A case study of CNOOC (China National Offshore Oil Corporation) – the future of Chinese state owned enterprises

Master Thesis in International Business and Entrepreneurship

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Abstract

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Program: International Business and Entrepreneurship

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Problem Statement: How CNOOC as a Chinese state-owned enterprise became a multinational enterprise?

Purpose: The main purpose of this dissertation is to understand why CNOOC needs to be a multinational enterprise and what kind of expansion process that CNOOC is taking, which theories could explain those CNOOC’s internationalization activities. According to the successful experience of CNOOC, we will try to find an appropriate developing way for other Chinese state-owned enterprises.

Method: We will explain why we chose the target company how we perform our research process, how we collect primary data and secondary data and what sort of analytical approach we have chosen.

Theoretical Framework: We start with the definitions of state-owned enterprise and multinational enterprise, the development direction from SOE to MNE; then the market entry mode of internationalization, follows by the entrepreneurial perspective which is the internal factors of the transformation, and end with the relationship between politics and economy perspective.

Conclusion: The process of CNOOC became a multinational enterprise is a gradual process. By fully using and integrating of its internal strength and resources, the strong support from government, ensuring its competitive advantage and position in the domestic market as a premise, persisting in international development strategy, using flexible market entry mode and diversified development patterns, CNOOC had successfully achieved the transformation from the state-owned enterprises to multinational enterprise.
Acknowledgement

Finally, it comes to last stage of our master thesis. It is a tough time and it is later than other groups since we met a lot of problems during our thesis process. We had many different thoughts and arguments about the thesis, however, we have tried our best get through all the contradictions, both of us have learned how to cooperate and have a good communication with each other, which means a lot to us. During our thesis process, many people have helped us to make our possible. We would like to take this opportunity to express our gratitude to all those who have been encouraging us and giving us advice all the time.

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Authors,
Ye Li & Xin Tong
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1. Introduction

With the fast developing of Chinese economy, more and more companies are doing international business as internationalization had become an unavoidable trend for Chinese firms. Since the end of the 1990s of last century, after going out of the shade of Asian financial crisis, Chinese economy has been stepped into a ten years gold development age. During this period, the “high growth, low inflation” is the situation of Chinese economy, the growth rate of GDP is 12%. By taking this economic express, a lot of Chinese enterprise developed rapidly, some of them increased their profit reach up to 30%. The quantity of Chinese corporations which entered the Fortune 500 also increased fast. (Chinabyte.com, 2005)

As same as all other countries, natural resources are the basis of China relies for existence. Those state-owned enterprises in China which are doing the business of prospecting and exploitation of crucial resources such as petroleum, natural gas, coal, iron ore, etc. are mainly controlled by Chinese government (China security, 2006). By the reason of the world distributing imbalance and the limited reserves of the natural resources, Chinese state-owned energy enterprises have to join the competitions on international market.

For the reasons of the importance of energy resources and Chinese centralized regime, most of the Chinese large energy corporations are state-owned. As a consequence, on one the hand, these state-owned corporations cannot be internationalized easily as other private-owned companies. But on the other hand, the economic globalization forces these state-owned corporations which depend on the Chinese government to acclimate the new opportunities and risks of world market. Compare with other developed countries’ mature multinational corporations, Chinese state-owned corporations are inexperienced on internationalization. Chinese stat-owned enterprises are trying to discover their own internationalization mode by using the successful internationalization experience of foreign companies as reference. Although the way of mergers and acquisitions which adopted presently by many Chinese state-owned companies seems the most valuable way, but many of the attempts failed at the end, e.g. State Grid Corporation of China quit the public bidding of Philippine TransCo (NJLH.gov.cn, 2007); the Haier Group (China) failed on public bidding of MayTag the third biggest American kitchen and laundry company (Chinabyte.com, 2005); CNOOC gave up the invited public bidding of American Unocal Oil Corporation.
(CNOOC, 2005). To find an appropriately internationalized way has became the most urgent affair for all Chinese state-owned enterprises currently.

However, there are also many successful samples for the Chinese state-owned enterprises to walk onto world stage, such as TCL cooperate with THOMSON and ALCATEL which increased the TCL’s brand influence in the world market (Tcl.com, 2009.) Lenovo acquired IBM which is also very famous in the world, after the acquisition, Lenovo became the world’s third largest PC giant after DELL and HP. The acquisition sharpened Lenovo's competitive advantage in the global market by taking advantage of IBM's advanced technology and global sales network (Lenovo.com, 2009). And there are also lots of Chinese corporations through listed as good examples: China Telecom, China Netcom, China Mobile, China Unicom, Sinopec, Bank of China, Construction Bank, Bank for Trade and Industry, etc.

China National Petroleum Corporation, China Petrochemical Corporation and China National Offshore Oil Corporation are the three biggest state-owned energy corporations of China. The China National Offshore Oil Corporation (we will use CNOOC to replace it below) is the most internationalized oil corporation among them (Xinhuanet, 2005). During the company growing process, CNOOC try to take the full advantage of international capital market and energy market to become one of the biggest global petroleum and natural gas corporations by develop its domestic and international business areas continuously. The most impressive action of CNOOC is the acquisition for Unocal Corporation which is the ninth biggest oil corporation of America on 2005. Unfortunately, because of the intervener from American Congress, the acquisition was failed eventually. But it didn’t stop the process of CNOOC’s international acquisition activities (CNOOC.com, 2009).

The investigation of our dissertation could afford some good points of internationalization process for helping other inexperienced Chinese state-owned corporations. Our research will be submitted to the authority department of CNOOC as we will provide important theoretical information concerning their internationalization process. Some other researchers and scholars would have interests on our dissertation as well.

### 1.1 Background of the company

The China National Offshore Oil Corporation (CNOOC) is one of the largest state-owned oil giants, and it is one of the largest offshore oil and gas producers in China.

In 1982, Chinese government decided to introduce a popular international
model in oil industry worldwide, which named production sharing contract (PSC) to tap its offshore hydrocarbon resource. CNOOC was incorporated at that time, authorized under the Regulations of the People's Republic of China; it is allowed to exploit Offshore Petroleum Resources in Cooperation with Foreign Enterprises. By cooperate with overseas partners, CNOOC discovered many new offshore petroleum and gas fields, which have been steadily exploited. By the end of 2006, CNOOC had signed 182 petroleum contracts and cooperated with more than 76 petroleum corporations from 21 countries and regions. Now the headquartered of CNOOC is in Beijing, it has a total staff of 51,000 with a registered capital of RMB 94.9 billion. (CNOOC.com, 2009)

1.2 Research question

How CNOOC as a Chinese state-owned enterprise became a multinational enterprise?

1.3 Purpose of Study

The main purpose of this dissertation is to understand why CNOOC needs to be a multinational enterprise and what kind of expansion process that CNOOC is taking, which theories could explain those CNOOC’s internationalization activities. According to the successful experience of CNOOC, we will try to find an appropriate developing way for other Chinese state-owned enterprises.

1.4 The Choice of Theory

Relate to our case, we will focus on the growth of firm theory, the internationalization theory, and International Entrepreneurship as our core theories.
2. Method

In this section, to make readers understand our research approach, we will explain why we chose the target company how we perform our research process, how we collect primary data and secondary data and what sort of analytical approach we have chosen.

2.1 Interest

In recent years, an increasing number of Chinese firms become internationalized, among them, the Chinese state-owned enterprise perform pretty well. CNOOC is the one of the best, which the internationalization degree is very high, and its growth is very representative, even the Financial Crisis could not slow down its developing process, so we are very interested in the developing process of CNOOC. We believed, according the research and study of CNOOC’s development, we will find the generality of development of Chinese state-owned enterprise.

2.2 Access

There is another reason for us finally chose CNOOC because one of our members, Xin Tong is from Beijing and his parents are working in CNOOC. Thus, it is easier for us to get the primary information of CNOOC. Both of us think this is very important for our research.
2.3 research process

![Diagram of research process]

The research process began with selecting an interesting firm (CNOOC). At the same time, we selected an interesting topic, after collection some information and literature, the research questions and aim for the topic was decided. Then authors tried to build the whole framework, meanwhile, authors tried to collect qualitative data. According to analysis, it comes up the conclusion.

