

# CKGSB

CHEUNG KONG  
GRADUATE SCHOOL  
OF BUSINESS  
MAGAZINE

OCTOBER 2012



## Separating China's Innovators from Imitators

Investment secrets from real estate mogul Sam Zell

China's aging population presents a huge opportunity but it is not easy to win in this market

John Little, the Founding Father of Marketing Science, looks back



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**16** **IMITATION. INNOVATION.**

**Cover Story**

Three erstwhile copycats innovate through trial and error, to fight the fierce war over the online classified market



**China Insight 25**

**No Silver Bullet**  
Catching the opportunities in China's senior-care market is far from easy

**28** **China Insight**

**Gone Fishing**  
China's domination of the global seafood export sector is under threat



**12** **Cover Story**

**Taking the Hard Road**  
Warren Buffet may have bet on the wrong horse with BYD, a car company that's headed for a crash



**Dialogue 21**

**"Any Time You Don't Sell, You Buy"**  
The investment philosophy of real estate mogul Sam Zell

**China Insight 6** **Snapshot 8**

**The New Big Spenders**  
Luxury brands change tactics to drive sales in tier-two and tier-three cities

**Tweet. Retweet. Follow.**  
China's social media stars take flight



**31** **Transformation**

**Charting a New Course**  
Vantone chairman Feng Lun on pioneering a new business model for China's real estate industry



Yu Miaojie: China could use a shot in the arm from the government

**Debate Room: China's Stimulus Package**

**10**

Li Wei: The slowdown is a natural stage of China's growth. We should grin and bear it





Issue: Oct 2012

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**57** Downtime  
**The Homes of Huizhou**  
Amidst wanton cultural destruction, one millionaire is saving Anhui's traditional architecture. Even if it means moving it to Beijing

**60** Bookshelf  
**Connecting the Dots**  
Jennifer Li, CFO of Baidu, on her eclectic reading habits

Interviews

**38**

Marketing Special

**John Little on Marketing Science**

How the pathbreaker created a new field of research



**40**

The Thinker Interview

**Leadership's Blue-Eyed Boy**

Marshall Goldsmith changed the way we think about leadership. What makes his teachings so popular?

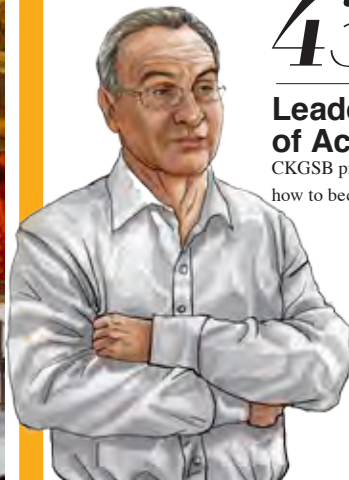


**43**

Management

**Leadership is a Series of Acts**

CKGSB professor Shalom Saada Saar on how to become a well-rounded leader



**35**

C-Suite

**The New Idea Factories**

Xiang Weiming of GE Aviation on how the conglomerate views emerging markets



Inside CKGSB

**49** Steady Steps to a Promising Future

**52** Marketing thought leaders share cutting-edge ideas

**50** Kai-Fu Lee on tech innovation in China

**54** Platform for international dialogue and thought leadership

**51** CKGSB and Oxford presents Emerging Market Series

**56** Leading executives update their China knowledge



**46**

Invisible Hand Revealed

**Beijing's Taxi Problems**

How simple economics can solve such a vexing problem

**47**

China Insight

**Snaring the Dragon**

What can stall China's growth and what can be done about it

# The Dawn of Made in China 2.0

To many of those who live outside China, ‘Made in China’ is seen as equivalent to low-cost and low-quality products, with little or no innovation from Chinese companies. That, to my mind, is only partially true. Here at CKGSB, we are observing some under-the-radar trends that are redefining ‘Made in China’. Despite the fact that a massive number of ‘me too’ companies started their business by copying successful products, services and business models of global companies, most of those Chinese copycats that were unable to evolve and expand their offerings beyond what they had copied, have vanished sooner or later. To survive in the long run and to win business—even within China—a Chinese company must quickly adapt to the local context and develop new features, new products and new services for Chinese customers who are different from their counterparts elsewhere in the world. Otherwise they will stand no chance in the severely competitive Chinese market, where almost everyone competes at the lowest possible price. Thus, the value of the offering becomes the differentiator.

Those who follow the Chinese IT market may know of Tencent, a Chinese company that initially began as an instant messaging (IM) company emulating ICQ and Microsoft’s MSN Messenger. Tencent is now the fourth-largest internet company in the world in terms of market capitalization after Google, Amazon and eBay. Few can answer the question: “Why has Tencent dominated the IM market in China?” Our observation is that Tencent has succeeded because it continuously provides new features (Chinese language-based IM), products (online games) and services (e-commerce) to its Chinese clientele.

That brings me to the theme we have chosen to highlight in this issue of *CKGSB Magazine*: the evolution of Chinese companies that started off by emulating global companies. On page 16, we have a story on online classified advertising companies such as 58.com, Ganji and Baixing, all of which got their original inspiration from Craigslist, a hugely successful company in the US. Each of these companies eventually forged a different path to address the specific needs of Chinese consumers. This model seems to have paid off in the long run. Meanwhile, other Chinese companies that also copied Craigslist, but failed to differentiate and localize their offering, went bust. The lessons from these companies is clear: no matter how you begin, if you want to succeed in the long run, you must find a smart way to adapt and innovate your model for the Chinese market. Companies that fail to realize that soon enough begin to

struggle as is the case of BYD (page 12).

Elsewhere in this issue, we bring you interviews with leading global thinkers. One of them is with John Little, the ‘Founding Father of Marketing Science’, who looks back at his life’s work and talks of how Chinese companies can learn from the US experience in adopting data-driven mathematical models in marketing. The second one is with Marshall Goldsmith, who is acknowledged as a leading executive coach and leadership expert globally. This is part of a thought leader interview series we are kicking off from this issue. What we found fascinating is that many of Goldsmith’s ideas have been shaped by Buddhist philosophy. In the interview he cautions readers against the great “Western disease” of always hankering after money and status, and refers to the Buddha’s teaching of learning to accept *what is*. Over the next few issues, we plan to bring you many more thought-provoking ideas from the finest minds around the world.

We also have a no-holds-barred conversation with American real estate and media mogul Sam Zell, and an interview with CKGSB Professor of Managerial Practice and acclaimed leadership expert Shalom Saada Saar, who has unique insights on both Chinese and global leaders.

As in each of the previous issues, we bring you new insights about China. In this issue, we take a look at how China’s changing demographics are opening up new opportunities in the ‘elder care’ consumer segment and how some companies are trying to tap that opportunity. We also take a look at second- and third-tier cities that are increasingly driving the growth of luxury goods sales in China.

Our goal is to provide unique insights for our readers to better understand the real China, its economy and business, as well as the cultural and social issues around them. Please write to us if you have any comments at [magazine@ckgsb.edu.cn](mailto:magazine@ckgsb.edu.cn)

I hope you enjoy reading this issue. For more articles and insights on business in China, you are welcome to visit our research and knowledge site, [CKGSB Knowledge \(knowledge.ckgsb.edu.cn\)](http://knowledge.ckgsb.edu.cn).



  
Zhou Li  
Assistant Dean, CKGSB



China Investment Corp.'s rough year was a good one for China's top CEOs. Meanwhile, CNOOC's going abroad again, and global warming might be good news for Chinese traders.

If at First You Don't Succeed...



State-owned oil giant, China National Offshore Oil Corp. (CNOOC), is at it again. China's largest offshore oil and gas producer has offered \$15.1 billion to buy Canadian oil company Nexen, which has shale drilling expertise and significant holdings in tar sands. CNOOC will pay \$27.5 for each Nexen share, a 61% premium on its July 20 closing price, and will also buy all of Nexen's preferred shares for \$26 each. The deal has won the approval of the boards of directors of both CNOOC and Nexen, but still needs approval from the governments of Canada, China and the United States, which is a mighty hurdle indeed. Last time CNOOC tried to buy up a North American oil company, Uncle Sam slammed the door in their faces, for ostensibly political reasons. Given North America's complete monopoly in shale fracking and tar sands extraction, it wouldn't be surprising if CNOOC receives a similarly cold greeting.

Risky Business

Last year saw China's \$500 billion sovereign wealth fund singing the blues after it lost 4.3% on its outbound investment, down from 11.7% in 2010. This makes 2011 its worst year ever since 2007 when the fund was set up, according to China Investment Corp's (CIC) annual report. The performance was affected by the weak market and the volatility of some listed energy and resources companies in which CIC invested. It received another \$30 billion injection from the government last year. As of the end of 2011, CIC managed \$482 billion in assets, and its overseas assets totaled \$147 billion.

Mr. Megabucks

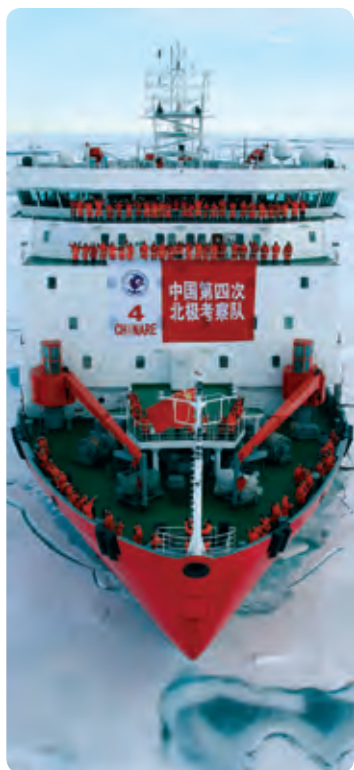
Vanke Real Estate President, Yu Liang earned RMB 13 million (\$2.04 million) last year, making him the highest grossing executive of all publicly listed companies in China. Ping An Insurance CEO, Ma Mingzhe ranked second with RMB 9.9 million in annual pay package and Mai Boliang, President of China International Marine Containers, was a close third grossing RMB 9.6 million. The report published in May by the Shanghai-based Sino Sound Consulting also shows that executives in finance and insurance are the highest paid with an average salary of RMB 2.7 million,

followed by real estate (RMB 0.97 million) and the wholesale and retail (RMB 0.76 million) industries. Meanwhile, Lenovo CEO Yang Yuanqing decided to spread the wealth and gave away RMB 19 million (\$3 million) from his bonus to the 10,000 junior-level employees worldwide—including receptionists and factory workers—in appreciation of their hard work.



