

# CKGSB

M A G A Z I N E

CHEUNG KONG  
GRADUATE SCHOOL  
OF BUSINESS

Volume No. 8  
DECEMBER 2012

## A New Path for China's Growth

China's strategies to expand abroad meet varied results

The state of foreign private equity funds in China

The lure of China's fourth-tier consumer markets

The formula for China's manufacturing success

Special  
Section  
on CKGSB's  
10th Anniversary



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**Editor-in-Chief**

Zhou Li

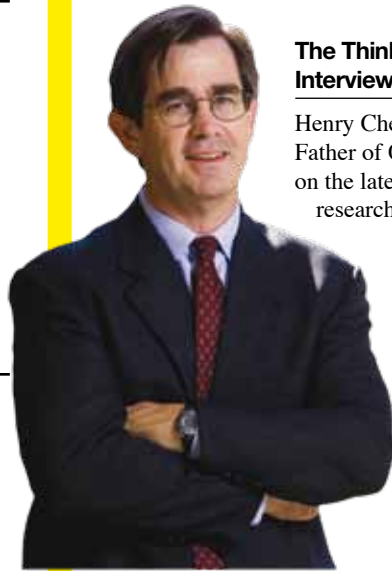
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# Still Going Strong

“What do you really think of the Chinese economy?” “Is this the end of the high-growth era for the second-largest economy in the world?” Over the last few months, every time I have attended a conference or a forum on China in Europe or the US, I have been pulled aside and asked these questions.

Indeed, the Chinese economy seems to have run out of steam—it has reported declining growth rates of 8.1%, 7.6% and 7.4% for the first three quarters in 2012. It is quite understandable that our friends who live outside of China suspect that the trend is going to lead to a possible “hard landing” and that China will eventually follow the path that the Japanese economy has taken in the last 2-3 decades.

In late August, CKGSB held its Global Business Strategy-China program in collaboration with Columbia Business School in New York. We were happy to have Jack Perkowski, also known as ‘Mr. China’, talk to a class of American executives interested in the Chinese market. He opened his talk with the following remarks: “I opened the newspaper upon landing in the US. When I read the news about China, I was about to cancel my return ticket to Beijing.”

Most of our readers who live in China, like Mr. Perkowski, have a more positive assessment of the Chinese economy than what is reported in the Western media. They will well remember that just a few months back the Chinese government was doing all it could to cool down an overheated economy. They can also see with their own eyes that the current infrastructure, natural resources and the environment cannot support double-digit growth any longer.

On the other hand, the Chinese economy will remain strong despite the slower growth rate, which, by the way, is still one of the highest in the world. As you will read in this issue of our magazine, the manufacturing advantages that China has built over the past 30 years will not be easily transferred to other countries despite their lower labor costs (‘China’s Manufacturing Metropolises’, page 18). More importantly, China’s reliance on the export market will be decline as its domestic market is growing at a much faster rate. People will find more opportunities generated from the further urbanization of hundreds and millions of people, the fast-growing service sector, and other areas that this issue of our magazine discusses. Another factor that will contribute significantly to the further growth of the Chinese economy is



the change of the regulatory policy in those industries where only a few state-owned enterprises are allowed to operate currently. I hope you will have a more balanced view of the Chinese economy after reading this issue of *CKGSB Magazine*.

In the October issue of *CKGSB Magazine*, we kicked off a special section called The Thinker Interview to bring you the latest ideas and opinions from thought leaders around the world. In this issue, we bring you an interview with Henry Chesbrough, widely acknowledged as the Father of Open Innovation. He talks about his latest research on the growth of innovation communities, a concept that could find fertile ground in China.

The globalization of Chinese companies is not a new trend—but it has started gaining momentum recently. From our vantage point in China, we have started to observe certain distinct patterns and trends in the globalization of Chinese companies. We have tried to connect the dots for you. Our cover story this issue looks at the globalization track record of Chinese companies, the strategies that have led to success and the ones that have resulted in failure. This will be immensely helpful for Chinese companies trying to craft their globalization strategies, and for those trying to understand them. To read the story, please turn to page 22.

This November marks the 10th Anniversary of CKGSB (See page 48). It’s been an exciting journey so far and as you will read, we have accomplished many milestones. But there’s still a long way to go. I would like to take this opportunity to thank you and all the others who have supported CKGSB and particularly *CKGSB Magazine* in one way or the other in the past years. We look forward to working more closely with you to enhance the information, knowledge, insights and business exchanges between China and the rest of the world.

Yours Sincerely,

Zhou Li  
Assistant Dean, CKGSB

For more insights on the Chinese business and economy, please log on to <http://knowledge.ckgsb.edu.cn/>

The number of 3G users in China reaches an all-time high, the RMB continues to gain global acceptance, China's women entrepreneurs power ahead, and foreign companies get ready to dabble in China's lucrative shale-gas reserves

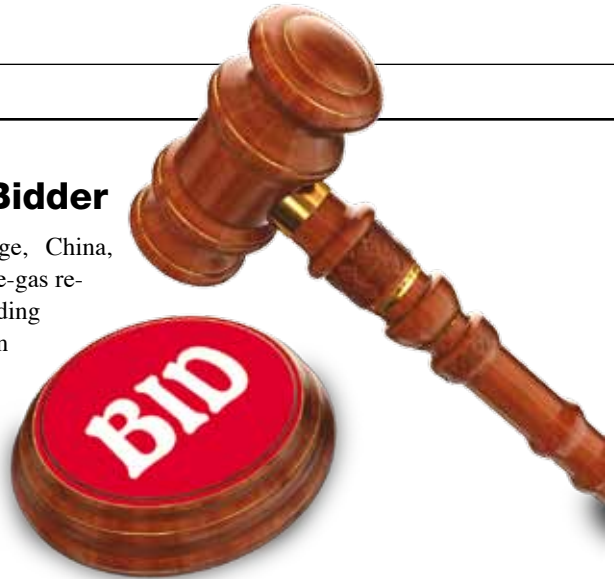


### Battle of the Brews

Coffee giants Nestlé and Starbucks are battling for ground in China's emerging coffee market, *Bloomberg* reported. Nestlé, the largest high-end coffee corporation in Europe through its Nespresso brand, introduced the single-serve coffee capsules in China to great success. The US coffee chain Starbucks plans to introduce single-serve capsules in 2013. With China's drinking habits expected to continue changing, analysts describe the Chinese coffee market as one of the major growth markets, but advised preparing for the long haul. Overall coffee retail sales in China are set to double to \$1.96 billion by 2015, *Bloomberg* reported.

### To the Highest Bidder

In a major policy change, China, which has the largest shale-gas reserves in the world according to the US Energy Information Administration, has opened its lucrative shale-gas market to foreign investment. The aim is to gain insights into the industry's development. At least six publicly traded international companies participated in a shale-gas auction in Beijing in November, bidding on shale-gas blocks in eight Chinese provinces. Western energy companies such as BP and Royal Dutch Shell have been involved in exploratory joint ventures in shale gas prospects in China, but only now have been allowed to bid directly, according a *Financial Times* report. China opening its shale gas sector to foreign companies is the latest measure the country has taken to increase its technical capabilities in expanding its energy resources.



\$59.1 bn

### World's Money Goes to China

China became the top destination for foreign direct investments (FDI) during the first half of 2012, according to the United Nations Conference on Trade and Development (UNCTAD). Overtaking the US in the top position, China's FDI totaled \$59.1 billion during the first half of the year, \$1.7 billion more than the US figure. This is the first time that a developing economy has matched a developed economy as an FDI destination. China is continuing to attract foreign investment funds to restructure its economy away from low-cost manufacturing. But the report said that global foreign direct investment inflows dropped 8% overall in the same period.

### 'I am Woman, Hear Me Roar'

Eleven Chinese entrepreneurs represent half of the world's self-made female billionaires, according to the 2012 Hurun Rich List. Of the report's top 10 women, seven were Chinese. Real estate tycoon Wu Yajun, founder and executive director of Longfor Properties, topped the list with a reported \$6 billion in personal assets. Hurun Report chairman and chief researcher Rupert Hoogewerf said the Chinese female entrepreneurs had the same position in global wealth rankings as China's table tennis team, "absolute number one." The Hurun list also included five billionaires from the United States and three from the United Kingdom. Overall, the number of females worth at least \$1 billion fell from 28 to 22 since 2011. The average wealth on the 2012 list is \$2.2 billion, an overall decrease of 6.8% over the past year.



Wu Yajun, Chairwoman and Executive Director of Longfor Properties Co., Ltd.

## The 3G Revolution

The number of 3G users in China climbed beyond 200 million in September, signifying a doubling in growth to twice the pace in 2012. It took two years for Chinese users to reach the 100-million mark since 3G was first introduced into here in 2009, and only one additional year to double that number. The increase is keeping pace with the growth in consumer use of Internet services, such as Sina's Weibo microblogging site. The Ministry of Industry and Information Technology said the user base grew to 202.6 million users in September, 10.1 million of which were added in September alone, *ZDnet* reported. The government plans to wait a minimum of two years before introducing 4G in China, leaving room for continued expansion of 3G users.

## More Bang for your Yuan

The Chinese currency, Renminbi (RMB), is making progress toward becoming a major trade currency. An HSBC survey of China-based companies forecasted that one in three trades would be settled in RMB by 2015, and 30% of them plan to invest using RMB in the upcoming year. Half of the surveyed firms also indicated willingness to offer better prices or terms when settling a trade in RMB. HSBC Bank Australia CEO Paulo Maia told the *Financial Standard* that the RMB is becoming a currency to reckon with. The Chinese government has simplified the exchange flexibility and transaction processing, enhancing the currency's cross-border dynamics, HSBC said.

## Lenovo Comes Calling

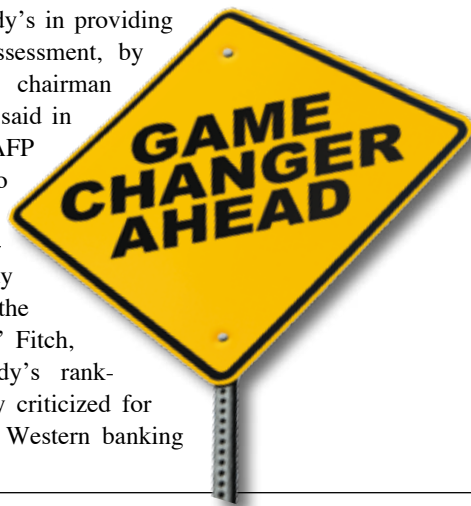
Personal-computer maker Lenovo plans to focus on expanding its smartphone sales internationally. The decision comes during an economic slowdown in China and a global slowdown in demand for PCs, Lenovo's main product. Lenovo currently sells its smartphones in the Chinese market, but the *Wall Street Journal* quoted analysts as saying the company's phone division is not profitable. Lenovo will begin India sales in December, and has recently entered the phone market in the Philippines and Vietnam, taking on global rivals Samsung and Apple. Lenovo's Asia-Pacific and Latin America President Milko van Duijl said in a statement to the *Wall Street Journal* that the company will need more time before expanding into developed markets, but that, "we are looking at any opportunity that allows us to grow."



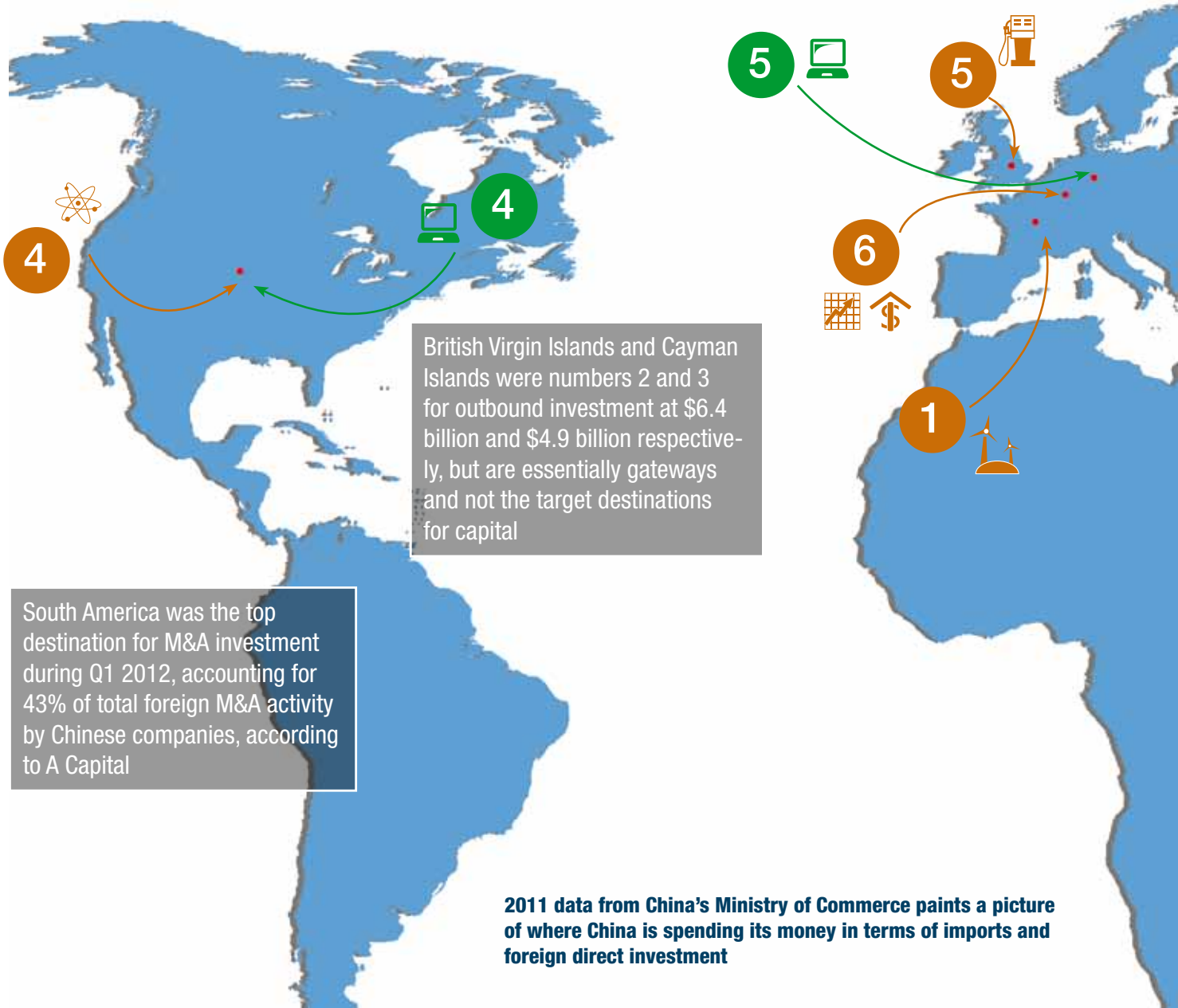
Lenovo partners with Intel to launch its LePhone K800 in China

## New Rating Firm Shakes Things Up

A new firm in China is planning to challenge the U.S.'s dominance in assessing private and governmental debt. China's Dagong, US-based Egan-Jones Rating and Russia's RusRating plan to set up a joint venture in Hong Kong, AFP reported. The group aims to break the monopoly held by American-based Fitch, Standard & Poor's [S&P] and Moody's in providing investors risk assessment, by 2017. Dagong chairman Guan Jianzhong said in a statement to AFP that their goal is to "form a new system with the synergy of everybody that will balance the existing system." Fitch, S&P and Moody's rankings were widely criticized for their role in the Western banking crisis of 2008.



# Where is China Spending its Billions?

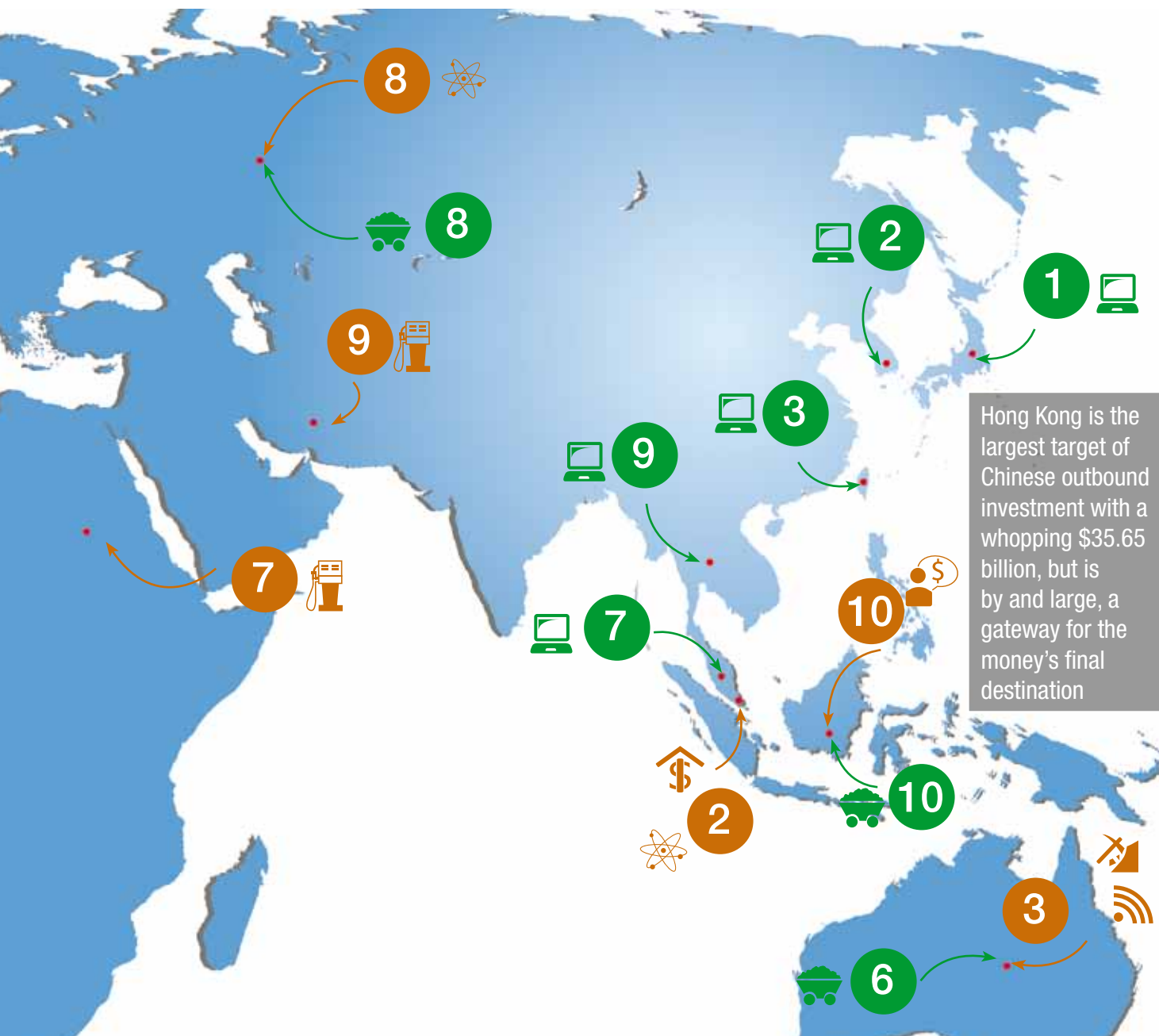


## WHERE CHINA IS SHOPPING

- |  |  |
|--|--|
| <b>1   Japan:</b> \$194.7 bn, Machinery & Electrical Equipment         | <b>6   Australia:</b> \$82.7 mn, Mineral Products                |
| <b>2   Korea:</b> \$162.7 bn, Machinery & Electrical Equipment         | <b>7   Malaysia:</b> \$62.1 mn, Machinery & Electrical Equipment |
| <b>3   Taiwan:</b> \$124.9 bn, Machinery & Electrical Equipment        | <b>8   Russia:</b> \$40.3 mn, Mineral Products                   |
| <b>4   United States:</b> \$122.9 bn, Machinery & Electrical Equipment | <b>9   Thailand:</b> \$39 mn, Machinery & Electrical Equipment   |
| <b>5   Germany:</b> \$92.7 mn, Machinery & Electrical Equipment        | <b>10   Indonesia:</b> \$31.3 mn, Mineral Products               |



**A map of top destinations for China's money shows neighbors Japan and Korea top the imports list, while Sudan and Iran are among the top 10 recipients of China's FDI**



### WHERE CHINA IS INVESTING

- |   |   |
|---|---|
| <b>1</b>   <b>France:</b> \$3.5 bn, Alternative Energy, High Tech & Equipment | <b>6</b>   <b>Luxembourg:</b> \$1.2 bn, Investment Funds              |
| <b>2</b>   <b>Singapore:</b> \$3.3 bn, Energy & Real Estate                   | <b>7</b>   <b>Sudan:</b> \$911.9 mn, Oil & Infrastructure             |
| <b>3</b>   <b>Australia:</b> \$3.2 bn, Mining, Infrastructure & Telecom       | <b>8</b>   <b>Russia:</b> \$715.8 mn, Energy & Infrastructure         |
| <b>4</b>   <b>United States:</b> \$1.8 bn, Energy                             | <b>9</b>   <b>Iran:</b> \$615 mn, Oil                                 |
| <b>5</b>   <b>United Kingdom:</b> \$1.4 bn, Oil and Gas                       | <b>10</b>   <b>Indonesia:</b> \$596 mn, Minerals & Financial Services |

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# The Road Less Worn

**China's fourth-tier consumer markets  
come into their own**

By Berken Byrne



If you travel to China's poorest fourth-tier-cities such as Jiangsu Province's Taixing in the hope of leaving behind the international brands that dominate the major coastal cities, then you will be disappointed. The familiar grin of KFC's iconic Colonel Sanders is there to greet you outside the local bus station, along with a giant video screen projecting 3D images of a future mall—replete with such brands as Calvin Klein, Dior and Starbucks. China's lower-tier cities are no longer, by any stretch of the imagination, isolated.

Taixing is still, by Chinese standards, a small community—in the downtown area, there is only one building over 10 stories, automobiles are easily outnumbered by two-wheelers, and one sign outside a clothing store offers “All outfits 9.90 yuan!” (around \$1.50). Yet on the same downtown block is another KFC and three retailers displaying large Apple logos.

This penetration of the big wide world and its powerful brands into China's interior has occurred with phenomenal speed. “The KFCs and all three ‘Apple’ stores showed up just this year,” says Yusha, a 42-year-old saleswoman working at a cell phone outlet in a small nearby mini-mall.

### Big Brands, Big Journey

The Taixing experience is being repeated in countless fourth-tier and county-level cities around China, officially defined by the level of government overseeing these

cities, which is the county or prefecture government. The average annual income in the county-level cities in 2011 was around RMB 27,000, and has risen consistently over the past two decades. More and more national Chinese and international brands are laying the groundwork in what they have identified as a massive market. Retail sales of consumer goods at and below county level totaled RMB 1.74 trillion between January and August 2012, up 14.3% year on year. The market research firm Nielsen estimates lower-tier cities account for 64% of retail sales.

The expansion trend encompasses all sectors. Home Inns, owner of the successful Motel 168 brand, opened around 280 new hotels in 2011, around half of them in third and fourth-tier cities. In clothing, Chinese brand Yishion, scarce in upper-tier cities, anticipates earnings of RMB 8 billion in 2012 mostly from its smaller town stores, while French brand Cache Cache, which has opened 500 stores since 2005, has also largely ignored tier-one markets in its expansion plans.

Luxury products are also seeing growth in the remote interior cities and towns, especially automobiles. BMW sales in fourth- or fifth-tier cities grew by 50% year-on-year in the first seven months of 2012 according to company data. The German brand had stores in 290 locations across China in 2011, and planned to open 30 new stores in 2012. Volvo, similarly,

has announced plans to expand from 109 to 250 dealerships over the next five years, most of them in third- or fourth-tier cities.

She Duanzhi, Vice-President of Dutch appliance maker Philips China, told *CKGSB Magazine* that the company's new moderately priced line of home appliances was aimed squarely at this market. “It's part of our tier expansion strategy,” She says.

Philips analyzes a variety of indicators for different cities, She says, including GDP and amount of disposable income, to determine the appropriate strategy for each place. “There's a concern that the tier-one mega-cities are slowing down in terms of consumption and growth. In contrast, in inland provinces, and tier-three and four cities in particular, consumer purchasing power and incomes are growing very fast.”

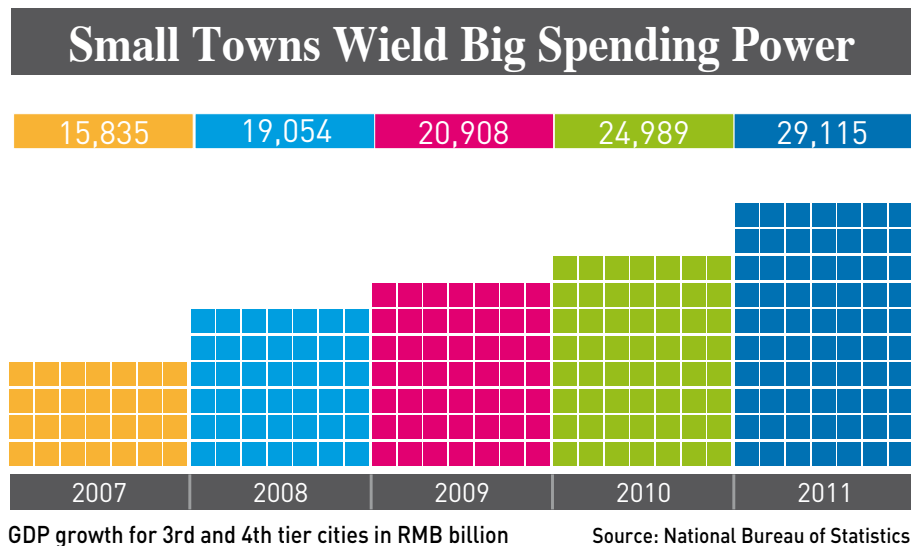
### Ready to Shop

While older fourth-tier consumers are generally price conscious and more comfortable with local brands, the younger generation is different. For them, the popularity and status of large, global brands is becoming more and more an attractive investment. “Foreign brands are fashionable,” says Jenny, a 23-year-old woman using an iPhone, who declined to give her surname. “And their quality is high too.”

“In China, the generation gaps are huge,” says Alan MacCharles, partner and China market consultant at the accounting and consultancy firm, Deloitte, adding that the younger generation spends a much higher percentage of their income and has a different approach to valuing products.

“They're now looking to show off their new wealth,” Chris Devonshire-Ellis, founder of market entry consulting firm Dezan Shira, told *CKGSB Magazine*, explaining that rising wages and government subsidies for some consumer products are major factors.

Part of the draw of bigger brands is that more and more fourth-tier youths have spent time studying, working, and traveling to the coastal metropolises. “I'm definitely influenced by what's going on in bigger cities, since I studied in Nanjing and have spent time in Shanghai and



Hangzhou,” says Jenny.

The result is that younger fourth-tier consumers are close in their buying habits and choices to their first-tier counterparts. But a 42-year-old worker at the Taixing bus station, Wang Hong, says that young people all over are much the same: “They all love what’s fashionable.”

### Reaching the Consumer

The rise in demand from young smaller city consumers speaks of greater opportunity for brands currently established in large coastal cities. The next step for them is to devise a marketing approach that reaches consumers on both sides of the generation gap.