2.4 Data collection

Qualitative data will be collected by through interviews and secondary information. The primary data was mainly by interviews. The secondary data sources from websites, books, articles, journals, TV and so on. Our interviewee is a senior manager in the department of international development. He is very familiar with CNOOC’s international tactics.
2.4.1 Primary data

Primary data is information collected for the specific research by the researcher conducting the study, which offers a chance to collect data that is needed for the analysis. There are many ways to gather primary data. They could be mail or internet-surveys, interviews, observations and so on. Interview is the mainly we will use to collect primary data in this study, which could give us a better understanding and insight about CNOOC. The semi-structured interviews are mainly used. We made two phone conversations, and then made an appointment with the manager for a face to face interview, because the manager is very busy, so we only have one time interview, but this interview which helps us gain a lot of valuable internal information directly from the manager. The interview questions were constructed according the theories we chose, which most of the information is hard to find on internet or from books, and we also asked question about some recommended theories and how the theories applied in CNOOC. The interview was arranged on July. Our interviewee is Mr. Yang, who is the manager of international development department in Beijing. The interview was in Chinese and then we translated into English.

The interview questions:

Question 1: Compare with other state-owned petroleum companies, what is the competitive advantage of CNOOC?

Question 2: Facing the competition form the whole world, what have CNOOC done?

Question 3: What is the developing process of CNOOC? What strategy does CNOOC apply to enter in a new market?

Question 4: What is the role that government plays in CNOOC’s internationalization process?

Question 5: The acquisition of Unocal ended in failure, what are the reasons from your point of view? And what is the subsequent effect?

Question 6: How to fix the problem after mergers & acquisitions?

Question 7: Talk about your leader Mr. Fu Chengyu.

The responds from Mr. Yang of the main questions, authors will present in the finding part.
2.4.2 Secondary data

The secondary data and information mainly search via the database of MDH library, and we read many literatures about internationalization theories on related academic journals, articles and internet websites. We choose CNOOC’s official website, the source about the background of the company, the successful operation cases etc. and we choose the government website, as a state-owned company, the national policies and the tendency of the market will give CNOOC a bigger influence than some other firms. Watching some interview programs which is also a good way for collecting secondary data, it is more directly and more practical. Interview program is easy to find on internet, some organizations invited some successful persons who have rich experiences in some particular fields and interview them, which are welcome by Chinese spectators. We watched some interviews of the CEO of CNOOC Mr. Fu. We took a lot of useful information from the interviews. And most of the related journal articles form reliable search engines, like ABI/INFORM, Google Scholar, JSTOR and Emerald, etc. We insure those data we used in this thesis are reliable.

2.5 Data Analysis

In this thesis, we adopt the deductive approach. We study the theories which were already established, they were the concept of MNE, internationalization theories and entrepreneur theories. Most portion of this thesis would be done mainly using interpretive approach. The information which we have collected would be sorted since not all of them are useful for the thesis. The selected information and data are a good foundation for finding and analysis, which will be helpful for the conclusions.
3. Theoretical framework

In this section, we start with the definitions of state-owned enterprise and multinational enterprise, the development direction from SOE to MNE; then the market entry mode of internationalization, follows by the entrepreneurial perspective which is the internal factors of the transformation, and end with the relationship between politics and economy perspective.

3.1 SOE and MNE

3.1.1 State-owned enterprise (SOE)

According to the book ‘State-owned enterprise in the western economies’ which wrote by Raymond and Yair (1981), state-owned enterprises (SOEs) are the enterprises which managed by bureaucracy with values and objectives that can be distinguished from those of the public sector at large; they are the target of a complex set of pressures emanating from government offices and interests groups; they operate in highly imperfect market and are frequently in a position to make choices in those markets. These enterprises occupy the key positions in the national economies.

The history of SOE could retrospect to the ancient Roman time. For the reasons of the Great Depression and worldwide financial crises in 20th century, SOE developed rapidly as a result. During World War Two, many enterprises were taking governmental wartime tasks or taken over as properties of governments. After the war, governments also played an important role on recovering the destruction of industries. A plenty of nationalized companies were founded and took the key positions in strategic sectors such as energy, transportation, banking, etc. (Raymond Vernon, Yair Aharoni, 1981)

For economic reason, SOE could help government to sustain economy interests particularly, to develop and control crucial industries which need high financial support and high technologies that private enterprise can’t afford, to take high risk for private sectors and entire national economy, to accelerate the economy growth of low developed regions of the country. For social reason, SOE could help government to maintain social stability and equality by create new employments. For financial reason, SOE could guarantee the fiscal income for government and develop social welfare system. (Organization for Economic Co-operation and Development, 2005)
Along with the rapid growth speed of economy, the shortcomings of SOE (Low productive, lack of budget discipline, high financial burden, etc) had become more and more serious. The development of new technologies and increased globalization request those enterprises to be more flexible in the world market. Since 1980s, many SOEs started to be privatized to boost economy efficiency and growth (OECD, 2005, p22). Thereby, SOE had become a real entity which involved in market competition.

3.1.2 Multinational enterprise (MNE)

In John H. Dunning and Sarianna M. Lundan's literature (2008), they mentioned that a multinational or transnational enterprise is an enterprise that pursues foreign direct investment (FDI) affair, takes control over and manages production and services activities in other countries than the country where headquarters located. Ownership advantage, Location advantage and Internalization advantage (OLI) paradigm are the three elements of MNE. Ownership advantage is the precondition of other two, location advantage shows which country should company goes into, internalization advantage shows why company should internalized. According to Penrose (1959), Dunning and Lundan (2008), the firm is a collection of productive resources, in consequence, the ownership advantage should including the physical assert (‘plants, equipments, land and natural resources, raw material, semi-finished goods, waste products and by-products, stocks, unsold stocks of finished goods. etc), human resources (unskilled and skilled labor, clerical administrative, financial legal, technical and managerial staff), special knowledge, technology, and information. Grazia letto-Gillies (2005) developed the conception that the ownership advantage is also including the special access to markets, market position, knowledge of technology, knowledge of organization, knowledge of market, low cost innovation process and experience of international trade. The location advantage should take account for the differences of each country such as tax system, law, culture, etc. By seeking such resource and knowledge, company will locate the countries where these resource and knowledge exist consequently. In another word, it is a process of global resource and knowledge acquisition. The internalization advantage is the benefit from the inter-operation and hierarchy. These three elements are related by interaction effects. (Pitelis, 2007)

To judge an enterprise’s multi-nationality degree, Dunning and Lundan (2008) gave seven standards in their literature: the number or size of foreign units that the enterprise owns or controls; the number of foreign countries that the enterprise entered; the number or amount of assets, income and employees that the enterprise has in other countries; the degree of internationalization in management system; the international degree of research and development;
the degree of network in other countries; the extent of decision and strategy to commit resources into a specific foreign market or operations.

### 3.1.3 The direction of firm expansion

Each company will have a specific expansion direction by long-run profit motivation all the time. And the expansion is influenced by numerous external and internal factors. However, there also have some obstacles being in the way of expansion direction, some from outside and some from inside of the firm. Edith Penrose (1959) argued that the external inducements to firm expansion are to fulfill the new market requirement of production, to adopt new technology, to get more opportunities for better market position, to compete with market new entrants. The external obstacles are high cost and high competition on particular products and entry to new marker area, lack of special management personnel and technology, problems with new suppliers, non-government organizations and government. The internal inducements are unused productive services, resources and knowledge. The internal obstacles are normally the capability of managerial team and technical skills. The direction and modes of expansion is determined by these complications.