Breaking the Ice

The Chinese icebreaker, *Xuelong*, or "Snow Dragon" has become the first Chinese ship to cross the Arctic Ocean, where a record thaw caused by melting of Arctic ice may open new trade routes. Climate change has a positive side for business as it may open new trade routes that China is testing in its expansion into the Arctic—an oil and gas-rich area—which can also be utilized as a commercial shipping lane between the Atlantic and Pacific oceans. Sea ice floating on the Arctic is on track to beat a record low set in 2007, making the region more accessible, and the melt is gradually opening up the Arctic as a short-cut to open new trade routes.



### Self-starters

Facing mounting GDP pressure, local governments aren't waiting for largesse from Beijing and are taking their own initiative. Changsha, capital city of Central China's Hunan Province, has unveiled an RMB 800 billion (\$125.76 billion) investment plan to boost its local economy. The projects range from airport expansion and road building to waste treatment, and makeovers for older areas in the city. In a similar spirit, Guizhou Province has announced a RMB 3 trillion stimulus plan to boost cultural and ecological tourism, according to *The Economic Observer*.



Photo:CFP

### City Mice Rising

For the first time in its history, China's city dwellers now outnumber their country counterparts according to *The Urban Blue Book*, recently published by the Chinese Academy of Social Sciences. The report says the country's urbanization rate has reached 51.27%. This marks a significant change in the country's social structure, which according to the report, ushers in a new era of "city-based society". The ratio of disposable income earned by urbanites to that of rural residents is about 5.2:1, up from 3.13:1 last year. However, China still has a long road to walk in order to become truly city-based, *The Blue Book* argued, as the majority of migrant workers and farmers-turned-city dwellers find it hard to adjust to urban life. Most Chinese cities lack familiar features and cultures that reflect the newly arrived country cousins' rural roots.



Photo:geethimages



Photo:geethimages

### Chinese Cities to Lead Global Growth

Don't know where Foshan is? Never heard of Wuhan? It's time to look them up. They are two of the 29 Chinese cities that are expected to be among the world's 75 fastest growing metropolises over the next 15 years, according to a new report released by *Foreign Policy* magazine in association with McKinsey Global Institute. Three Chinese cities—Shanghai, Beijing and Tianjin—take the top three positions of the list. Further, just 440 cities, half of which are in China, will account for around 50% of global GDP. Yet only one in five corporate decision-makers base their strategies on cities as the fundamental unit rather than countries.

### Football Soft Power

State-owned enterprise China Railway Construction has decided to kick it Italian style and paid \$600 million for a 15% stake in Inter Milan, becoming the second-biggest shareholder of Italy's top football club. The deal includes building a stadium for the team, but the financial details are yet to be released, according to *Bloomberg News*.



### Bullish on Europe

In non-athletic dealings, China's investment in Europe increased by as much as 200% last year to \$10 billion, according to the recent research by the American consultancy Rhodium Group and China International Capital Corporation. The research shows that 63% of Chinese investment in Europe comes from private companies, despite the Eurozone economic woes. The top five Chinese private investors in Europe are Geely, Huawei, Lenovo, Sany and Wolong Group. Chinese investment has created 45,000 jobs in the EU. It predicts China's investment in the region will range between \$250 billion and \$500 billion at the end of 2020. In the meantime, Chinese deals worth a total of \$7.8 billion are going into the US for the first eight months, approaching the full-year record of \$8.9 billion set in 2007, according to data from Dealogic.



Photo:IC

Facing a nearly 25% unemployment rate, people in Valencia, Spain, get subsidized meals at a charity dining hall



# The New Big Spenders

Luxury brands change tactics to drive sales in tier-two and tier-three cities

By Matthew Jukes and Yan Ruiying

Just a decade ago, Jiefangbei Pedestrian Street in downtown Chongqing was a bustling hub of cheap goods and low-end domestic brands. To see a woman stroll down the street toting a Louis Vuitton bag wouldn't have been unusual: everyone would have just assumed it was an inexpensive knock-off. Those days are now long gone.

Rising labor costs have driven manufacturers from Shanghai and Guangzhou to the interior, and the economy of this one-time backwater has boomed. The street now boasts four malls, all within a stone's throw of each other, and Louis Vuitton has arrived, in the flesh. Housed in a mall named Maison Mode, Louis Vuitton's 1,500 square meter store sells RMB 6,100 Speedy 30 bags like hotcakes. And it's not alone. Across the flag-stoned pedestrian street there's the unmistakable gold-lettered Gucci sign, a glistening beacon calling out to Chongqing's conspicuous consumers. Nearby, visible through the plate glass windows of the neighboring Times Square Mall, there's an Armani outlet.

All three stores have opened in the past two years and are signs of intensified interest in lower tier cities like Chongqing among luxury brands in China. Louis Vuitton's store opening in Chongqing came right after a store just two hours down the road in Sichuan's provincial capital, Chengdu.

Say goodbye to Shanghai's Bund, luxury brand marketers, the future of opulence is right here: in China's inland cities.

## Luxury leaders

First-quarter sales of the LVMH Moët Hennessy group (which owns Louis Vuitton), jumped 25%, a rise attributed by the group to



The 2010 launch of Louis Vuitton's flagship store in Chengdu, a second-tier city in Western China

sales in China. Other winners from China's luxury impulses include Italy's Prada SpA, whose first-quarter profit more than doubled, in part thanks to strong sales of company favorites like their perforated leather handbags which retail in Chinese boutiques for RMB 25,000.

Strong results published by leading firms will be encouraging for luxury brands depending on growth in China to make up for weaker Eurozone sales. But brands are finding they have to move deeper into China's

interior to keep driving sales growth. Smaller cities like Yiwu, Shijiazhuang and Ordos are driving the future growth of luxury goods sales in China, explains Zhou Ting, director of the Fortune Character China Institute (FCCI), a consultancy that researches the lifestyle of China's rich. "The global luxury market is dependent on China's market, but China's market is dependent on its second- and third-tier cities," says Zhou.

According to FCCI research, luxury brand sales in tier-two and three cities have now



surpassed sales in tier-one municipalities. “Brands now see tier-one cities as a platform for brand promotion, but the main sales action is in smaller cities,” says Zhou. She points to high-end Italian clothing brand Kition: its highest sales are in Hangzhou while Louis Vuitton’s highest revenue store is in far-westerly Urumqi. The less-than-glamorous cities of Taiyuan, Ordos and Zhengzhou rank in the top five city markets for car maker, Bentley.

China is on pace to top Japan as the world’s largest market for luxury goods, according to McKinsey & Co., which estimates sales will surge 18% annually to hit \$27 billion by 2015. That’s a fifth of the worldwide total and up from just \$10 billion in 2009. Who wins the biggest market share may be decided by who plays the second- and third-tiers.

According to the GroupM Knowledge Hurun Wealth Report 2012, there are over a million Chinese people with personal assets over RMB 10 million, only a third of whom live in Beijing, Shanghai and Guangzhou. Success for luxury brands may depend on how well brands can cater to the wealthy outside China’s top-tier cities.

### Taking Back Control

Brands are learning to adapt their business models in China to penetrate regional markets. That means building a larger presence and taking direct control. “Global brands are buying back direct control over their businesses from Chinese local business partners,” says Sun Baohong, Dean’s Distinguished Chair Professor of Marketing, CKGSB. “For luxury brands before, when they expanded to second- and third-tier cities they used local businesses to manage and they could quickly expand into those markets. Before their strategy was to use established channels to do the branding, now they’re in control of their operations.”

While many companies in the past have left management in China to an Asia-Pacific regional office, some have begun to open regional offices across China to drive sales. “With the tier-two and three markets developing fast, these brands will increase their regional management,” says Zhou. She points to Bentley, which has divided its China operations into North and South management zones.

### Movin’ on up

Other luxury market watchers point to a transition in consumption patterns with wealthy in first-tier cities increasingly making their purchases overseas, while lower tier consumers grow increasingly demanding



that as much as 80% of all Hermès products bought online in China were fake.

### Regional Differences

Luxury brands will have to tailor marketing campaigns to individual cities. Different media markets mean consumers in lower-tier cities are less familiar with luxury brands, says Zhou. “Glossy fashion magazines loaded with carefully targeted adverts are a staple on the newsstands of Beijing and Shanghai but remain highly focused on large cities. Smaller cities are more served by state-run local newspapers,” remarks Zhou, who thinks luxury brands will have to spend a lot more time researching regional markets. “They have to proactively establish sales terminals, and work to increase consumer loyalty,” he adds.

The roll out of high-end malls to regional Chinese cities is another growth driver for luxury brands. Sun explains that luxury brands are opening stores in the second- and third-tier cities not only because of demand. “The infrastructure is now there too,” says Sun. “They want high-end malls and that is paving the way for luxury brands to be in those cities.”

There are, however, clouds on the horizon. A slowdown in China’s economy was blamed by Hong Kong retailers for dragging the city’s retail-sales growth to the weakest pace since 2009 as shoppers visiting from the mainland cut back on purchases of luxury goods such as jewelry and watches.