The most important considerations for brands looking to enter these smaller markets are price and utility. “Our tastes aren’t like those of people in Shanghai,” says Wang Hong at the Taixing bus station. “We pay attention to practicality. They can afford to be extravagant.”

According to a 2009 survey conducted by Deloitte, 45% of respondents in the fourth-tier cities of Changshu, Jiangsu and Xinmin, Liaoning, purchased shoes for less than RMB 300 a pair, compared to 37% in Shanghai. Meanwhile, less than 20% of Changshu and Xinmin residents owned international-brand shoes, next to 35% in Shanghai.

“I wouldn’t buy anything just because it’s an elite brand,” says Yusha. “Buying something to gain face is foolish.”

T.B. Song, Chairman of advertising and marketing firm Ogilvy & Mather China, cites Nike and Adidas as two companies that could benefit from focusing efforts in the fourth-tier for their low-end products. “Product is not the issue,” he says. “I think price is the issue.”

Deloitte’s MacCharles names apparel and electronics as examples of sectors where tier four residents desire similar products to consumers elsewhere, but insist on paying less.

“In apparel, they want comfort, brand, value for money—the same things everyone wants. They don’t even buy that many fewer units, they just spend less. Then, in electronics, it’s just getting the most you can for the price. So international brands

sell fewer than domestic brands, which are feature-laden and cheap,” says MacCharles.

Price sensitivity is an issue well heeded by many large Chinese brands. Chinese computer maker Lenovo, for instance, had found great success targeting smaller markets with a computer that sells for only RMB 1,499.

Philips’ cheaper line of home appliances includes a rechargeable RMB 99 razor, a product Philips has never before sold for less than RMB 200. In a nod to



Our tastes aren’t like those of people in Shanghai, we pay attention to practicality. They can afford to be extravagant

Wang Hong, Taixing resident

penny-pinching practicality, Phillips also advertises a toothbrush that requires no toothpaste. “In general, people want to use branded products but they can’t afford high prices,” says Philips’ She.

### It’s the Journey that Counts

There is more to entering the fourth-tier than coming up with the right product and

the right price. One of the biggest challenges that food and beverage companies must overcome if they want to expand into this growth market is logistics, particularly cold-chain logistics and storage.

Devonshire-Ellis points to the difficulty of shipping products to the city of Changxing in Zhejiang Province as an example of the difficulty of setting up shop in these markets.

“Changxing relies on transportation along the Yangtze River. The problem is that the port operators are state-owned and they do not welcome competition. So the result is a really, horrendously inefficient service getting goods into and out of [the city]—because they’re state-owned and don’t really care—at extremely high prices,” he says. “The central and western parts of China in terms of infrastructure, politics, and commercial mindset, are about 10 to 15 years behind the East coast.”

One way to make products widely available despite remote locations and a lack of infrastructure is to use third-party distributors that already have local stores and logistics in place. Such outfits can bridge the gap for companies with limited resources aiming to sell directly to local markets. Sports apparel firms like Li Ning, Anta, and 361 have all found success with this model. “They’ve done surprisingly well,” says MacCharles. “When you go down the main street in a lower-tier city you tend to see big sportswear brands and a lot of those are distributor stores.”

Chinese brand Ming Le is one such company. The sportswear brand uses 24 different distributors to reach over 3,324 retail outlets in China, approximately 87% of which are located in more than 1,000 tier three and four cities.

The trade-off with such a model for larger companies is that they are typically unable to access detailed information on what is being sold where and how much inventory is being held, which hinders efficiency. “Someone else deals with how to position you and where to position you locally, so you’ve got less control,” says MacCharles. “It’s a question of how much you’re willing to let go.”

For companies determined to maintain

control, the cost of setting up one's own distribution network may be astronomical, but so may be the eventual profits. Chinese appliance maker Haier set up a subsidiary Ririshun in 2003 to handle distribution and franchise stores in tier-three, tier-four, and rural areas and the company quickly expanded to handle distribution and retailing for competitors as well, and in 2009 reached revenues of RMB 45 billion.

In cases where it's not feasible to carve out a physical presence, consumers can now be reached through e-commerce. Internet usage is now common in all corners of the country. "It's not a lower-tier or upper-tier thing—everyone's online," says MacCharles. "Particularly people with the money to buy your products."

"There aren't many places to shop in Taixing and you can't expect to find every brand, so I shop online a lot," says Jenny.

Hancao, a herbal cigarette maker that relies largely on the appeal of its Chinese medicine ingredients, has had success in lower-tier markets using third-party re-

gional distributors. But it also operates a flagship store on Taobao.com, China's largest consumer-to-consumer website.

### Building Awareness

The problem of building brand awareness in China's interior is well illustrated by Deloitte's 2009 survey, which found that 38% of those surveyed in fourth-tier Changshu and Xinmin thought Nike and Adidas were domestic brands. What's more, people who grew up before Western brands began to exert their current influence in the market often find many of the brands intimidating.

Taixing's Kuang Meiying, 34, says she strongly prefers local brands. "It's not just that Chinese brands are cheaper. I can't make sense of foreign brands."

"It's been [decades] since most brands began arriving in Shanghai, so consumers have had some time to absorb them and what values they represent," says MacCharles. "In fourth tier cities, brands have only been getting there recently."

One way of increasing familiarity with your product is through local sales events, which tend to have much greater impact for the marketing outlay than in the coastal cities. "Sales events are more effective in fourth-tier cities because they haven't had a chance to experience the product before," says Song.

He points to P&G as a successful example. "They do product tests in small cities and the sales lady explains the product to consumers. They've already been doing these sorts of events in smaller cities for three or four years. Partially because of this, most P&G brands are quite successful in third- and fourth-tier cities, especially shampoo."

The Internet, meanwhile, is proving useful in terms of awareness as well as availability. Philips' She Duanzhi emphasizes the importance of online promotional events and agreements with e-commerce websites to support Philips lower-tier strategy. "We have very good collaboration agreements with e-commerce players like Jingdong and we do promotions on there from time to time."

### A Limitless Future

Ultimately, while China's fourth-tier market can be a tough nut to crack, the future will be even tougher for companies that decide to shy away from the challenge now.

"If you are content to stay in Shanghai, ultimately you will face increased competition," says Devonshire-Ellis. "If you get out into the fourth-tier cities, there is less competition. It's tougher, but it's an 'early bird catches the worm' scenario."

Besides rising incomes, growing urbanization is also a factor. China's urban population topped 50% for the first time this year, and the consulting firm McKinsey predicts that China's cities will be home to more than 1 billion people by 2030. Much of that growth in urban residents will occur in the third- and fourth-tier cities.

"In the near future, maybe 80% of Chinese will live in cities," says Song. "And fourth-tier cities will become third-tier cities, while third tier cities become second tier cities."



Residents of Yuexi in Anhui Province motor through town where international brands have had a go at success



# Chasing the Deals

Foreign private equity in China is down, but far from out

By Susie Gordon

**F**or most people, having too much money in the bank is hardly a concern, particularly in the current economic climate. For those in the private equity (PE) industry, however, it's an unpleasant reminder of how much the world has changed since the go-go years of the PE boom from 2005-2007.

As of the end of last year, the industry was sitting on around \$900 billion of unused capital, or "dry powder" in the industry jargon, according to Preqin, a research outfit. The reason is that managers are investing far less than they used to. While global figures are patchy, the total volume of PE transactions in the US market alone

dropped from \$405 billion in 2007 to just \$88 billion last year.

It's not hard to see why executives are reluctant to deploy their capital. Credit—the lifeblood of leveraged buy-outs—is a shadow of what it was before the economic downturn. And the global landscape is dismal: growth in the US is hovering at

a paltry 2%, while Japan and Europe are flirting with another recession.

China is the exception. Growth has certainly slowed this year, but at around 7.5%, it is still well ahead of the developed world and other large emerging markets like India (expected to grow about 5.5% this year) and Brazil (2.5%). Small wonder private equity deal-making in the country rose almost 10% to hit a record high of \$15.2 billion last year, according to a report by the consulting firm Bain & Co and Asian Venture Capital Journal (AVCJ).

But foreign private equity firms are not able to ride the China private equity boom like they once did. Over the past five years, new regulations have restricted their investment options. The industry has also become much more competitive due to a surge of small, well-connected domestic PE firms. But with so few other fast-growing markets in which to put their money, foreign private equity firms are looking to adapt, rather than exit, the Chinese market.

### Crowding the Field

Foreign private equity funds are no strangers to the Chinese market, and some have proven talented money-makers. To take just one example, a consortium of private equity buyers including Blackstone, Morgan Stanley and Goldman Sachs were early minority investors in Ping An Insurance, now one of China's biggest insurance and financial services firms. In 2005 the group sold a 9.9% stake in the firm for \$1 billion, posting a healthy 1,300%-plus return on its initial \$70 million investment.

Besides business smarts, foreign PE firms have benefitted in the past from the lack of traditional (i.e. bank) financing available to many small and medium-sized businesses in China, as well as opportunities to pounce on badly-run state-owned enterprises sold off during the 1990s and 2000s.

Today the field has become much more crowded, and making stellar returns is a lot harder. "If you look at the investments that were made within this time [before around 2007], there was far less competition," says Liu Jing, Professor of Accounting and Finance at Cheung Kong

Graduate School of Business. "Firms now have to compete for a limited number of deals, and prices are increasing."

The biggest impact has been the explosion of homegrown PE firms. China's National Reform and Development Commission (NDRC) officially recorded 882 Chinese private equity and venture capital firms as of the end of 2011, with assets of almost RMB 220 billion (\$35 billion). The true figure, however, is likely much



Firms now have to compete for a limited number of deals, and prices are increasing

Liu Jing, Professor of Accounting and Finance at CKGSB

higher. Liu of CKGSB reckons there to be around 3,000-4,000. Jonathan Zhu, Managing Director at Bain Capital Asia, said at a forum in Beijing in March that there could be as many as 20,000. "I'd be happy with 8,000 competitors," he quipped wryly, no doubt reflecting the feeling of many foreign PE firms.

### New Kids on the Block

The surge is due at least in part to government design. Beginning in 2006-2007, both Beijing and local governments took a series of steps intended to cultivate a domestic PE industry. The idea, argues Chris DeAngelis, a Beijing-based principal at

Alliance Development Group, was to keep the entire process within China—everything from raising funds from Chinese individuals to investing in Chinese companies and eventually listing on Chinese markets.

To that end, the government allowed PE firms to raise yuan-denominated funds and changed their legal status from corporate investment houses to limited partnerships, effectively allowing them to fundraise from wealthy Chinese individuals. The government also began closing loopholes that allowed Chinese companies to accept US dollar-denominated funding from foreign PE firms via offshore holding entities. The clampdown did not totally block the channel, but it did make the process much slower and more cumbersome.

The upshot is that the playing field has clearly tilted in favor of domestic funds, which have important advantages of their own. For one, they are often well-connected, giving them access to the best deals. One China-based analyst covering the industry, who declined to be named because of the sensitive nature of the topic, says that many of the smaller Chinese PE funds are so intertwined with local officials that they are now "more or less de facto agencies" of local governments.

Beyond better connections, these firms can be more nimble than their big foreign rivals—not just in quickly sourcing and signing new deals, but also in terms of the speed at which they can get their yuan-denominated funding into company coffers. DeAngelis of Alliance Development Group notes that investing dollar-denominated PE funding into China is simply logistically difficult. "China doesn't have the [regulatory] structure to deal with [foreign PE firms]."

### The Equity Strikes Back

Yet foreign PE firms are hardly throwing in the towel in the face of stiffer competition and tougher regulation; many still have big competitive advantages. For starters, the likes of the Carlyle Group, TPG, KKR and Blackstone are more experienced than all but the biggest Chinese PE firms, and boast some of the world's



best talent at spotting and growing promising start-ups.

Moreover, American and European PE firms can borrow capital much more cheaply than their Chinese competitors, thanks to ultra-low interest rates across the developed world. Their huge size also gives them access to big deals, important because the vast majority of Chinese PE firms compete at the smaller end of the market.

“The nature of Chinese PE is very different from its international counterpart,” says Joseph Chan, a Shanghai-based partner at the law firm Sidley Austin, who works on private equity deals. “Internationally, one deal could be massive, and [that] is the traditional model.” In China, by contrast, he says a typical investment might be just \$50 million—a small sum by Western standards.

Many foreign PE firms have also teamed up with local Chinese governments to mitigate their regulatory disadvantages. Carlyle has raised yuan-denominated private equity funds in partnership with both the Beijing and Shanghai municipal governments; TPG has also partnered with Shanghai, and Goldman Sachs is working with Beijing, among other tie-ups.

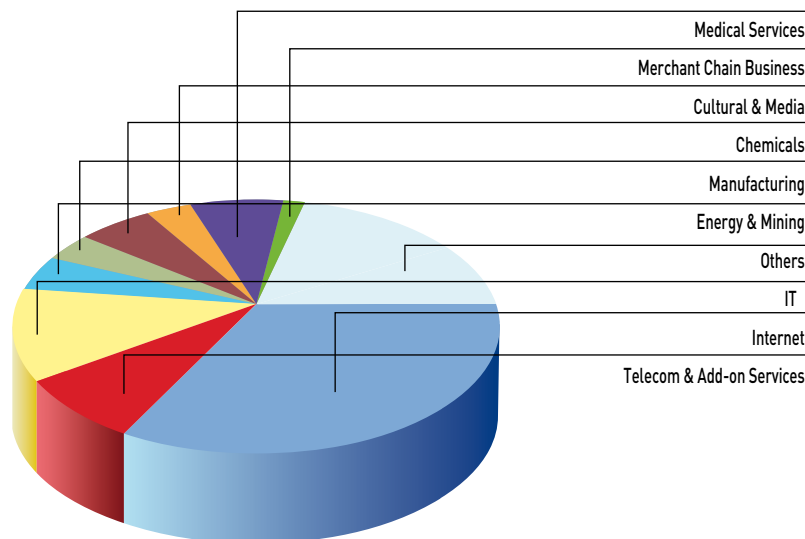
Furthermore, the big global players have taken to scouring non-traditional sectors for investment opportunities. “Focus has diversified,” says Chan.

For example, he notes that many of the foreign PE investments in the past were focused on China’s technology sector. He cites Ctrip as a typical case; the online travel site has received investment from foreign private equity firms such as Morningside Technologies, Tiger Global Management and others. (Its rivals, such as Elong and iTour, have also received plenty of PE funding.) As new Chinese funds have flooded in, however, the sector has become too crowded, deals too pricey and many foreign players are now turning their attention elsewhere.

One of these areas is clean technology. Five of the 10 biggest IPOs in China last year were exits from clean-tech deals. A further 11 deals worth \$2.6 billion were exited via IPOs on global markets, including blockbusters such as Goldwind’s

## Where’s the Private Equity Money Going?

Popular industries for venture capital and private equity firms, by number of investments



Source: ChinaVenture Investment Consulting Ltd

\$920 million IPO in Hong Kong. Chan notes that besides the economic case for investing in renewable energy, the industry is also an important beneficiary of the government’s 12th Five-Year Plan. “Anything in new materials and clean tech will be important—investors can expect a lot of subsidies and tax breaks,” he says.

### One Eye on the Exit

To be sure, serious challenges remain. In a report on China’s private equity industry in 2012, Peter Fuhrman, Chairman of China First Capital, argued that future returns in China’s PE industry could decline substantially due to shrinking opportunities for PE firms to cash out companies on stock markets.

The reason lies in the nature of PE exits in China. “In a market like the US, around two-thirds of exits by [private equity or venture capitalists] are a form of M&A—you fund the company, and it will eventually be bought by a big player like Microsoft,” says Chan of Sidley Austin. In China, by contrast, “it’s all about IPOs,” which have become much less attractive than they once were.

Valuations of companies on mainland Chinese stock exchanges are still high, but

regulatory approval to list is hard to come by. Meanwhile, valuations for Chinese companies listed in the US and even Hong Kong have sagged in recent months. Ernst & Young, a professional services firm, attributes a decline in the number of PE deals in China this year to weak investor sentiment in global stock markets.

Still, for all the challenges, few foreign PE firms are backing out of China. Quite the opposite: a 2012 report by Bain and AVCJ found that many foreign PE firms including Carlyle have reacted to a tougher environment by increasing their staff on the ground in China, in order to scope out deals others may have overlooked. One out of every 12 employees at Carlyle, for example, is now based in China.

It’s not hard to see why. With the rest of the world either facing anemic growth prospects or even recession, China still has more potential investments than just about anywhere else. Bain Capital estimates that the private equity industry still has about \$43 billion in “dry powder” targeted specifically at China. The shots may be fewer and more carefully aimed than they once were, but foreign PE firms are likely to keep taking shots in China for a long time to come.

# China's Manufacturing Metropolises

Why and how China will remain the factory of the world

By Berken Byrne



Hon Hai's massive Longhua facility outside of Shenzhen employs more workers than any other factory in the world

In 1974, 23-year-old Terry Gou founded his own business on a \$7,500 loan from his mother. It was enough to rent a small space and buy a couple of machines to mold hunks of plastic into television dials. In truth, what he had was a shed masquerading as a factory.

These days, Gou's company Hon Hai, better known by its affiliate Foxconn, operates metropolises masquerading as factories.

"These places aren't like cities," says Thomas Dinges, Senior Principal Analyst at market research firm iSuppli. "They are cities."

That is the reality for the more than 300,000 Chinese—roughly the population of most county-level Chinese cities—living and working inside Hon Hai's three-square-kilometer Longhua industrial park near Shenzhen in southern China. The workers ride their bikes down the wide avenues of the compound, sleep in dormitories and eat at KFC and McDonald's on site, and even shop at internal bookstores where they can buy biographies of Terry Gou.

The scale of the operation is such that even cafeteria meat is supplied by Hon Hai's own chicken farms, part of the Longhua complex. The facility even has a certain amount of autonomy to govern its own affairs, as employees' emergency calls to the police are redirected to a thousand-person-strong on-site security force.

"Longhua's like a huge college campus, only half the population of San Francisco lives there, works there, and doesn't leave," says Dinges, who has visited.

There has been much talk about which countries or regions might replace China as the world's factory, and the possible impact of robotics in manufacturing. But China's unique massive factory compounds make a convincing argument that its title as reigning champion of global manufacturing won't be snatched away any time soon.

### A New Manufacturing City

A standard city exists to serve the needs of its residents, but Longhua exists to serve the needs of its customers, the most important of which is Apple Inc. The facility has

become a model for other integrated and self-contained manufacturing complexes around China.

The formula, adopted by other Chinese manufacturing firms including Flextronics, Compal, Quanta, and Wistron, involves the creation of a finely-tuned ecosystem, starting with suppliers. By locating much of the supply chain on campus, or very close by, feeding materials into an intensely focused production process, efficiency is maximized.

In addition, these mega manufacturers make as many components as possible on campus to supplement parts supplied from elsewhere. Each iPhone that Hon Hai manufactures is made up of parts from an array of internationally famous brands, but also contains components it makes itself on-site. This boosts Hon Hai's own share in the overall profit, while making the supply chain tighter and more focused.

"For very-high-volume products with stable output, it makes sense for manufacturers to make certain components themselves, for reasons of profit, logistics, quality, and responsiveness," says Tim Sturgeon, Senior Research Affiliate at MIT's Industrial Performance Center. He points out that Apple itself internalizes much of its chip design for the same reasons.

The phenomenon of clustering final-assembly manufacturers and their suppliers together is nothing new. After all, Detroit is known as Motor City for its collection of automotive firms. What distinguishes China's manufacturers, is their scale in terms of numbers of workers and production capacity, and the remarkably closed-circuit nature of production. They provide economies of scale that allow for production at cost levels attractive to very demanding customers.

While Hon Hai has expanded these ecosystems to the greatest extent yet seen anywhere in the world, other manufacturing firms in China run similarly complex compounds, including the Shanghai-Singapore-based electronics manufacturing service company Flextronics International Ltd.

Located in Zhuhai not far from the Hon Hai's Longhua facility, Flextronics' Doumen facility employs 53,000 workers.

Flextronics CEO Michael Marks told *Businessweek* in 2010 that his firm's Chinese facilities began basing chicken farms and tool-makers on-site after seeing Hon Hai do so.

"I went to the Flextronics facility in Doumen, which is their biggest industrial park in the world, and there's everything there—soccer fields, dormitories, and all that," iSuppli analyst Dinges says. "But you can take a bus ride around it in 10 minutes. In Longhua you get lost."

Longhua is a manufacturing ecosystem of phenomenal proportions and reach, with facilities for prototyping new designs quickly alone employing more than 2,000 machinists.

"All of these things add up to speed and volume, which are essential when you're introducing a new product in a competitive market where timing is critical," says Jason Dedrick, Associate Professor of Information Studies at Syracuse University. "There might be demand for millions of units as soon as the product is released."

Companies like Hon Hai have taken the phrase "manufacturing city," once used to describe a city like Detroit, and brought it to life in the most literal way possible. It has removed all excess elements that aren't in some way a part of the production process, including staff housing, parks, and nightlife. "You won't find anyone working at Ford (in the US) who lives in a dormitory and whose entire daily life and schedule is dictated by his company," says Dinges.

### A Hon Hai World?

From its earliest days, Hon Hai found success through a cutthroat business strategy. "They'd look at the competitor's lowest bid, knock 10% off, and bid that," says Dinges. "Get in there, get the business, let the economies of scale grow, and then they'd begin to make money."

Hon Hai lays claim to the highest economies of scale in the industry, vital to



**Foxconn workers can produce roughly 90 iPhones per minute**

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## Foxconn's World: A manufacturing presence the world over

But China is still the clear victor as Foxconn's main production base



maximizing efficiency and creating profit with massive volume and low margins. “Now that Foxconn is the biggest player around, it can keep costs low by placing pressure on its subcontractors and suppliers in a way that it could not have dreamed of doing when it was just an obscure niche player,” says Gijsbert van Liemt, who has written research papers on the subject for Geneva’s International Labour Office.

This is especially true for manufacturers serving brands like Apple, where the massive scale offsets relatively low profit margins. “The profit margin per unit is only a few percentage points,” says Ding-es, “but you multiple that by 10 million iPhones sold and it’s a huge difference.”

The production scale and intensity has made Hon Hai’s Longhua plant difficult to replicate outside of China, despite the allure of lower wages in places like Vietnam, Indonesia, and India. Even in China, running such a giant facility with consistency and efficiency on such thin margins is a tightrope walk.

Hon Hai has also had its share of problems, including an incident in September when more than 2,000 workers rioted in its Taiyuan plant after a guard allegedly hit a

worker. Another incident involved a strike at Foxconn’s Zhengzhou plant over workload pressures related to quality requirements for the iPhone 5.

“There can be dis-economies of scale,” says Zheng Yusheng, Professor of Operations Management, CKGSB. “It creates a huge problem in terms of management.” The difficulties that managers of large organizations have in terms of controlling what is happening many management layers below them is just the start of the issue.

But in spite of the challenges, creating and operating such a tightly controlled and hyper-efficient facility in other parts of the developing world could be even more difficult. So many pieces of the equation must fall into place—population, infrastructure, government support, and supply chain concentration—that many doubt the creation of such a facility is now possible.

“Foxconn’s Longhua facility could only be done in China,” says Ou Jihong, Associate Professor of Operations Management, CKGSB.

That’s not to say that the appeal of other manufacturing sources isn’t real, both for the iconic iPhone maker and for other companies. Vietnam drew much attention

five years ago when dozens of major manufacturers began planning facilities there to take advantage of low wages. Hon Hai itself proposed a \$5 billion investment in Vietnam, and while it has since built five smaller factories there, it has encountered numerous production delays, including three years for one \$200 million factory. None of the Vietnamese facilities have created a gravity shift away from China’s manufacturing metropolises.

“If Foxconn really considered Vietnam a potential base for serving strategic customers, it would have implemented its promised project over the past four years,” Man Ngoc Ly, director of a Vietnamese economic zone, told a local journal in 2011.

China’s advantage in labor is probably the biggest reason the Longhua model has not yet been replicated outside of China. In November 2010, Hon Hai was unable to recruit even the 5,000 workers needed to man one of its Vietnamese assembly lines. One recruitment issue that has been cited by many sources is worker skill levels. Foxconn’s Chinese employees are more highly skilled, making recruitment much easier. In Vietnam, recruitment

on the scale of China would have to be coupled with a massive training program, with a cost that would offset the benefits of lower wages. Chinese recruits still turn up in large numbers at the Foxconn/Hon Hai plants, even after media coverage of a number of employee suicides in 2010 impacted on the company's reputation.

Countries like Indonesia and India have large populations, but companies have still found it difficult to acquire large groups of reliable workers. "In China there's a Confucian attitude—a willingness to sacrifice today for a better tomorrow," says CKGSB's Ou. "In India and Indonesia it's harder for people to organize such a huge number of people together."

Another factor contributing to China's appeal as a manufacturing center is government support, as shown by its efforts to improve the infrastructure attached to large-scale manufacturing facilities. In 2009, the Chongqing government agreed to lengthen its airport runway by 400 meters in order to accommodate Hon Hai and other manufacturers' request for better logistical infrastructure. In addition to improving its infrastructure, Chongqing's government granted Hon Hai a discounted corporate tax rate of 15%, 10% lower than the standard rate. In Chengdu, meanwhile, the local government agreed in 2010 to provide low-cost housing and other social benefits for workers in order to secure a \$3.5 billion Hon Hai investment.

This level of support is not so easily found in democratic countries like India, Indonesia, and Brazil. "In India, for example, it's a democracy, so the government sometimes cannot do the things they want to do," said Ou.

This may change. In September of this year, Foxconn signed a memorandum of understanding with Brazil that will result in an investment of \$500 million and the creation of 10,000 new jobs in a nation where 8,000 of its citizens are already under Foxconn's employment. While a very initial step, should the relationship between government endorsement and manufacturing development mature to reach China levels, Brazil stands a chance of matching China as a desirable destination for manufacturing. Not only is the na-



## Foxconn's Longhua facility could only be done in China

Ou Jihong, Associate Professor of Operations Management, CKGSB

tion of a size to support massive industrial parks, but it's also an attractive consumer market, blessed with proximity to the largest market in the world, the United States.

Closer to home lies yet another potential competitor, Indonesia, where Hon Hai has proposed \$5-10 billion worth of investment over the next five years.

"The one thing Indonesia does have, unlike Vietnam and Brazil, is population and, from what I've heard, a trainable, reasonably educated workforce. It will be interesting to watch," says Dinges.

The maturing of Brazil and Indonesia into manufacturing powerhouses capable of seriously challenging China's well-developed manufacturing networks is still a ways in the future. That is not to say that the ecosystems could never move somewhere else, but given China's entrenched position, such a trend could take decades to reach fruition.

"In Chinese we call companies like Foxconn *'longtou'*—*'the head of the dragon'*", says CKGSB's Zheng. "They rely on the suppliers and the whole ecological cycle here. The upstream, downstream, components manufacturing, and so on is not something where just one company moves. If you move, you have to move the whole industry."

As such, China remains well positioned, but is far from invulnerable. "China has the

supply chain density and logistics infrastructure to maintain its position as a high-volume manufacturer of electronics even as labor costs rise," says Sturgeon. "But things are still mobile, make no mistake."

For mobility, the latest buzz surrounds automated production and robotics. Hon Hai's Louis Woo, Chairman of Foxconn's retail unit and special assistant to CEO Terry Gou, says that Hon Hai plans to invest in one million robots by 2014. He said this will make Chinese labor even more cost-effective. On the other hand, China is not the only country investing in such technology.