From Penrose’s view, resources are the key point of expansion. If a company has enough its own resources that the company already had and other resources that the company could obtain from new market, the expansion will succeed. To fully use the resources in the process of expansion, it requires diversification of production or service to meet the new situation in new markets. Enterprising firms should be innovative to combine those owned and unused productive services into new competitive advantages such as new services, new production or new administrative organizations. (Penrose, 1959)

### 3.1.4 Expansion through merger and acquisition

Why firms have to expand by merger and acquisition? Penrose believed that there is a growth limitation for any firm. When a company reached its critical point, it only has three choices: ‘to sell out, to stop growing significantly, or gradually to become more inefficient and fail’. The best option is to sell out to a corporation which has enough financial resources, enough productive resources that the company can’t afford. (Penrose, 1959) No company would be sold to others by a lower price than the present value of itself unless it comes to end. For small to medium size firms, they could be sold because of owner may want to quit from the business, or the business of company doing badly, or some capital liquidity problem. For large company, they would sell part of its own organizations or assets to reduce costs and concentrate on its main stream business. To those individual enterprising firms which are
developing significantly, there are two methods of expansion, set up new production facilities, new organizations and explore new market or acquire other corporations and markets which are already exists. In another word, merger and acquisition is part of the firm growing process. A successful company will choose to expand through acquisition or merger only when it is more profitable than internal expansion operations. (Penrose, 1959)

3.1.5 Diversification of MNE

Since firm is a collection of physical resources and services, thus, to break the limitation of growth it requires firm to be diversified of output by full use of already exist resources and more resources will be acquired. Diversification is to increase the diversity of production, to increase business integration and to increase the volume of market position. As a result, diversification will lead firm to create new production or services in new market with new technologies. (Penrose, 1959, p109-p120)

Diversification could be achieved by internal activities on doing research and development new technology or new inventions. On the other hand, it also could be achieved by acquiring other plants, or companies which already exist through merger and acquisition to reduce costs, obtain market position, managerial experience and other productive resources in new markets. Sometime, the acquisition method might be the only way for those companies that have weak financial support or extremely depend on unitary production. When firm can produce more new products or services, then it will get more customers from new domestic or foreign markets. (Penrose, 1959, p127-p140)

3.2 Market entry modes of MNE

3.2.1 Market entry modes

Obviously, to become MNE, state-owned enterprises need to go abroad. Normally they start their business in local market firstly, then go to the familiar markets in other areas of the home country and gradually expand their foreign operations to more distant and unfamiliar markets in other countries. To get into the foreign markets, firms should concern the strategy of market entry modes and make decisions. The choice of market entry mode is associated with the cost of market commitments and activities. (Mtigewe, 2006)

Each entry mode gives the volume of business that a firm plans to undertake in a market. The cost will include the mode set-up cost, recurrent fixed cost and
recurrernt variable cost. A given entry mode may have high fixed and variable costs at the planned volumes of business so that the cost of using that mode may not be recoverable. Therefore a firm will be internationalized via the most cost efficient mode at all times (Mtigewe, 2006). According to Hill Chareles (2007), there are six different modes to enter foreign markets: exporting, turnkey projects, licensing, franchising, establishing joint ventures with a host-country firm, or set up a new wholly owned subsidiary in the host country. Beside these, mergers and acquire an established enterprise in the foreign country to get local market position is also a commonly method for entry foreign market. When firms make decision, they should also concern ‘transport costs, trade barriers, political risks, economic risks, business risks, costs and firm strategy’ at the same time.

3.2.2 Joint venture

Many MNEs choose the Joint venture mode to establish a firm which owned by two or more independent firms. It is a very common way for firms to entry a new foreign market. The advantages are:

- It is reduce the psychical distance, a firm joint with a local partner, it will more familiar with the local condition, like the culture, language, political rules and competitive conditions. The foreign firm can gain knowledge from this and it good for the technology learning. Two companies could learn each other’s advanced technologies.
- Sharing the costs and risks, this is good for small firms or the starting stage of the firms.
- Avoiding some government interference, joint with the local partners will face a low risk of government interference.

3.2.3 FDI (Foreign Direct Investment)

According to Penrose (1959), the Foreign Direct Investment (FDI) is the action that acquiring or establishing productive organizations or other facilities abroad. Different from other internationalization modes, FDI has the high degree of control that other modes haven’t. There are three main reasons for firms invest abroad. They are market imperfections, financial factors and international product life cycle. The driving forces for invest abroad are: desire to find new market, access raw materials, achieve production efficiencies, gain new technologies, gain managerial expertise, enhance political safety of the firm’s operations, and respond to competitive in the external environment (Ball, 2008, P.93)
3.2.4 Merger and acquisition

Merger and acquisition is a short cut of FDI for large firms to entry other domestic or foreign markets, which are frequently used to pursue rapid growth for those enterprises which have abundant productive resources. According to Kou Huai (2008), merger and acquisition is a kind of economic behavior that an enterprise acquire operation controlling right and all or part of asserts from another (or more than one) enterprise by certain costs or price.

The larger the resources that the acquiring enterprise has, the easier it will be to obtain the acquired company. The reason why enterprises use mergers and acquisitions as the method is that it can help the firm to access into a new product or market area faster rather than gradually. Another reason for mergers and acquisitions might the acquiring company lack for more resource for growth or customers. When mergers and acquisitions happen, it means that a company acquires a brand, or takes a position and the distribution channels in other markets. However, this is a time-consuming, expensive path and full of risks (Burns, 2007 p.231). We should consider the product and market strategy when acquisition happens. Acquisition can maintain market position and give a competitive reaction to competitors. If a firm wants to develop a new products or a new market, and it does not have the capability to do so. At this time, the acquisition strategy could be considered even it has high-risk and uncertainty (Burns, 2007 p.232).

Kou Huai (2008) argued that there are three types of Merger and acquisition: horizontal Merger and acquisition; vertical Merger and acquisition and omnibus Merger and acquisition. The horizontal Merger and acquisition happens when the acquiring company and acquired company are in same industry. The vertical Merger and acquisition happens when the production of acquired company is the upstream or downstream production; the relationship between acquiring company and acquired company is supplier and buyer or producer and seller. The omnibus Merger and acquisition means the acquiring company and acquired company belong to different industries, different market and there is no direct connection of productive technology. The motivations of Merger and acquisition are: synergy effects (it is the result of scale economy merit which including enhancement of income, diminution of production cost, diminution of tax, diminution of capital cost); control benefits (take advantage by control the acquired company such as increase market share, offset productive weakness, reduce investment risk. etc); to create more value; driving of managerial advantage; expansion requirement; to obtain special knowledge, technology and human resource; to diversified business; to take underestimated assets; tax avoidance; and speculation. (Kou huai, 2008, p27-38)
3.3 Entrepreneurship in MNE

3.3.1 Risk taker and profit maker

Penrose (1959) argued that a company is not only a business organization but also an administrative organization. The decision makers are the actor of current market activities for example increase investment or reduce the commitment on foreign market and they make strategies for their corporations. They are both risk taker and profit maker. Entrepreneurial behavior of individuals and firms are the basis of the entry mode for foreign market.

According to McDougall and Oviatt (2005), the definition of internationalization entrepreneurship is the design; estimation and discovery of opportunities in the international marketplace and take advantage by create products and services. It is a comprehensive definition of which combines innovative, proactive and risk-seeking behaviors. Entrepreneurship including two parts, the first is opportunities taker or risk taker; the second are individuals who take advantage or profit from these opportunities or risks. Creating productive opportunities is a main character of entrepreneurship, and take advantage is the result of the entrepreneurship behavior.

Consequently, the entrepreneurship in multinational enterprise is an organizational process that to pursue productive opportunities and create the competitive advantages from foreign market associate with its own enterprise culture. The process of multinational expansion will be restricted when the enterprise can not see the opportunities, can not get profit or without drive which from proper organizational culture.

The entrepreneurial management strength of MNE which carried out by entrepreneurs is the function to lead the whole enterprise and its subsidiary to the innovation of technology products and markets (Alain and Wenlong, in MIR 2007, p243). From a Penrose perspective, entrepreneurship is always related with personal characters and individualities. Paul Burn (2007) defined that “Entrepreneurs use innovation to exploit or create change and opportunities for the purpose of making profit. They do this by shifting economic resources from an area of lower productivity into an area of high productivity and greater yield, accepting a high degree of risk and uncertainty in doing so." The most restrictive thing for MNE’s expansion is entrepreneur’s lack of interests on new productive activities and new geographic places.
3.3.2 Entrepreneurial culture in MNE

Dimitratos & Plakoyinnak (2003) suggested that the international entrepreneurship should take account of organizational culture as well. A proper multinational enterprise culture should be expressed through six dimensions: international market orientation, international learning orientation, international innovation propensity, international risk attitude, international networking dimension, and international motivation (Dimitratos & Plakoyinnaki, 2003, p. 194).

3.3.2.1 International market orientation

According the requirement of customers in foreign markets, firms adopt behavior to create value. Narver and Slater study (as cited in Dimitratos & Plakoyinnaki, 2003, p. 194) there are three elements of market orientation: customer needs, inter-functional coordination and competitor orientation. Inter-functional coordination means make use of all corporate resources to create a market responsive firm. And competitor orientation means through the rapid response to create the competitive advantage.

3.3.2.2 International learning orientation

International learning orientation has three steps; the first is the information acquisition, and then is the information dissemination, the last is information use, through these steps, firms obtain and use its advantage intelligence actively on foreign markets. (Moorman, 1995, as cited in Dimitratos & Plakoyinnaki, 2003, p. 198) the purpose of this culture formation is to create an adaptation firm in the external environment.