Similarly, German fashion house Hugo Boss saw growth in China sales slow down to only 1% in the second quarter of 2012, according to the company’s official results. In a statement announcing its first-quarter results the firm referred to “double-digit” growth in China, without specifying a figure. Hugo Boss’s Asia-Pacific sales as a whole grew 4% in the period, compared to 9% growth in the first quarter. Others such as German automakers Mercedes-Benz, Audi and BMW are expected to report smaller profit margins from the Chinese market in the coming months as they cut prices across the board.

It may be that the days of double-digit GDP growth rates are over, but experts still see prospects for solid sales growth in luxury goods in China. Zhang says though GDP growth slowed to 7.6% at the end of June, there’s no sign that the overall upward trend will be reversed. Brands like Hugo Boss, however, will have to work harder for future gains in China, says Aaron Fischer, a Hong Kong-based analyst at CLSA, an investment bank. “Rivalries will intensify,” he told *The Wall Street Journal*. ■



The global luxury market is dependent on China’s market, but China’s market is dependent on its second- and third-tier cities

Zhou Ting, director of the Fortune Character China Institute

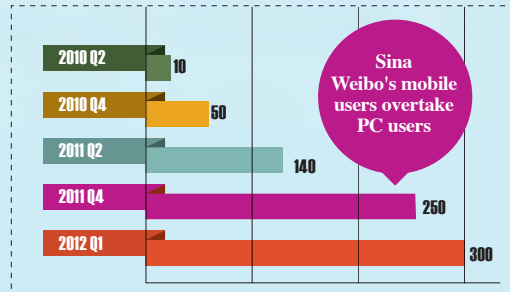
and savvy. CKGSB Assistant Professor of Marketing, Zhang Kaifu, identifies what he sees as three types of Chinese luxury consumers. Top of the pecking order are the first-tier city consumers who increasingly buy abroad, followed by purchasers of products sold in China through official channels, increasingly in second- and third-tier cities. A third type of buyer purchases counterfeit items.

“The counterfeits market used to be huge... and remains a big threat,” says Zhang. “But now the consumers in second-tier cities are shifting from buying counterfeits to buying the real thing... I think they are all advancing one tier above what they used to purchase.” In June this year, Hermès CEO Patrick Thomas told *Women’s Wear Daily*



**Tweet.  
Retweet.  
Follow.**

The biggest and most influential Chinese social media products that should be on your radar



Source: Sina's Weibo division, financial reports Unit: Million

Founding Year

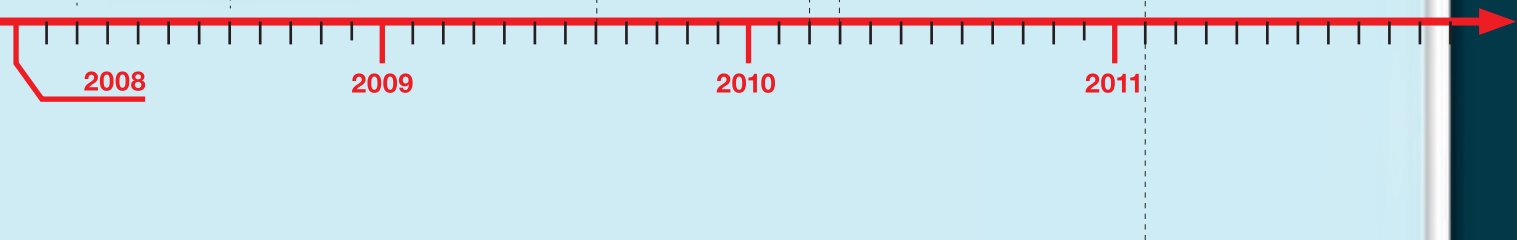


Figures in the bubbles represents the current number of users of top social media sites



### The Weibo Fad

Weibo, the 140-character microblogging service, is evolving far beyond the original Twitter concept to dominate the SNS (social networking service) space in China. As the first to enter the game, Sina got a headstart on Tencent and other heavyweight players such as Sohu and Netease. Sina leverages its media resources and links up with celebrities to give ordinary users a chance to interact with stars. The total number of registered accounts on Sina Weibo was over 320 million at the end of March 2012.



### The Mobile Boom

WeChat, a voice, video and photo messaging application launched by Chinese internet giant Tencent last year, has a cool, sleek interface. As Tencent's youngest SNS product, WeChat was a born star. It garnered 100 million users in just under 15 months. It gives Tencent access to high-end users, something that the company found elusive in its previous offerings, QQ and Qzone, which urbanites considered unsophisticated.

- instant messaging
- group messaging
- image sharing
- voice messaging
- location sharing
- video calling

Source: Data compiled from the most recent company reports



# It Could Energize the Faltering Economy

By Yu Miaojie

China's 2008 economic stimulus has led to concerns that if another such package were to be introduced today, it would lead to similar problems of overinvestment, overcapacity, increased social inequality and rising local debts. I, however, feel that these fears are misplaced. Since 2008, the Chinese economy has recovered relatively well.

We cannot know how much worse the economy would have fared had we not implemented a stimulus. We need a new government investment in targeted, specific industries to combat the low gross domestic product (GDP) growth rate and rising unemployment.

China's GDP grew at a rate of 7.6% in the second quarter of 2012, a clear slowdown compared to 9.5% in the same period in 2011. This is not a healthy sign if we have to maintain the country's macro-level economic growth.

In order to maintain an 8% GDP growth rate, China's total factor productivity (TFP) needs to be at least 7%. The TFP—an index for measuring the production efficiency of companies—provides the micro-level growth that ensures China's macro-level economic growth.

If there is no new stimulus package, with current levels of export to be maintained for the second half of 2012, China's GDP growth rate could fall to 7% or lower. In turn, this could lead to a high unemployment rate and a dissatisfied populace.

A new stimulus package should focus on how to increase the overall wealth and improve the living standards of all Chinese citizens. As China makes the move from exporting labor-intensive products to high-value-added products, the government should support companies' research and development costs to increase their global competitiveness.

Specifically, a new government stimulus should target three areas: farm irrigation facilities to benefit farmers and thereby the



whole country; upgrade emerging industries such as LED and solar industries; and lastly, highway and railway infrastructure. The last area, although controversial, could help make inroads into underdeveloped central and western China, where products can then be shipped.

Increasing exports to emerging economies, like Brazil and Indonesia, could help China's growth in the long-term if other global economic conditions are met. But for now, we need a clear strategy for the short-term.

I favor government investment over private investment, as any increase in private investments will not be effective to spur economic activity. In addition, a tax reduction or any business tax will not help the companies that are still not profiting.

Some argue that a new stimulus package will add overcapacity, increase production and stimulate corruption, as evidenced by the cement and steel industries overproduction from 2008. With a new stimulus, the government can initiate infrastructure projects to put this cement and steel overstock

into use, and no longer approve more projects in the over-stocked sectors.

Some also point to the problem of rising local debt to argue against a new stimulus. I think that a stimulus of RMB 500 billion or RMB 1 trillion should come from the central government (whereas in 2008 half of the stimulus came from the central government and the other half from local governments). If you do a global comparison, China's government debt ratio is among the lowest, at less than 50%, so central fiscal revenue should be sufficient to support these investments.

While the government has been promoting mass consumption for the past two years, the expectation is premature because we still face the problems of a developing country, including limited access to quality education, medical care and housing for common citizens.

When we compare China's 2011 GDP per capita of \$5,500 to the US GDP per capita of \$40,000-50,000, we see why ordinary Chinese citizens would rather save than spend. If an average farmer's monthly income is RMB 1,000, when given an extra RMB 100, consumption will not be his first goal. Targeting the middle class or the top 25% earners of the population is more effective. In addition, when China's GDP per capita surpasses RMB 10,000, consumption will rise naturally.

Focusing on exports and consumption will not help the Chinese economy in the short-term. Perhaps with a new government stimulus package, next year China will recover as an export-driven economy. After three to five years with steady GDP increases, the per capita income could reach \$10,000, and only then will consumption drive the economy.

Yu Miaojie is Associate Professor at the National School of Development at Peking University and Advisor to Ministry of Finance.



## warrant another stimulus package?

# Some Pain is Necessary in the Short Run

By Li Wei



The slow recovery of the US economy and the deep recession in the Eurozone have cast a long shadow on the global economy. Given the strong headwinds faced by China's exporters and the weak domestic demand, many have advocated another stimulus package to arrest the impending economic slowdown. I am against any stimulus package that does not include much-needed structural adjustments.

After more than 30 years of breakneck growth, the Chinese economy is experiencing growing pains. Although the current downturn is triggered mainly by economic weaknesses in China's trading partners, China cannot maintain its high growth rate by relying on ever-increasing investment and export demand. Currency appreciation and higher inflation at home has significantly eroded the price competitiveness of Chinese exports. The high investment rate is unsustainable in the long run. China's existing growth model may have reached its natural limits. Without making meaningful structural adjustments, an economic slowdown is inevitable. The global economic downturn may be the trigger, but should not be seen as a structural cause of China's economic slowdown. To continue to raise productivity and to increase gainful employment opportunities, China needs to reengage in structural reforms that enlarge the role of the private sector and competitive markets.

An economic stimulus that focuses mainly on investment will likely be ineffective, if not wasteful. China's infrastructure, especially in urban areas, already rivals that of some developed countries in multiple dimensions. And there are already signs of excess capacity in many key industrial sectors, such as steel, cement, solar panels and heavy equipment.

If a stimulus such as the 2008 RMB 4 trillion-package focuses once again on investment, the gross domestic product (GDP) will rise in the short run. But without strong effective demand both at home and abroad, it will worsen the existing structural problems by stockpiling more inventories and expanding industrial capacity. With nearly 50% of



China's GDP going towards investment in the last 10 years, we have to ask whether we can expect to earn the required socioeconomic returns from yet more investment directed by the government. A possible silver lining is that employment would increase, but that too, would likely be unsustainable.