In September, US candy-maker Hershey invested \$300 million in a US plant that uses automated IT systems, never before seen in candy production, designed to maintain production 24/7. This plant requires little more than one-seventh of its current Pennsylvania workforce. Such automation could allow manufacturers from developed countries to take advantage of their infrastructure. For Hershey, that means short distances between its plant and its milk suppliers.

### The Next Revolution

Tightly integrated manufacturing ecosystems are likely to play an even bigger role in global manufacturing in the future. For guidance on that future, Gou could look to the man behind the old-school manufacturing city of Detroit, Henry Ford.

Like Henry Ford a century ago, these Chinese behemoths have revolutionized manufacturing with a renewed focus on vertical integration. Also like Ford—whose firm was only surpassed in market share when Toyota re-invented the supply chain concept for auto factories—the Chinese manufacturers will likely weather rising wages and economic uncertainties to retain dominance in their field.

Robotics is widely predicted to be the next tectonic shift in manufacturing and Hon Hai's recent focus on robotics is clearly aimed at keeping the company ahead of the curve.

"The only way you can see such a huge advantage diminishing is if, all of a sudden, people are taken out of the manufacturing equation," says Dinges. "When that day comes, anything can happen." ■

# Stepping Out into the World

**Chinese companies are globalizing on an unprecedented scale, but with mixed success**

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By Christopher Beddor



For the investors, it was all backwards. In early 2011, Chinese dairy producer Bright Food convened a meeting with outside investors and consultants. The company had mountains of cash, priceless connections and Beijing's blessing. Having grown to become China's second-biggest food and drink company, it was now looking to expand into the UK market. All it needed was something to actually sell there.

"We asked them, 'So you're planning to sell Guangming milk [the company's flagship milk brand] in Manchester?'" says Paul French, founder of market research firm Access Asia and one of the consultants at the meeting. Bright Food executives responded that yes, they were. "We just said, 'Well then, good luck with that one.'"

The episode, compounded by later failed attempts to acquire brands like United Biscuits and Yoplait, illustrates in part why caution—bordering on skepticism—is by far the most common theme that cuts across conversations with consultants, investors and managers involved in cross-border Chinese expansion.

"Don't do it," laughs Torsten Stocker, a China-based partner at the consulting firm Monitor, when asked for the advice he gives to Chinese companies expanding abroad. "Or at least, really think about why you're doing it. These things sound easy and look great on a Powerpoint slide,

but in reality they're very, very difficult to do."

That may be an understatement. Of the 300-odd foreign mergers and acquisitions Chinese companies conducted between 2008 and 2010, around 90% failed (by definition of losing 40-50% or more of their initial purchase value), according to a report by the Brookings Institution, a US-based think tank. Many Chinese companies have little experience in M&A, much less of the complexities involved in cross-border M&A.

Get past the obligatory notes of caution, however, and nearly everyone in the field says business is booming like never before, thanks to a combination of bigger and more ambitious Chinese companies, fiercer competition and a slowing economy at home. Outbound Chinese investment grew by an average annual rate of 45% between 2002 and 2011. It surged by almost 50% in the first half of this year, and the sub-category of outbound mergers and acquisitions jumped by 29%, according to data from Dealogic. China is now the world's sixth-biggest global investor, and is on track to invest \$1-2 trillion abroad by 2020, estimates the research outfit Rhodium Group.

Moreover, the global success of at least some Chinese companies is now undeniable, bolstered in no small part by their dominance in the world's second-biggest economy. Haier is the world's largest manufacturer of major home ap-

pliances by volume. Huawei is the biggest telecoms equipment maker. Lenovo may soon overtake HP as the largest computer maker. PetroChina is the world's fifth-biggest resource company.

Chinese companies vary widely in why they choose to go global, how they go about it and their ultimate success. But those studying and involved with cross-border Chinese investment say it is still possible to tease out some basic patterns and approaches, and identify what works—and what doesn't.

### Sell Where You Know

By far the most common approach cited by those in the field is for Chinese companies to first expand into other emerging markets. Over 80% of China's outbound investment in 2011 flowed into developing countries (though that figure also includes resource-related investments), according to the National Bureau of Statistics. There are compelling reasons why Chinese companies generally find emerging markets a natural springboard for international expansion.

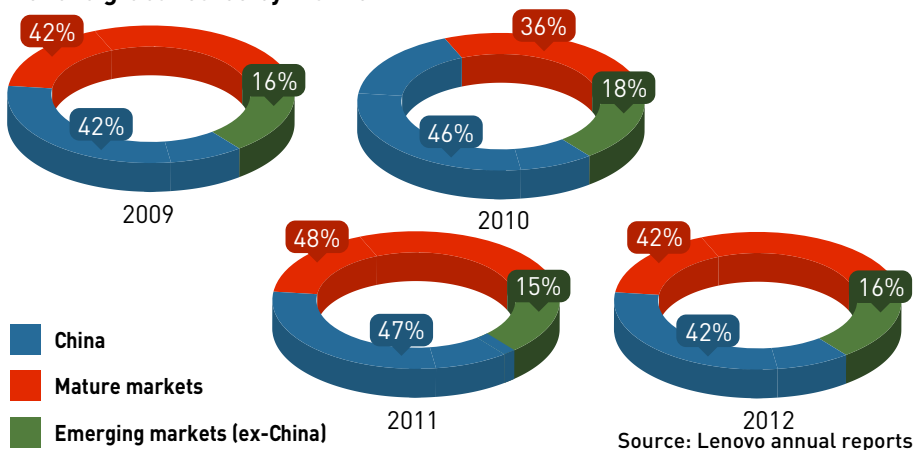
For starters, many industries in developing countries are underserved by big developed-world companies, which offer products that are either ill-suited or too expensive for local consumers. They provide an opportunity for low-cost Chinese manufacturers to edge in, usually without the need to overhaul their products.

Take the Chinese motorbike manufacturer Chongqing Lifan Industry, today a major auto manufacturer with annual revenues of around \$1.37 billion. In the late 1990s, China's motorbike industry was in a painful squeeze; supply far outstripped demand, forcing manufacturers to slash prices to break-even levels. In an industry with plenty of deep-pocketed state-owned companies, the seven-year-old Lifan's chances didn't look good.

Then the company's CEO, Yin Mingshan, took a trip to Vietnam. He found that country's motorbike market almost entirely supplied by Japanese brands like Honda and Suzuki, which were far more expensive than Lifan's own "Hongda" brand (itself more than a little inspired both in name and design by Japanese auto

## Lenovo Rakes it in the World Over

Lenovo global sales by market



makers).

In 1999 Lifan moved in, selling and distributing motorcycles at lower prices than comparable Honda and Suzuki bikes. Even so, they were still priced higher than what the same Lifan models were going for back in China, and Lifan pocketed the difference. The company then took those profits and used them to subsidize its sales at home, thereby gaining market share.

Within two years of entering Vietnam, Lifan leapt from a middling player to China's biggest motorcycle manufacturer. Today it exports vehicles to over 160 countries and regions around the world, and sales abroad accounted for over 40% of the revenue it generated in 2011.

Lifan is the model many other Chinese manufacturers look to when going global, says French of Access Asia. Not only do many also find themselves with products that could sell well to consumers in other emerging markets, but they also look to foreign expansion as a way to subsidize their operations back in China.

He pointed to Haier's expansion in Africa as another example with a similar strategy. The appliance maker has sold cut-price air conditioners, washing machines and refrigerators in the region for nearly two decades. Haier then pools revenues from these lower-end products to fund R&D and sales of premium and higher-margin appliances at home in China and in other, more mature markets.

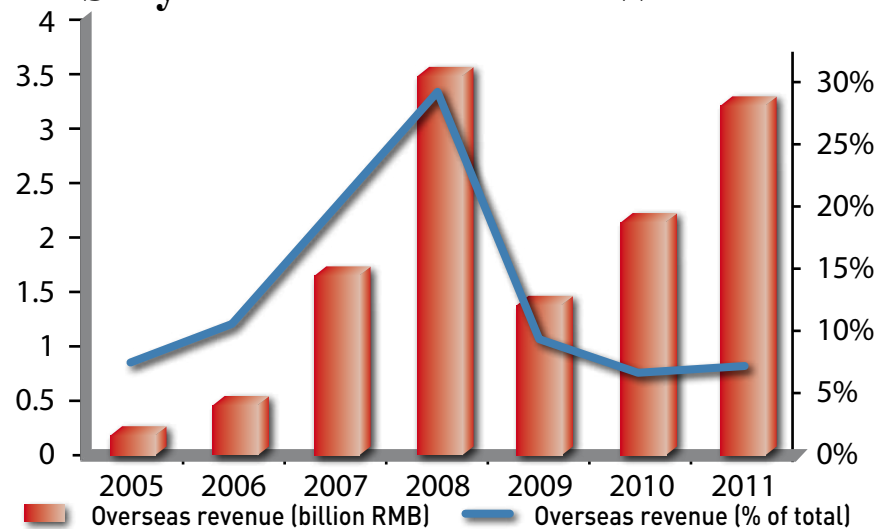
### Finding the Bottom Billion

Some companies also say they their experience in China gives them a better feel for what consumers in developing countries are looking for.

"We've gotten really good at developing technologies and products that are appropriate for [emerging] markets," says Kaiser Kuo, director of international communications at Baidu. The internet search giant is currently making forays into Egypt (where it can access users across much of the Arabic-speaking Middle East), South-east Asia and Brazil.

These are early days, but the company is optimistic about its prospects in emerging markets. Unlike Baidu's ill-fated venture into the Japanese market, where it met

## Sany Takes its Piece of the World Pie



Source: Sany Group annual report, Cheung Kong Graduate School of Business

“These things sound easy and look great on a Powerpoint slide, but in reality they're very, very difficult to do

Torsten Stocker, Partner, Monitor

stiff competition from Google and Yahoo! Japan, there are few dominant players in developing countries, says Jennifer Li, Baidu's CFO. Perhaps even more importantly, she argues that Baidu's experience

with Chinese users in rural and less developed areas has helped it learn how to cater to less sophisticated consumers.

"The beautiful thing is people who are from less developed, less sophisticated markets, they actually expect more of technology, so it is actually a spur to innovation," says Kuo. He cites the example of rural Chinese users who are unfamiliar with traditional smartphone inputs. To better serve these users, Baidu has ramped up investment in voice-enabled inputs and application activation—a technology that could transfer well into other developing countries.

"It doesn't require us to make a 'dumbed-down' version—quite the opposite, in fact," he said. "We actually make smarter products."

These "smarter products" may also be a gateway into more mature markets like the US, Europe and Japan. Steven Veldhoen, a Beijing-based partner at the consulting firm Booz & Company, points to a new trend of what his company calls "mid-market innovation": Chinese companies expanding into developed countries by selling low-priced but adequate-quality ("good enough") products. These companies target the high end of bottom-tier markets and the low end of top-tier markets.

To illustrate the trend, Booz points to Mindray Medical International, a Shen-



zhen-based medical devices company. The firm started in 1991 by supplying low-cost but functional in vitro diagnostic tools and life support systems to Chinese hospitals. Each year it ploughed about 10% of its revenue back into research and development to refine its products.

Beginning in the 2000s Mindray discovered that American hospitals were also interested in its “good enough” systems. In 2006 it listed on the New York Stock Exchange, and now ranks both as China’s biggest medical equipment provider and a strong player in the US market.

Mid-market stories are inspiring, but serious caveats apply. For one, almost all Chinese companies that have achieved a measure of success in mature markets—such as Huawei and Lenovo—derive a large share of their revenues from business-to-business (B2B) operations.

This is particularly true in the field of industrial equipment, where China’s building boom has given rise to a handful of companies that have developed the scale, capital and products to smoothly transfer business into other markets, argues Xiang Bing, Founding Dean and Professor of Accounting at the Cheung Kong Graduate School of Business, in a recent report on Chinese corporate globalization.

He points to the example of Sany Heavy Industry, an industrial equipment maker whose overseas sales jumped from around 2% of total revenue in 2005 to around 30% last year. That year the company purchased Putzmeister, a German concrete pump maker, instantly giving it access to several new markets across Europe, Asia and the Americas. The company said its international revenue more than doubled in the first half of 2012, buttressing the construction slowdown at home.

### Model or a Fluke?

A notable exception to the B2B rule may be Haier. It entered the rich world by targeting the niche US home appliance market of student dorms and small fridges in the early 1990s, then expanded outwards. It has a modest presence in Europe (about 1% of large appliance market share), and thanks to a series of aggressive acquisitions this year now has a sales and a dis-

tribution network throughout much of Japan and Southeast Asia. Most recently, in September the company made a bid for Auckland-based appliance manufacturer Fisher and Paykel, giving it greater access to Australia and New Zealand.

brands that have done a stellar job of succeeding in developed markets,” said Jessica Vaughn, trends strategist at marketing firm JWT and author of “Remaking Made in China,” report on Chinese branding in developed markets.

Making inroads with consumers in these markets requires lots of time and money to develop brand equity, she argues not least because Chinese brands must grapple with the “Made in China” stigma of inferior quality. While some, such as Lenovo, TCL, Haier and others have launched marketing campaigns in rich countries, they “are still fighting an uphill battle,” says Vaughn, and predicts that a “slow and arduous” journey to Western markets lies ahead.

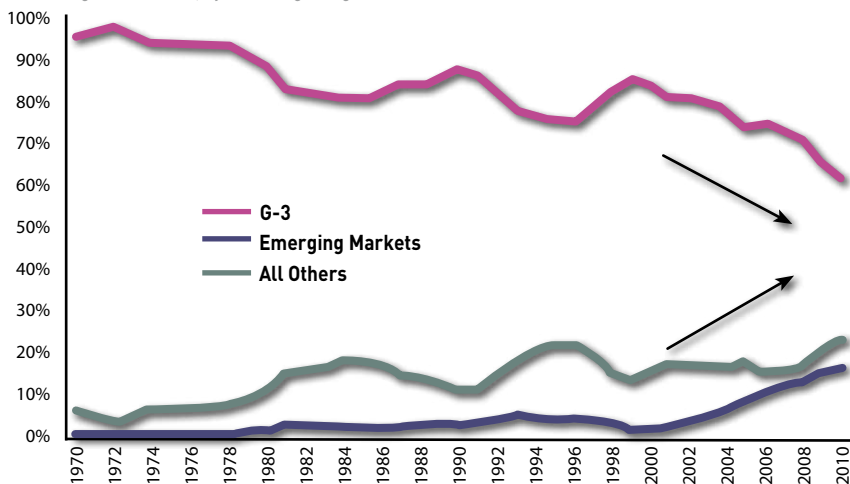
To be fair, mature markets

are tough for Chinese companies of any stripe, says Siu Fung Chan, a Shanghai-based partner covering technology and industrial equipment at Monitor. He notes even Chinese companies that appear to be thriving in mature markets are not examples of unambiguous successes; Huawei makes headlines in Europe but still generates most of its revenue from emerging markets, and Lenovo, which acquired IBM’s PC unit in 2005, has squarely focused most of its expansion efforts on countries like Brazil, Russia, and India.

Part of the problem is that, as Baidu discovered in Japan, industries in mature markets are usually dominated by powerful incumbent players. What’s more, the competitive and regulatory environment in developed countries is often very different from what Chinese companies are used to at home. Various forms of protectionism also play a role, such as America’s Committee for Foreign Investment in the Unit-

## Why China’s Companies like Emerging Markets

Percent of global OFDI flows, 3 years moving average



Source: Rhodium Group, June 2012

tribution network throughout much of Japan and Southeast Asia. Most recently, in September the company made a bid for Auckland-based appliance manufacturer Fisher and Paykel, giving it greater access to Australia and New Zealand.

But the jury is still out on Haier’s chances of success in mature markets, according to consumer goods analysts. Moreover, the home appliances industry may be so unique that Chinese companies cannot easily replicate Haier’s model in other sectors. “I think what Haier is doing works for Haier,” says Stocker of Monitor. “But is it something that Chinese consumer goods companies in other sectors can follow? I would say no, because in other sectors both the demand dynamics and [competitive] landscape are different.”

Haier aside, Chinese business-to-consumer companies tend to fare poorly in the US, Europe and Japan. “There aren’t too many examples of Chinese [consumer]

ed States (CIFIUS), a panel that screens Chinese investment and has repeatedly blocked deals.

This mismatch was behind one of the most spectacular blow-ups of Chinese outbound investment, the acquisition in 2005 of Siemens Mobile by BenQ, a Taiwan-based mobile handset manufacturer. At the time, BenQ was among the world's biggest low-end manufacturers of mobile phones, pumping out cheap handsets for

the likes of Nokia and Motorola. But its ambition was to move upmarket into the more high-margin branded mobile phone market, and when Siemens put its mobile division up for sale, BenQ pounced.

But the company belatedly discovered that European labor market rules restricted its plans to fire the German workforce, close European factories and move the production line to Taiwan. After floundering for little more than a year, the acquired

unit declared bankruptcy in 2006. Some analysts say BenQ, which wrote off nearly the entire \$1.1 billion investment, never fully recovered from the fiasco.

### Bringing it Home

Many of the most successful Chinese expansions into mature markets don't involve selling anything there at all, says Andre Losesekrug-Pietri, founder and CEO of A Capital, a fund that helps Chi-



## Double Take

When international expansion is an expensive marketing campaign

On the surface, Bosideng is just another Chinese company going global. In July the apparel company launched its first foreign store right in the heart of London's swanky Oxford Street shopping district offering expensive, limited edition suits for men.

Dig deeper, however, and Bosideng is unusual. It is well regarded in China not for its high-end menswear but for its mid-range down jackets. Odder still, most of the advertisements at its London store are almost entirely in Chinese—hardly enticing for attract British customers. What's going on?

It's all about branding, says Paul French, founder of the market research firm Access Asia. Bosideng is globalizing and its London store is aimed at Chinese consumers. The company is hoping that newly affluent Chinese consumers will see its up-scale store as they tour the city, leaving them with the impression the company is becoming a global brand and encouraging them to purchase more Bosideng products back home.

It's a risky gambit, and French is skeptical it will pay off, especially given the high costs. "Not many people are going to be willing to follow Bosideng's lead when they discover the

rents in central London," he said.

Many other Chinese firms have run foreign marketing campaigns to attract the attention of Chinese eyeballs. Yili, a dairy company, bought ads on 400 of London's red double-decker buses during the Olympics, many only in Chinese. Sportswear retailer Li Ning launched a store in Portland, Oregon in 2010, but closed it this year in the face of tougher business at home.

Chinese companies are always eager to gain a "seal of approval" from Western icons and brands because it boosts Chinese labels in the eyes of consumers, said Jessica Vaughn, trends strategist at marketing firm JWT. She noted that Li Ning and its rival, Anta, have recently struck deals with foreign sports talent, including US basketball player Kevin Garnett. Meanwhile, Meeters/bonwe, a mid-range Chinese apparel company, purchased product placement space in the *Transformers* movie, and has been collaborating with the online game *World of Warcraft*.

Reports suggest the product placement approach is enjoying some success, said Vaughn. For all its chutzpah, the same cannot yet be said of Bosideng's London play. ■

nese companies invest abroad.

“You have a lot of Chinese companies that are really waking up to the fact that they have rising labor costs but they don’t have a brand or technology,” he said. “So when you look at these companies, they’re still growing very fast, but the margins are getting thinner and thinner.” In response, many are now looking to acquire foreign technology and human capital in order to boost competitiveness back home.

To illustrate this point, Chan of Monitor pointed to a deal announced in August in which Wanxiang Group, one of China’s biggest auto parts makers, agreed to pay \$465 million to acquire A123 Systems, an American battery maker.

A123 was founded in 2001 to develop advanced lithium-ion battery technology for use in electric and hybrid vehicles in the US. When the market for electric cars failed to take off as quickly as the firm expected however, A123’s share price collapsed.

For Wanxiang, the acquisition provided a chance to purchase next-generation electric battery technology, production facilities, as well as the company’s talent (Wanxiang’s memorandum of understanding with A123 includes plenty of incentives to keep the brains on board). The acquisition also bolsters Wanxiang’s position in the Chinese auto parts market, because A123 was a supplier to one of China’s biggest auto manufacturers, Shanghai Automotive Industry Corporation (SAIC).

For Chinese companies looking to acquire operational know-how rather than assets or patents, minority equity stakes are the more popular route of choice. By taking a minority stake in experienced Western firms, Chinese companies can usually strike side deals to swap employees, customers and advice on improving operations at home in China. Such minority equity stakes made up a whopping 70% of Chinese investment in Europe during the second quarter of 2012, according to figures from investment fund A Capital.

They have been particularly useful in the natural resources sector because they avoid the political backlash that could

“  
What else are  
you going to do  
with the money?  
Maybe buy a  
chain of hotels  
in Hainan or  
something

Paul French,  
Founder, Access Asia

come with full takeovers, says Thilo Hanemann, research director at Rhodium Group.

China National Offshore Oil Corporation (CNOOC), for example, made a \$18.5 billion offer for US-based oil and gas firm Unocal in 2005 that was blocked by opposition in Congress. After withdrawing its bid, CNOOC re-focused on acquiring unconventional oil and gas extraction techniques from North American companies for use on shale deposits in China.

The company re-entered the American market in 2010 when it bought a \$2.2 billion minority stake in Chesapeake Energy. It has since increased that stake, and taken additional stakes in MEG Energy, Norway’s Statoil (which owns some US-based resource assets), and others. “In many cases, it has worked out better than 100% ownership,” says Hanemann.

### A Bright idea

Yet for all the clever and counter-intuitive reasons Chinese firms choose to go global,

few are as unexpected as that of Bright Food. After the meeting with investors last year, the company announced in May 2012 that it would purchase a controlling stake in Weetabix, an iconic UK cereal brand, in a deal that valued the company at nearly \$2 billion.

Breakfast cereals are a fast-growing market in China, particularly in the muesli category (in which Weetabix owns the valuable Alpen brand). Besides distribution opportunities in China, Weetabix could lend Bright Food some brand cachet.

But cereals (and foods of any kind) tend to be unique to certain regions, and it will be tough to transplant Weetabix’s offerings to the China market, say analysts. While these are still early days, neither Bright Food nor Weetabix has yet announced any plans to make major changes to their product line-up or distribution. French of Access Asia says he’s spoken with executives at Weetabix, who report that Bright Food has taken a hands-off approach to the company.

Rather, the acquisition probably had a much more mundane purpose. “The logic [to the takeover] is that you’ve got a lot of cash in a very high currency that you need to do something with,” says French. With asset prices in the US and Europe at record lows, Bright Food reckoned it was a good time to go shopping for Western food brands.

If the British economy improves it could yet prove a smart buy, especially considering the alternatives. “What else are you going to do with the money? Maybe buy a chain of hotels in Hainan or something,” French muses.

That one of China’s biggest outbound deals of the year might simply have been a portfolio investment will disappoint those in the British press who muttered darkly about a Chinese state-owned company stealing their prized cereal brand. But Chinese companies have long defied easy assumptions, and will no doubt continue to do so as they globalize and achieve success at an international level. After all, says French, they never really planned to sell Guangming milk in Manchester. ■

# TO SERVE OR NOT TO SERVE?

**Companies need to step-up their service in China  
to satisfy the new sophisticated customer**

By Mark Andrews



lining up for a table at the Hai Di Lao Sichuan hotpot restaurant in Beijing is not such a bad experience—you get served tea and snacks and can even opt for a manicure while you wait—a welcome reprieve from other restaurants where creature comforts are an afterthought.

The latest battleground in the retail world of China is customer service. Competition is forcing companies from state banks and airlines to restaurants and auto showrooms to take greater care to attract and keep customers happy because Chinese consumers are becoming more savvy about, and insistent on, good service.

Up to the mid-1990s, poor service was expected. In a typical shopping interaction, a customer would approach a counter behind which were arranged goods guarded by an indifferent salesperson reading the newspaper, talking to another assistant or napping. A request to see a product was often rebuffed with a *meiyou* (not in stock), even when the product was evidently on the shelf.

That was the result of little competition, according to Ed Dean, founder of Shanghai-based customer service consultants group JETT. “For those businesses, it didn’t really matter if they sold anything, they weren’t going to go out of business,” he says.

But in China’s increasingly competitive consumer markets, good service matters and businesses are fighting for



People are now aware of what they didn’t have before

Ed Dean  
Founder, JETT

the attention of increasingly wealthy Chinese consumers. Expectations are rising amongst the middle-class particularly given an ever-growing number of people returning from study or work overseas with a radically revised view of service.

The inroads multinational companies have made in the Chinese market are also impacting overall standards. Apple’s stores provide a stark contrast in China to a walk around a local computer mall.

“People are now aware of what they didn’t have before,” says Dean.

Old habits die hard however, and many companies are simply unable to live up to the new expectations of consumers.

“Most of the working staff in China have only a very vague idea about what customer service means,” says 35-year-old Mihkay Rose, a Shanghai resident originally from Xinjiang. “They maintain traditional market thinking which simply means a sell and buy relationship.”

Chengdu native Jimi He is more blunt: “Either they don’t give a damn about the customers, or they promote their goods in the wrong way.”

Li Wei, Professor of Accounting and Finance at CKGSB, says that this gap between expectation and what is delivered is a big issue in China. “Consumer needs are rising every day but the development of customer service is not as fast,” he says.

### Filling the Gap

The customer service gap is exacerbated by the changing characteristics of both consumers and products.

Benjamin Cavender of Shanghai-based China Market Research Group points out that the 18 to 35 age group is driving spending, and tending to be only children. They’re used to being doted upon, “so they are demanding a lot more from companies when they go to shop for products.”

In an increasingly competitive market, companies have an “incentive to provide better customer service,” says Li.

Dean agrees: “You need to care about repeat business and this comes from a good reputation. A good reputation comes from having a good brand and good service.”

The McKinsey consultancy group, in a recent report on Building Brands in Emerging Markets, referred to the crucial impact of customer service in the retail decision-making process.

“The in-store experience is by far the biggest factor in finalizing emerging-market consumers’ flat-screen-TV purchase decisions, and Chinese consumers are almost two times more likely to switch brand preferences while shopping for fast-moving consumer goods than US consumers are,” the report says.

As China becomes richer, customers are often buying products for the first time. McKinsey pointed out that first-time buyers account for 60% of auto purchasers

## Less to Feel Sore About



Source: China Consumer’s Association

in China. With consumer electronics, between 30% and 40% of laptop purchases in China are made by first-time buyers, says the McKinsey report.

“They’re purchasing products they haven’t bought before and so they are expecting education (from sales staff) to go with that,” says Cavender.

It is not only tier-one and two markets that are seeking a better customer service experience, says Jeffrey Tan, research director at Starcom MediaVest and author of the firm’s Yangtze Study. In fact consumers in remote areas need more help in deciding what to buy: “Consumers need more guidance in lower tiers and so there is a more important role for shop keepers and sales people.”

Another emerging issue for customer service representatives is post-sale assistance.

CKGSB’s Li says that transactions for products like automobiles and computers, where follow-up care and maintenance are at play, aren’t necessarily done when the sale is made, and customer service has to extend to after-sales support. As Chinese consumers continue to increase their consumption of these high-value items, so must the attention to the service surrounding these purchases.

“I have seen many businesses in China succeed through better customer service,” says Jason Inch, author of China’s Economic *Supertrends* and founder of In China Corporate Training. “These include domestic Chinese companies such as Haier, with its after-sales service, and Hai Di Lao Hot Pot’s famous waiting area service.”

