. It will also be the location of the Beijing Olympic Games sailing events.

ADVERTISING AVAILABLE IN FALL USCB HOUSING & BUILDING PRODUCTS NEWSPAPER

Reach thousands of readers by advertising in Issue 6 of the Chinese-language US Housing Industry & Building Materials Newspaper.

Each issue of the newspaper contains information about US building materials, energy efficient products and design, project and product profiles, industry innovations, and question and answer columns. The paper is mailed to our database of over 8,000 companies, posted on the US-China Build Chinese-language website, and distributed at trade shows and seminars.



The Fall issue will also be distributed to developers, architects, specifiers, and other construction professionals attending the US-China Build September 2004 Sales Mission & Seminar Series in Shanghai, Beijing, and Ningbo—China from September 13—17.

Each advertiser placing a 1/4 page or larger advertisement will receive a free 250 word product profile with one photo.

Ad Rates

Ad Size	Non-member Rate	EBPA Member Rate
Full Page	\$1935	\$1742
1/2 Page	\$1305	\$1175
1/4 Page	\$900	\$810
1/6 Page	\$720	\$648
1/12	\$473	\$426

Page dimensions are 14.5"x10". Color ads are also available for an additional 10% of the standard ad price.

For more information about advertising, distribution, or product profiles, please see the insert in this newsletter or contact Rose Braden at (206) 543-0700 or rbraden@uschinabuild.org

A SUCCESSFUL AMERICAN HOUSING PROJECT IN BEIJING

By Zhang Yu-zhong – General Manager, Beijing Guangming Hotel

This article first appeared in the US-China Build Program's May 2004 Chinese-language US Housing & Building Materials Newspaper. The Beijing Guangming Hotel introduced an American wood frame villa project to the market in 1999. Mr. Zhang also spoke to an audience in Beijing about his experiences building and leasing wood frame homes during the September 2003 US-China Build Seminar Series and Sales Mission.

Beijing Guangming Hotel completed its first wood-frame project in 1999 as part of a larger hotel development that included 495,000 square feet of floor area. The project is comprised of apartments, office buildings, and a hotel with restaurants, shops, and health/entertainment facilities. The development also includes "Guangming Apartment", a subdivision of 160 Japanese- and American-style single-family wood-frame homes (villas) available for lease.

The first phase of the project included 135 Japanese-style wood-frame villas. Completed in April 1996, the homes average 1,450 square feet each. Designed and constructed by Japanese Sanze Residence Corp., all of the structural and interior building materials were imported from Japan.

The second phase of the project consisted of 25 American-style wood-frame homes, in three different styles and ranging in size from 2,000 to 2,350 square feet. The project was designed by Daniel Corp., a North Carolina-based company. American Palgan Corp. supplied the American-made building materials used for the project and provided a project manager to guide the construction process. The homes are furnished with furniture imported from the US and GE appliances. Started in June 1998, the project was completed in 14 months.

Guangming Hotel decision to build wood-frame homes was based on the structural integrity and resilience that wood-frame homes demonstrated during the 1995 Kobe, Japan earthquake. While the developer built the first phase of the development with building materials from Japan, the appreciation of the yen made the project too costly, prompting a switch to American building materials for the second phase. Wood-frame was also chosen to cater to the hotel's Japanese, American, and other international renters.

Market Analysis of American wood frame project

Beijing Guangming has said that their 25 Western-style wood frame homes quickly stood apart from Beijing's villa market and Beijing Guangming's other projects. According to Mr. Zhang, the rentals have maintained "three highs":

High rent rates. From August 1999 when the apartments were made available, and October of the same year, rents increased by more than 80%. By the end of the year they had almost doubled to US\$6000 a month.

High rate of return on investment and fast return.

Guangming Hotel had a 100% return on its initial investment within four years after the American villas were made available.

High in overall villa revenue. The 25 American villas represent only 15% of Guangming Hotel's villas, yet they generate more than 30% of Phase I and Phase II revenue.

The Benefits of Wood-Frame Construction

Beijing Guangming had several reasons for building with wood. Among them are long life-span, improved energy efficiency, fire resistance, performance during earthquakes, and design flexibility. In addition, Mr. Zhang noted the standardized construction process and quality of imported materials as positive benefits. He said wood projects can be completed faster than brick or concrete construction, meaning less interest paid to the bank, lower labor expenses, lower risk of market change, and lower financial risk. He also said Beijing Guangming was able to produce higher quality homes because imported wood products are graded. Beijing Guangming provides a five-



Beijing Guangming's 25 American-style wood frame homes took 14 months to complete, and rent for US\$6000 a month.

year maintenance warranty for major components of each home, because of their confidence in the quality of wood-frame homes. Developers of brick-concrete homes typically offer no more than a three-year warranty.

Mr. Zhang also noted two other aspects not commonly promoted by US builders. First is ease of repairs. In wood-frame structures, the plumbing and electrical lines are contained in the wall and floor cavities with a pre-determined maintenance entrance, ensuring easy access for repairs. Second, is the ability to create larger living spaces with wood-frame versus concrete. The outside structural wall is relatively thin in a 2x4 stud with a single-layer 12mm OSB board. Drywall can be fixed on the foundation wall stud, thus the total thickness is only 89mm. The walls of traditional brick-concrete structures are typically 240mm.

Beijing Guangming also chose to build wood-frame homes as a means of attracting customers. According to Mr. Zhang, wood-frame construction is readily accepted by foreigners and Chinese who have studied or lived abroad.

(Beijing Development continued on page 6)