China should instead focus on reengaging in structural reforms: enlarge the role of the private sector, expand the role of competitive markets, and offer structural tax cuts to raise disposable income and to lower the tax burdens on consumers and producers. It is good to note that the government has rolled out some such reforms and is expected to do more.

In 2008, the Chinese economy was undergoing policy-induced adjustments. The onset of the global recession in the last quarter of 2008 further exposed many structural problems that China faced. For example, many firms and individuals that borrowed short-term funds to invest in longer term projects or to speculate in the housing market faced the risk of

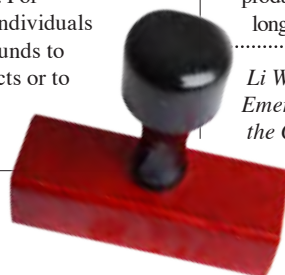
bankruptcy when market liquidity dried up and they found it difficult to refinance. The 2008 stimulus rescued many of them. This cannot be a viable policy in the long term. By providing a safety net for risk-taking firms and individuals, we encourage them to take more risk than is socially optimal. We should encourage market competition by embracing the disciplinary functions of markets.

The economy is like an only child being raised by overprotective parents. Shielding the child from the stumbles and scrapes of everyday activities does not make him stronger. Rather it robs the child of his chance to learn from his own mistakes when most of his mistakes are rather harmless. Would we expect such a child to make good judgments later in life?

To avoid the middle-income trap and to restore high and balanced growth, we need to implement structural reforms sooner. The moment of reckoning is now and we should seize it. It is better to experience a growth rate of 5% and start the process of structural adjustment now than to delay it and face a truly hard landing in the future with potentially negative growth and longer lasting recessions.

China has transitioned from a poor economy barely able to feed its population to a relatively prosperous middle-income nation in just 34 years. This transformation is a testament to the ingenuity of the Chinese policymakers in reforming economic institutions that allowed entrepreneurship to flourish and encouraged families to better the next generations by investing in education and market-oriented skills. For China to graduate from the middle-income class, further economic liberalization will be necessary to create a level-playing field for individuals and firms to compete both domestically and globally. Only through this new round of institutional reforms can China see sustainable rising wages and productivity—and steady, balanced growth in the long run.

*Li Wei is Professor of Economics and Emerging Markets Finance and Director of the Case Center at CKGSB.*



# Taking the Hard Road

BYD is finding it tough to  
shift gears from imitation  
to innovation

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By Bradley Gardner





It used to take a cheeky sense of pride in copying, then beating much bigger rivals. Low costs and imitation made BYD one of China's top five carmakers in an incredibly short space of time, even inviting a high-profile \$232-million investment from Warren Buffett. Since its attempt to move up the value chain, however, the Shenzhen-based automaker, noted for its *'shanzhai'* or copycat versions of better-known marques, has been having a rough time.

First applied to cheap imitations of brand name cell phones produced in southern China, the term *'shanzhai'* has now come to denote an inexpensive—and often poor quality—copy. BYD's efforts to drop the *shanzhai* label lay in tatters after a fatal accident in Shenzhen in May this year which saw a BYD E6 go up in flames after colliding with a Nissan sports car. The explosion of the E6 was particularly bad news given that it was BYD's flagship car in the electric vehicle market.

BYD once promoted itself as a global leader in e-vehicle technology and only three years ago made claims that it would be the biggest car company in the world by 2025. Company exports chief, Henry Li, was quoted earlier this year as saying BYD's electric vehicle platform is "one of the most advanced in the world". Despite this, the firm is now struggling to compete with other domestic Chinese car companies, let alone the international car brands it would face in developed markets.

BYD's stock price has dropped 80% from its 2009 high, and 40% since April 2012, while the commercial release of its electric cars has been pushed further down the road.

## Shifting Up a Gear

BYD's problems are in many ways linked to its efforts to move upmarket, from imitation to innovation and higher-margin vehicles. Like many other Chinese low-end manufacturers, BYD has responded to rapidly rising costs by trying to develop a respected brand which will allow the firm to expand its margins, and market share. "You have to acquire capabilities to differentiate your brand, otherwise you're going to be fighting a commodity battle at a low price point," argues Bill Russo, Senior Advisor at Booz & Co, a management consulting firm. "Chinese car companies are in a war of attrition and only the strong will survive."

BYD began its operations in Shenzhen, producing cell phone batteries at 30% of the cost of competitors like Sony and Sanyo. Like many *shanzhai* operators, BYD at first largely eschewed machines in favor of an army of workers: as of 2011, the company had 178,000 employees in both its automotive and battery businesses. Ford



In what has been reported as "China's first fatal crash involving a pure-electric car", two passengers in a BYD E6 taxicab and the driver were killed in Shenzhen on May 26 after being rammed by a Nissan sports car at high speed

Motor Company, by contrast, had 164,000 employees globally achieving five times the auto sales recorded by BYD.

Controversially, in its earlier years BYD was known for reverse engineering everything its competitors made, in an effort to learn the technology and see if they could figure out how to do the same thing cheaper. BYD's bestselling car, the F3, is similar enough to the Toyota Corolla that it can use parts for the latter but sells at half the price. "A core competency of BYD is that they are more willing and more aggressive in copycatting some of the bestselling models globally," says Teng Bingsheng, Associate Dean and Associate Professor of Strategic Management at CKGSB. "You can call it a core competency because they have been very good at it."

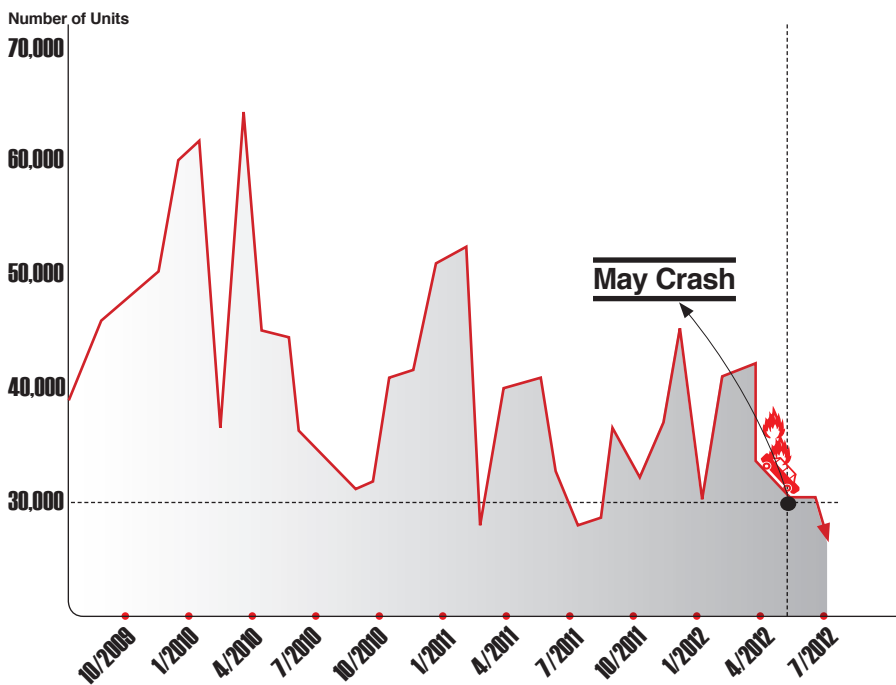
BYD didn't, however, necessarily eat into the market share of the Toyotas it copied. BYD cars may look like Toyotas but on the road the F3 doesn't match the performance of the car it imitates. "An automobile has some of the most complex engineering of any consumer product," says Russo. "You can copy the hardware, but not the soft stuff. Two cars with the exact

same hardware can perform completely differently on the road."

Russo argues that this is why Toyota, unlike BYD's competitors in the battery industry, has not bothered to take legal action against the company. Learning from imitating your competitors is something done everywhere, particularly as countries develop their markets. But there it doesn't have to be a negative for the company being copied. "In China, people buying Toyota Camrys are not cross-shopping with the F6 [another BYD imitation]," says Russo "There is some gray area here. It isn't necessarily hurting the companies who are having their goods copied and it could improve their brand."

## Shanzhai Successes

BYD's *shanzhai*-style imitations of Toyota didn't take the company beyond the cut-throat, low-price segment of China's auto market. There are, however, solid examples of *shanzhai* players taking market share from competitors they've copied, particularly in the handset market where *shanzhai*-style upstarts make phones for a low-income but trend-savvy market. Among the most notorious examples, the Shenzhen-manufactured



## Collision Course

BYD China Auto Sales 2009-2012

Source: Bloomberg Market Data

GooApple handset looks uncannily like the iPhone 4 but runs on the Android 2.2 system, and retails at RMB 1,060 compared to the RMB 4,000-price tag of the iPhone 4.

Navigating its way upmarket out of the *shanzhai* space, phone maker Tianyu started out making cheap knockoffs of trendy handsets but has since invested heavily in 3G products. Tianyu's cheap-chic approach helped it leapfrog Lenovo and nip at the heels of leading players like Nokia and Samsung in terms of handset sales. Selling under the K-Touch brand name, Tianyu showed its intent for export sales when it showed its Android handset at this year's Mobile World Congress, "Today, Tianyu is a mainstream player virtually unrecognizable from its *shanzhai* beginning thanks largely to increased efforts in R&D and brand building," says a Booz and Co. 2009 report titled '*Shanzhai* a Chinese Phenomenon'.

Other winners in the *shanzhai* economy include QQ, originally a *shanzhai* version of ICQ, which now commands 75% of China's online instant-messaging market according to data for 2011 published by iResearch, a consultancy. Future Cola meanwhile has gone from copying Pepsi and Coca Cola (whose red-white packaging livery it most resembles) to become the third-largest player in the local carbonated soft drinks market, just behind Pepsi,



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according to 2011 data published by Euromonitor International.