Middle-class consumers seem increasingly prepared to base their purchasing decisions on customer service.

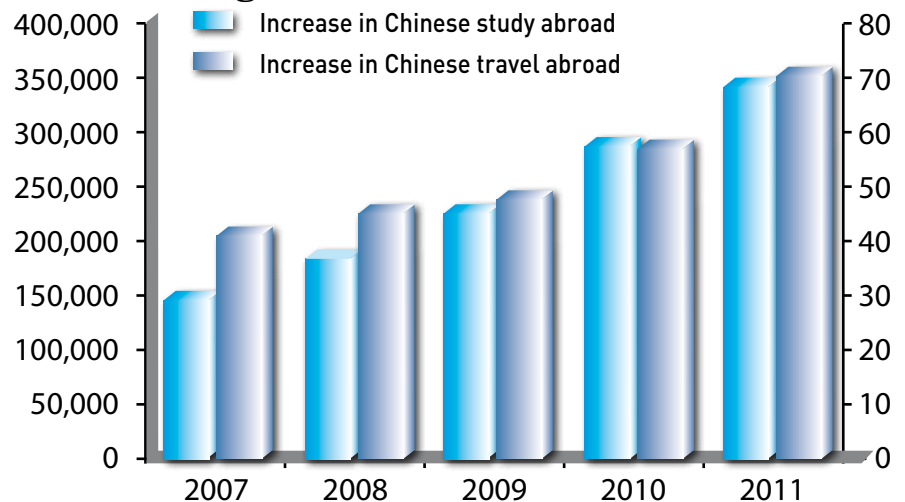
“It directly decides if I would consider using their service or not the next time,” says Rose.

Such attitudes contrast starkly against past ones in China where price and function were the only considerations.

### The Bumpy Path to Service

There are several challenges to delivering better customer service in China, but first and foremost is finding and training the staff.

## Coming Home with More Demands



Source: Ministry of Education, National Tourism Administration

Cavender says this is particularly clear with in-store sales. “It’s difficult to train them to really know the products—as they need some level of experience with them—and to know how to interest the customer,” he says. “It is also very difficult to teach someone to cross-sell. Most service staff aren’t able to suggest what will go well with, say, a suit because they haven’t been taught it or received that kind of service themselves. It’s something the customer in China absolutely wants but it is very difficult for them to get.”

One reason it is so difficult to find the right people is that service jobs are sometimes viewed negatively, with a subconscious belief amongst Chinese people that it is demeaning to serve.

Chinese parents prefer their children to work in a ‘more respectable’ environment, such as an office. Dean recounts an example of parents in Suzhou marching into a hotel where their daughter was employed and telling her that she was no longer to work there, but at an office job they had found for her.

Once the staff are hired, there is still the question of keeping them motivated to provide good service.

CKGSB’s Li says ‘reciprocity’ can be problematic. In the hospitality industry of most mature markets, there is a ready-made prescription for dealing with difficult customers, one usually stemming from a ‘customer is always right’ philoso-

phy. In China however, nasty customers can have a much graver impact on employee morale. When training, Dean said he encountered reluctance from hotel staff to even greet customers because of their lack of response.

The cultural concept of ‘losing face’ makes the rapport between staff and customers particularly crucial when Chinese consumers are purchasing high-value goods such as vehicles and computers, and doubly so for first-time buyers.

Li says it is important that customers feel like the company cares about them and they are given respect, particularly when things go wrong.

While the indifferent sales person has probably retired by now, stories of poor service are still rife. One Bank of China customer, who prefers to be unnamed, tells of having to fly from Guangzhou to Shanghai to get a replacement bankcard simply because his account was opened in Shanghai.

Banks in China are notoriously inefficient, a problem common to many of China’s state-owned enterprises, thereby holding back the average level of service in China, says Li.

For some Chinese companies, their very structure may be the cause of inefficiency and ineffective customer service. A global Accenture customer service survey shows that one key factor to gaining a rating of ‘satisfied’ from a customer is the ‘one-stop-shop’ factor. Many large stores

in China take a fragmented approach to problem solving, where a simple refund can involve anywhere from two to five people up the command chain, leaving the customer less than satisfied.

### Getting it Right

Some companies are overcoming the obstacle of cultural attitudes by going on the offensive, and making their work environment irresistible to would-be employees. This allows them to generate high morale, which is reflected in the way the customer is treated.

In an industry known for high turnover amongst staff, Element Fresh—a China-based restaurant chain—has over 300 people who have been with them for more than three years, and they have been ranked one of China’s Top Employers by the CRF Institute, a UK-based global human resources research organization, every year since 2009.

“Service 10 years ago was very basic, and mostly reactive, guests waving and calling ‘*fuwuyuan*’ (waiter),” says Frank Rasche, Managing Partner of Element Fresh. One of the ways they have overcome this and achieved staff retention is by building a strong team with a cohesive culture, “a team that stays together and develops.”

Rasche attributes the chain’s quick expansion in China’s major cities to their service approach. “We treat guests like friends,” says Rasche. “We encourage our team to interact with a friendly yet confident attitude. We are not asking our staff to be subservient.”

Rasche is one of many who agree that training is crucial to improving customer service. But it is also a big investment with only long-term payoffs, deterring many Chinese companies, says Cavender.

Every sector has a balance that must be struck in which competitive pricing and customer service complement one another, and lopsided attention to one over the other is not always the best approach. Too much stress on customer service, to the detriment of margins, is also something companies have to avoid.

Mark Ray, Director at the Shanghai branch of market research firm JLJ Group, points to Best Buy’s unsuccessful foray



Only  
management  
buy-in is going  
to change the  
systemic issues  
in a company

Mark Ray  
Director, JLJ Group

into China saying there was “an overemphasis on the importance of the custom experience, in an industry that demanded tight margins in order to compete.”

Before closing, Shanghai’s principal Best Buy location was across the street from the famed Pacific Digital Plaza, where every tech product under the sun is sold and haggling prices to half their original amount is commonplace. This was simply not a boutique market location.

In striking the balance, some businesses are incorporating training that gives their employees a peek into different markets with more developed service approaches, to compensate for a lack of first-hand service experience.

Jason Inch describes KFC’s entry into Beijing, where trainees watched recordings of their Hong Kong and Singapore operations to show staff the expected service. To further the understanding, Inch says role-play is effective in building empathy for the expectations of the customer. Videotaping interactions and then reviewing “helps them to improve attitude and see how they could have solved a problem in other ways,” says Inch.

The current lack of staff with first-hand

experience of quality customer service is likely to be less and less of a problem in the future. With increasing numbers of college graduates entering the job market, there will be an increase of better-educated personnel in these jobs.

“We are going to get people filling these roles going forward who will have had some experience with these products and services, but it is going to be a gradual change,” says Cavender.

Regardless of the anticipated influx of educated personnel, nothing is a substitute for management acceptance of the concept of customer service.

“Only management buy-in is going to change the systemic issues in a company, so I think the challenge is first to change the processes, and then train for the new desired behavior,” says Inch.

Travel booking firm Ctrip uses a process of “six sigma” to standardize the travel service experience. Call monitoring is used to ensure consistent use and to create continual improvement. Ctrip’s emphasis on customer service has earned them a more than 40% share in all major segments of the OTA market, according to a 2011 China Internet Network Information Center survey.

Continual improvement is important, says JLJ Group’s Ray: “Those who have been successful will tell you that it is an ongoing process that never stops; with the most successful just as focused on the customer experience as with innovation. Think Apple.”

Another area where management buy-in helps is support for staff. Inch believes it’s important for staff to see how what they do impacts the company, and for them to be noticed provides initiative to offer good service. “So-called extrinsic motivators are very important for younger Chinese workers, who want individualized recognition,” he says.

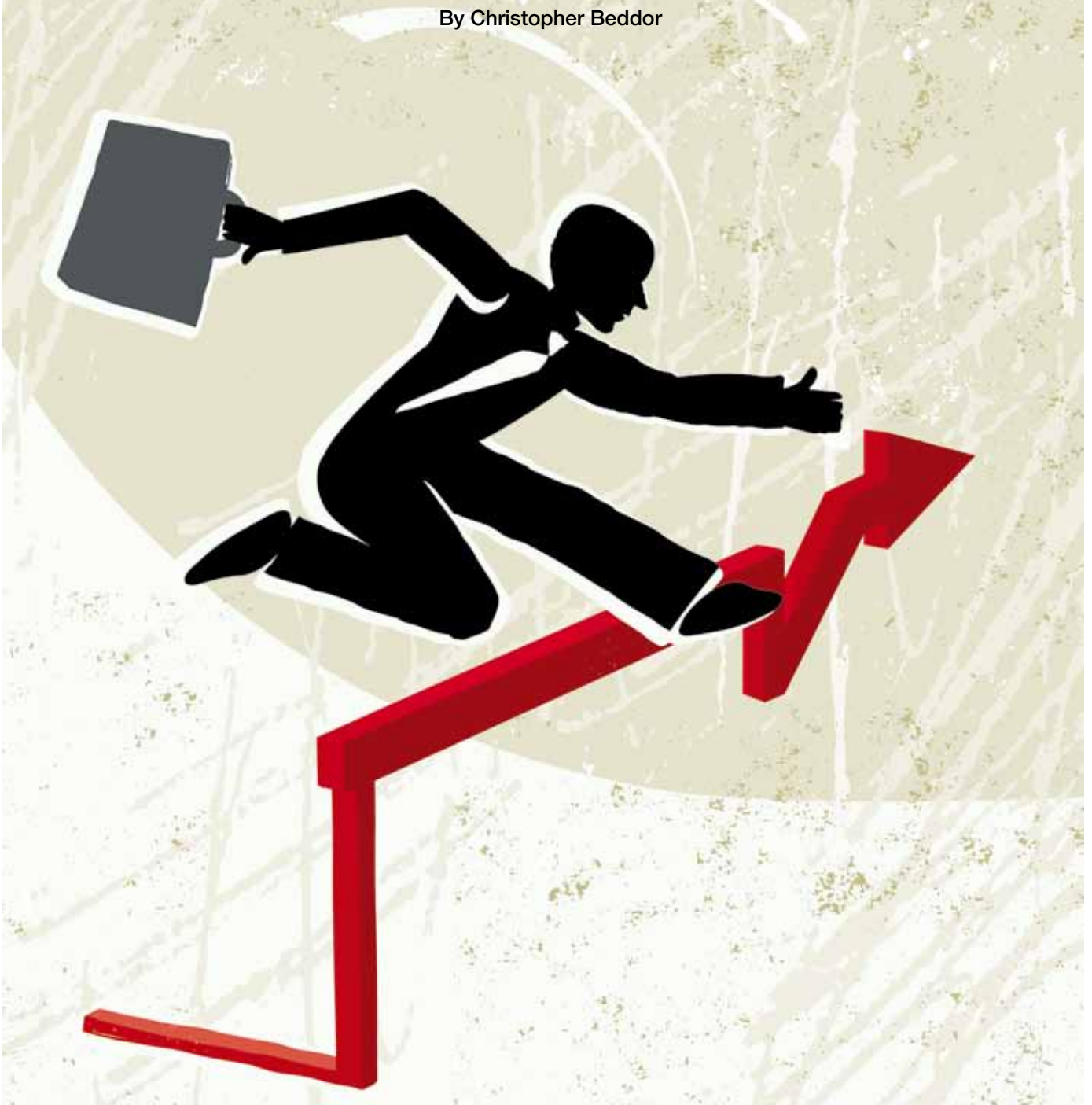
In China, the next growth story will be the lower-tier cities. In these markets, the personal touch can be an even more effective weapon in gaining market share.

“They are not as exposed to information. They’re looking for people who can guide them and enrich them with knowledge,” says Starcom’s Jeffrey Tan. ■

# Clearing the Hurdle

**Chinese companies facing low valuations on US stock exchanges  
have some options left on the table**

By Christopher Beddor





**W**hen investors think a company's market price is undervalued, they can buy the company's shares. But when a company thinks itself to be undervalued by the market, it sometimes opts to buy out the investors.

Such is the case with Focus Media, a Nasdaq-listed company that operates ad displays in elevators, supermarkets and subways across China. The company announced in August that it was in talks with a group of investment funds to go private. The \$3.5-billion deal is still pending, but if it goes through, it will be the biggest leveraged buyout ever of a China-based company.

Focus Media is one of a number of victims of short-seller attacks on US-listed Chinese firms over the past two years, based on reports of alleged fraudulent practices of various kinds. The assault on Focus Media followed a report in November of 2011 alleging the company had overpaid for acquisitions. It did not force a delisting, but its shares have languished for months at a low valuation, along with most other small- and medium-sized Chinese companies listed in the US. The buyout announcement effectively signals that the big-name funds involved—including the Carlyle Group, FountainVest Partners, CITIC Capital Partners and Temasek—have concluded that the basic problem is not with the Chinese company, but with the US markets.

They are not alone. Focus Media is only the biggest of a growing number of Chinese companies looking to delist from the US, fed up with low valuations there.

"Some [Chinese] companies felt disappointed after listing in the US," says Zhu Guofan, CEO of the Chinese foot massage chain Beijing Tailian Liangzi Health & Fitness.

Other Chinese companies are scrapping plans to list in the US. China's technology firm Huawei recently told CNN that it had 'no plans' to list on an international exchange, largely due to negative reports about the company in the US.

Chinese companies already listed on American exchanges have various options to consider. For starters, they could look to try their luck on another exchange, as

Focus Media seems to be looking to do. They can arrange cash to buy out investors and "go private."

But another option for companies is to improve their systems, ensure compliance with market requirements, improve transparency and their public image to ward off short-seller attacks and low valuations. Some US-listed Chinese companies are doing just that and in the long run such reforms could pay off handsomely.



A couple of years ago, we would go to China and every company wanted to do a reverse merger in the US

Kevin Pollack, Managing Director,  
Paragon Capital

### Good Old Days

"A couple of years ago, we would go to China and *every* company wanted to do a reverse merger in the US," recalls Kevin Pollack, Managing Director at Paragon Capital, a fund that invests in US-listed Chinese companies. Reverse mergers—the process of buying out a company already listed in the US and inserting assets from the buyer—were a popular "backdoor" route to American markets for Chinese companies too small to afford an IPO.

That came to a sudden halt in 2011 due to a rash of short-seller attacks and finan-

cial accounting scandals among US-listed Chinese companies. The Bloomberg Chinese Reverse Mergers Index crashed by around 65% over the course of that year, and the Halter USX China Index—an index of US-listed companies that derive most of their revenue from China—fell by almost 30% over the same period.

The most famous, an attack by research outfit Muddy Waters on the Toronto-listed Chinese lumber firm Sino-Forest, eventually led to a fraud investigation and the humiliation of John Paulson, the manager of a multi-billion dollar hedge fund that had bet heavily on the stock.

Short-seller attacks have since become rare. But the stigma remains, and nearly every index of US-listed Chinese stocks continues to plumb new depths independent of the overall market direction. "Investor sentiment has not really improved," says Pollack of Paragon Capital. "I know a lot of funds that got burned and have said they'll never invest in another Chinese company again. It's going to be very hard to bring those investors back in."

Little wonder, then, that many US-listed Chinese companies have given up even trying, opting instead to delist from the American markets. In 2011, 10 Chinese companies worth a combined \$3.5 billion delisted from US exchanges (up from zero in 2010), according to data from Roth Capital Partners. By contrast, new listings from Chinese companies fell by almost half to \$2.2 billion in 2011, meaning US markets experienced a net outflow of Chinese equities.

Estimates of the number of Chinese firms that have or plan to delist this year vary, but Groves of DAC Management puts the outstanding figure at around two dozen.

### Rebels Without a Cause

Delisting is not necessarily an easy course for frustrated US-listed Chinese firms. For one thing, they must reach agreement to buy out US investors, says Groves. Lawsuits are often involved.

In terms of re-listing, Hong Kong is an attractive option, but some Chinese companies are experimenting with smaller exchanges like Sydney, Frankfurt, Singapore

## Disillusioned, Chinese Companies Pack their Bags

Delisted		Applying for Delisting	
Longtop Financial Technologies	NYSE	7 Days Group Holdings	Nasdaq
Harbin Electric	Nasdaq	Feihe International	NYSE
China Biotics	Nasdaq	Lizhan Environmental	Nasdaq
Duoyuan Printing	NYSE	Syswin Inc	NYSE
Duoyuan Global Water	NYSE	China Valves Technology	Nasdaq
Rino International Corporation	Nasdaq		
China Mediaexpress Hldgs Inc	Nasdaq		
Jiangbo Pharmaceuticals Inc	Nasdaq		

Source: Reuters, Bloomberg

or Seoul. China King-Highway Holdings Ltd., Global SM Tech Ltd and China Engine Group, for example, listed with Korean exchange KOSDAQ in 2009. But these bourses are much less liquid than the US, and generally offer even lower valuations.

Instead, many Chinese investment banks are now pitching US-listed China companies to re-list on the Shanghai or Shenzhen exchanges, says Groves. Bankers say these markets offer valuations several times higher than what companies are getting in the US.

That may be true but it misses the point, argues Li Wei, Professor of Economics and Emerging Market Finance at the Cheung Kong Graduate School of Business. Unlike regulators in the US, the China Securities and Regulatory Commission (CSRC) approves for listing only companies it thinks are surefire winners. Peter Fuhrman, chairman of the private equity fund China First Capital, has estimated about 10-15% of applicants were approved in 2010.

Because listing is so exclusive and Chinese investors have few other asset classes in which to invest, valuations on Chinese stock markets can be high. "If you've got a quota to be on the list [of approved IPOs] by the CSRC, it's as if you've got a machine to print money," says Li. But delisting from the US without a guaranteed spot in China would be very risky.

The bottom line is that there's no obvious substitute for the US markets.

"What is the right path?" asks Pollack of Paragon Capital. "Today it's no longer clear, there is no right answer."

### Charm Offensive

For Chinese companies that do stick it out in the US, there are other ways to boost investor confidence and perhaps their valuation, says Pollack.

Many Chinese companies claim to have lots of cash on hand—something hard for investors to independently verify. They could demonstrate their bona fides through a big stock buy-back, which would double as a signal of management's faith in the company. They might also consider giving the money back to investors via dividends.

US-listed Chinese companies could also upgrade their audit and legal service providers to big-name global brands (despite the issues many of these brands, especially auditors, have had in China). Finally, advises Pollack, hit the road: "Management teams still need to spend time in the US meeting with investors and sharing their story," he says. At the very least, they might find someone willing to take them private.

Pollack points to two companies that have successfully pursued such strategies after being attacked by short-sellers. After its report on Sino-Forest, Muddy Waters hit Spectrum, a Chinese communications firm, in late June 2011. The firm "responded very well," said Pollack, by addressing the allegations, buying back stock and issuing dividends to investors. Silvercorp Metals, a natural resource firm targeted by short-seller Alfred Little, pursued a similar strategy with success.

These are smart steps, but many—including Pollack—caution that the road

back into investor graces is not an easy one. Small and medium-sized Chinese companies are often behind on their US financial filings, and all the buttering up in the world can't undo the fact that should something go awry, US-based investors are now aware that it is very difficult getting at the underlying assets of Chinese companies.

"It's funny—as we're talking to [Chinese executives], all of a sudden the light bulb goes on and the Chinese company realizes that if they just take their company and leave, it's very difficult for the foreign investors to get paid back," he says. Smart US investors discount Chinese shares as insurance against such a possibility.

### Here be Regulators

Tensions between American and Chinese regulators also impact the valuations of Chinese companies listed in the US. One dispute is over whether US financial regulators should be allowed to inspect the books of auditors overseeing US-listed Chinese companies (which China claims is a violation of its sovereignty). Negotiations have hardened over the past year, to the point that some speculate that all Chinese firms could be forced to de-list from US markets.

But despite all the obstacles, many investors expect small and medium-sized Chinese companies to eventually return in force to the US market and valuations to rise. "I'm still very bullish on China—there's some good companies out there that are undervalued," says Pollack of Paragon Capital.



# Transitioning Online

Sun Weiming, Vice-President of China's electronics giant Suning, on the company's foray into e-commerce and the synergies between brick-and-mortar and online

By Crystal Niu

One of the biggest “3C” (computer, communication and consumer-electronics) retailers in China, Suning Appliances operates more than 1,700 chain stores, with one seemingly on every street corner of Mainland China. In a recent survey, Suning was named as one of the top three private enterprises in China (the others being steelmaker Jiangsu Shagang and Huawei Technologies). With continued expansion into overseas markets and further acquisition, Suning is poised to become China's answer to Best Buy, the well-known US consumer electronics retailer.

With e-commerce booming in China, Suning has been working to dramatically expand its business-to-consumer (B2C) online store, and the move has given Suning a boost both in terms of its market positioning and also its financial results. As

Suning Vice-President Sun Weimin says, the company today is focused on both online and offline business.

Vice-President Sun, a graduate in Psychology from Beijing Normal University, has helped Suning become one of the biggest 3C retail companies in China. With a strong marketing background, Sun shares his ideas on the ideal relationship between brick-and-mortar stores and online retail, as well as the status of the retail industry in China as a whole.

*Q. Suning has expanded its sales network with more chain stores, but it opened less stores this year than in previous years. What factors are driving this? Is it a statement on the Chinese economy or on the status of brick-and-mortar stores?*

A. We plan to open around 200 stores this year, which is a little fewer than last

year. However, we are focusing on the improvement of the service by optimizing our stores. Frankly, it [the decrease] has to some extent impacted our business as a whole, but I do not think it is merely because of the decrease in the numbers of stores. The macro-economic environment from the outside world is one of the major factors.

*Q. With so much attention being given to brick-and-mortar stores opening online outlets this year, what do you see as the right relationship between stores and their online components?*

A. For my part, they are both good channels for marketing. On one hand, we try to fuse the two approaches—brick-and-mortar stores and online outlets—by posting our products at the same time and by selling them at the same price; on the other hand,

we hope to expand our market with the aid of the Internet, as it will be the ideal platform for enriching our products and services.

*Q. An article in Global Entrepreneur suggested that Chinese brick-and-mortar stores are following the US model, where more than half of the most successful online retailers are related to major retail outlets such as Walmart and Macy's. Do you agree? To what extent is there or can there be a Chinese model?*

A. There are big differences between the retail business in the US and China. In the US, consumers rely on their cars and highways to shop even if the big stores are nearby. However, in China, most of the stores, especially the superstores, are located in the core shopping zones of big cities. For the past decade, there have been many first-class e-retailers emerging in the US, such as Amazon; while even more e-retailers originate from the traditional brick-and-mortar stores. By contrast, China is a late starter in terms of e-business. What we should do now is set up the codes and standards so that more offline retailers are allowed to develop their online business.

*Q. How does Suning.com distinguish itself from other B2C online outlets? You have said that Taobao's [an online trade platform, owned by Alibaba] platform can be difficult for beginners to master. To what extent is user-friendliness a key focus of Suning's online store?*

A. Firstly, I think Suning has a head start in the 3C business market in China; and this is our main advantage. Secondly, we have accumulated resources in this sector for more than 20 years, especially in terms of management and logistics service. Last but not least, we have acquired abundant capital to further develop our business. As the third-party platform, we serve not only the suppliers, but also the consumers. We attempt to provide an all-around, one-stop shopping service for our customers in order to meet their demands.

*Q. You recently said that Suning is attempting to raise up to \$1.26 billion*



We try to fuse the two approaches—brick-and-mortar stores and online outlets by posting our products at the same time and selling them at the same price

*through bond sales in order to achieve a cash balance of \$5.21 million. How is it going, and how will Suning spend the cash?*

A. Right. The fact that we have raised RMB 4 billion (approx. \$640 million) and RMB 8 billion (approx. \$1.3 billion) separately in this July and August is based on our development strategy for 2015, which aims to improve our logistics and data-center system. In this way, we're preparing to build up both the online and offline retail outlets across the country with this money.

*Q. Suning ran into some trouble with the NDRC [National Development and Reform Commission], along with other e-commerce retailers such as 360buy.com*

*and Gome, due to price claims made on their respective websites not being followed through in the actual stores. Do you feel this exposes a general weakness of online shopping in China that should be addressed? If yes, how?*

A. It is not uncommon to see such competition among the e-businesses, such as the price war between these three companies. Now, China still needs further improvement on determining whether or not the basic rules can be effectively implemented in online business. For example, have the online outlets legally registered or paid taxes? Are the online stores doing illegal business such as selling smuggled goods? I think it's both important and urgent that we set up an effective system to better supervise these operations.

*Q. Are brick-and-mortar stores here to stay? Where is the next growth push come from?*

A. Before 2005, we focused on the big cities of China. Since then, we have attempted to extend our products and services in every region of China. So far, we have built our brick-and-mortar stores in more than 600 cities across the country. We plan to develop our business in two major areas: first, to upgrade our retail stores in terms of quality and quantity; and second, to focus on the market expansion of some third- and fourth-tier cities in China.

*Q. Suning is now the major shareholder of the Japanese home electronics chain, Laox. What was the main goal of the acquisition and how has the strategy worked so far?*

A. Laox was once ranking in the top 10 electronic stores in Japan. However, last decade has seen its fall in sales, so we decided to buy it in 2010. By acquiring Laox, we hope to accumulate more experience for our globalization strategy. As one of the most successful home-appliance retail companies in Japan, Laox can help us learn a lot so that we could do better for our customers in the future. So far, this project has worked well. We have provided financial support for Laox and helped it develop in the Japanese market. ■



# Rebooting Innovation

**Henry Chesbrough believes that in the future, innovation communities will push the boundaries of Open Innovation, the concept he pioneered**

By Neelima Mahajan

In the year 2000, the then CEO of Procter & Gamble A.G. Lafley, decided that it was time to crank up his company's innovation machinery. The old model of relying on internal research and development capabilities had worked well when the company was worth a mere \$25 billion. But when it became a \$70 billion company, P&G needed something strong to propel future growth. And so, Lafley boldly proclaimed that 50% of all P&G's innovations had to come from outside the company. It seemed like a radical idea to many, but Lafley had figured out something that many CEOs have a hard time grasping: there are limits to how much a company's internal R&D can do.

P&G set up Connect+Develop, a program which identified innovative ideas from outside the company and developed them. The ideas came from many sources

including consumers, inventors, suppliers, competitors and university labs. The experiment paid off, and led to many innovative products. Febreze, for instance, began as a household textile deodorizer in 1998. When the company decided to extend the brand to include air fresheners, car perfumes and odor eliminating candles, it used Connect+Develop to reach out to external partners with proven expertise in these areas. Fast forward a few years, and Febreze has become a \$1-billion brand for P&G. Buoyed by the success of the program, the company is now aiming to generate more than \$3 billion of new business each year through Connect+Develop by 2015.

Over the last 10-15 years, many companies have, like P&G, discovered the benefits of innovation coming from outside the boundaries of the firm, something that Henry Chesbrough calls Open Innovation.

Chesbrough, Adjunct Professor and Executive Director of the Garwood Center for Corporate Innovation at University of California, Berkeley's Haas School of Business, is widely regarded as the father of Open Innovation. When he first came up with the concept after observing strands of it play out at both Xerox's Palo Alto Research Center and his old employer Quantum Corporation, it had few takers. Academic journals refused to publish his research because it was very hard to prove why Open Innovation was better than Closed (or firm-centric) Innovation.