3.3.2.3 International innovation propensity

Firm pursuit competitive advantage through creative ideas, products, services, or processes designed in foreign markets (Lumpkin and Ddss, 1996, as cited in Dimitratos & Plakoyinnaki, 2003, p. 199) innovation is a significant behavior for a MNE.

3.3.2.4 International risk attitude

International entrepreneurial firms are likely to do some risk-taking behavior in the international marketplace. International risk attitude means firm is prepared
to undertake some risky behavior in foreign markets (Miller and Friesen, 1978, as cited in Dimitratos & Plakoyinnaki, 2003, p. 200). Risk attitude is vital for a international entrepreneurial firm, because innovation is a significant behavior for it, and sometimes innovation behavior will take risk for a firm. Always keep the risk attitude is a good character of International entrepreneurial firm.

3.3.2.5 International networking orientation

International networking refers to firm gain advantage through alliance or social embeddedness to use in its activities in foreign markets. (Granovetter, 1973, 1985; Gulati, 1998, as cited in Dimitratos & Plakoyinnaki, 2003, p. 202)

3.3.2.6 International motivation

Human capital is the key force for the firm to take advantage of entrepreneurial opportunities in the across nation border. Motivation should make organizational participants have good performances. The meaning of international motivation is to lead and energized the human behavior of organizational members regarding ventures in the international marketplace. (Geen and Shea, 1997, as cited in Dimitratos & Plakoyinnaki, 2003, p. 203)

3.4 Political influence on growth of MNE

The internationalization process of multinational enterprise is concerns the role of the state in shaping what activities are carried out by the enterprise; the influence of state policy on its strategy and industrial relations; opportunities for MNE to take advantage from multiple states by influencing capability of its home country government (Westney, 2005). As a consequence, when doing international expansion, MNEs will carry the specific institution characteristics of their home countries at the same time. It is relating to the level of commitment, the choice of foreign market entry mode and multinational activities (Mauro & Sandra, in Ghoshal & Westney 2005, p123).

According to Mauro & Sandra (2005), institutions have both two characteristics: constraining and enabling. They direct actors, guide actions and limit behaviors. However, institutions also help actors to “engage in socially meaningful actions by making them legitimate and knowledgeable in a given situation”. As a consequence, MNEs are sometimes regarded as ‘intruders’ or ‘contributors’ by local institutional system of foreign market when they attempt to enter the market. In highly sensitive industries as oil, mining, and public utilities sometimes foreign MNEs are looked as villains to be
avoided so as to ‘preserve national sovereignty and independence’. The balance of bargaining power between foreign country and MNEs is delicate. The bargaining power of foreign country will increased when the country owns the resource that the corporation wants or with the degree of competitions and number of competitors in the foreign market. The institution conflicts between them arise from the interface between the political environment and the corporation’s behaviors, especially the routine functioning of the political process.
4. Finding

In this section, we present the growing process of CNOOC, the two happened significant overseas merger and acquisition events, the chairman of the company and the answers of the interview.

4.1 The growth of CNOOC

China’s offshore oil industry started from 1957. After Chinese government began to execute reform and opening-up policy, China’s offshore oil industry field was firstly opened to the world in 1980s. After 30 January 1982, the ‘Regulations of the People's Republic of China Concerning the Exploitation of Offshore Petroleum Resources in Cooperation with Overseas Partners’ was promulgated by the Chinese State Council, Chinese government decided to establish their own oil enterprise -- the China National Offshore Oil Corporation to develop Chinese offshore oil industry. CNOOC was granted by government to completely take charge of the business of exploiting oil resources and international cooperation with overseas partners. Since it established, unlike other Chinese state-owned corporations, CNOOC took an entirely new mode of all-round opening to the world and extensive international cooperation on introducing capital and advanced technology. (CNOOC.com, 2009)

Till present, the leader group of CNOOC has changed for five times, but the internationalization strategy of CNOOC had never changed. The first leader group started the relationship with foreign partners and began to participate in international bids. The second leader group adopted the principle of conducting cooperation with foreign collaborator. The third leader group established and implemented trans-global strategic objectives and the high-speed and high-efficient development of the corporation began to take shape. To increase the corporation's international competitive advantage, by the fourth leader group leadership, CNOOC successfully entered the international capital market in New York and Hong Kong stock markets on 2001. The present leader group is led by Mr. Fu Chengyu who initiated so far the biggest international merger and acquisition of Unocal (American) with about 18.5 billion dollar. CNOOC now is becoming one of the top energy companies in the world (CNOOC.com, 2009).

During the international cooperation with the overseas partners which are including many world famous oil companies such as BP Global Oil Company, Shell, Exxon Mobil, etc., CNOOC accumulated much through learning and
exploring process. The internationalization process of CNOOC has two stages: the first stage is from 1982 to 2000. In this stage, CNOOC mainly focus on China’s inshore oil and gas exploration by foreign capital, technology and management experience. Within the development of overseas cooperation, CNOOC extent its cooperate operations continually. From 2001 to present, especially after successfully enter overseas stock market, CNOOC gradually started to become a real competitor in the foreign market by overseas merger and acquisitions. Until end of 2006, CNOOC already explored 24 inshore oil fields with overseas partners and signed 172 cooperation contracts and agreements with 78 oil companies of 23 countries and regions (CPEChina.com, 2007). Through the internationalization strategies, assets reforming, overseas mergers and acquisitions, combination of upstream and downstream businesses, the company has strengthened its competitive ability and shaped into a highly efficient international oil corporation. According to the annual report of year 2007, CNOOC had achieved sales of 162.0 billion Yuan and net income profit of 56.5 billion Yuan. The total and net assets had reached 300.0 billion Yuan and 170.0 billion Yuan (CNOOC Annual Report, 2007).

**Figure 2 CAGR: Compound Annual Growth Rate of CNOOC**

Financial Data

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
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<tbody>
<tr>
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<td>25.4%</td>
<td>48.9%</td>
<td>22.1%</td>
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<tr>
<td>Income growth</td>
<td>61.7%</td>
<td>60.1%</td>
<td>26.3%</td>
<td>15.2%</td>
</tr>
<tr>
<td>Net profit growth</td>
<td>61.8%</td>
<td>62.3%</td>
<td>25.5%</td>
<td>15.1%</td>
</tr>
<tr>
<td>Assets growth</td>
<td>27.9%</td>
<td>24.9%</td>
<td>31.0%</td>
<td>23.3%</td>
</tr>
<tr>
<td>Return on equity</td>
<td>15.5%</td>
<td>20.3%</td>
<td>19.8%</td>
<td>18.1%</td>
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<tr>
<td>Return on assets</td>
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<tr>
<td>Gross margin</td>
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<td>36.8%</td>
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<tr>
<td>Debt to assets ratio</td>
<td>32.6%</td>
<td>31.3%</td>
<td>27.9%</td>
<td>26.2%</td>
</tr>
<tr>
<td>Accumulated ratio of capital</td>
<td>21.3%</td>
<td>27.0%</td>
<td>30.0%</td>
<td>22.3%</td>
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**Figure 3 Annual Financial Data of CNOOC (2004-2007)**

As a state-owned corporation, the internationalization process of CNOOC filled with distinct political flavor from its establishment to now. CNOOC was founded by Chinese State Council and managed by Chinese Ministry of Petroleum Industry. On July 1988, the ministry was abrogated and replaced by the department of energy functioned governmental management. On 1996, the department of energy was abolished, CNOOC then was in charged by State Development Planning Commission. Economic and Trade Commission took over it since 1998. Now CNOOC is under the supervising of State-owned Assets Supervision and Administration Commission of the State Council (SASAC) (CNOOC, 2009).

**Figure 4 Annual Payments to Government (1982-2007)**
4.2 Mergers and acquisitions

Mergers and acquisitions are the main ways for the firm’s expansion. It is also a strategy of CNOOC. The acquisition of American Unocal and the acquisition of Awilco of Norway are the most outstanding and meaningful examples.

4.2.1 The acquisition war of Unocal

Even though CNOOC declares over and over again that CNOOC is an internationalized corporation, but it can hardly seemed as an independent business entity by other countries when CNOOC doing overseas merges and acquisitions. The most typical example is the acquisition war of Unocal (American) Oil Company between CNOOC and American Chevron Corp., the second-largest U.S. oil company on 2005.