### A More Orthodox Approach

Forced by competition and rising costs to target higher-value and global markets, BYD has had to change the design of a number of its cars, including the F3, in order to avoid lawsuits overseas. "We are working to develop a unique brand identity as we grow to meet our customers' demands," says Sherry Li, a representative for the company. "We are very proud of our design evolutions." But with the design changes, BYD lost market share and the F3 is now the 24th best seller in China, down from first a few years earlier. In the first six months of 2012, sales of the F3 dropped 40%, a sales decline larger than any other car in the top 50.

BYD may have to wait some time to regain sales momentum as it moves from the *shanzhai* model in search of higher margins. BYD is following much the same path taken by another privately owned Chinese carmaker Geely (lambasted by the global auto press for its Geely GE, a brazen imitation of Rolls Royce's iconic Phantom, among others), which has looked to foreign companies to bring in expertise. In 2007, the company opened a joint venture with Manganese Bronze Holdings, which manufactures London black taxis. The joint venture led to the development of the Englon, Geely's mid-range model, and the company is in talks with the UK government to electrify the London taxi fleet. In 2009, Geely acquired Drivetrain Systems International, a global transmission developer, and finally in 2010, bought the Volvo brand from Ford, bringing access to global markets with it.

By slowly building capacity and know-how, Geely has been able to gain high-value and high-margin customers. "It took the better part of 10 years to get where they are today, but it is paying off in terms of how their brands are performing," says Russo.

BYD is slowly coming around to the same approach, in part by entering into a 50:50 partnership with Daimler-Mercedes. The partnership is mostly focused on electric vehicles, but according to BYD spokesperson Li, it is affecting other parts of the business as well. "BYD's partnership with Daimler-Mercedes relocated over 100 engineers and quality professionals to BYD headquarters," she says. "We have acknowledged many improvements in our design and production processes with the help of our partners." Experts feel that more such partnerships will be the only way that BYD can catch up to its competitors.

"BYD [needs] partnerships so they can be technologically competitive," says CKGSB's





Spot the difference: BYD has been accused of modeling their vehicles too closely on foreign cars, such as the BYD L3, which is similar to Toyota's Corolla

Teng. "State-owned car companies have been doing this for 30 years, so they have an advantage in the mid- and high-level [market]. But even in the lower-end, companies are finding they need competitive advantages."

The company is no longer claiming it will reach market-leading status in the next decade, but rather it is reaching "foreign-OEM [original equipment manufacturer] brand quality", according to Li. In other words, they are catching up with two of China's 'Big Four' automakers, SAIC and FAW, and are still a long way off from the Japanese, Korean and American brands the firm once gleefully imitated.

This new modesty has turned into concrete business development. The company is developing its own drivetrain system, as well as mechanizing much of its production line, which, according to Chinese media reports, previously had error rates of 20-30%.

## Electric Options

Unlike many other brands with a *shanzhai* past, BYD has an ace to play if it can retain a reputation for innovation in electric vehicles. BYD is a household name now, both within and outside of China, and much of that has to do with their electric vehicle business, even though it's not been doing very well. "The company barely sells any electric vehicles, but it gives their company the aura of a high-tech company," says Han Xiong, automotive editor at the Guangzhou-based *Yangcheng Evening News* and a popular blogger on China's auto market.

This strong brand is an incredibly valuable asset to BYD. "Chinese companies need to develop capacities that improve the image of their brand," says Russo. "The worst thing is to have technology that you can't

price." But BYD "over-promised and under-delivered", he adds.

Having come up with the concept for the world's first mass-produced, plug-in hybrid vehicle (three years before the GM Volt), the F3DM—BYD's fully electric car—came out in China two years behind schedule, and it is still facing delays with its planned US release. The company and analysts are in disagreement as to how much of the delay was due to a shortage of related infrastructure, versus deficiencies in the engineering, and safety concerns.

Industry analysts were bullish about BYD because of its background in battery making, giving it a possible edge in the electric car business. In 2008 Warren Buffett took a 10% stake in BYD for \$230 million, praising the firm's battery technology and its role as a leading player in electric vehicles.

Proving a reputation for innovation may restore BYD's fortunes. In the meantime, other one-time *shanzhai* operators may also be making the move from imitation to innovation. Booz and Co.'s '2012 China Innovation Survey: Innovation—China's Next Advantage?' shows that 45% of multinationals active in five sectors in China reported that Chinese peers were equally or more innovative than themselves. Chinese firms (38% compared to 30% of MNCs) are "need-seekers"—firms that research their customers' needs and design products accordingly. While 53% of Chinese firms said they're collaborating with foreign partners on R&D, another 40% said they're pursuing their own R&D.

By tailoring products quickly to local needs and pockets—and then investing in R&D and marketing—the *shanzhai* path pursued by Tianyu and BYD is largely similar. However the future of that model is now uncertain as government leans on

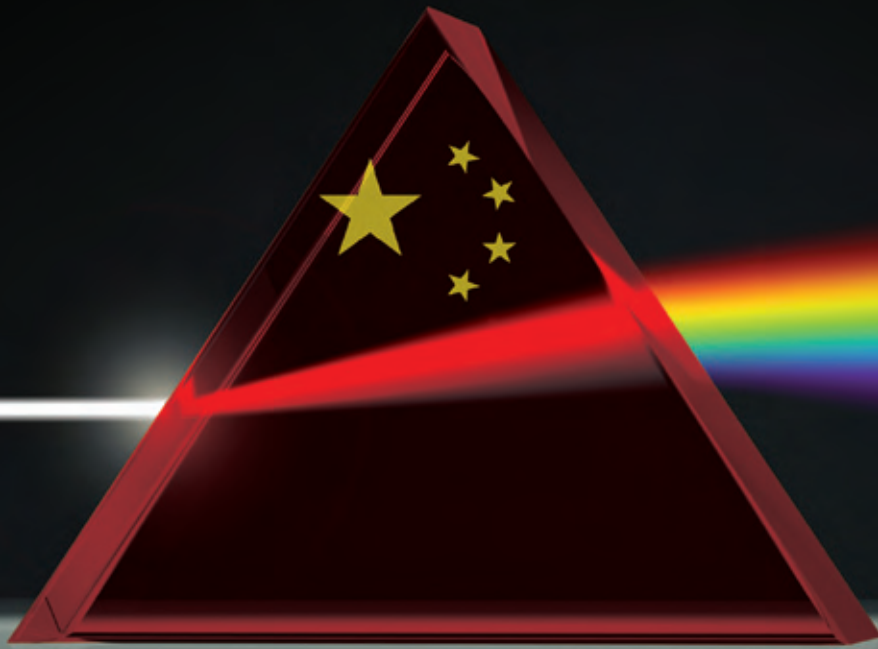
IPR infringers, through more aggressive prosecution of offenders, to encourage innovation. Competition in the domestic market and ambitions to export will force more Chinese manufacturers to make a choice similar to the one faced by BYD and Tianyu.

Nonetheless, there will be space for low-cost imitators in China's vast lower-income markets. While labor costs have risen, the key factor in the success of the *shanzhai* model—China's manufacturing capacity—remains intact. *Shanzhai* handset makers, for instance, are still churning out new models in Shenzhen, leveraging an ecosystem of 30,000 highly specialized companies which collaborate across the entire mobile phone value chain from design to sourcing, production and distribution.

Facing possibly the toughest period in its short history, BYD has a chance to redeem itself and emerge as a serious global player, if it can prove its abilities to innovate in electric vehicles. That will be difficult. Russo warns that, if anything, Chinese companies are at a disadvantage to foreign companies when developing electric vehicles because they lack the deep engineering experience that comes with decades in the business. "Whether or not BYD can develop feasible battery technology, that is the most critical issue here," say Teng. "So far it has been much more difficult than expected."

*Shanzhai* companies have boomed in China on the back of innovative cost-cutting and aggressive business models, but there is still a substantial need for outside experience for companies wanting to go global. Copying can bring you to the technological frontier, but pushing past it requires hard-won experience. It's the sort of thing BYD needs a lot of, fast. ■

# IMITATION.





# INNOVATION.

Three erstwhile copycats innovate through trial and error, to fight the fierce war over the online classifieds market

By Yan Ruiying and Wang Fanfan

A few years back Ren Jinglei, a university student interning at an IT company in Beijing, decided to buy a bicycle to ease his commute to the office. Like an increasing number of Chinese people, Ren prefers to do his shopping online and he promptly turned to the internet for help.

However, this time around the problem was a wee bit pricklier than usual: Ren wanted a second-hand bike—compared to a new bike, the odds of someone stealing it were low. But all the e-commerce sites like Taobao, Dangdang and 360buy.com deal with new products. “Taobao is great for shopping, but it doesn’t have second-hand options,” says Ren. “I figured that some other site must have them.” So Ren did the next best thing, and entered his query in Baidu, the most popular search engine in China.

The Baidu search results pointed him to Ganji.com, a site that markets itself with the slogan: “Ganji, we have everything.” It was smooth sailing from there on. Ren zeroed in on advertisements for second-hand bicycles available in Chaoyang District, where he worked—it would be easier to collect it from somewhere close to his office. When he finally found what he was looking for, he set up a meeting time with the owner. The next day Ren simply walked to a subway station near his office, handed over RMB 320 to the owner and got his bike.

Ganji, as its slogan claims, *has everything*—if you are looking for a second-hand bike like Ren, the site will help you find one. If you are looking for an apartment to rent in a specific part of town, it will give you enough options to choose from. And if you want a boyfriend for that matter, Ganji will rustle up a list of potential beaus in a matter of seconds.

Ganji is the brainchild of 38-year-old Yang Haoyong, one of the many young entrepreneurs behind the vibrant start-up scene in Beijing’s Haidian district. After studying computer science at Yale University in the early 2000s, Yang moved to San Francisco and worked in technology companies such as Juniper Networks and co-founded Triomphe Networks. It was then that he became a big fan of Craigslist.org, a hugely popular classified advertising website in North America.