So Chesbrough ended up writing his observations in his book *Open Innovation: the New Imperative for Creating and Profiting from Technology* (See 'The Genesis of Open Innovation'). The book was a hit and helped establish Open Innovation as a game-changing idea in the management

landscape. Chesbrough followed it up with two more books advancing the idea further. Many companies such as have IBM, GE, Hewlett-Packard, Nokia and Reckitt-Benckiser have adopted Open Innovation to some extent. In a variant of the idea, entire companies—such as InnoCentive which was spun-off from pharmaceutical giant Eli Lilly—are based on the concept of Open Innovation.

Open Innovation is a popular and established concept now, but Chesbrough believes that its potential hasn't yet been fully explored. He feels that the next big push will come not from companies, but from what he calls 'innovation communities'. Early signs of this are already visible. Chesbrough recently did a study on General Electric's ecoimagination Challenge, an initiative that aims to create innovative solutions to counter environmental challenges. "(GE Energy's) traditional customers were power plant generation companies, utilities and big entities which bought megawatts of power from GE turbines and things like that," says Chesbrough. The company noticed that there were a lot of small ventures coming up in the energy space, which unlike

the big, traditional companies, produced power in kilowatts rather than megawatts and were selling power to households or commercial establishments outside of the grid.

GE wanted to be a part of this, but given their business model, it was a space they didn't understand too well. "They created a process and committed \$100 million to put out a call for proposals for ideas that could be used to start up new ventures in these green and renewable spaces where they themselves were not well represented," says Chesbrough. For a company of GE's size, that was a pretty sizeable chunk of money being set aside for an R&D approach whose pay-off was uncertain. Instead of doing it alone, GE involved a bunch of other venture capital (VC) firms that put in another \$100 million. Each of these VCs had their own independent investment authority. Together, they invited submissions and ended up funding 23 ventures.

Interestingly, GE Energy made sure that ecoimagination was set up at an arm's length from its internal corporate process, and run through their venture capital arm which does venture investing for the group

businesses. The logic was simple: if a new initiative, radically different from the current business model, is set up within the organization, chances are established systems and processes might stifle it. With the venture capital organization, they were able to "plant a number of seeds (and) establish a process that lets those seed grow in a very unimpeded way".

"But they do make a number of connections," says Chesbrough. "The GE internal research organization was part of the due-diligence in reviewing these external technologies. So that was also like an infusion of a whole different set of perspectives to the research part of the organization which was traditionally serving very large companies." With the emergence of different business models, new customers and new technologies, the company needed a new education on the research side as well and ecoimagination helped fill that gap.

While GE has the right to invest or not invest in a venture, interestingly, it does not have any formal right of first refusal. This sounds counterintuitive. "If you are an investor in a company that's got some promising technology and it matures to a point where it's actually ready to go public or may be considered as an acquisition from a big company, you want as many active bidders as possible to get the price as high as possible, so you get the biggest return. And, anything that would give GE a preferential advantage in that stage will actually diminish the potential to get the best price and diminish your return," says Chesbrough.

The payoff from ecoimagination was big: at the end of the vetting process, 23 ventures got funded. But there is more to this. In the process of inviting ideas, GE also got around 70,000 contributors—people making comments, suggestions and submitting ideas. As a resource, these 70,000 contributors were a potential goldmine in terms of breakthrough innovations and ideas that might emerge in the future. "In essence, it was a by-product of the initial intent, but the punchline in the story was that they actually decided to hire and create a new giant title—Community Innovation Manager at GE—to keep this community alive and engaged," says Chesbrough.

### The Genesis of Open Innovation

In the 1980s, as Henry Chesbrough conducted studies on a variety of companies including computer disk manufacturer Quantum Corp, Lucent and Cisco as well as Xerox Corp and its Palo Alto Research Center, it dawned on him that the days of traditional firm-centric innovation were over. It was time for companies to look beyond their boundaries for new sources of innovation. This approach led to ideas from a variety of sources, and proved to be more cost-effective compared to internal R&D. It also led to out-of-the-box thinking, more relevant products, and consequently became a source of competitive advantage.

Chesbrough's findings led to his 2003 book titled *Open Innovation: the New Imperative for Creating and Profiting from Technology* in which he coined the term Open Innovation. The book was a roaring success. It helped that companies such as P&G, Lucent and innovation intermediary InnoCentive were already practicing Open Innovation in some way or the other.

Since then, the Open Innovation movement has continued to grow. For many companies like P&G and IBM, Open Innovation has become an integral part of their business model. Later, Chesbrough advanced the concept of Open Innovation with two more books—*Open Business Models: How to Thrive in the New Innovation Landscape* and *Open Services Innovation: Rethinking your Business to Grow and Compete in a New Era*. The first book was about how companies can navigate this new innovation landscape, while the second one looked at combining Open Innovation with a services approach.

He feels that bringing in external ideas is only half the story. The other half is about ensuring that ideas that haven't been used are allowed to thrive elsewhere. GE ensures this in three ways. One, the Community Innovation Manager helps GE pull things from the community, and also helps the community connect with each other, help each other and connect with external entities who might help them develop the idea further. "(GE) used their social networks—their social capital, rather than financial capital—to help some of these projects advance," says Chesbrough. Two, they instituted a 'people's choice award' in which they identified five projects that they didn't fund as investments. They were each given a sizeable sum of money just to keep going. Since this is not equity, there's no ownership attached. Three, some ideas can be licensed to others, donated to the Commons or universities where they can evolve.

"A lot of these things you can do to take things from the inside to the outside, in essence become options for the future," says Chesbrough. "You have the opportunity, but not the requirement to do something." So tomorrow if in some parts of the world, water becomes scarce and expensive, a waterless technology might become valuable, while it wouldn't in other countries. "A company like GE can and should have multiple options in play, so that whatever state of the world emerges, they've got some ways that advantage them, that they wouldn't have had if they'd put those out there," he says.

It's a win-win. GE benefits from the diversity of ideas, most of which are different from its traditional business. "It's really in (GE's) long-term interest to have a very fertile growing set of ideas taking root upstream, because they will have a first look even though they cannot actually control what happens to them," says Chesbrough. As for the individuals in this innovation community, being a part of it increases the odds of their ideas developing into something meaningful.

But initiatives such as ecoimagination aren't quick-return businesses, so companies looking just for easy profits should stay away. "It's going to be years before



## A company like GE can and should have multiple options in play



these things have any real revenue generation," says Chesbrough. "For GE Energy, a \$40-billion business, it's going to be a very long time before these things make any dent. You have to give GE some credit for thinking fairly long-term in this regard."

Even though ecoimagination has been around for eight years, few companies have dabbled with similar Open Innovation communities. Adoption is slow because of various challenges that impede the growth of Open Innovation in general. For instance, who owns the intellectual property? When this issue showed up in GE's case, the company went against the advice of its lawyers and decided that the ownership of the ideas would be retained by those who submit them. "Once the ventures are funded, ... GE might be an investor in the company, so indirectly they would have some ownership, but because they are not the majority owner, they would still be in minority position," says Chesbrough.

There is also the issue of contamination. When internal research staff look at these external ideas, there is always the possibility of them unknowingly internalizing some of the thoughts and then passing them off as their own. To guard against such a possibility, GE Energy put in place some protocols "to make sure that the people who were doing the reviewing were trained on where the red lines were". Instead of a large group, only a small number of people were allowed to see these

ideas and they were trained ahead of time on the protocols. "And these (ideas) are again very far upstream and away from GE's traditional strengths and they also may have judged that the likelihood that this was going to drive stuff within GE's own product roadmap was sufficiently smaller than the risk they were taking. But there's also a concern in any of these activities, where you inadvertently contaminate your own downstream development activities," says Chesbrough.

Another potential impediment to adoption in such innovation communities is the lack of an internal champion. "At this point, it's still just an idea or early technology, it's not fully formed, not commercially ready, it's not (ready to be) sold in the market the next day. Months or years of additional work are needed to get it through. The ideas that come out through the internal R&D process have to go through a number of hurdles and screening and in the process, they do attract internal champions to carry forward. These external ones often lack those champions," says Chesbrough.

Companies like P&G have successfully countered this challenge, and their experience provides some lessons. In the case of Connect+Develop, they start by "meeting the businesses and getting a 'shopping list' of the things that are priorities for them, that are holding back the technology part of the business from delivering as much value as quickly as P&G would like". That helps them to decide what kind of ideas they need to look for, which increases the chances of the ideas being accepted internally.

Looking back, Chesbrough says he initially underestimated just how hard it is for companies to really adopt and practice Open Innovation.

"It really affects many parts of your organization in a pretty systemic way, and so it is a root-and-branch transformation of the company," he says. "To my great delight, there are job titles in many companies now called 'director or vice-president of Open Innovation'."

Clearly, his idea is here to stay.

*For the full interview please log on to <http://knowledge.ckgsb.edu.cn/>*



# Consumer Behavior 2.0

**Wharton's David Bell elaborates on the possible directions e-commerce in China could take in future**

By Zhang Kaifu

The rise of online shopping in China is dizzying. With cyber consumption accounting for \$36.56 billion in the first quarter of this year, purchases have risen 40.9% compared with the same period last year. Analysts predict that the country's e-commerce market will be the world's most valuable by 2015, which seemingly rings the death knell for brick-and-mortar shops. David Bell, Xinmei Zhang and Yongge Dai Professor, Professor of Marketing, Wharton School, is an eminent authority on the behavior of e-consumers and has researched similar trends in the US. Published widely in academic journals including the *Journal of Marketing Research* and *Marketing Science*, Bell's areas of research interest cover e-commerce and inter-dependent choice, social contagion and neighbor-

hood effects, among others. Bell draws from his experience to explain the behavior of China's online shoppers and provides companies targeting the cyber population with advice.

During a recent visit to Beijing, Bell sat down with Zhang Kaifu, Assistant Professor of Marketing, CKGSB, for a wide-ranging discussion on the implications of his research for the Chinese e-commerce market. Excerpts from the conversation.

*Q. Most consumer research focuses on first- and second-tier cities. What insights do you have into e-commerce in third- and fourth-tier cities? Should e-commerce retailers be focusing on these cities?*

A. There is a lower density of retailers in third- or fourth-tier cities, so people in these markets are really under-served and

there is high pent-up demand for various products and services. The Internet can aggregate demand in all these cities, which means you can offer all customers, in one realm, a lot of variety. Based on my research, the more remote the area, the higher the propensity to consume from the Internet. People in these cities are developing earning potential and disposable income, they're aware of new brands and want to consume as much as their friends in the first-tier cities. If someone wants to serve these locations, they could potentially do very well.

In a sense, it would be better to target smaller cities. You would face less online competition and you could generate interesting brand loyalty, because you have been receptive to customers' needs. We call this demographic "preference mi-



norities". They have things they want, but can't get, because not enough other people share their preferences. Isolated people are very good for e-commerce businesses.

*Q. If I am an electronics seller and I want to focus on third- and fourth-tier cities, what would be your advice?*

A. You should look for people that are particularly under-served. You should try to understand the pain point of customers and reinforce their pain. The aim is to remind them how painful it is to do without these goods and services and bring these things to them.

*Q. In China, 70% of customers pay in cash, which may entail cash on delivery and the possibility that a product may be rejected and payment won't be received. What strategy would you suggest to deal with this possibility of sunk cost?*

A. The only solution is to deliver exceptional goods and services to people that really want them. Part of the problem is using low prices to entice customers, which can lead to attracting very poor customers. This is called the 'Groupon problem'. In theory, if I deliver to you something you really want, you should be willing to pay. Rejection comes from mis-targeting—and too much of a price focus in the beginning.

There is a company in the US called Trunk Club, which is targeted towards men. An advisor from the company will interview a customer to assess his style, and put together a collection of clothing that is delivered to his house. The customer purchases only what he wants. Shipping 10 things is not much more costly than shipping one and you get more inventory into the hands of the customer, which may increase the chance of him buying. It's a good method to increase the probability of sale. The incremental cost of shipping is not proportional to the items shipped. If you deliver one thing, the probability of a sale may be 20%, however, if you deliver 10 items, it is not 10 times more expensive and the probability of a purchase will increase.

*Q. Online companies in China seem to have a larger proportion of the market*



A business model will survive (in the) long term if it creates value. The question is how the value should be divided



*share than their offline competitors. Despite this, many online companies are not making profits even though their sales are high. Is there any way to get around this issue?*

A. A business model will survive (in the) long term if it creates value. The question is how the value should be divided. If I make \$1 of value, I don't want to give 99 cents or \$1.02 to the end customer, as that would be a losing strategy. So you should divide value so some of it is returned to the company. It is a mistake to focus exclusively on market share and customer acquisition, because ultimately this will not provide you with a profit. It is also difficult to raise prices when customers get used to low prices. Chinese e-commerce companies need to think of the total value and make sure that a piece of that is retained. Otherwise it becomes a race to the bottom, where no one wins.

The first thing that you can do is target less price-sensitive customers. The second thing you can do is differentiate your brand.

*Q. Do you think Chinese online retailers will be able to go global despite the reputation that some have of providing poor-quality products?*

A. There are no shortcuts. In marketing, we say that perception is the reality, so if the perception is that your quality is not good, this perception will be very hard to overcome. What we've seen over the last few years is US companies building successful brands, but using the expertise and high-quality manufacturing in China to source the product. The next challenge for China is to take high-quality manufacturing and market it in a way that builds a brand that customers can rely on. Maybe China can take the lead in a certain sector and that sector becomes synonymous with a new level of quality. For example, Korea: most customers in the US consider Samsung or LG to be the best TV brands you can buy. That leadership in consumer electronics is carried into cell phones and automobiles.

If you do something well, it gets magnified online through social media, the same thing happens if you do something poorly. Being online creates transparency, which is good if you're better, but not if you're worse. It allows things to happen more quickly, but the substance still needs to be there.

*Q. How do you leverage the e-commerce framework to create other alternative business models?*

A. More Internet business models are about ultimate access. Not price, convenience or standardization, but about high-end products that may take a long time to reach you, but are completely customized. Also some Internet companies are based on experiential grounds. For example, Bespoke Beijing gives you access to things you can do that you might not otherwise know about. This model is not using price to attract you, but will give you knowledge to enhance your experience. So there are two lessons to learn: firstly, find the customers' pain point and secondly, don't give everything away. Retain some value for the firm. You'll need that to grow in future and to build the company, which leads to better products and services going forward. ■



# ‘Creating’ Creativity

**Darren Dahl of the Sauder School of Business shares his perspective on how to stay creative in business**

By Zhang Kaifu

A recent global IBM CEO survey says that the majority of CEOs who participated believe the key to navigating today’s uncertain economic climes is creativity. Creating an innovative workplace is an essential part of business today, but implementing practices that actually nurture creativity is much more difficult than supporting it in theory.

Many in the tech industry regard Apple’s approach to innovation as key to their phenomenal success. Apple has consistently carved out new markets where there were none by adding never-before-seen value to existing products. As a result, the Apple stock has grown by an astounding 4,500% in 10 years flat. Apple is a classic case in discovering ‘blue

oceans,’ or new markets, a term coined by W. Chan Kim and Renée Mauborgne in their groundbreaking book *Blue Ocean Strategy*. But for those who are firmly entrenched in crowded markets, or what Kim and Mauborgne call ‘red oceans’, it is not that easy to maintain innovation and creativity as a focal point when the call of the bottom-line is as loud as ever.

During a recent visit to CKGSB, Darren Dahl, Professor of Applied Marketing Research at Sauder School of Business in Vancouver, Canada, offered his ideas and insights into the fundamentals of fostering creativity in the workplace in a compelling conversation with Zhang Kaifu, Assistant Professor of Marketing, CKGSB. Excerpts from an interview:

*Q. How should a company manage its creative talent in order to achieve innovation?*

A. Creativity in an organization starts with hiring. If you are hiring someone to be creative, don’t necessarily hire the same person that you are hiring for the accounting department or the finance department. The creative individual often will break rules, they’ll challenge people, and sometimes they don’t fit in. But that’s what you want, because those are individuals that will give you new insight on how to change the way you are doing business. They’ll make you think about what you take for granted.

The second thing is workspace and environment. What research has shown is that having a cube farm or separated offices isn’t

really the best way to facilitate creativity. Creativity occurs when you allow the ‘intersection’ of your workers, you allow them to be physically near one another, to conflict with one another, to have discussions, and really communicate with one another. You don’t want the same people right next to each other. This will be useful because they will be able to provide insights on the way they see the world.

*Q. How can companies foster creative and innovative thinking?*

A. If you get stuck in a job, you may have been really creative when you started, but after doing it for five or 10 years, you kind of lose your spark. So, if you want creativity in your organization, you have to be dedicated to having some type of training, or activity, or refresher on what it means to be creative. That seems obvious, but it’s not easy to do.

It ranges [from] having the consulting arm of Lego, the children’s building block company from Denmark, to actually come to your company and they’ll have you play with them and build things and create things for a day. That’s just fun, right? But the idea behind that, is it gets you back to being creative, to being a child.

Big companies, Fortune 500 companies, do that because they want to get some of that creativity back in the workplace. That’s one end, which is more of a playful end, to another end, which is utilizing very specific creative tools. There is a book written on creative templates, which forces you and helps you to use metaphors to be creative. It’s a process. Other types of creative processes are Design Thinking or de Bono’s Six Hats. These are structured protocols that help you be creative. Very different than the Lego play, but again, some training to give you ideas on how to get that creativity back in organizations. You have to spend time at it.

*Q. How about incentives? Is creativity something we can actually incentivize people for?*

A. There is a lot of debate on that. We have done some research. What we’ve found is a huge variation. There is no real pattern. Some companies don’t have



Being open and exploring different cultures, and seeing the way people do different things is only going to help you



incentives. They say its part of why you were hired, we expect you to be creative, whereas other companies have financial rewards. If you produce a patent, for example, you receive some kind of financial reward. Other companies have social rewards, so they are recognized by their peers, or receive a promotion. When we talk about rewards, there are lots of different ways to go.

One thing that we’ve found in some of the research we’ve done is that if you are going to create incentive structures for creativity, your employees have to be very aware of what you mean by being creative, and they have to be given the ability or the training or the know-how to actually reach the finish line. Otherwise they lose their motivation and it doesn’t go well.

*Q. How can different players within business ecosystems help firms become more innovative?*

A. One of the first things you have to look at is education. Some have argued that our education systems, in North America, in China, around the world, aren’t that conducive to creativity. What is easy to measure is analytical thinking, critical thinking. Training to write a GMAT test or an SAT or an IQ, these types of structured thinking have dominated in our early years. We get into very rigid testing systems that eliminate the creative ability. A lot of people feel that we are much more creative when we are young, then the school system kind of beats it out of us. That’s where we have gone wrong. That the more standardized you become as an individual, [the more] you give up creativity.

In China, [people] are very good at taking an idea and making it better, but coming up with that idea is where they need to grow. Some would say education is where it starts.

*Q. What are the elements in the other education systems, such as in North America, which actually preserve or encourage this creativity?*

A. What is interesting is that the American education system feels that they are losing creativity. That’s what they think themselves.

What I would say is there is a greater appreciation for finding yourself, for trying different types of courses, not being so focused. It’s more about having an experience and truly trying different things, being experimental.

[There’s also] the notion that you should travel. Recent academic research has said that people who travel more to other countries are more creative, because they see different things, different cultures. Being open and exploring different cultures, and seeing the way people do different things, is only going to help you try new things and add new ideas to your society.

When you think about China, it is certainly now opening up over the last 10 or 15 years, [they have] much more ability to see the world, to have their try at different things. I think that’s only going to increase, moving forward. ■



# Slow and Steady Wins the Race

China should adopt a measured but determined approach to banking reform

**Liu Jing**

Associate Dean, Professor of Accounting and Finance, CKGSB

There is no doubt that banking reform must happen in China. With more than 80% of China's leverage coming from banks, and lending going predominantly to large state-owned enterprises (SOE), growth is not likely to take its traditionally strong foothold in small and medium-sized enterprises (SME) without reform.

From the theoretical point of view, China's banking reform should be bold and swift. The old growth model is predicated on unfettered international absorption of Chinese supply, but that demand is drying up. With Europe in crisis and demand from Japan and the US weakened, the Chinese economy now depends on domestic demand. Therefore, the allocation of capital should be tilted to support the growth of domestic demand, rather than further exacerbating the over supply problem. But from a pragmatic point of view, reform should not be too fast.

There are two main pillars supporting the velocity of banking reform, each needing anywhere from five to 10 years to reach adequate height.

Firstly, there is political will. The central government must be loud about banking reform, even while the pace seems a crawl more than a run. Just because reform is slow doesn't mean it's not decisive, and small business owners need to know that. SMEs must buy into reform, both as those with the most to gain and as those with the most to give. SMEs generate growth, and with no sweeping stimulus in sight as we

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Just because  
it's slow, doesn't  
mean it's not  
decisive

.....  
saw in 2008, the growth they generate will become more and more vital. The bolder the central government is with their rhetoric, the more likely they are to generate political backing from the SMEs, without which momentum becomes very difficult. Even in peak campaigning conditions, getting the political climate right for reform is time consuming, particularly with a change of leadership.

Secondly, there's the issue of managing risk. Presently, the central government is the primary risk manager for the country. Local governments act as businesses, always enacting measures to grow ventures such as infrastructure and other facets of city development, but they don't manage risk. The companies that local governments turn to in such ventures are by and large SOEs, also known as 'urban planning and development companies,' set up to aid local governments in circumventing

regulations prohibiting them from borrowing. Local governments then typically use land requisitioned from residents as collateral. But an increasing amount of lower value urban development projects, such as sewage or green development, combined with an increased cost of re-locating residents, leads to an unsettling influx of non-performing loans. Such was the cause for lending guidelines being put into place by the central government in 2009. This dynamic cannot continue. Local governments must manage their own risk, but for that to happen there must be a fundamental change in the mindset between the local and central governments, and that will take a considerable amount of time.

The reform history of China shows us that integrating market forces into domains that traditionally belong to the state is a laborious task. In an economy where the banking sector and the financial sector are synonymous, big movements merit serious integrity tests. Are the banks strong enough to be wielded by market forces? This is a question the central government must answer prior to taking action. Before the actual policy is put into place, merely stabilizing the institutions themselves could take the length of a single five-year-plan. As it stands, local and regional banks don't have the capital to withstand an increase in non-performing loans, and this must be corrected. Whether it's philosophically desirable or not, realistically this is the way it has to be; slow and steady wins the reform race. ■

## Business Bestsellers in the US

- No. 1 **Steve Jobs**  
by Walter Isaacson
- 
- No. 2 **The Power of Habit**  
Charles Duhigg
- 
- No. 3 **Imagine**  
by Jonah Lehrer
- 
- No. 4 **Thinking, Fast and Slow**  
by Daniel Kahneman
- 
- No. 5 **Mobile Wave**  
by Michael Saylor
- 
- No. 6 **The Price of Inequality**  
by Joseph E. Stiglitz
- 
- No. 7 **Unintended Consequences**  
by Edward Conard
- 
- No. 8 **The Total Money Makeover**  
by Dave Ramsey
- 
- No. 9 **The \$100 Startup**  
by Chris Guillebeau
- 
- No. 10 **The 4-hour Workweek**  
by Timothy Ferriss

Source: New York Times

## Business Bestsellers in China

- No. 1 **The Third Industrial Revolution**  
by Jeremy Rifkin
- 
- No. 2 **China's Economy Hits The Brink**  
by Larry H.P. Lang & Sun Jin
- 
- No. 3 **Only One Bustling Corner**  
by Chen Wen Qian
- 
- No. 4 **How to Play the Economic Chess Game**  
by Shi Hanbin
- 
- No. 5 **King, Economics Story**  
by Guo Kai
- 
- No. 6 **Three Tumultuous Decades**  
by Wu Xiaobo
- 
- No. 7 **Predictably Irrational**  
by Dan Ariely
- 
- No. 8 **The World is Flat**  
by Thomas L. Friedman
- 
- No. 9 **The Wealth of Nations**  
by Adam Smith
- 
- No. 10 **Start-Up Nation**  
by Dan Senor & Saul Singer

Source: Dangdang.com

# Reading is Brainstorming

**Jinya Chen, the Asia-Pacific Regional President and Global Vice-President of aluminum production company Alcoa, shares his thoughts on the books that have most influenced his business practices, and his personal outlook on the key international business relationships of our era**

I don't take reading lightly, or for granted. I spent three years in northeast China during the Cultural Revolution. In those days, it was extremely hard to find something to read where I lived. Any book I could get was a real lifesaver for me.

I now read intensively. Like a man suffering from hunger for a long time, when you finally get a drink or food, you binge.

Recently, I've been reading American classics such as *Huckleberry Finn* and *Tom Sawyer*, as well as Henry Kissinger's *On China* and the Brookings Institute's *Bending History: Barack Obama's Foreign Policy*. Books like these last two provide me with greater insight into China's diplomatic and financial strategies with the world. It helps that building mutual trust lays the foundation for everything

I would attribute some of my success to my active engagement with books. I think reading is a kind of brainstorming. You try to communicate with the book, and you sometimes agree, sometimes you disagree. When you read, you will brainstorm some great ideas. Engaging yourself with the book like this is really important and a wonderful experience.

During business travels, I al-



ways save time to read books, mostly relevant to work and business management.

One I have been reading recently, and would recommend, is *Tough Minded Management: A Guide for Managers Who Are Too Nice for Their Own Good* by Gareth Gardiner, about how to really manage a high-performance team. All successful companies have high-performance teams. Companies that have failed maybe had good teams but didn't know how to manage them. This book strengthened my belief in creativity in the initial phases of a task, as well as the importance of disciplined execution. We have to be creative and innovative in business, but as soon as we start implementation, it really has to be disciplined. These books coach me to reach that goal.

# Five-Course Dinner

A breakdown of Chinese food by region, taste and experience

By Suzanne Edwards



Chef and author Jen Lin Liu cooks in her Beijing-based restaurant and cooking school Black Sesame Kitchen

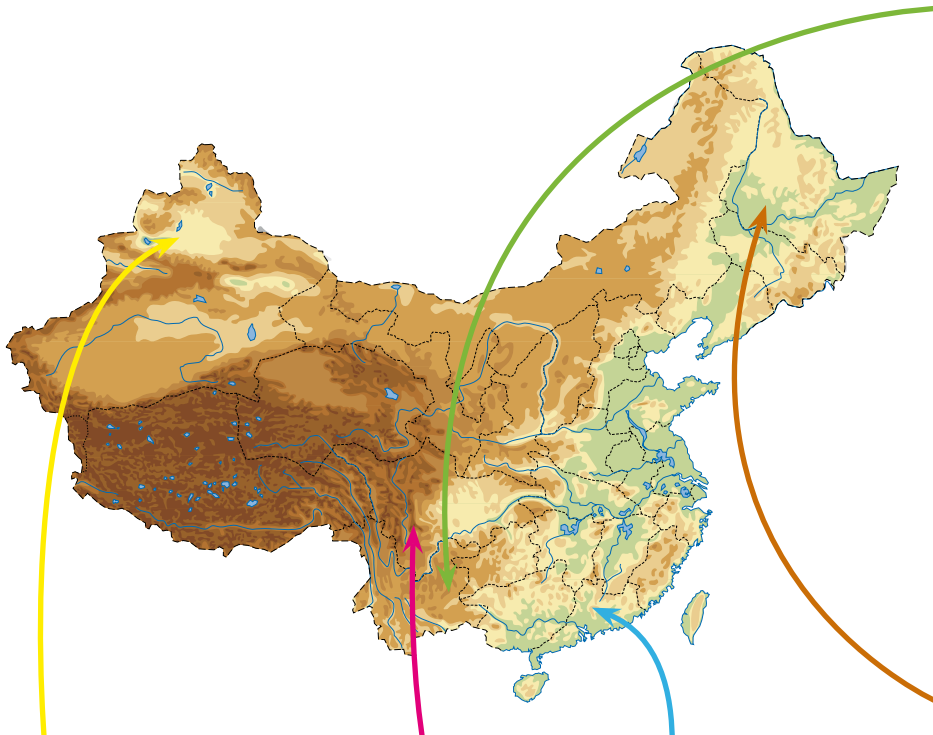
Jen Lin Liu, author of *Serve the People: A Stir-Fried Journey Through China* and founder of Beijing's Black Sesame Kitchen, knows more than most people about China's seemingly endless variety of local and regional dishes, but even she is humbled by the topic: "You could live your whole life in China and not learn all there is to know about Chinese cuisine."