Before the acquisition, many members of the United States Congress already had extremely dissatisfied with the Chinese government about the RMB exchange rate, textiles-dumping and intellectual property issues which unresolved for a long time. The U.S. Congress was preparing a series of proposals, trying to resolve the trade disputes between China. None of the above-mentioned issues have signs of the time to resolve, the acquisitions became more complex. On June 17, the California Republican Congressman Pombo (Richard W. Pombo) and Hunter (Duncan Hunter) sent a letter to the White House, urging President Bush to protect national security in accordance with a federal bill which passed by the appointment of Treasury Secretary in 1988; appointed John Snow, the president of the United States Foreign Investment Committee to do a comprehensive review of the acquisition (New York time, 2005).

Until June 23 2005, CNOOC announced a merger proposal by an 18.5 billion USD all cash bid for Unocal, the acquisition was strongly opposed by American politicians again. Another 41 Democratic and Republican parties jointly sent a letter to members of the Bush administration to ask the Ministry of Finance to investigate the case, check the transfer of technology and assets of Unocal Corporation whether or not pose a threat to American national security. They specially referenced in the letter that the competition between Chevron and CNOOC is unfair because CNOOC is supported by Chinese government’s sponsorship, but Chevron have failed to get such treatment. On June 30, the U.S. House of Representatives adopted a legally non-binding motion by 398 votes in favor and 15 votes against to calling on the Bush administration to reconsider the acquisition of Unocal (Peopledaily, 2005).

Compare with the powerful rival, although CNOOC gave a more than 1.5
billion higher offer and promised CNOOC will retain employees and managerial team of Unocal but it underestimated the strength of the U.S. political cycles. Under the obstacles and pressures from American politicians, CNOOC had to withdraw its acquisition offer for Unocal Oil Company at the end.

4.2.2 The acquisition of Norwegian Awilco

CNOOC never stop its target to buy a western oil firm since the failed bid for Unocal in 2005.

Awilco offshore is an international offshore drilling contractor. It established in January of 2005, and listed on Stock exchange of Olso in May of 2005. It provides drilling services for other oil companies. Its business scope covers Norway, the Us, Singapore, India, Brunei, Malaysia, Australia, Vietnam, Saudi Arabia, China and Mediterranean 11 countries and regions. This company has 5 newly-launched self-elevated drilling platforms, 2 accommodation platforms, with 3 launched self-elevated drilling platforms and 3 semi-submersible platforms in the process of construction, and there are also 2 further semi-sub (Maverick Chen, December 18, 2008). It owned the world’s eighth largest fleet of oil rigs, and had the world classic technology.

On 08th, July, 2008, CNOOC launched a US$2.5 billion buyout of Norwegian offshore-oil firm Awilco. CNOOC should pay 85 kroner for each share, and there is an 18.7% premium to last week’s closing price. This is the highest price for oversea acquisitions of Chinese state-owned company.

Four days later about this acquisition, the price of crude in the NY futures market hit a record breaking US$147.27 per barrel. But on December 5th, the oil price fell to US$40 per barrel (Maverick Chen, December 18, 2008). According this, the chairman of CNOOC Fu Chengyu did not worried about it, as he said, he did not see anything wrong with this purchase, and they were buying the technology for offshore oil-drilling not the oil itself. This acquisition became the most technological acquisition of Chinese energy enterprises, and it is also the first victory of Chinese state-owned enterprises overseas acquisition.

4.3 Fu Chengyu – the Chairman of CNOOC

The president Fu Chengyu was born in 1951. He is geology Bachelor of Northeast Petroleum Institute of China and he also received a Master's degree in Petroleum Engineering from the University of Southern California in the United States. He has over 30 years of experience in the oil industry and he worked in China’s Daqing, Liaohe and Huabei oilfields in succession
(CNOOC.com, 2009). He worked started from very basic work, like drag for the sand for the drilling crew, and he did the dragging job for three years. He grew up from the basic unit, so he had deep basic training.

In 1982, he joined CNOOC. He served as the Chinese Deputy Chief Representative, Chief Representative, and Secretary to the Management Committees and Chairman of the Management Committees formed through joint ventures between CNOOC and Amoco, Chevron, Texaco, Phillips, Shell and Agip respectively (CNOOC.com, 2009). From 1994 to 1999, Mr. Fu was the Vice President of Phillips China Inc. During this period, there were about sixty or seventy American-European staff members working for him, so he was very familiar with the occidentals’ working way.

In September 1999, he was coming back with full of international working experience, who appointed as an Executive Director, an Executive Vice President and the Chief Operating Officer of CNOOC Limited, a subsidiary of CNOOC. In August 2002, he was appointed Chairman of the Board of Directors and Chief Executive Officer of China Oilfield Services Limited (COSL), a subsidiary of CNOOC. Currently he is the Chairman of COSL. Since October 2003, Mr. Fu has served as President and Party Leadership Group Secretary of CNOOC. (CNOOC.com, 2009)

After his getting back to CNOOC, he gave full play of his international experience. CNOOC was seen as the most international state-owned enterprises of China, there are 8 members of board of directors, 4 of them are the foreigners or external personage, so the director’s meeting was always in English, this could not be imagined for a state-owned enterprise.

4.4 Interviews

Question 1: Compare with other state-owned petroleum companies, what is the competitive advantage of CNOOC?

The others should be PetroChina and Sinopec, and we are all state-owned energy enterprises. Compared with PetroChina and Sinopec, we should say we are still young. Both of them are very good petroleum companies, and they did very good job in the world market. We are not completely competition relationships. We will not do the industries which they have already developed, which is our differentiation developing strategy. But to a certain extent, the competitions exist, as the biggest offshore oil company; obviously, there are more resources which are waiting for us to develop. But the main competitive advantage should be the internationalized degree. We have a higher level
degree of internationalization. These make us have a higher efficiency in the international marketplace, which you can see from the growth speed, even in the economic crisis of last year, we also have a good developing rate. This can be proved by the annual report of CNOOC in 2008.

![Figure 5 Compound Annual Growth Rate](Resource: CNOOC Annual Report 2008)

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![Figure 6 Financial Data of CNOOC](Resource: CNOOC Annual Report 2008)

And we also have a sustainable development idea, which is a vital part for the future competitive. We want to make CNOOC to be a world-class big firm. But we know the resource of petroleum is limit, finding some substitute of petroleum is also a developing way of CNOOC. Now we are researching and developing offshore wind energy technology and so on, which make some certain achievement, now I could not say it can substitute the petroleum resources in the future, but this is definitely an important technology of company’s sustainable development. To sum up, we choose a sustainable strategy, but in the competitive area, our competitive advantage is the higher degree of internationalization.

**Question 2:** Facing the competition form the whole world, what have
CNOOC done?

There are a lot of things to do, especially in these years. We had to face to worldwide economic crisis. We are mainly focus on diversification. This embodies in the integration of whole oil industry, we try to develop upstream to downstream and the exploitation of new energy and production. In the upstream, in 2008, the company continued to achieve good results in exploration, with 13 new discovers and 11 successful appraisals. The net profit amounted to RMB 44.38 billion, representing an increase of 42% year over year; it is a new record for CNOOC.

In the mid and downstream, CNOOC Gas & power Group is the main force. In 2008, 11 shareholding construction projects and 3 front-end research projects progressed on schedule, and 2 oversea acquisitions with Qatargas and Total were done. The refining segment is another main force into mid and downstream business. Huizhou Refinery project is the first large-scale downstream project by CNOOC. The annual capacity is about 12 million tons. It is the largest single train refinery in China and the refinery specially designed to process high acid heavy offshore crude in the world. In downstream products, the 36-1 heavy traffic bitumen and low sulfur fuel oil open up new markets and begun to export to Chad and Zanzibar in Africa. In 2008, CNOOC produced 1.95 million tons of urea and 690000tons of methanol. The revenue is RMB 5.52 billion and a gross profit is RMB 2.04 billion.

We also focus on the developing of new energy. The new energy is a sustainable development idea, which is a vital part for the future competitive. We want to make CNOOC to be a world-class big firm. So finding some substitute of petroleum is also a developing way of CNOOC. New energy business mainly covers the wind power, biomass energy, clean coal energy, solar energy, hydrogen energy and CDM. In the field of wind power, the power project in Inner Mongolia and Hainan are ready for construction soon. About biomass energy, Hainan project started construction.