Craigslist, founded by San Francisco-based computer programmer Craig Newmark in 1995, is a trailblazer of sorts. While it started out as a listing service for Newmark’s friends (hence the curious name), Craigslist has grown to become the ninth-most trafficked site in the US, according to web information company Alexa.com. It allows users to advertise online for sales, services, housing and jobs, among other things. Despite its popularity (it attracts 50 million users in

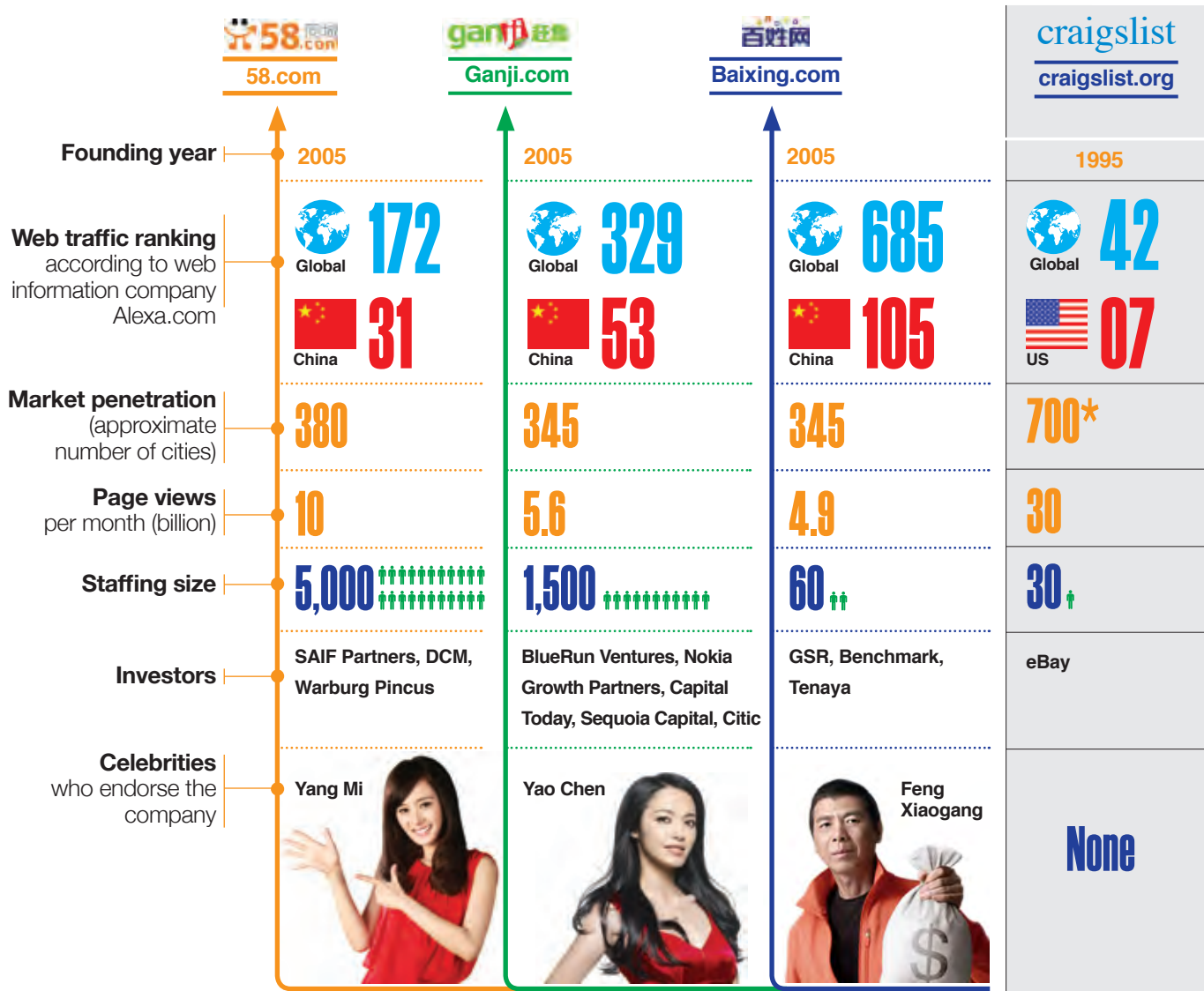
the US alone and 30 billion page views per month), the site doggedly sticks to its original simple formatting and eschews advertisements. Craigslist’s killer app? The fact that users across the 700-odd cities (US and elsewhere) it operates in can advertise for free. There are a few exceptions though—such as job advertisements in 18 US cities (at a nominal \$25 per listing, except for San Francisco where it is \$75), and apartment classifieds in New York (\$10 per ad).

Time went by, and Silicon Valley’s infectious entrepreneurial energy rubbed off on Yang. As he toyed with possible start-up ideas, he thought of replicating the idea of Craigslist in China. So in 2005, Yang packed his bags and headed home. He borrowed \$100,000 from his friends and set up Ganji.com.

At first, Ganji was simply what it set out to be—a Craigslist copycat. And the opportunity was huge too—the number of internet users in China was exploding. But Yang was not the only one to set sights on the opportunity—while no one has the exact number, it is rumored that in 2005, 2,000-3,000 Craigslist wannabes sprouted all across China in just three months. What would have been an empty space, was crowded from the first day on. And even though the size of the pie was growing, the number of companies that wanted to have a share of that pie was huge.

Yang’s fledgling company had to deal with competition from similar start-ups such as Zhantai and Renren, and also from the Big Boys of Chinese Internet—Sina, Sohu, Netease and Tencent—all of which launched their own versions of web classified sites. Competition was brutal. “The first two to three years were not about the business model or how big you can be, but about survival—and differentiation,” says Yang. To cut through the clutter, Ganji had to ensure that it was strategically focused on a few segments. “We chose to focus on one city (Beijing) and just two categories—‘housing’ and ‘for sale,’” says Yang. The idea was simple: gain some experience in these categories, learn and then expand to other cities.

At the heart of Yang’s strategy is a careful segmentation of customers, and his value proposition of “local” and “life-related”. He segments potential customers for internet businesses into four categories: brand name customers which sit “at the top of the food chain” (like Coca-Cola and Nike), small-to-medium businesses (with 50-100 employees and typically customers of sites like Alibaba and Baidu), local small businesses (with 1-5 employees) and virtual goods companies. Ganji is strictly targeting the local small business segment. “They are flower stores, moving companies, laundries, housekeeping services, babysitters



## How They Stack Up

Data compiled from the company websites, Alexa.com, iResearch and interviews

\*The number of Craigslist's sites worldwide

and plumbers—their service range is within 1-2 miles... and everybody uses that kind of service every day,” says Yang. “They account for the biggest segment in China—probably 10 million or so.”

Seven years have gone by, and the web classifieds industry has witnessed a shakeout. The 2,000-odd websites have been whittled down to only a handful. Data from iResearch, a Chinese internet research company, shows that as of August 2012, only 26 classified websites were still active. Those that fell by the wayside include, somewhat surprisingly, high-flying serial entrepreneur Joseph Chen’s Renren (after the company went bust in 2007, Chen used the domain for the popular social networking service Renren.com). Tencent pulled the plug on its classified section. Some sites were acquired by bigger players—such as 263.com, a subsidiary of the internet company 263 Network Communication Co., which was snapped up by Ganji in 2011.

The biggest lesson from the shakeout was that a pure copy of Craigslist will just not work in China. A case in point is Zhantai, a once popular classified site that is almost defunct now. Zhantai had hoped to emulate Craigslist with an easy-to-use, advertisement-free classified

website. It also shared many of Craigslist’s altruistic goals. When Craigslist was created, it had no competition and was able to slowly build its indispensable status. Zhantai, on the other hand, faced deep-pocketed competition that used advertisements to siphon off users. According to iResearch, Zhantai is now operating with a skeleton staff and unstable servers.

Of the few survivors, 58.com, Baixing, and Yang’s Ganji lead the pack—and are growing at a frantic pace. Market leader 58.com has monthly page views of 10 billion, followed by Ganji’s 5.6 billion and Baixing’s 4.9 billion. All three are miles ahead of eDeng, number four in the pecking order, which has only 0.7 billion monthly page views. (In contrast, Craigslist, which has been around much longer, claims to get 30 billion page views per month.) iResearch’s most recent data also shows that 58.com’s average daily visits are 5.71 million, almost half of the total 12.7 million visits to classified websites, while Ganji has 3.86 million and Baixing has 3.21 million (see ‘How They Stack Up’). While 58.com covers about 380 cities, Ganji and Baixing each has about 345. According to a Deloitte ranking and CEO survey, ‘2011 Deloitte



Technology Fast 50 China', Ganji witnessed a revenue growth of 2,186% in the three years ending 2011 and ranked fourth among the fastest growing companies in China.

The sector has been attracting significant funding as well. In 2009, Ganji acquired four rounds of funding and has already accumulated a total investment of "more than \$100 million" from investors such as BlueRun Ventures, Sequoia Capital, Capital Today, Citic, Nokia Growth Partners and a "very big private equity investor" they haven't announced yet. The company hopes to break even by the end of this year. 58.com, on the other hand, received \$85-million funding from Softbank Asia Infrastructure Fund Partners, DCM and Warburg Pincus. *TechWeb* reported that CEO Yao Jinbo invested \$5 million from his own pocket following Warburg Pincus' \$60 million Round C investment. Although Yao declines to comment on it, unconfirmed reports say that 58.com is now planning an IPO on the Nasdaq.

The sector can only grow further. According to a May 2012 report by internet research company iResearch, there are currently more than 143 million Chinese classified website users—a number that is increasing every year.

## Not a Copycat Anymore

Clearly, these companies have come a long way from the crazy days of 2005, when everyone jumped into the game armed with just two things: a cookie-cutter approach, and the aim to be China's Craigslist. But climbing up the growth curve hasn't been all that easy. Newmark created Craigslist in the internet's fledgling days and helped shape people's relationships with the internet.