Liu shares with *CKGSB Magazine* her experience with five key regional Chinese cuisines, and with some of the star chefs. "For many of them, it's not glamorous, it's a way to make an honest living," she says. "But I do feel that there is pride in what they do, and seeing how impressed foreigners are by their skill is an enormous pleasure (for them)." She doesn't shy away from sampling some of the more exotic dishes China has to offer. "I've had fried grasshoppers and they're not bad, they taste like popcorn, very light and crunchy."

From lemongrass in Yunnan to the spices of Sichuan, each region has its unique ingredients, scents, tastes and textures. Liu gives us a crash course in each region's approach to pleasing the palate.

## Do it Yourself

"Know your ingredients; that makes it all a lot easier. Learn the things to stock your pantry with, the right soy sauce, the right vinegar, the right sesame oil," says Liu. She reminds her students that preparing China's most treasured treats isn't the glitzy affair of Western cooking shows. "Keep in mind that it's really hard work," she says. For those not cut out for cooking, experiencing the thousands of dishes and cooking styles in restaurants is easily pleasure enough.



**XINJIANG—Meat & Bread**



Xinjiang is the vast northwest region of China. The cuisine, also known as

Uyghur food, is predominantly Islamic and known for its roast meats, chiefly lamb and mutton, dairy products and dense breads. Liu recalls a trip with her husband to the Xinjiang city of Kashgar, where after fasting for the day in observance of Ramadan, they feasted on the delicacies of a street-food vendor in the old quarter of the city. “They served these amazing baked lamb buns, almost like a bagel, flaked with lamb, delicious.” You can sample Xinjiang cuisine in most Chinese cities now thanks to the hand-pulled noodle establishments that are typically owned and operated by Uyghur migrants. The Islamic cuisine is now expanding its repertoire, however, and reconfiguring its scope to include higher-end joints. Xinjiang is no exception when it comes to different regions of China racing to elevate the status of their food.

**GUANGDONG—Style**



Comfortably perched at the top of China’s food status ladder is Guangdong cuisine. The southern province represents China’s most sophisticated

palate. “They’re known for preserving the authentic taste of the ingredient,” says Liu. Guangdong food is characterized by sautéed vegetables, steamy soups and grilled meats, such as pigeons cooked in rose wine, and exotic snacks, like fried insects. With roots in Cantonese cuisine, Liu recalls her grandmother boiling chicken in soup for hours upon end and making thick congee (porridge) brimming with chicken, pork and preserved egg. Liu admires Cantonese food for not smothering the ingredients in sauces and oil. “I think there is something to be said for teasing out the natural flavors of the ingredients,” she says. Guangdong food is a source of pride for the region’s people, but culinary patriotism is perhaps at its height in the zest-filled province of Sichuan.

**YUNNAN—Up and Comer**



Bordering Vietnam, Laos and Myanmar, Yunnan embodies a unique amalgamation

of homegrown ingredients and taste sensibilities. “I like that it’s not what you would expect of Chinese food,” says Liu. “The spicy sour lemongrass flavor is really unusual.” Liu says the lemongrass works particularly well in conjunction with the region’s tasty pan-seared goat cheese.

**DONGBEI—Hardy Stock**



“Fancy” food is foregone in northeast China in favor of hardier comfort foods. northeast food,

or Dongbei cuisine, comes from the region spanning Heilongjiang, Jilin and Liaoning provinces. The region is noted for its heavy meat dishes, dense starches and oily seasonings. “The Dongbei flavor is hardy, salty and oily. Lots of potatoes and starches, breads and flatbreads, very heavy in the meats with lots of braised and stewed dishes,” says Liu, who chose this indulgent region to establish her cooking school.

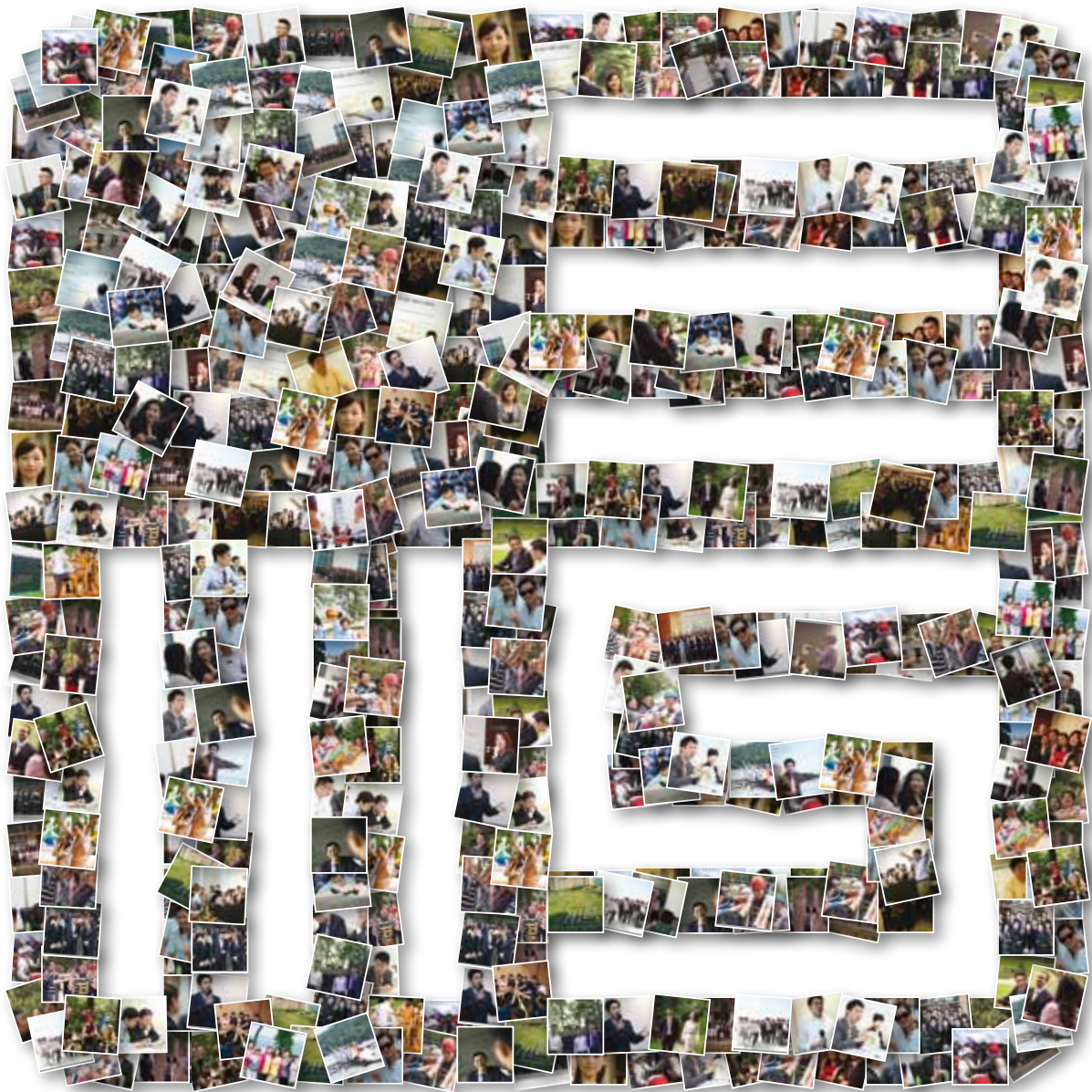
**SICHUAN—The Champ**



“They [Sichuanese] pretty much only eat Sichuan food.” says Liu, adding

that the chilies, peppercorns and spicy bean paste found in many dishes are addictive. “I love it all. It’s an acquired taste, but many acquired tastes have addictive qualities.” Liu, having recently moved to the region’s capital of Chengdu, observes that Sichuan cuisine is evolving to celebrate a new range of ingredients. “I’m seeing use of prime ingredients, like really choice cuts of beef,” says Liu. “They’re also a huge fan of fried rabbit with chilies.”

# CELEBRATING 10 YEARS OF EXCELLENCE





A portrait of Mr. Li Ka-shing, an elderly man with glasses, wearing a dark blue suit, white shirt, and light blue tie. He is sitting at a desk with his hands resting on it. The background is softly blurred, showing what appears to be a window with light coming through.

## What is a Business Leader?

*CKGSB was founded through the generous support of the Li Ka Shing Foundation and its founder, Mr. Li Ka-shing—Asia's most successful entrepreneur.*

"While you might have achieved financial success and attained control over your own life and future, this does not make you a true business leader. I believe true business leaders answer yes to the following: Am I able to live my life by the ideals and principles that I choose? Am I able to use my knowledge and good fortune to create wealth and affluence in my community? In this rapidly changing world, do my wisdom and skills contribute to the happiness of my nation and people? Only those who answer these questions in the affirmative can truly be called business leaders."

A piece of calligraphy in black ink on a white background, representing the name 'Li Ka-shing' in Chinese characters (李嘉誠).

# 10 Years of Excellence



*Dear Friend of CKGSB,*

On November 22, CKGSB celebrates the 10th anniversary of its founding. It gives me immense pride to reflect on the thousands of business leaders from China and around the globe who have benefited over the past decade from CKGSB's world-class faculty and unrivaled insights.

The business leaders who have made CKGSB their preferred choice for management education include:

- More than 2,500 CEOs and chairmen among the 5,000 graduates of our MBA, Finance MBA and Executive MBA degree programs
- More than 10,000 Chinese executive education participants from a range of firms including: state-owned enterprises such as Bank of China and Sinopec; innovative private-sector companies such as Huawei and Lenovo; and successful multinationals such as Amazon and Apple
- More than 1,200 international participants in our English-language executive education programs, including entrepreneurs such as billionaire philanthropist Sir Tom Hunter and executive management teams from leading global organizations such as top-ten law firm Clifford Chance and engine and power systems maker Cummins

I am proud because we have helped these business leaders grow in myriad ways, both professionally and personally. They emerge from CKGSB with profound insights on China in the global context, the role of culture in business, leadership and the responsible application of wealth.

As measured by the impact and influence of CKGSB's unique alumni community, these first 10 years have been more successful than we could have imagined at the outset. Educating these world-class business leaders requires world-class resources; in this regard CKGSB owes its deep gratitude to the generous support of the Li Ka Shing Foundation. This support has enabled the school to maintain our academic and administrative independence.

Today, as in 2002, CKGSB is the only business school in China with true faculty governance. Faculty governance is vital because it is the basis for academic independence and free scholarly inquiry. Without these qualities, CKGSB would not have been able to recruit the world-class business scholars who form our 49-member faculty. These scholars, in turn, guide the research efforts that have made CKGSB a recognized global leader in generating new business insights.

Over the coming decade, CKGSB will attract more world-class scholars, doubling the size of our faculty. This will allow us to expand the volume and scope of our research and offer cutting-edge management education to many more of the world's brightest and most influential business leaders.

CKGSB will also partner with leading organizations around the world to open new programs covering topics such as the state-business relationship, advanced agriculture, 3D manufacturing and exponential technologies.

As in our past endeavors, we will depend on friends and partners around the globe to launch these ambitious programs. I encourage you to explore ways to participate in CKGSB's global community so that we can work together to meet the challenges of tomorrow.

*Yours Sincerely,*

A large, fluid handwritten signature in black ink that reads "Xiang Bing". The signature is written in a cursive style with a large, sweeping loop at the end.

*Dr Xiang Bing  
Founding Dean, CKGSB*

# The Changing Face of Business Education

**Emerging markets are increasingly taking center-stage in the world of business education**

By Suzanne Edwards

Over the last decade or so, the job of business school deans in the West got a lot tougher. Preparing students to engage in an increasingly multipolar global economy meant arming them with new skills, not necessarily the kind that Western business schools were equipped to teach.

Peter Lorange, then the dean of IMD in Laussane, Switzerland, and the author of a book on business education, was early in identifying this shift taking place, in the 1990s. “Our clients (executive students) were running into things like difficulty with understanding different cultures and such,” Lorange, now the founder of Lorange Institute of Business in Zurich, recalls.

“We also felt that the growth wasn’t really coming from Europe, but from Asia and other parts of the world,” adds Lorange. This observation led to a major shift at IMD. Lorange pioneered an effort to bring IMD clients into close interface with the market of interest. Among other things, Lorange started globalizing IMD’s programs and set up a diverse committee in which each faculty member or administrator was assigned to a certain part of the world for study, analysis and exploring immersion opportunities.

It’s not hard to see why IMD engi-

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Even in the face of economic upheaval in much of the world, investors are generally bullish in their approach to emerging markets, especially China

neered such a major change in its strategy. Even as the global economy grapples with a slowdown, in many ways the BRIC countries (Brazil, Russia, India and China), and other emerging economies are powering growth. A Forbes report in late 2011 asserted that long-term growth in the major BRIC economies is intact. A 2011 report by consulting firm McKinsey predicted that the collective GDP of emerging markets will overtake that of developed countries by 2020. The report also projected that consumer spending in emerging markets will grow three times faster than that in developed countries over the next 10 years.

Most multinationals have already taken this into account—for a lot of them, emerging markets are contributing an increasing proportion of their global revenues. In fact, in some cases, revenues from emerging markets have outstripped those from their home markets. Increasingly, the world’s biggest companies are realigning their strategy to take part in the incredible growth story of these markets, particularly India and China.

Even in the face of economic upheaval in much of the world, investors are generally bullish in their approach to emerging markets, especially China. According to surveys conducted in both Shanghai

## A Softer Touch

Over the years, business education has repeatedly come under the scanner. In the mid-2000s, critics such as Henry Mintzberg, Warren Bennis and Jeffrey Pfeffer questioned the cookie-cutter approach of most business schools and questioned their relevance. Among other things, they vociferously criticized the ‘silo-based’ approach to teaching, the emphasis on hard skills vis-a-vis soft skills, the lack of focus on ethics, and lack of cultural sensitivity. Fortunately, this



CKGSB Alumni Outdoor Hiking Club, during the Xuanzang Road Business School Gobi Challenge, which raises funds for underprivileged children

encouraged many business schools to do some soul-searching and address the criticism by undertaking curriculum reform and rethinking their role in society. After the financial crisis, the conduct of senior executives dragged business education under the scanner once again, sparking off a debate on the role of business schools in instilling ethical behavior in students. Some schools like CKGSB keep this at the center of their existence. As Dean Xiang Bing says, “We’re concerned with far more than just how to make more money. We’re concerned about the issue of why we do business in the first place.” Xiang employs a variety of tools to keep this concern on the minds of CKGSB’s Executive MBA students. Among these are courses that examine the ethical obligations of Confucianism, a requirement that students donate six days of their time to doing community development work before receiving their degrees and a student-led rural development initiative that has raised \$3.85 million to install reading rooms in more than 650 rural primary schools.

Another issue is creating cultural awareness. According to a 2011 CIES

report on the potential for developing privately-funded higher education institutions in emerging countries, the anticipated benefits of the approach were accompanied by apprehension about the potential for an overly Westernized approach to education in such countries and a concurrent disintegration of local cultures and education values. As more and more companies have discovered, doing business in emerging markets is essential to future growth. In markets like China and India, cultural awareness is no longer a *nice-to-have* but rather a *must-have*. In an article for Forbes.com in May this year, Doug Guthrie, dean of the George Washington University School of Business, said, “A deeper understanding of culture and history gives us keener insights into political motivations, cultural nuance and social habits, all of which are crucial for understanding the business environment.” Schools like CKGSB approach these traditional problems with programs rich in overseas cultural immersion and humanities studies, reflecting the need for students to enrich their understandings of society, even when it can seem disconnected from the business agenda. ■

and Beijing by the American Chamber of Commerce this year, American multinational companies are still seeing a higher average return on their investments in China than they are globally.

### New Forms of Engagement

As the pressure to understand emerging markets increases, business schools like IMD are increasingly finding ways to engage with these countries. The Fontainebleau, France-based INSEAD School of Business broke away from tradition by setting up a Singapore campus in 2000 after a 40-year history in Europe. There were no precedents, and the stakes were high. But as the then INSEAD dean Gabriel Hawawini saw it, having a presence in Asia was essential to globalizing the school. Similarly, University of Chicago’s Booth School of Business inaugurated its Singapore campus in 2000 while Richard Ivey School of Business set up a presence in Hong Kong as early as 1998. In addition, schools such as Harvard and Wharton have expanded through partnerships and research centers all over the world in an unceasing effort to globalize their research and curriculum.

While these schools were ahead of the curve in identifying the shifting center of gravity in business education, others have explored globalization in different ways. Today, there is now not a single high-profile business education program that has not incorporated in one way or another, emerging market immersion. Eight of the top 10 Executive MBA programs in the world in 2011, according to *The Financial Times*, have now established global partnerships or campuses in emerging markets and other destinations. Yet other schools give students global exposure through dual-degree programs and student exchange.

### A New Breed of B-Schools

In the past, the top North American business schools competed only with each other, but they are now part of a larger, and significantly more international, pool of schools that are gaining global renown. Increasingly, schools from emerging markets—including the likes of the Indian

School of Business (ISB), CKGSB, and Fundacao Dom Cabral (FDC) in Brazil—are reshaping global business education.

These schools are nothing short of world-class, and also have a tremendous emerging market advantage. For instance, the ISB, based in Hyderabad, India, currently ranks at number 20 on *The Financial Times'* Global Top MBA Rankings. The school was set up in 2002 as the result of a collaboration between two of the biggest names in business education, Kellogg and Wharton.

“They said, ‘you could never open a world-class business institution in India.’ We’ve proven that wrong,” says Ajit Rangnekar, Dean of ISB. “I think we have an opportunity.”

In its decade-long journey, ISB has become one of the handful of schools that are pioneering emerging market-focused business education. As a result, it is increasingly attracting students from the West who wish to be exposed to cultures not part of their mental mainframe. Earlier this year, Thomas Hyland, an MBA applicant to ISB was quoted in the *New York Times* on his perspective of business education as an entry strategy for other markets. “India is a tough place to show up from the outside and try to do business. So much of business and daily life here depends on relationships,” said Hyland, an American who began his career at Goldman Sachs in San Francisco.

Rangnekar agrees. “You learn, and you expect and you accept that there may be any number of problems in the supply chain, and you have to think on your feet,” he says. “Nothing is predictable, and living in that and managing in that unexpected environment is very valuable.”

The same is true for China, where business realities are very different from the West. “In the West we don’t understand China, there are a lot of misconceptions,” Scottish entrepreneur Sir Tom Hunter told the *Times of London* in October—by way of explaining why he had chosen to study at CKGSB. “When I was building my career, I didn’t know anything about China from a business perspective. If I was starting again I would be spending a lot of time over there.”

Given their unique position, these schools are able to give students a firsthand experience of business realities in the world’s fastest growing economies. At ISB, for instance, students from developed markets also have the opportunity to understand the so-called bottom-of-the-pyramid consumers and develop a social consciousness, skills a lot of multinationals now find invaluable. CKGSB leverages its status as a premier destination for Chinese business and government leaders to offer its Western students the sort of firsthand perspective and peer networking that business schools from outside would be hard-pressed to match.

There was a time when emerging country business schools had to deal with various challenges, such as finding good faculty, creating strong research credentials and attracting funding—these countries don’t have a tradition of corporate funding or students giving back to their alma mater. That is changing now. CKGSB, for instance, was set up with financial support from the Li Ka Shing Foundation while ISB gets significant funding from Indian corporates and in recent times, some of its projects have attracted funding from

billionaire George Soros, eBay founder Pierre Omidyar and Google.

As for faculty, CKGSB has been able to attract 33 full-time professors who previously held tenured positions at top North American business schools. This is not an easy feat. What helped the most was the creation of an enabling research environment.

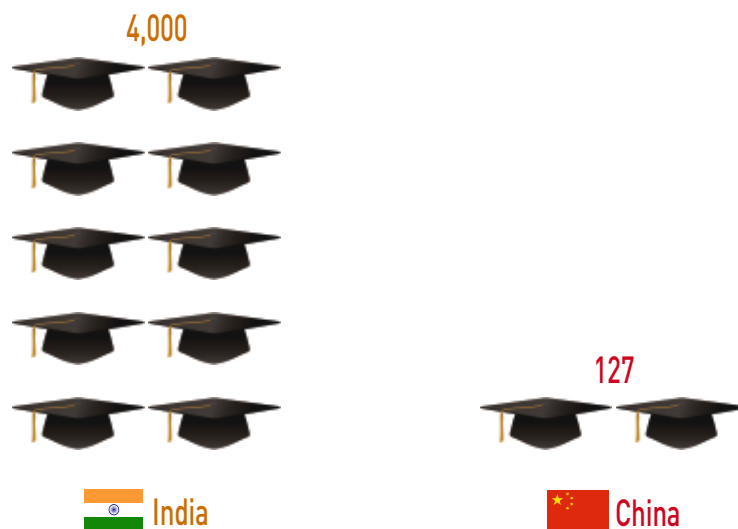
Take, for instance, Li Wei, Professor of Economics and Emerging Markets Finance at CKGSB, who left his tenured position at the University of Virginia’s Darden School of Business to connect with his research in a way that wasn’t possible in the US.

“I felt like coming here [China] once a year was not enough,” says Li. “I’m working on the Chinese economy so for me it’s very natural to be here. If you want to continue this line of research and the ongoing practical end of things, then China is definitely the best place to be.”

Replace “China” with any number of the world’s rapidly emerging economies, multiply by thousands of professors at dozens of new top institutions on three new continents and you have a glimpse of the changing face of business education. ■

## India’s Management Fever

Number of business schools in 2 key markets



Source: China Ministry of Education  
Reuters

# From Doing Business to Defining Business

**CKGSB's Executive MBA students discover a holistic approach to management**

By Alissa Haupt



Associate Dean of Global Programs, Director of the CIM Center and Dean's Distinguished Chair Professor of Marketing, Sun Baohong believes CKGSB provides a unique environment in which students grow from businessmen, to become business leaders

To succeed in business in China, companies and their leaders need special tools. They need access to other business leaders that represent a range of sectors, understanding of the optimal relationships between different industries, and of the soft skills necessary to make inroads with business leaders in China.

With 80% of the student body at the CKGSB coming from senior management levels of vice president and above, the CKGSB Executive MBA program give its students access to the vital tools that will help them define business trends.

"The faculty aside, there is also a horde of heavy-weights who are widely known in the Internet business on the student roll," says EMBA graduate Henry Yang, founder and CEO of consulting firm, iResearch.

This community of graduates from China and overseas allows for an exchange of ideas and strategies that produces a more in-depth understanding of the domestic market.

In addition to fostering a valuable business network in CKGSB's graduates, the EMBA program itself is quite vigorous in its requirements with regard to elevating the manner in which students conduct business. According to EMBA program graduate Liu Zhouwei, Founder and Editor-in-Chief of *21st Century Business Herald* a leading Chinese business publication, it is just as much about soft skills as it is about mathematics.

"Xiang Bing's humanities program is a good balance, not only for offering enlightening education for Chinese businesspersons, but also because doing business is

not all about just business," says Liu.

"Our program is suitable for our students who are running multi-national corporations because it's not about only learning how to do business in China. They must understand the impact of the globalization of Chinese companies," says Xiang Bing, Founding Dean and Professor of Accounting at CKGSB.

Sun Baohong, the Dean's Distinguished Chair Professor of Marketing and the Associate Dean of Global Programs, describes the school's approach to cultural understanding and to self-governance as

“  
CKGSB attracts  
business leaders  
with a culture  
that bridges  
Chinese and  
Western cultures

Sun Baohong,  
Associate Dean, CKGSB

key elements in providing the educational experience her students demand.

“CKGSB attracts business leaders with a culture that bridges Chinese and Western cultures, and a brand-new system of governance. It will create future leaders for Chinese business,” Sun said.

The unique interaction that CKGSB’s EMBA students have with one another allows them to maximize their knowledge of the different management approaches in different sectors.

“I used to focus only on business management and mode in my own segment and have a sketchy knowledge of other

trades,” says Yang. “Each industry has its own know-how in running business, and gaining access to some of the critical know-how and core operation philosophy can give a boost to business development.”

CKGSB research centers are also connecting EMBA students to insights which impact the student’s own understanding of markets, and assist other business leaders, multinational corporations and policy-makers drive markets in China.

“Once we have this data, this data is not only used for industry players but also for policy-makers,” says CKGSB Professor Li Wei of his recent survey of busi-

ness leader confidence, the CKGSB China Business Confidence Index (CBCI).

EMBA students, by participating in this kind of research, are creating a framework for positive changes in the informational landscape that allows for forecasts and decision-making in the various business sectors in China.

With campuses in Beijing, Shanghai and Guangzhou, the EMBA program lets students connect to critical locations, the key centers of China’s industries, where students are not merely running their businesses, but are also creating the path that other businesses are sure to follow. ■

## A Platform for Success in China

Adam Steinberg was not content with watching from the sidelines

By Adam Steinberg

**T**he CKGSB MBA has provided me with a tremendous career platform - a platform to network with Chinese innovators and members of the business elite and a platform to allow me to more fully understand China’s business environment.

Many of my CKGSB MBA classmates leveraged their MBA as an opportunity to make a career pivot—and they pivoted to PE, VC and consulting with both aplomb and credibility. I leveraged my time at CKGSB to transition from an already successful career in corporate communications to the much more niche sub-field of investor relations and financial PR.

Investor relations combines knowledge of corporate communications, financial accounting, corporate finance, equities trading and securities law. Since graduating from CKGSB, I’ve worked for a Chinese boutique financial communications consultancy in Beijing, conducting business entirely in Chinese and working on behalf of some of the world’s best-known private equity firms, hedge funds and financial institutions.

I was honored to be elected by the Board of The Hedge Fund Association—a US-based hedge fund industry trade association—to be their volunteer Director for China. In September 2012, I organized a hedge fund panel discussion in partnership with CKGSB featuring CKGSB Visiting Professor of Finance, Li Haitao. CKGSB has given me a platform for building on my China and career experience.

My reason for remaining in China can be summed up in just two words: “Two weeks.”

Two weeks is the typical amount of time a USA MBA program visits China for their version of the China Module. American MBA students visit China for about two weeks to get a base



understanding of China’s business environment. They visit Beijing, Shanghai and Hong Kong and they meet with some local business leaders and innovators.

That’s it. Just two weeks in China.

During my CKGSB MBA entrance interview, Associate Dean Teng Bingsheng asked me why I wanted to pursue my MBA at a burgeoning program in Beijing rather than back home in the US. My answer to Dean Teng was shaped by my knowledge of the condensed tours of most US MBA students visiting China.