**Question 3: What is the developing process of CNOOC? What strategy does CNOOC apply to enter in a new market?**

The developing process of CNOOC is also the internationalization process of CNOOC. We are not just focus on the Chinese market; we also pay lots of attention to the world market. The internationalization of CNOOC is an incremental process. Now it is the third biggest petroleum company in China. CNOOC was born in 1982 as a state-owned company, the government decided to make it internationalized. I think it is a born-global company, from 1982, it has began its internationalization way. In 1993, we had a big change. We reformed the four old companies, and turned them into four regional companies.
and 10 specialized companies. In 1999, we had a great change too. From that year, the key enterprises were listed, which were a big step of internationalization. In 2005, we finished the internal structural adjustment, mainly operate the international business.

At first, we cooperate with some foreign companies, by ways of turnkey projects and joint ventures, after we got bigger and had enough funds and advanced technology, we prefer to FDI or mergers and acquisitions. They are the main methods we were using recent years.

**Question 4: What is the role that government plays in CNOOC’s internationalization process?**

Since CNOOC established, our company had got much attention and support from central government and local governments. Government created a well conditioned market for our development. From this perspective, government is the strongest backup force for CNOOC’s internationalization.

**Question 5: The acquisition of Unocal ended in failure, what are the reasons from your point of view? And what is the subsequent effect?**

This is the biggest oversea acquisition of Chinese firms in the history. The amount of acquisition is about 18.5 billion dollars, which did not only shake the petroleum industry and capital market of the world, but also brought U.S. government’s attention at the same time. On 23rd, June, 2005, CNOOC proposed to acquire UNOCAL, the next day, 41 congressmen of the US Congress jointly appealed to stop this acquisition. After one month, we decided quit this acquisition, and this acquisition failed. To my point of view, the reason of this failure is the work of public relations with U.S.A. did not done well before; we should do it 1 or 2 years before the acquisition.

Talking about the influence of this failure, lots of people thought this failure blocked the internationalization steps of CNOOC. Actually, we should say it is not a block for CNOOC. During the first month of acquisition, the stock of CNOOC rose to 30 billion dollars from 22 billion dollars. And it increased a sum of intangible assets for our company, which increased the position of our company in the world, and the popularity of the brand and its influence power. I have to say it is a fantastic advertisement, after that, CNOOC jumped onto the world stage. It is well-known as a power company, and this took a lot of opportunities for our future developing, and lots of companies proposed cooperation initatively.

**Question 6: How to fix the problem after mergers & acquisitions?**

26
According the statistics, in the case of mergers & acquisitions, 70% of them are not successful. One of vital problems is the combination of culture. As we know, culture change is a slow process. But this is not a problem for us. Our culture is a kind of entrepreneurship culture, the new acquisition company would be a part of our big family, this is the character of our cultures. And this culture makes us easily finish the acquisitions again and again.

**Question 7: Talk about your leader Mr. Fu Chengyu.**

Our boss is really an entrepreneur, he is good at creating opportunities and then hold of those opportunities. In 2005, his bold decision of acquisition of Unocal make the whole world shocked, form then, he and his CNOOC became famous. After that he won the respect of western countries. He brings the innovation mind to CNOOC, in 2008, he said by the overlook of great environment of enterprise’s development, he thought economic crisis, environment crisis and resource environment are the three challenges for our industry; innovation is the way to go. He is the kind of boss, who always has new ideas.
5. Analysis

In this section, our analysis starts with the roles that CNOOC plays on economical and political perspectives; what is the specialty of Chinese SOEs; if CNOOC is a real multinational corporation; why CNOOC using merger and acquisition to expansion; why CNOOC needs to be diversified and how entrepreneurship and entrepreneurial culture embodies in the expansion process of CNOOC.

5.1 A double-role MNE -- CNOOC

5.1.1 The role of SOE in national economy

To view the throughout history of the state-owned enterprise in Western countries, we found that most SOEs are the outcome of market activities. According to OECD (2005), there are four derivations: national monopoly, public goods demand, particular goods requirement and external effects. First, SOE is an embodiment of national monopoly. SOE can minimize the costs from regular market competition, and SOEs can get stable raw and processed materials, services from internal suppliers, customers or financial support from governments. Second, the quantity and the quality of public facilities and goods need strong supervising from government. Third, some special goods such as medical facilities or education require the provision from SOE. Forth, to eliminate the negative impacts from out-of-order market competition and overproduction, to adjust the balance of social resource distribution, it is necessary to develop a certain degree of SOE in national economy (OECD, 2005, p20). SOE still playing a decisive strategic role in national economy and it is an integral part of national economy.

Chinese state-owned enterprises were established as a result of Chinese socialistic and planned economic system. Since 1978, the policies of reform and opening up had performed and implemented in China for 30 years. Chinese SOE had been through three developing phases: highly centralized planned economic system time, from highly centralized planned economic system to market economic system time, from market economic system to internationalization time. Presently, more and more Chinese SOEs are trying to become multinational enterprises by establishment of modern enterprise system.
5.1.2 The relationship between SOE and government

The relationship between SOE and government is an interdependence relationship. On the one hand, the development of state-owned enterprises needs to rely on government support; On the other hand, government needs state-owned enterprises to control country’s economic lifeline, to sustain emerging industries, to solve employment problem, to obtain taxes.

From the all aspects, CNOOC undoubtedly is a state-owned enterprise even it is the most internationalized company that compare to other Chinese state-owned enterprises. CNOOC can not get rid of the identity and governmental responsibility because of the specialty and importance of offshore oil industry in the national economy. As we written above, every government has two kinds of functions: constraining and enabling. According to Chinese present regime system, economy system and degree of market development, the governmental intervention for present China’s national condition is necessary. The function of Chinese government also has two side effects on Chinese state-owned enterprise’s expansion process especially on merger and acquiring. For negative, overmuch political flavor will develop into the opposite direction. For instance, when CNOOC tried to acquire Unocal, western media and American government was too fussy to CNOOC’s political background. They even thought the acquisition had threatened Unite States national security. For positive, good political environment and relationship is the precondition for cooperation. For example, the good relationship between Chinese government and Nigerian government reduced risk when CNOOC bought oil exploration interest from Nigeria on 2006 (Caijing.com.cn, 2009).

5.1.3 From SOE to MNE

At present, the worldwide community of large-scale production networks has been formed, the traditional growth mode with natural resources, product-based division of labor pattern has been broken, the activities of multinational corporations in the world economy increasingly evident in the prominent role. The trend of globalization requires companies to be internationalized. Internationalization of Chinese SOE’s operations is the inevitable but also unavoidable trend of economic development. Foreign Multinational corporations already came into Chinese market for quite a long period of time. To respond the challenges of foreign MNEs, the best way is to become multinational enterprise. Indeed, for the internationalization process of the enterprises, there are not only significant opportunities, but also need them to face enormous risks and challenges. Opportunities come from the accumulation of capital, technology and economic results, how to use domestic and international markets effectively; internal and external productive
resources. The ultimate aim is to strengthen the country's economic strength. To seek a position in international market, SOE not only can make their own development of enterprises and improve the competitiveness of the basic strategic planning, it is also the pressure and power to force the enterprises to circumvent the existing constraints and limitations, seeking the path of self-innovation and expand the living space.

Offshore oil industry is a high investment, high risk and high technology industry. These characters forced CNOOC to go abroad to seek omnidirectional international cooperation to attract foreign capital, obtain new advanced technologies, to reduce risks and uncertainties. CNOOC is playing a double role as an economic entity which is affected by markets and a political unit which is controlled by bureaucracy at the same time. For most of the Chinese state-owned enterprises, it is a thorny and suffering journey to become a real multinational company. However, since CNOOC successfully entered the international capital market in New York and Hong Kong stock markets on 2001, only in less than 3 years, its proportion of main production such as overseas oil and gas production has increased sharply from less than 3% to the nearly 25%, laying the foundation for CNOOC to become an international energy company (CNOOC.com, 2009).

After 27 years of development, CNOOC has more than 70 percent asserts from foreign stock market; 20 percent overseas recoverable reserves of offshore oil and 25 percent overseas oil and gas production; It spent 1.23 billion U.S. dollars successfully completed three major overseas oil and gas mergers and acquisitions since 2008, and became one of the world's top-class international oil and gas developers like BP, Shell and other international oil companies. CNOOC has signed more than 150 contracts, agreements about producing, distribution, technology with 70 companies in 18 countries and regions, directly used 9 billion U.S. dollars of foreign capital. The number of foreign workers has reached 1,000 (CNOOC.com, 2009). To a certain extent, CNOOC has become a real multinational enterprise.