Chinese classified sites, on the other hand, entered a mature market where users were already familiar with the internet, and somewhat set in their ways. At this stage, the crucial battle was to attract users. Which is why, Ganji, as mentioned earlier, initially chose to focus its energies on just one city and two categories, learn, and then expand into other cities and categories. They made some mistakes along the way—such as a botched attempt at getting into the group buying segment—but learned from the experience, and moved on.

Baixing has been trying to position itself as "a local community" where users can share and get different information in order to make their lives easier. As CEO Wang Jianshuo puts it, "There's an awful lot of people out there who want to buy things, and many more who want to sell things. Linking them could change their lives for the better." As for 58.com, they have decided to focus on housing, recruiting and dating services.

Even though these sites began as copycats of Craigslist, over time they have acquired nuances of their own that distinguish them from their original inspiration. Take for instance, Craigslist's policy to shun advertisements. Chinese classified sites, on the other hand, rely heavily on advertising for revenue. Advertising revenue comes from third-party ads, and commission and advertising from property agencies with adverts for consumer goods a second source of cash.

Ganji's Yang takes his inspiration from the concept of "freemium", a business model in which services are provided free, but users need to pay for additional features and functionality. Globally many products and services—such as file-sharing service Dropbox and note-taking and archiving software Evernote—are based on the freemium model. "For



Chinese classified sites entered a mature market where users were already familiar with the internet, and somewhat set in their ways. At this stage, the crucial battle was to attract users

housing agents, moving companies, house-cleaning, the post is free but if you want better performance and better results, you pay," says Yang. He adds that paid services account for less than 20% of their daily traffic.

## Playing Matchmaker

Craigslist operates with a skeletal staff of 30-odd people—and it has always been this way. That's because the majority of Craigslist's transactions are user-to-user—interactions where individual users create listings for other individual users, without any intervention from Craigslist. The Chinese sites, on the other hand, are keen to play matchmaker.

Both Ganji and 58.com (Baixing is an exception) employ an army of sales and customer service staff. Out of Ganji's total 1,500 employees, 1,000-odd are sales personnel. Interestingly, many of Ganji's sales people used to work for the newspaper classified business. "They already had (clients)," says CEO Yang. "We simply hired them and made them try a new medium." While 58.com CEO, Yao Jinbo, refuses to disclose the exact numbers, out of the nearly 6,000 employees on its payroll, the company reportedly has 5,000 sales people.

Ganji and 58.com are moving towards interactions where they help match businesses with local buyers. 58.com's salespeople help connect the site's users with merchants, a process that happens naturally on Craigslist. "The US is a service environment based on individuals," says 58.com's Yao. "But in China, the service environment is based on third parties—we provide a platform for small and medium local businesses. This is unique to China."

But there's also another reason why Chinese classified advertisement sites have so many employees. While Craigslist relies on its users to police themselves and administrators eventually step in to remove any listings that are flagged as inappropriate by users, both 58.com and Ganji employees scrutinize listings and ensure that they are indeed legitimate. Ganji employs editors who organize listings into specific categories and weed out fakes. (Baixing's system to control fake information is much like Craigslist's.)

## New Revenue Opportunities

While classified advertising continues to be the mainstay for these sites, they have forayed into adjacent spaces as well. Ganji, for instance, experimented with group buying (and burned its fingers because "competition was way too fierce") and a short-term apartment rental channel, akin to Airbnb in the US. Through a sister site, mayi.com, Ganji offers options to people planning to stay in a city for more than three days. "By developing a forum to match landlords with potential tenants, Ganji hopes to target a more diverse client base and offer prices cheaper than hotels are able to," explains Yang.

There are other revenue streams as well. Globally large-scale recruitment does not fall within the domain of classified advertising. In 2008, 58.com launched an experiment in this area—it signed a deal with Wal-Mart in which the retail giant agreed to hire 3,000 people per year via 58.com.

Another innovation in the Chinese classified websites market is the introduction of mobile phone apps. Yao says his firm has considered mobile as "one of our main focus areas". From using mobile internet for news and entertainment, people are now also using their phones for shopping and other aspects of daily living. Qi Jianzhe, senior



A Baixing.com ad declares, "Just sell the stuff you don't need!"

analyst at Analysys International, says that while mobile phone apps offer room for growth, they don't deal with a key obstacle: a lack of accurate information. "The success of a mobile terminal depends on whether it can provide accurate information because the main feature of mobile applications is to provide the user with useful information from nearby," Qi says. Let us suppose that a user is looking for an apartment within a one mile radius and his mobile app throws up an option. However, he later discovers that the apartment is actually three miles away and this sours his experience. To compete in this market, user experience is the decisive factor.

### From Craigslist to Taobao?

In early July 58.com CEO Yao Jinbo appeared on the reality TV recruiting program *Fei Ni Mo Shu* (loosely translated as "No One Else But You") and offered a salary of RMB 400,000 plus stock options to hire a promising young e-commerce expert who had racked up sales of RMB 1.5 billion on a Taobao store. That set tongues wagging. "This is an obvious hint of 58.com's plan of turning into an e-commerce platform," says Huang Yuanpu, an analyst from iResearch.

Experts like Huang see classifieds sites gradually encroaching into the territory of e-commerce platforms, Taobao and Alibaba. 58.com's Yao agrees, saying that his site is already offering e-commerce in local services, but with a twist. "This is totally different from Taobao because they are into e-commerce of products. Our plan is to become powerful allies for local life for our users by helping them to get the information and save money," he says. "We are changing from a pure information service platform to a platform for publishers, merchants and users." Local business owners can continue to post product or service information on 58.com and make the transactions offline, or they can pay several thousands of RMB each year to have an online store on *Wang Lin Tong* (loosely translated as 'internet communication for neighbors'), a corporate platform that 58.com created for its VIP customers to promote business. In the meantime, Yao is preparing to launch an online transaction platform similar to

PayPal and Alibaba's Alipay.

Huang doesn't think that foraying into e-commerce is such a great idea. "For the classified ad websites, the expense is several times the revenue. Thus, each player faces the pressure of monetization. E-commerce is a hopeless choice, because the competition in this area is already very fierce," he says.

### In for the Long Haul?

Anyone who rides the Beijing subway regularly or watches national television has probably seen—or heard—the advertisement for Ganji starring actress Yao Chen. She rides an animated donkey and yells, "Ganji la!" ("Let's go to the market!"). Subway riders will also be familiar with another commercial in which TV actress Yang Mi shouts, "Wu Ba, tong cheng!" ("58, we are in the same city!"). In the battle for users, Ganji and 58.com have each been splurging money left, right and center on staff and marketing.

Chinese media has reported that 58.com and Ganji have each spent RMB 500 million and RMB 400 million respectively on advertising in 2011 alone. This is unsustainable in the long run, as the ad spends are higher than the revenues. *TechWeb* reported that 58.com's total expenditure in 2011 reached \$130 million (RMB 825 million) while it only raked in \$40 million (RMB 254 million) as revenues. iResearch's Huang cautions against this game of outspending competitors to gain market share.

Analysts are also worried about the fact that many sites are still pretty much the same. Analysys International's Qi has studied the strategies of Chinese classified sites. "I am not optimistic about the future of classified websites," he says, "because I have not seen a breakthrough in the profit model of any classified websites." He believes websites which focus on niches have a greater chance of succeeding. In each category, Ganji and 58.com will inevitably face competition from specialized players, such as dating website baihe.com or recruitment site 51job.com.

Willingness to pay for ads continues to be a concern. "From our survey, less than 10% of users are willing to pay for the information they get from the classified sites," says iResearch's Huang. "Chinese consumers still haven't developed the habit of paying for information they get online." Also since these sites mainly target low-end users, their propensity to pay for advertising is low and it's hard for the sites to monetize their traffic.

While new revenue models for China's classified sites are as yet unproven, what is certain is that in the future, China's classified websites will continue to plow a different path from Craigslist. Craigslist fan and Ganji boss Yang believes the website's fate is in the hands of hard-won users. "Even though you (might be) number one on PC, there might be players on mobile and social platforms which create better user experiences that can beat you," Yang says. "Those are the things we need to think about in future." But he remains optimistic. Ask him about future projections, and pat comes the reply: "We cover 100 million monthly users right now. In three years, we'll cover 200-300 million."



# “Any Time You Don’t Sell, You Buy”

**Billionaire investment czar Sam  
Zell shares his investing secrets**





## Dialogue

*Billionaire property mogul and chairman of Equity Group Investments, Sam Zell, made his first foray into the real estate market while he was still in college. His strategy was simple: buy cheap real estate from distressed owners and sell when the price was high. This tactic paid off and less than two decades later, Zell made his debut on the Forbes 400, a list of the richest Americans. Today his estimated net worth is \$4.9 billion, and he is ranked 68 on Forbes' list of billionaires in the US.*

*Zell's investments range from prime real estate across the US to finance, energy, transportation and communication. Zell is also the chairman of Equity Residential, Equity LifeStyle Properties, Capital Trust, Covanta Holding Corporation, Anixter and the Tribune Company (publisher of the Chicago Tribune and Los Angeles Times). He created three of the largest real estate investment trusts (REITs) in history. Zell is betting big on emerging markets and has been investing in countries like Brazil, China, Egypt and Mexico.*

*In late June, Zell was in Beijing to attend CKGSB's Investment Forum the theme of which was 'Challenging the Odds: Successful Investment in Adverse Markets'. In a lively exchange with Liu Jing, Associate Dean and Professor of Accounting and Finance at CKGSB, Zell shared his investment philosophy. Excerpts from the conversation:*

**Liu Jing:** We are very interested in you both as an investor and also personally. What factors helped you to become today's Sam Zell?