As an American who had already lived in China for more than eight years, I’ve seen many talented American friends return to the USA for their MBA. I count myself among the minority—I chose to remain in China and enhance my understanding of China’s uniquely dynamic business environment.

I was attracted to CKGSB specifically for a combination of reasons: the one-year MBA program, faculty who can offer both global best practices and successful, local China experience to the classroom, as well as the high-profile alumni network. Also, the fact that it was a private business school, so nimble and entrepreneurial, was a major plus for me. The one-year MBA program at CKGSB passed by quickly and we were forewarned by MBA alumni in advance to savor each and every moment. From our opening day at the Diaoyutai State Guesthouse to the Sanya Forum to the China Module to our DCP, it was over in a flash—and I treasure each and every experience. ■

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Adam Steinberg, MBA class of 2010, is a Senior Project Manager at New Alliance Consulting International, a Financial PR and Investor Relations firm.

# Educating the Top of the Pyramid

**True Business leaders seek ongoing learning to  
expand their knowledge and stay on top**

By Dan Siekman

In 2006, CKGSB launched a new executive education offering, the China CEO Program. Video footage captured during the inaugural edition reveals classroom scenes that are a far cry from the stereotypical business education environment. This is not basic financial theory and Porter's five forces with first-year MBA students. The China CEO Program students count their employees by the thousands and their revenue by the billions.

These students include Alibaba founder Jack Ma, TCL founder Li Dongsheng and CNOOC Chairman Fu Chengyu (Fu has since become Chairman of Sinopec) and dozens more of China's most celebrated businesspeople. Classroom discussion revolves around their own strategies, achievements and frustrations running some of China and the world's largest and most successful companies.

The China CEO program was a natural extension of CKGSB's founding strategy of focusing on educational needs of businesspeople who stand at the pinnacle of success: enrollment of Chairman and CEO-level students in the school's EMBA degree program has consistently exceeded 50 percent since it became CKGSB's first offering at the school's founding in 2002.

It may seem counterintuitive for such highly successful business leaders to go back to school for business education. But participants are quick to offer their own reasons, often based on the rationale that nobody and no organization, no matter how successful, can afford to stand still in the fast-paced modern business environment.

"Fail to understand what others are doing," said CNOOC's Fu, "and you can wake up in a few years and suddenly realize that the whole landscape has changed around you. I want to understand what other businesses are doing, what preparations they are making for the next decade and beyond, how will this impact [my business]? This is what I need to understand."

Li Dongsheng of TCL agreed with this sentiment, adding, "I hope that through

my participation in this CKGSB program, I will be better able to reflect on past experiences and lessons learnt, and from this gain a competitive edge in the future."

Crafting a program that meets the needs of this level of participant requires an unerring emphasis on quality, says CKGSB Dean, Xiang Bing. "World-class business leaders require world-class professors, top facilities and global vision," says Xiang. "They need to understand the



Mr Li Ka-shing with distinguished students of the first cohort of CKGSB's CEO Program in 2006



global implications of business and economic trends.”

Such sentiment was the basis for the China CEO Program’s eight global modules, delivered jointly by CKGSB professors and professors from leading partner schools on three continents, such as Frances’s INSEAD, Switzerland’s IMD.

Jump ahead to the present day and CKGSB has applied its expertise in catering to China’s top business leaders to develop new programs for successful businesspeople from outside of China who want to better understand the country and its place in the global business context.

Scottish entrepreneur, investor and philanthropist Sir Tom Hunter is one such business leader. He recently completed CKGSB’s “Global Business Strategy: China” course, delivered in partnership with Cambridge Judge Business School Executive Education.

“No business can afford to ignore China and the opportunities it presents, or underestimate the importance of its business sector to the current and future global



**Sir Tom Hunter, billionaire philanthropist, has enrolled in CKGSB’s Global Business Strategy China program to understand China better**

economy” he told The Scotsman newspaper earlier this year. “China’s growth potential is phenomenal and the West needs to learn from China’s economic development, flexibility, adaptability and vision.”

Understanding China in a global context is a common theme. The global management committee of top-ten global law firm Clifford Chance participated in a half-day CKGSB Boardroom China Briefing at CKGSB’s Beijing campus in May of 2012.

“We could go and talk to the leading European business schools, we could go and talk to the leading US business schools,” said Malcolm Sweeting, one of the firm’s senior partners. “But if you want to get a view on globalization through a China lens then it is much more valuable for our senior management to come to Beijing to listen to the views of experts at Cheung Kong Graduate School of Business.”



## Honing a China Strategy

### The China Country Manager Program

Unlike executives who manage global operations, multinational executives responsible for key elements of their organizations’ China operations have unique educational needs. It was with this spirit that CKGSB developed the China Country Manager Program, which zeros on critical strategic and cultural issues such as cultivating and retaining talent in China, Chinese consumer behavior, Chinese business decision-making and how China’s history truly shapes the contemporary business landscape.

Sandeep Bahl, Regional General Manager (Asia) for flag carrier Air New Zealand, had accumulated almost 15 year’s of experience working in China before he joined the first edition of the Country Manager program in 2008. “What I was missing was to understand China more deeply—not only the culture, not only the language, but deeply about the Chinese business mentality, the needs of Chinese consumers, and how the government and SOEs are working towards serving that kind of need,” explained Bahl in a discussion with *CKGSB Magazine*.

“The Country management program was dedicated towards making sure that the country managers who are coming from multinationals, coming and living and working in China, were clearly given in-depth knowledge about what is the need to be successful in doing business in China. The professors at CKGSB are from global universities: they have not only academic backgrounds, but also good business backgrounds. We had professors coming from the NDRC [National Development and Reform Commission], professors from Central Party government offices, which really made us feel we were learning in China with a global context, and at the same time getting in-depth knowledge of how to be successful in China.”

# It's What You Know And Who You Know

**CKGSB's progress in the European market in coming years will be aided by key figures such as Michael Queen, former Chief Executive of UK-based international investment firm 3i and a member of CKGSB's European Advisory Board**

**M**ichael Queen's position on the board was announced in September, 2011 at CKGSB's European launch in London, along with board members Sir Victor Blank, Business Ambassador of UKTI; Charles-Edouard Bouée, President, Asia of Roland Berger; Dr. Karl Ulrich-Kohler, CEO of Tata Steel Europe; James Richards, China Group Director of De La Rue; Sarah Turvill, Chairman of Willis International; Malcolm Sweeting, Senior Partner of Clifford Chance; and Dr. Ralf Speth, CEO of Jaguar Land Rover (Sir Tom Hunter, Trustee of The Hunter Foundation, has also since joined the advisory board).

Queen joined 3i in 1987 and retired from the position of Chief Executive in 2012. He was previously Managing Partner of 3i's Infrastructure business and Global Head of Growth Capital. Queen has invested across a broad range of sectors with a particular focus on healthcare and financial services.

We caught up with Queen in London at the European launch and asked him to share his thoughts on CKGSB's presence in Europe.

*Q. How did you first learn of CKGSB and what led you to accept its offer to serve on the European Advisory Board?*



**Queen joined the CKGSB Advisory Board in 2011 to advise the school on its exciting expansion into Europe**

A. Having followed CKGSB since its inception in 2002, it is clear to me that it has huge potential and a lot to offer the global business community. I saw parallels between my role as an investor in businesses, where there is a significant focus on growing companies (often through international expansion), and the opportunity to serve on the European Advisory Board.

*Q. What role do you envision the Advisory Board playing in CKGSB's growth in Europe?*

A. Together we bring substantial business experience and understanding of operating at the in-

ternational level. I hope that we will be able to use the lessons that we have learned from our successes (and failures) to help guide the expansion of CKGSB.

Each of us also has an extended network of contacts. I expect that knowing whom to call on and when is something that will be of great use to the school in this phase of development.

*Q. How can UK and other European business leaders benefit from CKGSB's presence in Europe?*

A. CKGSB is offering direct access to China, a country which will shortly regain its position as the world's largest economy. This is a relatively unique position among business schools and I think

there is a great opportunity for CKGSB to capitalize on this. That you now have a European branch will make it easy for business leaders to tap into this resource—whereas before CKGSB in Beijing may have seemed a long way away from London, it will now be hard to ignore a valuable resource on our doorstep.

*Q. Many Western business schools have set up operations in China, but CKGSB is an early mover going from East to West. What unique challenges do you think CKGSB will face in expanding into the West?*

A. As with any business, breaking into a new market can be a tough task. Name recognition is an important aspect of the business school culture and CKGSB is going to find itself competing in a market with well-established Western brands—the likes of Harvard, INSEAD and London Business School to name a few. However, CKGSB has some natural advantages, particularly the quality of its faculty—which for the large part has been sourced from precisely those just names mentioned. Through successful partnership with European and US business schools, I am confident that CKGSB will rapidly become a widely known and respected name outside of China.

*Q. As the former leader of 3i, the first European firm allowed to raise private equity in China, what general advice do you have for companies looking to enter the Chinese market?*

A. Companies need a detailed understanding of the geographies that they do business in. From my own experience, you will rarely find 3i making investments in countries where we did not have a local presence—we found we did much better deals when we fully understood what we were getting ourselves into! This is even more relevant for China, where there are great opportunities, but they are not the easiest to take advantage of—you really need to develop that local level of knowledge before you can hope to make a success of it.

*Q. It now seems all but certain that emerging economies, especially in Asia and the BRIC nations, will be the pillars of global*

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To succeed  
in the coming  
decades,  
western  
businesses will  
need to embrace  
the growth of the  
emerging world  
rather than see it  
as a challenge

Michael Queen, European  
Advisory Board member, CKGSB

*economic growth for many years to come. What will Western business leaders need to do to adapt to this new economic dynamic?*

A. You are right; a recent study showed that the combined GDP of the world's seven largest emerging economies is likely to overtake the GDP of the G7 on a PPP basis within the next 10 years. China itself looks set to displace the US as the world's largest economy sometime around 2018. However, this doesn't mean that western countries will stop growing; they will still move forward, just at a slower rate than the emerging economies.

To succeed in the coming decades, western businesses will need to embrace the growth of the emerging world rather

than see it as a challenge. As trade barriers fall, internationalization is going to become an increasingly vital factor in the success of any business and European companies need to be open to this.

You might easily take 3i as an example—up until the mid-1990s, 3i invested almost entirely in UK business and had been doing exactly that since 1945. However, as financial markets became more international, so did 3i. We saw some great opportunities for investment across the globe, and expanded to take advantage of them. Such international growth has been a fundamental driver of our business in recent years and we now operate across four continents.

*Q. What do you see as the major knowledge deficits among Western businesses about doing business in emerging economies? And in China, specifically?*

A. Companies need to be cautious not to show naivety when doing business in emerging economies. It is very easy for Western businesses to try and enforce business models that have succeeded in their home markets on emerging markets, but often there are fundamental differences, whether institutional or cultural, that prevent this from working. This is especially true for China, which has a very unique business environment that needs to be fully understood by any company wanting to do business there.

*Q. As a CKGSB advisory board member, can you share some advice on how the school can fill these knowledge deficits and contribute to a global business environment that is underpinned by mutual understanding, cooperation and prosperity?*

A. I would advise the school to focus on its ability to educate Western business leaders on doing business in China. CKGSB is in an excellent position to be able to bridge the gap between businesses' ambitions to do business in China and the understanding required to be able to do so. Through well-designed executive education and experience, these two factors can be brought closer together. ■

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*This interview originally appeared in Volume 5 (Fall 2011) of CKGSB Magazine.*

# Faculty Members in the Eyes of Their Students

Students recount how their professors inspired their learning and shaped their experience at CKGSB

CKGSB's 49 professors are China's top business faculty as defined by research output, educational backgrounds and past professorships at leading business schools. With a deep East-West bicultural understanding, CKGSB professors are able to frame their research in the contexts of both developed and emerging markets and draw on these meaningful findings in the classroom. Due to this key advantage and exemplary teaching skills developed at prestigious international teaching positions, CKGSB faculty offer their students an unrivalled learning experience.



Professor of Finance, **Mei Jianping**  
Ph.D., Princeton University



Professor Mei's research areas include emerging markets, real estate financing and investment in art collection. Many of his viewpoints were instructive. He is passionate about life and is an example to follow.

**Li Mingyu – Minsheng Bank, Beijing**



Professor of Economics, **Li Wei**  
Ph.D., University of Michigan



We've all studied macroeconomics and have often discussed the world economy. With regard to the US debt problems and the Eurozone crisis, however, our thoughts were mostly fragmented. Professor Li's enlightening explanation of these topics unraveled these confusing economic puzzles. Taking Li's classes is like communicating with an economics guru.

**Cui Xiangpeng – Vice President, Beijing Zhongrun Hongyuan Ltd..**



Professor of Finance, **Gan Jie**  
Ph.D., Massachusetts Institute of Technology



Professor Gan's research findings have won the highest academic awards in the US. Her lectures on complicated financial derivatives were enlightening and easy to understand. She is an approachable and inspiring professor.

**Meng Yue – Assistant Vice President, China Construction Bank International (China)**



Associate Professor of Strategy and Economics, **Brian Viard**  
Ph.D., University of Chicago



I feel extremely fortunate to have learnt from so many brilliant professors in one year [at CKGSB]. I admire their erudition, critical thinking and academic attitude. I studied corporate strategy and was taught by Professor Viard and Professor Teng. Viard, who is from America, taught us case studies from the perspective of economic fundamentals and strategy and guided us to rationally think about what was happening in China. Teng, who is Chinese, used a curve of management cost margin and transaction cost margin to explain how China's strict financial resource control was behind corporate China's impulse to diversify. I would like to thank the professors, who helped me make sense of my previously fragmented knowledge and helped me develop structured thoughts and business acumen.

**Wu Xiaoping, CKGSB MBA 2004**



Associate Dean and Associate Professor of Strategic Management, **Teng Bingsheng**  
Ph.D., City University of New York



Professor of Economics and Human Resource Management, **Wang Yijiang**  
Ph.D., Harvard University



Professor Wang is a strict, humorous and honorable professor.

**Liang Wentao, Deputy Director of Asia Division of China's Ministry of Commerce**



Professor Xue Yunkui's impressive classes taught me not only knowledge in the analysis of financial statements, but also gave me a broader worldview. Mr. Xue's thoughts matching CKGSB's combination of Chinese and western characteristics were very useful.

**Wu Jingwu – Vice President of Business Development, 99bill.com**



Associate Dean and Professor of Accounting, **Xue Yunkui**  
Ph.D., Xiamen University



Professor of Finance, **Zhou Chunsheng**  
Ph.D., Princeton University



Professor Zhou Chunsheng has a gift for explaining difficult financial theories through everyday life stories.

**Li Xiyong, Chairman of Shandong Energy Xinwen Mining Group Co.**

# Chinese Companies Up Close

Key case studies from CKGSB's first decade

By Heather Mowbray

**A**s a pioneer of the independent business school model in China, CKGSB has from the start placed a strong emphasis on producing original case studies. The CKGSB Case Research Center was founded in 2003, tasked with producing topical in-house teaching material. The center's output is oriented towards the operations of domestic and multinational firms in China, the interplay of competition and collaboration in emerging markets, and Chinese companies' efforts to engage in the global business environment. Reflecting a globalizing Chinese business landscape, the Case Research Center is a platform by which China can integrate with the world, and by which the world can strengthen its understanding of China.

Strategy cases comprise 53% of the total, marketing cases comprise 10%, economics cases 10%, operations cases 6%, human resources cases 6% and supply chain management cases 4%. Examples of strategy cases include China Dongxiang's integration of its Japanese acquisition, skiwear firm Phenix. The case looks at the massive cultural differences faced by Phenix's new owners, and how they were overcome by a combination of business brinkmanship and the longer term development of trust. Over the course of several years, Dongxiang was able to break the stranglehold of large suppliers and create an international supply chain leading back to China. Another example is a case on Huawei's joint venture with 3Com in the US, and whether or not Cisco's IPR was violated. The "Cisco case" helped encourage cooperation between Huawei and 3Com, but what were the other factors that contributed to this relationship? The case asks what kinds of challenges are faced by joint venture companies in a globalized economy.

CKGSB marketing case studies have often revealed very culturally specific insights. For example, a case study on Hengri, an engineering machinery company, reviews its quest to develop a brand and become a platform for similar products. It looks at how hard it is for a private company to create national sales channels, let alone international ones. Another marketing case study looks at a machine that brews high quality tea along the lines of the coffee pod. Is this the way to increase the convenience of tea drinking, and keep customers coming back to a particular brand? Having developed the machine, the case study looks at sales figures to show how customers regarded this novelty.

CKGSB's case studies cover ten major industries, of which the majority (30%) focus on non-daily-use consumer products, 21% focus on IT, 13% focus on daily use consumer products, 12% focus on heavy industry and 7% focus on finance. Two recent IT cases are particularly good examples of how CKGSB's Case Research Center is producing significant and unique insights into Chinese industry. The first is a case study on online gaming which looks at the relationship between regulators and interna-

tional online gaming firms. When American videogame developer and publisher, Blizzard Entertainment, decided to switch regulators, it lost millions of dollars in revenue when its main video game, World of Warcraft, was shut down. But in the long term did Blizzard make the right call? In another recent case about the collision between the conceptually open Internet and the traditionally closed business environment of China, U.S. Internet giant, Yahoo's Jerry Yang began a partnership with rising China e-commerce company, Alibaba Group's Jack Ma in 2005 by exchanging a \$1 billion investment and Yahoo China for a forty percent stake in Alibaba Group. Hopes were high that Alibaba's China expertise combined with Yahoo's search technology and deep pockets would help both companies dominate web business in China. Ma, however, soon began to resent Yahoo's influence over his company as Alibaba continued to grow rapidly, just as Yahoo's fortunes dwindled. This case is particularly relevant as background to the current dispute between the companies over the ownership of Alipay, an online payment system.

Over the past 30 years, private enterprises have been the main drivers of China's growth. Case studies are a strong medium to demonstrate the overall competitiveness of Chinese companies, and show how Chinese companies and multinationals compete and cooperate in the local and global business environment. To date, 62% of case studies have been about private companies, 26% have looked at state-owned companies and 12% have considered foreign-invested companies. However, a subtext of all these cases has been the workings of the state to aid or hinder the development of certain sectors. Two recent cases consider the government's response to very complex macro-economic dilemmas. The first, *Regulating Real Estate in China*, reviews how the government has tried to engineer a soft landing for the housing market, and considers reasons why prices continue to rise nonetheless. A case on *The Reemergence of China's Economy* shows how Deng Xiaoping's radical Reform and Opening Up policies unleashed market forces in the late 1970s, transforming a moribund planned economy into a bustling market. State-owned, private sector and foreign enterprises continue to contribute to the country's rapid economic renaissance but risks remain. Today China has become the world's second largest economy. How exactly did China get here and where is the country's economy heading next? ■

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*Heather Mowbray is a research manager CKGSB Case Research Center.*

*For more information including case abstracts and requests for access to cases please log onto [www.cheungkong-gsb.com/FacultyResearch/CaseCenter.aspx](http://www.cheungkong-gsb.com/FacultyResearch/CaseCenter.aspx) or contact Heather Mowbray at [heathermowbray@ckgsb.edu.cn](mailto:heathermowbray@ckgsb.edu.cn).*



# At the Heart of Business Forecast

CKGSB's Professor Li Wei provides new insights on company performance and market indicators with a ground-breaking survey of business leaders

By Alissa Haupt

**C**heung Kong Graduate School of Business' ground-breaking Case Center is pioneering new approaches to measuring company performance. The field of corporate performance measurement is awash with metrics like return on assets and return on equity, but at the heart of all these measurements is a missed opportunity—the CEOs themselves.

"All the data is embedded with every businessperson and CEO, because they see what is going on with their own firm. By collecting and aggregating that data, the people who are in possession of the data will be informed of what is really going on," says Li Wei, Professor of Economics and Emerging Markets Finance, Director of the Case Center at CKGSB.

Li Wei's research consists of surveys of senior management at medium and large-sized companies in China, providing a clear look into the operating conditions of current business, pricing changes, and market competition across the country.

Li, also the head of the Center for Responsible Business (CRB) at CKGSB, started the research center in order to offer an accurate source of solid data, in a country where data is often skewed by various incentives and forces. Officials in China

are evaluated based on their reported data, and many falsify their data in order to meet desired results.

"It is almost like Lake Woebegone," Li said, "where everything is above average".

Li and CKGSB share the goal of wanting to provide a widely accessible and accurate business index, in China.

"Businesses want to know where the economy is going and they really want to know if we can help them forecast what policy changes might come," Li said. "[But] the reliability of data in China is on a much lower level than that in developed countries".

In a mission to elevate the level of data reliability, Li's has created a business index based on responses to a bimonthly questionnaire sent to 112 of their Executive Master of Business (EMBA) students and alumni. The EMBA students are comprised of high-level managers and owners of businesses, and are able to provide exclusive data, particularly because it's not marred by a client-provider relationship.

"We report what we see and we don't have to mark it up or mark it down," Li says. "We are a school. We don't have a relationship, a loan and credit relations with our students, but we do have a rela-

tionship with them."


The school-based survey sample is an optimal starting place for knowledge creation in China, and has potential for growth as the CKGSB EMBA alumni network expands.

"Providing useful data has a lot of social value for the firm, the academic community and the government."

Li describes the overall research aim as piecing little fragments of information together to form a clear picture, while also acknowledging the improvement areas, such as the focus on Beijing.

"We can't say that we are a complete representation of China, but all of the foreign sectors are represented," says Li.

The center aims to hoping to expand the survey's sample size, with a goal to reach 400 firms by the middle of 2013. Once the survey reaches an optimum geographic representation, the center plans to open up the data on a national level, Li explains.

"We influence the people who then influence policy. That's what educational institutions do. We don't lobby. We don't directly do that, but we influence the opinions of the very people who then influence policy," Li said. 

# Exploring New Territory in M&A

As Chinese companies increase global M&A activity, the CKGSB Globalization Research Center investigates what's driving the deals

By Engen Tham

China has suddenly become a major player in mergers and acquisitions (M&As) around the world, with Chinese companies looking to buy foreign firms to acquire rights to intellectual property, establish a foothold in new markets and to simply diversify their business away from the home market. A new report by Xiang Bing, Founding Dean and Professor of Accounting at CKGSB, analyzes the most commonly adopted deal structures and provides recommendations and projections for the future.

The report, issued by CKGSB's Globalization Research Center, looks at the last 12 years of China's global M&A activity. It shows a steady increase in major M&A transactions by Chinese companies involving the takeover of firms in other countries, representing values of nearly \$200 million in recent years.

The Globalization Research Center, one of five research centers at CKGSB that cover customer information management, finance, multinational corporations, real estate and responsible business, considers Chinese cross-border M&As an important topic of research, as companies are increasingly using them as a vehicle for international expansion. Research for the report, released in September, was conducted along with Director Jiang Desong.

"A company can no longer operate in isolation, given the realities of globalization," Jiang told *CKGSB Magazine* in an interview. "It will not be able to compete if it uses only the resources accessible to it in its own country. If a company wishes to compete internationally and become a multinational corporation, it needs to source elements of its business globally. For example, it may need to utilize American talent, German and Japanese design, Chinese capital and Australia's natural resources. International M&A is an important strategy for a company wishing to integrate international resources."

"The scale of Chinese M&As and the number of these transactions are increasing, so it's one of the three most important research topics [covered by the center]," Jiang says.

The report indicates that China owes its growth in global M&A activity in part to its position as an emerging economy. While developed countries have faltered since 2008, China has been relatively less afflicted and has continued to expand. Meanwhile, China's domestic market continues to become more competitive and costs continue to rise, providing a further catalyst for firms to reach beyond for expertise, brand value and foreign markets.

The research report reviews the most common types of M&A, explaining the characteristics of each category and providing insight into the difficulties that each form faces. M&As in the service sector are the most popular, a pattern reflecting China's transition from a predominantly industrial economy to a service economy.

A key challenge faced by companies entering a transaction is aggressive competition, as firms from other emerging economies compete in the same markets. Firms also find it difficult to conform to foreign practices. "Chinese companies, when they go abroad, cannot conduct themselves as though they are still in China," says Jiang. "They should observe the laws in the countries they enter and observe the regulations that govern foreign workers. This is something that Chinese companies need to understand about doing business globally."

Many M&A deals also take place on a supply-demand basis, with companies merging with or acquiring a business further up or down the same supply chain. Most companies that undertake this form of M&A are state-owned companies, but such firms often face a plethora of approval processes before they can even start negotiations. The report also looks into cross-industry M&As and those that aim to lock-in foreign sales channels.

The report emphasizes that an economy dependent on exports is unsustainable. Chinese firms need to change their perspective on the benefits of dealings with foreign companies. They need to see investing in foreign markets not just as a way to control resources for domestic issues, but also as a way to create a global business presence and change practices with regard to innovation. Companies engaging in foreign investment should be less mercantile, as this has led to disputes and does not benefit either party.

On the "Made in China" question, the report says that companies should not just look abroad to resolve quality and innovation issues, but should instead resolve these problems domestically first. "The lack of innovation in Chinese companies should be solved domestically. This will eventually be solved with the return of overseas students and with the growth and development of domestic talent. It can be said that resolving this issue is a long-term goal," Jiang says. "[Tracking M&A trends] is one of our three most important research topics. We will continue to research the topic in line with current developments."



# Managing China's Growing Private Wealth

**CKGSB's Professor of Accounting and Finance, Liu Jing compares China's fledgling wealth management industry to that of developed markets**

By Suzanne Edwards

The expansion of personal wealth in China is now a familiar story. According to a recent Research and Markets report, the number of China's high net worth individuals has increased by more than 40% each year for the last four years, now totaling approximately 4 million individuals, a figure expected to double again by 2015.

Less familiar is the impact of this trend on private wealth management in China, and Liu Jing, Associate Dean and Professor of Accounting and Finance, CKGSB, aims to shed light on an often overlooked aspect of China's growth story.

Through an in-depth comparative analysis of private wealth management in China and overseas, Liu paints a clear picture of Chinese high net worth individuals, and the patterns characterizing their investment decisions.

"As an industry, private wealth management in China is still new, and the individuals are also very young, very hands-on," Liu says.

Liu's report shows a clear distinction between the trends in offshore investments on a global scale, and trends in China, where global offshore investments from developed markets have dropped significantly, while China's are increasing.

"There's already a practice [among Chinese high net worth individuals] of investing in real estate overseas," says Liu, adding that offshore investments are likely to increase, accounting for a larger percentage of overall asset allocation.

Liu's research indicates that China's high net worth individuals tend to invest more conservatively, in stark contrast to



the West where amounts allocated to individual investments have been traditionally very robust, with a comparatively higher amount of trust placed in financial advisors.

China's wealth management industry is growing at a dizzying pace, with great room for development of trust between investor and adviser. Liu suggests that we will see the results of this process soon. "We're likely to see a great increase in the value of investments from these individuals, and a lot more diversification."

The increase in individual wealth in China is outpacing the development of wealth management institutions, the report says, but a lack of awareness of China's uniqueness situation has resulted in awkward attempts by global investment houses to enter the local market.

"Multinational wealth companies come to China and try to fit China into their global model for wealth manage-

ment, and of course it doesn't work." Further compounding the difficulties of global firms is an attitude of distrust among China's wealthy. "Wealthy individuals are actually quite skeptical toward the wealth management industry," Liu says.

Liu predicts that within 10-15 years, Chinese wealth management firms will be able to fully match international players.