5.2 Merger and acquisition

As Penrose (1959), there is a growth limitation for any firm. When a company reached its critical point, there will be three results for the company, to sell out, to stop growing significantly, or fail at the end. On the other side, for a firm, there are two methods of expansion, develop new market or new products; or acquire other firm which is already exists. At this time, when a company wants to sell out and when a company wants to buy, the mergers and acquisition come out.
Mergers and acquisition are good way for a firm who wants to expand. For CNOOC, there are two types of mergers and acquisitions which CNOOC mainly used: horizontal mergers and acquisition and vertical mergers and acquisition. The horizontal mergers and acquisition means the acquisition happened in the same industry. The vertical merger and acquisition happens the production or the business in the upstream or downstream of acquired company.

Mergers and acquisition are the main way for CNOOC’s expansion. As a state-owned firm, CNOOC has a lot of resources and the larger the resources that the acquiring enterprise has, the easier it will be to obtain the acquired companies. Mergers and acquisition are not only for CNOOC’s expansion, it can help CNOOC to access into a new market area faster. Now CNOOC holds the exploration rights in America, Norway, Kenya, Equatorial Guinea and offshore Australia. After these acquisitions, it is much easier for CNOOC to develop its industries in these places. Another reason for mergers and acquisitions might the acquiring company lack for some resource for growth. The acquisition of Norwegian Awilco is a good example. About this case, if we can say the acquisition of Unocal make CNOOC famous in the world market, we could say the acquisition of Awilco make CNOOC real stronger.

Awilco offshore is an international offshore drilling contractor. The technological is what CNOOC wants, it is really important for the development of CNOOC, even the price of acquisition of Awilco is pretty high, but their technology is vital, this kind of resource is good for the growth of CNOOC.

The mergers and acquisition strategy is successful in CNOOC, most of the acquisition request was end up with successful. Only the acquisition of Unocal ended in failure, which was the biggest oversea acquisition of Chinese enterprises in the history. But even it was failure; it still did not block the developing process of CNOOC in the world market place. After that, CNOOC became a well-known powerful international company; the reputation would create more opportunities for its development in future.

Another reason that CNOOC should insist mergers and acquisition strategy is from the consideration of upstream industries. In the worldwide, most of the oilfield have been exploited by old petroleum corporations. As a new petroleum corporation, a lot of the oilfields have been taken, so if CNOOC could acquire some old petroleum corporations, it means to obtain the oilfields, and this reduced the cost and risk. From exploring, construction and investment, finally to obtain the oil, the process needs long time and full of risks.
5.3 Diversification development

Diversification is to increase the diversity of production, to increase business integration and to increase the volume of market position. As a result, diversification will lead firm to create new production or services in new market with new technologies. (Penrose, 1959, p109-p120) It will help the company create competitive advantage in the market place.

As Mr. Yang said, CNOOC is choosing a different developing strategy that mainly focuses on diversification (Yang, personal communication, July, 2009). CNOOC had developed an integrated oil industry construction from upstream to downstream industries by developing new energy and productions. It is really hard for a petroleum corporation to unify its upstream and downstream industries, but CNOOC did it. In the upstream, CNOOC achieve good results in exploration. And increasing 42% in 2008, which is a new record for CNOOC. In the mid and downstream part, the revenue in RMB 5.52 billion and a gross profit is RMB 2.04 billion in 2008. Because of the diversification strategy, CNOOC could still perform so well even in the economic crisis year.

5.4 Entrepreneurship in MNE

According to McDougall and Oviatt (2005), the definition of internationalization entrepreneurship is estimation and discovery of opportunities in the international marketplace and take advantage by create products and services. It is a comprehensive definition of which combines innovative, proactive and risk-seeking behaviors. From the definition, we can find there are two steps of entrepreneurship behavior. The first step is finding or creating the opportunities, the second step is trying to make profit in the opportunities. But every opportunity has risk, so entrepreneur are both risk taker and profit maker.

CNOOC is investing to exploit oil in the worldwide, that is a big cost, and the risk is high. But take the Chinese government as its backup force. It has more ability to undertake the risk. Utilizing the good relationship China and some Africa and Middle East countries, even some of these counties are turbulence, some old oil companies do not dare to invest there, but CNOOC dares to undertake the risk, dares to invest there and dares to take the first step and to be in front of other oil companies. These are all entrepreneur behavior.
5.5 Entrepreneurial culture in MNE

Entrepreneurial culture is important for CNOOC and CNOOC works hard to create entrepreneurial culture. Leading by Fu, Chengyu, CNOOC had becomes a firm full of vitality. Mr. Fu was the Vice President of Phillips China Inc. during 1994 to 1999. There were about sixty or seventy American and European staff members working for him, so he was very familiar with the occidentals’ working way. After his getting back to CNOOC, he gave full play of his international experience. CNOOC was seen as the most international state-owned enterprises of China, not only because there are eight members of Board of Directors, four of them are foreigners or external personages, and the director's meeting is always in English, but also because of all the CNOOC staff consider questions under the international background and they have the international innovation sense and the international risk attitude. And all this come to the entrepreneurial culture of CNOOC, which helps CNOOC fix the gap easily after mergers & acquisitions.
6. Summary and Conclusion

6.1 Summary

Our paper has concentrate on the growth of CNOOC and the main influencing factors for its internationalization process. We have tried to explain how CNOOC became a multinational enterprise successfully from a state-owned enterprise. In the theoretical framework section, distinguishing from other types of enterprise, we gave the definitions about state-owned enterprise and multinational enterprise. We used the seven standards which Dunning and Lundan (2008) described as the method to judge if an enterprise is a real multinational one. To understand the internal and external drivers about why state-owned enterprise needs and has possibilities to turn into multinational enterprise, we used Penrose’s theories about growing direction of firm, the merger and acquisition way of expansion and the necessities to be diversification.

A proper international market entry mode often determines company’s ability to successfully penetrate foreign markets in other countries; it is also a key to become multinational enterprises in a real sense. Merger and acquisition is a wise way for those enterprises which have adequate resources. Leadership or entrepreneurship is an indispensable factor for company’s expansion. Associated with entrepreneurship, entrepreneurial culture is an inducement for enterprise to participate in international market competition. The political or institutional factors cannot be ignored during the growing process of enterprise, especially for state-owned enterprise.

In the finding section, we presented the growth of CNOOC, two important acquisition actions and Fu Chengyu, the chairman of CNOOC. Except the secondary information, we got primary information through an interview with an inner manager of CNOOC. The content of the questions for the interview includes the advantages which CNOOC has, the industry construction of CNOOC, market entry strategy, merger and acquisition, the relationship with government, entrepreneurial culture and entrepreneur. In the analysis section, we compared the state-owned enterprise in the Occident and China. And it was confirmed that state-owned enterprise is a unity which has both economic and political traits. Political factor sometimes has more influence than economic factor. For the aim of long-run profit, state-owned enterprise need acquire more resources and to be diversified. The entrepreneur of state-owned enterprise is profit maker and risk taker. Entrepreneurial culture comes from all the members in an enterprise.
6.2 Research Conclusion

Our research question is ‘How CNOOC as a Chinese state-owned enterprise became a multinational enterprise?’ Through our arguments and analysis, we reached the following conclusion:

The process of CNOOC became a multinational enterprise is a gradual process. By fully using and integrating of its internal strength and resources, the strong support from government, ensuring its competitive advantage and position in the domestic market as a premise, persisting in international development strategy, using flexible market entry mode and diversified development patterns, CNOOC had successfully achieved the transformation from the state-owned enterprises to multinational enterprise.

6.3 Recommendation

The successful experience of CNOOC set a good example for the other Chinese state-owned enterprises. There are some the recommendations for those Chinese enterprises who want to go abroad:

First, establish the International Development Strategy. The Central part of the internationalization strategy is continuously innovating to improve the international competitiveness of enterprises. It is not only the demand of the enterprises themselves, but also the trend of economic globalization, the need of improving national competitiveness. To nurture the competitive ability, it needs enterprise to strive for various resources and allocate all the elements to be optimal, thereby obtain more market share and profits or higher return on investment.

Second, persist in managerial innovation. Innovation is the basis for the growth of enterprise. It continually adjusts and optimizes internal resources, the relationship between business owners, operators and other employees to stimulate their own inner power to improve company competitiveness in the international market.