Examining fundamental questions that impact the market is the primary goal of CKGSB's newly founded Investment Research Center, in addition to specifying the broader implications of investment trends through collecting and analyzing data. Liu Jing directs the center. Industry experts tend to examine the day-to-day deals and lose sight of the big picture.

"In terms of the data, we can gather it better than the industry can, and be more objective in terms of analyzing it," Liu says. "At the same time we try to advance theory in terms of explaining what's going on, so that's our advantage." In addition to advancing theory, students are given great opportunities to advance their businesses, such as getting to know real estate tycoon Sam Zell, Liu says. "The students get a huge amount of value from participating, I'd say they're the biggest beneficiaries of this project."

The CKGSB Investment Research Center is a platform that brings together scholars, students, CKGSB alumni and investment professionals for learning and exchange. The center conducts ongoing research on private and public markets investments and periodically holds investment forums and releases research reports.

# From the Rich Life to the Enriched Life

## CKGSB alumni are redefining success

By Finlay Walker

The study of humanities as a concept is not new, but it is being newly recognized for its true value. The financial crisis of 2008 revealed the excesses of Wall Street and the avarice of many CEOs and forced the world at large to consider more deeply what corporate success should really mean.

Long before then, some business schools had already recognized that the social value of entrepreneurial endeavors must be part of any business project and vision from the very start. CKGSB, for instance, aims to equip its students with the insights and education necessary to succeed while also instilling a sense of fairness and responsibility as a core part of that process. China, with its growing wealth gap and food safety and other trust-related issues, is ripe for a business approach that redefines the meaning of success in terms of something other than simple personal wealth creation.

CKGSB Founding Dean and Accounting Professor Xiang Bing says that if business schools adhere to a traditional model, in which students learn the cutting edge concepts of management and then apply the knowledge only to increase personal wealth, then business schools are actually detrimental to society.

“B-schools can be a disservice to the community, with regard to income inequality and wealth disparity, which could be increased because of the existence of the B-school,” says Xiang.

Corporate social responsibility programs are designed to allow companies to manage their business processes to produce an overall positive impact on society as a whole. They provide a framework for

business people to work to improve their social surroundings while also making money, but often CSR is an afterthought passed onto the marketing department as a chance to build a positive brand image. This is something CKGSB students would like to see change.

“A socially responsible company is good for itself, but also for the social development of all the citizens of a country,” says Wang Zhaoming, CKGSB alumnus and chairman of Mong Grass, a company dealing in the distribution of hybrid grass that reduces desertification to various regions in China.

CKGSB’s approach to educating students to be pioneers of socially responsible business is to not merely require a single token course on ethics, but to offer students a varied range of courses on history, religion and society that enrich the cultural sensitivity aspect of business.

“Our approach to solving some of the business problems today, I hope, is more holistic, and not just focused on ethics per se, but getting a much broader perspective,” says Dean Xiang.

The importance of fusing humanities into management education plays an ever-more dominant role in discussions across the globe in terms of the future of business education.

Peter Lorange, former head of IMD Business School in Switzerland and recent founder of the Lorange Institute, says that currently one of the main problems of business education is an over-compartmentalization of subjects.

“The future should be in a confluence of management education with other disciplines, like psychology, social sciences

and political science,” says Lorange.

CKGSB’s approach to encouraging a global perspective and empathy for all members of society is to offer a plethora of humanities courses, including Classical Chinese Philosophy, Classical Western Philosophy, The Rise of Nations and Reflections on Civilization and Humanism and Confucianism, to name but a few.

Many business schools overlook the humanities, says Andrew Luo, Assistant Dean of CKGSB.

“You must give more,” says Luo. “Therefore we have introduced humanities programs, covering not only traditional Chinese literature, but also major religions of the world. Students will be exposed to knowledge and understanding of various nationalities or religions.”

Wang of Mong Grass cites his study of Buddhism as a major influence in his approach to business.

“You can use Buddhism as a tool to manage a business, a country or a family, as it encompasses all social laws and ethics,” says Wang. “In Buddhism, there is no difference between laws and ethics.” This is surely a useful suggestion for any company that has suffered as a result of using loopholes in legal regulations governing the financial sector.

According to Luo, decision-making must be governed by something bigger than just profit margins and personal wealth acquisition.

“There’s a rationale behind the decisions they [the graduates] make, which is connected to humanity.”

CKGSB both promotes business success, and also encourages students to think about the effects of their decisions. The school’s humanities curriculum takes world religions and other approaches to the “big picture” ideas and uses them to show students how to examine problems holistically.

“I like to see our alumni as human beings. I do not perceive them as instruments to increase value for shareholders, they have a life to live and many, if not the majority, would like to live a rich life, but I think living an enriched life is very important, and if obtainable, perhaps living an enlightened life,” says Xiang. ■



# The Six Founding Fathers of CKGSB

A look back at the professors who launched a world-class business school

By Elizabeth Mahoney

Several professors met at Oriental Plaza in Beijing in late 2001 to discuss the possibility of founding a business school in China aimed at cultivating world-class entrepreneurs and the school attaining a global top 10 status within 10 years.

People thought they were insane. China's management courses at that time were generally poor in quality, and while China had just been admitted to the WTO and was already the world's sixth-largest economy, there was still a huge gap between China and the developed world.

Ten years on, the business school they conceived has gained a global reputation. Featuring lectures by world-class professors such as Li Lode and Zheng Yusheng who specialize in both Chinese and Western studies, the school has attracted top entrepreneurs like Jack Ma, Guo Guangchang, Zheng Yonggang and Jiang Nanchun.

The school is Cheung Kong Graduate School of Business (CKGSB), which shares its name with Li Ka-shing's Hong Kong-based business empire. It is the first non-state, independent business school approved by China's Ministry of Education.

## Gathering for a Dream

Xiang Bing, director of the EMBA and

senior manager training programs at Peking University's Guanghua School of Management, received a phone call from The Li Ka Shing Foundation in 2001 inviting him to help found CKGSB. Xiang had been engaged in executive education in China for eight years.

He returned to China in 1994, after receiving a Ph.D. in Business Administration from the University of Alberta in Canada, and lectured at the Hong Kong University of Science & Technology (HKUST). Xiang helped found China Europe International Business School (CEIBS) in 1999, and later Peking University's EMBA program.

Xiang was moved by Li Ka-shing's goals: the school would cultivate entrepreneurs for China, would be research-driven, operating within a not-for-profit framework which would encourage teaching and research excellence, and recruit renowned professors from around the world.

Xiang endorsed these goals. He had long thought that China must establish a world-class business school and considered Li Ka-shing to be a suitable investor and benefactor for China's first private, not-for-profit, faculty-governed business school.

Xiang left Peking University in 2001 at the age of 39 to prepare for the establish-

ment of CKGSB. He originally met Professors Li Lode, and Qi Daqing in Hong Kong in the late 1990s when Xiang and Li were teaching at HKUST. They agreed that founding a private business school was imperative to China's economic and corporate growth. Li was over 50 and had been teaching at Yale for years. He always had the dream of founding a first-class business school in China. When Xiang approached Li and Qi with the proposition of starting CKGSB, they both leapt at the chance.

Zheng Yusheng was the first professor approached by Li. Li and Zheng, both management professors, knew each other from when they were both in the US in the 1980s. Before joining CKGSB, Zheng taught at Wharton School of the University of Pennsylvania as its first Chinese tenured professor. But Zheng knew he could do more in a Chinese business school.

The addition of Professors Zeng Ming and Xue Yunkui strengthened CKGSB's growing team. On a March afternoon in 2002, Zeng, a strategy professor at INSEAD who also lectured at Peking University and CEIBS, got a call from Xiang and they arranged to meet and he quickly decided to help found CKGSB. The plan matched his own desire to found an influential business school in China.

Xue Yunkui, meanwhile, was one of the founders of the Shanghai National Accounting Institute and its Deputy Dean as well as a professor. He gave up his high-ranking position there to join CKGSB in 2002.

It was risky for these six professors to leave their positions and work on the founding of a business school. They had concerns about their families and health-care issues. But they all shared the same dream of building a world-class business school in China.

Establishing the school was an arduous yet rewarding project. Qi Daqing and Xue Yunkui recall working long hours, staying up late one day drafting the documents for the Ministry of Education for approval. They sat on the steps in front of a hotel, eating hamburgers and hammering out the details. Qi said it was the most meaningful and unforgettable period in his life.

### A School Ruled by Professors

To found a world-class business school, Xiang set out to hire world-class professors. CKGSB's plan was to hire 100 such professors in five to 10 years, 60% to 70% of them Chinese-speaking.

But world-class Chinese-speaking professors were a rarity and it was difficult to convince them to return to China. Li Lode was the first Academic Deputy Dean of CKGSB, responsible for hiring professors. In the summer of 2002, during the preparatory phase, CKGSB convened a meeting to seek advice from international Chinese-born economists and management professors. The result of the meeting was a decision to found a committee of professors to vet and approve all prospective members of faculty. Xiang considered this to be a prerequisite for a world-class institution. CKGSB wouldn't be appealing to world-class professors if its decisions were made by the administration, as was the case with other Asian business schools.

Faculty governance has long been a common practice in European and American business schools. How would CKGSB apply it? Li Lode faced this question as Academic Deputy Dean. Who decided professors' welfare? If it were up to professors, the school would go broke, so Li

decided that professors' welfare would be decided by the Dean and the academic Deputy Dean, based on market rates.

Over time, CKGSB has specified which decisions are and are not made by professors. Matters of principle and professor recruitment and promotion are up to professors. Student admission is not up to professors.

"CKGSB's professor team is always professional because professors here are hired by the other professors instead of the Dean," Zheng Yusheng said. "In the 'rule by administration' system where such a decision is made by the Dean, chances are that professors prioritize personal connections with the Dean."

CKGSB spearheaded the faculty governance system in China. A CKGSB professor has to be good at lecturing as well as doing research.

"It is hard to balance the two," Zeng Ming said. "Those with excellent research capability won't give lectures at all, but a school's reputation hinges on impressive lectures; research findings are indirect for a brand."

Li Lode, as the Academic Deputy Dean, had a hard time appraising professors' research results because research on management couldn't be quantified. Using the number of academic papers published as a criterion was not applicable, because there were very few of these published by Chinese academics at that point. So Li's advice was forgo assessing professors based on the number of their theses.

### Trial and Error

The first step is always the hardest. When CKGSB started enrollments, almost every professor helped in attracting students, including Xiang Bing. In fact, Xiang attracted half of the first batch of students. High tuition fees is part of CKGSB's strategy. Its EMBA program fee set a record of RMB 258,000 in China, and has been rising. Xiang said high expense was a necessary condition for a successful world-class business school.

It worked. For the first year they enrolled 105, including Lin Zuoming, a CPPCC candidate and Chairman of Avic Liming Aero Engine Group Corp., Wang

Junyao, a CPPCC member and Chairman of JuneYao Group, and Lin Yang, Executive Vice President of Digital China.

Students had high expectation for the class experience due to the high tuition fees. To make it impressive, Zeng Ming and Yan Aiming spent a month preparing for CKGSB's orientation class. If this class failed, half of the students would have quit. But the class was as good as expected, and set the tone for future classes in terms of interactivity. "We couldn't afford to botch it up," Zeng said.

There were times in the early days, says Zeng, when lecturers were booed by students. "Not many lecturers understood China, and not many foreign professors had experience in giving Executive Development Program and Executive MBA classes; so they had no idea how to deal with businesspeople-turned students," he says. "They were used to lecturing in English, and couldn't shift to Mandarin in class quickly."

CKGSB has focused on leveraging its unique resources to improve the student education and learning experience. Students in the first enrolment had discussed case studies involving Chinese companies such as technology firms Lenovo and Huawei and real estate company Vanke. Since many students worked at those firms, the discussions were enriched with first hand insights and provided a fruitful opportunity for peer-to-peer learning. "The interaction strengthened the bond between students," Zeng said.

CKGSB's first CEO program gained in fame after enrolling China's top entrepreneurs, including Alibaba Group's Jack Ma, Fosun's Guo Guangchang and Mengniu Dairy's Niu Gensheng. "Since we aim to be a world-class business school, we have to grow with China's best entrepreneurs," Zeng said. These top entrepreneurs said they joined the class because of CKGSB's association with "superman" Li Ka-shing, who graciously thanked the students with a welcome dinner at which he mingled with the students. Professor Zeng confessed that CKGSB would not have been established without the generous support of the Li Ka Shing Foundation and the vision of Mr. Li Ka-shing. 

# Branding a New Generation Business School

Renowned graphic designer, Alan Chan, on creating CKGSB's logo

By Alan Chan

**"In ancient times those who wanted to learn would seek out a teacher, one who could propagate the [Confucian] doctrine, impart professional knowledge, and resolve doubts. Since no one is born omniscient, who can claim to have no doubts? If one has doubts and is not willing to learn from a teacher, his doubts will never be resolved."**

– Han Yu (768–824), Tang dynasty Neo-Confucian essayist and poet.

I was first drawn to the Cheung Kong Graduate School of Business (CKGSB) a decade ago through a special request from the Li Ka Shing Foundation, to design the school's logo. Since then I have been inextricably linked to CKGSB.

I launched myself into a career in advertising after graduating in 1969. I attended night classes to study for 10 months but felt uninspired. Like many others, I was instantly attracted to CKGSB. I admire CKGSB for its core pedagogic philosophy which incorporates both Chinese and Western ideology, and for the school's determined ambition to be an innovative business school. Despite never attending such a high-level business school, I would relish the opportunity to study—one of life's most important pursuits—at such a world-class institute.

CKGSB's campus culture promotes teamwork, humanism and social responsibility—attributes I whole-heartedly endorse. I think teamwork creates an environment of equity, enthusiasm and cohesion while humanism and social responsibility are necessary conditions for success. These three key attributes—a keen team spirit, a humanistic approach to learning and a strong sense of civic duty—have made a profoundly positive impression on my relationship with CKGSB.

Ten years ago, when designing the CKGSB logo, I chose the concept of a traditional Chinese imperial seal to reflect the school's authority and credibility. The



CKGSB

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CKGSB's logo, designed by Alan Chan

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logo's imagery is synonymous with validity, authority and approval. The seal contains two stylized Chinese characters for "Cheung Kong", with the right half being "Cheung" and the lower half of the seal being "Kong", to match the name of the school. The horizontal and vertical lines symbolize the different Chinese and Western methods of storing books, with books being laid horizontally, as is tradition in China and being laid vertically, as is tradition in the west.

The seal also looks like the first hexagram in the *I Ching*, (Book of Changes), an ancient Chinese book on divination, which is interpreted to mean: "Just as Heaven persists powerfully through time, so must a gentleman strive unrelentingly [for greatness]." Blue, the theme color of the seal, represents wisdom, passion, advancement, technology and the surging waters of the Cheung Kong or Yangtze River. The seal's typeface retains a profes-

sional, low-key and yet grand style.

A good design is classic and will never be out of date. Ten years later I was asked to design an emblem for CKGSB's 10th anniversary based on the seal created 10 years ago. A celebratory pattern was added to the existing seal to commemorate the 10th anniversary of CKGSB, the golden hue evoking honor and glory.

From the beginning the design process was an experience marked by inspiration, and creativity. In order to create a logo that I would be proud of and would exceed the expectations of the CKGSB community, I had to reach an understanding of its intended sentiment. After gaining an understanding of CKGSB's value system, I began brainstorming to develop concepts. After a rigorous process of trial and development, the current logo was selected to best represent the spirit of CKGSB after a decade of leadership and excellence. Design, like education, is about detail and devotion. An innovative design depends on details; a good school depends on devotion. ■

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*Alan Chan is a renowned graphic designer based in Hong Kong and has produced iconic work for brands such as Coca-Cola (China) and won over 600 local and international awards during his 40 years in advertising and design. Chan has also won prestigious awards in fine arts, and was the first designer given a solo exhibition in 2007 at the Shanghai Museum of Art.*

# In Dialogue with the World

**Reaching a global audience of influential business leaders, CKGSB drives executive level dialogue across the globe**

CKGSB partners with leading international institutions to host annual forums in Asia, North America, and Europe. These global platforms link influential business leaders and participants in CKGSB's CEO Program and alumni network to share insights and discuss the global implications, challenges and opportunities of China's economic rise.

## CKGSB Annual Forum

The CKGSB Annual Forum, co-hosted by the Hainan Provincial Government connects leading scholars, government officials and business professionals—including more than 1,500 CKGSB students and alumni—to discuss critical issues facing Chinese companies. Held Sanya on Hainan Island, it is one of China's premier business meetings. The forum explores issues such as the globalization of Chinese companies, opportunities throughout Asia and China's predicted growth over the next decade.



*Founding Dean and Professor of Accounting, Xiang Bing (left), Ambassador Wu Jianmin (center), with Professor Tu Weiming (right) at the CKGSB Annual Forum in Sanya, 2012*



*CKGSB Professor of Finance, Chen Long at the China-Japan CEO Forum in Tokyo, 2012*

## China-Japan Business Forum

The China-Japan Business Forum brings together business and thought leaders from China and Japan to discuss critical issues affecting East Asian business in a global context. In 2012, CKGSB partnered with Nikkei Business Publications to host the annual forum in Tokyo.



*Lord Green of Hurstpierpoint, UK Minister of State for Trade and Investment, at the launch ceremony of the All-Party Parliamentary Group for East Asian Business in London, 2012*

## All-Party Parliamentary Group for East Asian Business

CKGSB is secretariat to the APPG for East Asian Business, a United Kingdom parliamentary body launched in February, 2012. The APPG, which draws officers from both the House of Lords and the House of Commons, supports good and sustainable business ties between the UK and East Asia. In its role as secretariat, CKGSB regularly organizes events at Westminster Palace and provides a platform for trade missions and research reports.



### Ernst & Young Entrepreneur of the Year China

CKGSB is exclusive knowledge partner at the Ernst & Young Entrepreneur of the Year China awards for 2011 and 2012. The annual award celebrates entrepreneurs who combine foresight and outstanding leadership abilities to achieve extraordinary business success. In 2011, CKGSB and Ernst & Young jointly produced a white paper, *Coping with the Global Economic Slowdown*, that reported the results of a survey of 100 of China's leading private entrepreneurs, including many CKGSB alumni.

*Associate Dean and Professor of Accounting and Finance, Liu Jing (right) at the Ernst & Young Entrepreneur of the Year China Awards round table in Beijing, 2011*



*Former CEO of Yuhan-Kimberly, Mr. Moon Kook-Hyun at the CKGSB Summer Forum in Yunnan, 2012*

### CKGSB Summer Forum

The CKGSB Summer Forum is a platform for students, alumni and friends of CKGSB to share knowledge on new business models in China and beyond. The forum is held annually in the southwestern city of Kunming, known as China's gateway to Southeast Asia.



*Sir Tom Hunter at CKGSB's Beijing Campus, 2012*

### CKGSB Distinguished Speaker Series

Through CKGSB's extensive global network, the school has unparalleled access to the highest level of academic and business leaders, whom CKGSB regularly invites to speak with students, alumni and the CKGSB community through an intimate lecture series. In 2012 CKGSB welcomed distinguished speakers such as Scotland's first Billionaire, Sir Tom Hunter and former CEO of Yuhan-Kimberly, Mr. Moon Kook-Hyun.

### China Institute Executive Summit

CKGSB co-organizes this high-level annual gathering in New York of businesspeople, economists, journalists and representatives from government agencies and non-profits. At the summit, CKGSB's world-class faculty members and influential alumni share insight into China's role in the changing world economy.



*Dean Xiang Bing with China Institute President Sara Judge McCalpin, Julie Nixon Eisenhower and Virginia Kamsky, CEO of Kamsky Associates Inc. at the China Institute Executive Summit in New York, 2011*



**CKGSB**  
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 CHEUNG KONG GRADUATE  
 SCHOOL OF BUSINESS



2012

- CKGSB celebrates 10 years of excellence in executive education
- CKGSB held the first China-UK Business Forum in Paris, France
- CKGSB unveiled its Knowledge website, [knowledge.ckgsb.edu.cn](http://knowledge.ckgsb.edu.cn), to serve as a multimedia platform for the school's research



- CKGSB opened its first European campus at St James Square, London

2011



- CKGSB opened offices in New York and Hong Kong to expand its global presence

2010



- CKGSB launched its Finance MBA Program, the first fully bilingual program offered by the school

2009



- After the 2008 Sichuan Wenchuan Earthquake, CKGSB's students donated over RMB 429 million in individual and corporate donations, accounting for 7% of Chinese corporate donations to earthquake victims (Source: Sina)

2008



- CKGSB established the China-Korean Business Forum, held in Shenzhen and attended by 35 CEOs of Korean companies
- CKGSB partnered with INSEAD to establish its China-India Business Forum

2007



- CKGSB launched the China CEO Program
- Cohort included 35 of China's premier business leaders including Alibaba's Jack Ma, SINOPEC's Fu Chengyu and TCL's Li Dongsheng

2006



- CKGSB's EMBA and MBA programs endorsed by the State Council Academic Degrees Committee
- CKGSB held the school's first EMBA and MBA Graduation Ceremony at the iconic Great Hall of the People in Beijing

2005



- CKGSB Alumni Association formed. Today, the association has 35 chapters across China and internationally
- CKGSB opened its Shanghai Campus

2004



- The CKGSB Case Center established to support scholarly research
- CKGSB enrolled its first MBA class. GMAT average score of 680 positioning CKGSB as leading Asian business school
- CKGSB launched its first Executive Development Program, "Finance for non-financial managers"

2003



- Cheung Kong Graduate School of Business founded with generous support from the Li Ka Shing Foundation and a personal endorsement from Mr Li Ka-shing
- CKGSB established its Beijing campus and enrolled 105 EMBA students

2002



# Looking Forward

Dean Xiang Bing shares his vision for the next 10 years at CKGSB

*Q. In what directions do you foresee CKGSB growing into the near future?*

A. CKGSB is strategically positioned to grow in two key directions over the next 10 years. Firstly, the East-Asian, Japanese, Korean and ASEAN bloc markets will be a prime focus for the school. Additionally, the BRIC nations and emerging markets, particularly South Africa, will be keen areas of interest and growth. I am confident that CKGSB will become one of the world's leading business schools over the next 10 years, contributing critical research and insights to the global business community. I look forward to launching degree and non-degree programs through our London and New York offices, which is a key component of our global strategy. The school will also pay particular attention to how the development of new sciences and technologies impact human lifestyles as sustainable development remains to be a significant issue for both business and government.

*Q. What is your vision for CKGSB over the next decade as the school becomes a true global leader in business school education?*

A. I hope that CKGSB will grow to become a shared platform for global business. We have a profound knowledge of Chinese, Western and global markets and an unmatched alumni network which spans all of these. In terms of becoming a true global leader in business school education, CKGSB is already well on the way to claiming this status, and already cooperates with the world's elite business schools. We have equally accomplished, world-class professors but are distinct from our European and North American partners in our knowledge of China and

the Asian region.

CKGSB and the world's top business schools maintain a reciprocal relationship. The key to our strategy rests in constructive innovation, encouraging ongoing and creative learning, and expanding the traditional view of what it is to do business. CKGSB's research assists business leaders in understanding China's growing importance in the world's industries and the impact of the globalization of Chinese companies. Furthermore, our alumni network, who if grouped collectively would currently form the world's 16th-largest economy, represent the highest echelon of Chinese and global business leaders. I think that CKGSB has already made a huge contribution to China, and the world's management education. For example, we have already introduced humanities programs, such as history and philosophy, to management education, a first for executive education globally.

*Q. CKGSB has already established research centers in the fields of globalization, investment, and customer information management to name a few. What are the key areas CKGSB's research centers will focus on in the future?*

A. We need to focus on traditional, fundamental fields of academic research but view them from a different perspective to how we have in the past. We must increase our research focus in the BRIC nations and East Asia. Our research will be characterized by parameters which are both academic and practical, and forward looking. The topics will be global in nature, such as sustainable development, and we will cooperate with strategically placed partners around the globe to generate these insights. CKGSB has a lot to

offer other business schools—we have world-class professors who are real experts in different sectors, and an extensive global network.

*Q. CKGSB will generate significant original research. What contribution do you hope this will make to the international business community?*

A. Academically, some of our new management concepts, including the mindset such as supply chain versus chain and viewing the Earth from the Moon, which I have explored, are different from that of the West. So the greatest contribution in the past decade is having opened the door for two-way communication. I hope we can broaden the practice in the next decade. China's economy is evolving to be increasingly influential and we are now the world's second-largest economic power. The biggest challenge is that we must have a global vision and mindset. We were the world's largest economy for 18 centuries. If China is to aim higher, we need more entrepreneurs with a wider global vision.

It requires a true global vision for China to effectively rise. I hope CKGSB will make historic contributions to China's business development.

*Q. CKGSB helped build a global vision for the entire Chinese economy in the past decade, and how will CKGSB continue to expand this vision moving forward?*

A. There's practically no limit to learning. In the past decade we helped build a platform for China's entrepreneurs to learn globally. One pre-requisite for China to be strong is we must remain modest and open. We must keep learning, learning from the world and learning to integrate global resources. I hope we can further ex-

pand the platform globally based on what we have achieved in the past five and six years and integrate more resources.

*Q. In comparison with the past decade, where do you see progress on the roadmap for the next decade?*


A. Globalization is without doubt an assured trend across various regions, with more attention to methodology. The other shared challenge is what I mean by short-term behavior. It can vary drastically to think short-term from long-term. I am in favor of measuring business development or urban development from a long-term point of view. I think it's of tremendous importance and the limitation of democracy is apparent on this point. All people, including me, can be short-sighted, and the whole community is getting increasingly short-sighted, which I think is a big challenge. If we are to become the

world's most influential business school, we must dedicate more resources to and take the lead in, addressing these social problems.

*Q. The theme for CKGSB's 10th anniversary ceremony is "Meeting the Challenges of Tomorrow." What message do you hope this will convey to the CKGSB community and how does this reflect CKGSB's goals for the next decade?*

A. CKGSB was founded through the generous support of the Li Ka Shing Foundation with guiding inspiration from Mr. Li Ka-shing, Asia's most successful entrepreneur, and the goal of becoming a world-class business school. With such ambitious beginnings, CKGSB has strived to uphold this entrepreneurial spirit in all aspects of the school's growth. Globally, we have an opportunity to impact people's thoughts on what it means to do business,

not just how but why, and what wealth truly means for both the businessman and society.

I think that the CKGSB community ought to be proud of what the school has accomplished over the past 10 years. It's natural to look back and reflect on the growth and development CKGSB has achieved with an overwhelming sense of pride. But we cannot become complacent. We cannot let this pride cloud our sense of direction or dampen our sense of purpose. There is a long road ahead for both the school and for China. We cannot rest on our laurels but must conscientiously reflect, recharge and start anew. CKGSB's alumni members each have their own unique strengths and weaknesses, yet united we embrace the vast opportunities and exciting challenges the future will bring. It is in this spirit that CKGSB greets the next 10 years. 





CKGSB ALUMNI SHAPE

**\$1 TRILLION**

IN REVENUE A YEAR

Cheung Kong Graduate School of Business has prepared more than **2,500** Chairmen and CEOs of China's leading companies to shape the future. They run companies that comprise **1/5** of China's most valuable brands, touch billions of customers across the world and together generate **\$1 trillion** in revenue a year. If CKGSB's alumni network were a nation it would be the **16th** largest economy on earth.

Now with our innovative global programs designed for senior business leaders you can become part of China's most influential alumni network.

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