Third, build up proper entrepreneurial culture. The most fundamental and crucial thing for a multinational enterprise is its leading-edge technology and innovative core products to form self-knowledge property and strong corporate brand image. However, in a market economy conditions, the corporate culture is becoming an increasing reflection of the competitive advantage. We can say that cultural competition is a future of market competition. To this level, the performance of the enterprise will concentrate on the expression of entrepreneurial culture as the ultimate competitive result.
Forth, accelerating the introduction of foreign capital, advancing technology and management at the same time, we should strengthen the introduction of foreign talents and local talents to enhance company’s knowledge strength and improve international competitive advantage.

Fifth, in specific market strategy, target market selection should be considered by the modes of entry. With the actual situation of local market, the products or services should meet the market demand of the countries. Higher previous accumulation of international business experience in state-owned enterprises will give the enterprises more chances to turn its attention to other countries.

Sixth, compared with domestic operations, there are more uncontrollable factors in the foreign market. Economic risks, including price risk, exchange rate risk and debt risk. It requires more careful consideration during the actual operation. Except economic risks, political risk sometime tends to be a deadly impact. Therefore, in multinational operations, research work should consider all the factors and minimum the risks.

Seventh, the current world economic is inseparable from politics, when state-owned enterprises is doing multinational activities, where necessary, it needs the support from the government. Some important policy and market decisions require timely communication with the government. Sometime it needs the government to negotiate with foreign governments.
Reference

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Appendix

The interview questions and answers:

**Question 1: Compare with other state-owned petroleum companies, what is the competitive advantage of CNOOC?**

The others should be PetroChina and Sinopec, and we are all state-owned energy empires. Compared with PetroChina and Sinopec, we should say we are still young. Both of them are very good petroleum companies, and they did very good job in the world market. We are not completely competition relationships. We will not do the industries which they have already developed, which is our differentiation developing strategy. But to a certain extent, the competitions exist, as the biggest offshore oil company; obviously, there are more resources which are waiting for us to develop. But the main competitive advantage should be the internationalized degree. We have a higher level degree of internationalization. These make us have a higher efficiency in the international marketplace, which you can see from the growth speed, even in the economic crisis of last year, we also have a good developing rate. This can be proved by the annual report of CNOOC in 2008.

![Figure 5 Compound Annual Growth Rate](Resource: CNOOC Annual Report 2008)
Financial Data

<table>
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<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
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<tbody>
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<td>25.4%</td>
<td>48.9%</td>
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<td>23.3%</td>
<td>21.2%</td>
</tr>
<tr>
<td>Return on equity</td>
<td>20.3%</td>
<td>19.8%</td>
<td>18.1%</td>
<td>17.0%</td>
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<tr>
<td>Return on assets</td>
<td>23.1%</td>
<td>22.4%</td>
<td>20.8%</td>
<td>18.5%</td>
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<tr>
<td>Gross margin</td>
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<tr>
<td>Debt to assets ratio</td>
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<tr>
<td>Accumulated ratio of capital</td>
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<td>30.0%</td>
<td>22.3%</td>
<td>13.7%</td>
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**Figure 6 Financial Data of CNOOC**


And we also have a sustainable development idea, which is a vital part for the future competitive. We want to make CNOOC to be a world-class big firm. But we know the resource of petroleum is limit, finding some substitute of petroleum is also a developing way of CNOOC. Now we are researching and developing offshore wind energy technology and so on, which make some certain achievement, now I could not say it can substitute the petroleum resources in the future, but this is definitely an important technology of company’s sustainable development. To sum up, we choose a sustainable strategy, but in the competitive area, our competitive advantage is the higher degree of internationalization.

**Question 2: Facing the competition form the whole world, what have CNOOC done?**

There are a lot of things to do, especially in these years. We had to face to worldwide economic crisis. We are mainly focus on diversification. This embodies in the integration of whole oil industry, we try to develop upstream to downstream and the exploitation of new energy and production. In the upstream, in 2008, the company continued to achieve good results in exploration, with 13 new discovers and 11 successful appraisals. The net profit amounted to RMB 44.38 billion, representing an increase of 42% year over year; it is a new record for CNOOC.

In the mid and downstream, CNOOC Gas & power Group is the main force. In 2008, 11 shareholding construction projects and 3 front-end research projects progressed on schedule, and 2 oversea acquisitions with Qatargas and Total were done. The refining segment is another main force into mid and downstream business. Huizhou Refinery project is the first large-scale downstream project by CNOOC. The annual capacity is about 12 million tons.
It is the largest single train refinery in China and the refinery specially designed to process high acid heavy offshore crude in the world. In downstream products, the 36-1 heavy traffic bitumen and low sulfur fuel oil open up new markets and begun to export to Chad and Zanzibar in Africa. In 2008, CNOOC produced 1.95 million tons of urea and 690000tons of methanol. The revenue is RMB 5.52 billion and a gross profit is RMB 2.04 billion.

We also focus on the developing of new energy. The new energy is a sustainable development idea, which is a vital part for the future competitive. We want to make CNOOC to be a world-class big firm. So finding some substitute of petroleum is also a developing way of CNOOC. New energy business mainly covers the wind power, biomass energy, clean coal energy, solar energy, hydrogen energy and CDM. In the field of wind power, the power project in Inner Mongolia and Hainan are ready for construction soon. About biomass energy, Hainan project started construction.

**Question 3: What is the developing process of CNOOC? What strategy does CNOOC apply to enter in a new market?**

The developing process of CNOOC is also the internationalization process of CNOOC. We are not just focus on the Chinese market; we also pay lots of attention to the world market. The internationalization of CNOOC is an incremental process. Now it is the third biggest petroleum company in China. CNOOC was born in 1982 as a state-owned company, the government decided to make it internationalized. I think it is a born-global company, from 1982, it has began its internationalization way. In 1993, we had a big change. We reformed the four old companies, and turned them into four regional companies and 10 specialized companies. In 1999, we had a great change too. From that year, the key enterprises were listed, which were a big step of internationalization. In 2005, we finished the internal structural adjustment, mainly operate the international business.

At first, we cooperate with some foreign companies, by ways of turnkey projects and joint ventures, after we got bigger and had enough funds and advanced technology, we prefer to FDI or mergers and acquisitions. They are the main methods we were using recent years.

**Question 4: What is the role that government plays in CNOOC’s internationalization process?**

Since CNOOC established, our company had got much attention and support from central government and local governments. Government created a well conditioned market for our development. From this perspective, government is the strongest backup force for CNOOC’s internationalization.
Question 5: The acquisition of Unocal ended in failure, what are the reasons from your point of view? And what is the subsequent effect?

This is the biggest oversea acquisition of Chinese firms in the history. The amount of acquisition is about 18.5 billion dollars, which did not only shake the petroleum industry and capital market of the world, but also brought U.S. government’s attention at the same time. On 23rd, June, 2005, CNOOC proposed to acquire UNOCAL, the next day, 41 congressmen of the US Congress jointly appealed to stop this acquisition. After one month, we decided quit this acquisition, and this acquisition failed. To my point of view, the reason of this failure is the work of public relations with U.S.A. did not done well before; we should do it 1 or 2 years before the acquisition.

Talking about the influence of this failure, lots of people thought this failure blocked the internationalization steps of CNOOC. Actually, we should say it is not a block for CNOOC. During the first month of acquisition, the stock of CNOOC rose to 30 billion dollars from 22 billion dollars. And it increased a sum of intangible assets for our company, which increased the position of our company in the world, and the popularity of the brand and its influence power. I have to say it is a fantastic advertisement, after that, CNOOC jumped onto the world stage. It is well-known as a power company, and this took a lot of opportunities for our future developing, and lots of companies proposed cooperation initiatively.

Question 6: How to fix the problem after mergers & acquisitions?

According the statistics, in the case of mergers & acquisitions, 70% of them are not successful. One of vital problems is the combination of culture. As we know, culture change is a slow process. But this is not a problem for us. Our culture is a kind of entrepreneurship culture, the new acquisition company would be a part of our big family, this is the character of our cultures. And this culture makes us easily finish the acquisitions again and again.

Question 7: Talk about your leader Mr. Fu Chengyu.

Our boss is really an entrepreneur, he is good at creating opportunities and then hold of those opportunities. In 2005, his bold decision of acquisition of Unocal make the whole world shocked, form then, he and his CNOOC became famous. After that he won the respect of western countries. He brings the innovation mind to CNOOC, in 2008, he said by the overlook of great environment of enterprise’s development, he thought economic crisis, environment crisis and resource environment are the three challenges for our industry; innovation is the way to go. He is the kind of boss, who always has
new ideas.