**Sam Zell:** As a starting point, my philosophy is that any time you don't sell, you buy. So if we had chosen not to sell Equity Office [to Blackstone] for \$39 billion, we would be buying Equity Office for \$39 billion. At all times, we are keenly aware of what our exposure is. As a result, we are much more of a Benjamin Graham kind of investor. We are very focused on what the liquidation value is. I think it was Bernard Baruch, a very famous financier in 1920s, who said nobody ever went broke taking a profit. In the same manner, I have never suffered from any transaction turning out to be "too good". The real issue is "what is the downside", and more than anything else, at every point in our process, we address the question of "what is the downside" so that we know the risk we are taking.

In 1993, I bought what at that time was one of the largest department store companies in the US. They had 79 stores in malls around the western part of the US. Before we made the investment, I sent my team out and I said to them, "I want you to liquidate the entire company on paper. I want you to tell [me] what the inventory's worth. I want you to tell [me] what we can get by selling the leases. I want you to tell me all of the elements of value. And then come back to me." They spent three weeks on the road. They came back and said that their liquidation value was worth 80% of what we were paying. What that did for me is it identified the risk. That was that 20%. I could then decide, with that exposure, whether I was getting a sufficient return for the risk undertaken. Interestingly enough, that transaction did not work out well. We suffered through earthquakes, and fires and race riots and all kinds of terrible stuff. We ultimately sold the deal and got out. What did we get out for? Eighty percent. So, although we lost our 20%, the key to the investment from a philosophy point of view

was to quantify the risk in terms of dollars. What percent of the total investment is basically non-risk and where is the exposure? Focusing on that is an incredibly important part of investment discipline.

**LJ:** In terms of career development, what got you to start investing in real estate and distressed assets?

**SZ:** We have been most famous for the ability to see around the corner. It is all about both recognizing change and being able to execute accordingly. There have been many examples in my career where a change occurred and we had the ability to recognize [it] and execute a plan accordingly. In 1995, we invested \$50 million in an over-leveraged radio station company. At that time, under the law, you were only allowed to own 17 stations. A year and a half later the government changed the law and allowed you to own as many stations as you wanted to, but you couldn't own more than a 40% share in any market. I looked at that change in the law and I said, "This is it."



## The Grave Dancer

Sam Zell is a billionaire real estate investor who made his fortune by profiting from distressed real estate assets, earning the epithet of “grave dancer”. He is the chairman of Equity Group Investments, a private, entrepreneurial investment firm he founded 40 years ago. An avid biker, Zell is often seen riding his Ducati and organizes motorbike trips across the world

So I called in the management and said, “I want you to go out and buy every radio station in America that you can, and somehow I will figure out how to finance it.” We went from 17 stations to 234 in two years, and we sold the company to Clear Channel Communications for \$6.4 billion. So again, [this was about] recognizing the opportunity, executing accordingly, and then recognizing when it was time to exit.

**LJ:** Our students have identified the major factors in your investment thinking: value, liquidity and leverage. Do you agree with the assessment?

**SZ:** I think that is one of those least understood issues, and that is you can have all of the assets in the world you want, but if you have no liquidity, it doesn't matter. In 1990, which was one of the toughest [years for] real estate in the US, I was worth well over a billion dollars and I was worried about making payroll on Friday because I had a huge asset collection but insufficient cash flow. The problem with

leverage is that you have to pay it back. An awful lot of people have taken a lot of leverage without focusing on how to pay it back. The biggest measure of success or failure is how entrepreneurs address and deal with leverage. If you are in the real estate business without leverage, that's like being a boxer in the ring without a glove.

**LJ:** Liquidity seems to be quite elusive for a lot of people. How would you judge leverage?

**SZ:** Liquidity has never been more important than it is today. People talk today about the fact that interest rates, and therefore, the cost of capital is very cheap. The truth is that the cost of capital today is very expensive. If you're investment grade, you can get all the money you want at below the inflation rate. If you are non-investment grade, money is very expensive. And yet because we have a significant worldwide shortage of liquidity, the cost of capital, despite the apparent cheapness, is very expensive.

**LJ:** So you are basically referring to the liquidity of risky assets.

**SZ:** I think that very un-risky assets are very over-leveraged. We have office buildings in New York that are no different than single family houses where the debt is significantly higher than the value. And yet the asset itself is terrific. The General Motors building was over-leveraged at one point. It is still probably the best office building in America, but it was over-leveraged. It is not whether it is a risky property or not. It is really a question of: give me the cash flow, tell me what the debt is, tell me where the debt service is, tell me how I am going to pay it off, and then I can deal with the leverage. I do believe that over the next four or five years, we, as a world, have got to de-leverage. It is just too much debt relative to the income flows, particularly in real estate.

**LJ:** But that seems to be more of a problem for the developed market, right? For example, in China the leverage issue is kind of manageable if you use the international standard.

**SZ:** Well, I think the answer is there is different leverage in different places. In Brazil the leverage level is very low, much lower than here. And yet the availability of capital



Liu Jing chats with Sam Zell at the CKGSB Investment Forum in Beijing

in Brazil is much less than it is here. So half the leverage in a scenario where availability of capital is limited is perhaps more difficult than twice the amount of leverage in a different market. That is why in the developed world there is very high leverage. In developing markets there is significantly lower leverage because the flow of capital and availability of capital is diminished and therefore, you have to have even less leverage to operate in that environment.

**LJ:** In 2007 you did two really big deals: the sale of Equity Office and buying the *Chicago Tribune*. Was there some conflict in your thinking, do you think the market was overvalued at that time?

**SZ:** As far as Equity Office was concerned, as with all of our REITs, we did the NAV [net asset value] analysis every 90 days. So every 90 days we had an opinion as to what the asset values of Equity Office were and what the liquidation value was. When Blackstone came along and gave us an offer of \$48.50, our internal NAV was \$41. So from our perspective that was such a premium over what we thought the values were that we had to pay attention. The key to that transaction, and maybe the most difficult negotiation with Blackstone, was over the break-up fee. Blackstone wanted a huge break-up fee to discourage any other players and I wanted no break-up fee. We settled our break-up fee at \$200 million on a \$35 billion transaction. That attracted Vornado Realty Trust which started to come out of the woods and make noise. We went back to Blackstone and got them to increase the price to \$55.50 per share or \$39 billion, and then we increased the break-up fee to \$700 million. The net effect of which was as the price increased, so too did the barrier against anybody else interfering in the transaction.

**LJ:** What about margin of safety? It seems that you are very confident about your own evaluation. But there might be a gray area where you say, "I am not totally sure", right?

**SZ:** I am a lot of things, but "not sure" is [not one of them]. The answer is I controlled the situation, and I didn't get lost in the \$39 billion number. I just looked at it as a very simple transaction, and I had to keep control of it if I was going to get the maximum value. Going back to the *Tribune*, what I would tell you is there was no connection between the two transactions. And in the case of the *Tribune*, I recognized when I did the transaction that it was a very highly leveraged transaction. However, the risk-reward ratio was extraordinary.



The real reason China should have REITs is that China needs to provide its population with appropriate investment vehicles. And the investment opportunities in this country are very closed with a relatively small group of people. In effect, you're democratizing real estate when you create REITs

My investment was \$300 million. If it worked, and if it worked without taking any extraordinary risk, we would have the opportunity to make 20 to 40 times our money. So risk and reward was there. During that five-year period [prior to our purchase] the revenue of the *Tribune* went down by 3% each year. We, in turn, underwrote the deal with a revenue suppression of 6% and felt that would protect us from the erosion of the newspaper business. The first month we owned the *Tribune*, revenue was down 30%. That was the equivalent of a black swan. Nobody had ever seen a 30% reduction. We obviously couldn't have underwritten it. We lost. If the circumstances were identical, there is no doubt I would do the *Tribune* again today even though I know it didn't work. But the risk-reward ratio is what it is all about. And measuring and gauging that all the time is the biggest safety issue every investor has.

**LJ:** You are often called the 'father of the modern American REITs industry'. Should we develop a REITs industry in China?

**SZ:** The REITs industry in the US was created by a passage of a law in the end of 1960. The goal of the original REIT

legislation was to provide an opportunity for the little investor to basically buy pieces of very high-quality commercial real estate. The concept was terrific. The problem was that, during that 30-year period of time, the private market was so much more attractive than the public market. Then in 1990 all forms of real estate financing disappeared and the only access to capital was the public markets. I began, along with a number of other people over a three or four-year period, converting most of the commercial real estate market from private to public. To give you a frame of reference, today the REIT market is about \$500 billion. So from 1960 to 1990 it grew from zero to \$6 billion and from 1993 to 2000 it grew from \$6 billion to \$500 billion. So, obviously, it fulfilled the need and demand from the investment community for income and a piece of the action. It also did tremendous things for the commercial real estate market by creating dramatic amounts of additional new liquidity that didn't exist.

**LJ:** So is that a good idea for China?

**SZ:** I think it's a good idea for every country in the world because it results in taking massive amounts of holdings that are generally very concentrated and spreading them out throughout the population.

**LJ:** Here in China investing in real estate is a very big deal for many investors. What is your advice to them?

**SZ:** Wouldn't a Chinese investor be better off owning liquid stock with a dividend than owning an apartment in some complex that needs to be taken care of and that has no liquidity by definition? The real reason China should have REITs is that China needs to provide its population with appropriate investment vehicles. And the investment opportunities in this country are very closed within a relatively small group of people. In effect, you're democratizing real estate when you create REITs. ■

#### About Liu Jing

Liu Jing is Associate Dean and Professor of Accounting and Finance at CKGSB. He formerly served as a tenured faculty member at the Anderson School of Management at the University of California at Los Angeles (UCLA-Anderson). He is an internationally recognized expert on capital markets, equity valuation and securities analysis. He holds a Ph.D from Columbia University.

For the full version and videos of the forum, please log on to CKGSB Knowledge: [knowledge.ckgsb.edu.cn](http://knowledge.ckgsb.edu.cn)



# No Silver Bullet

China's burgeoning market of retirees presents a big business opportunity. But tapping it is far from easy

By Li Xiaoshu

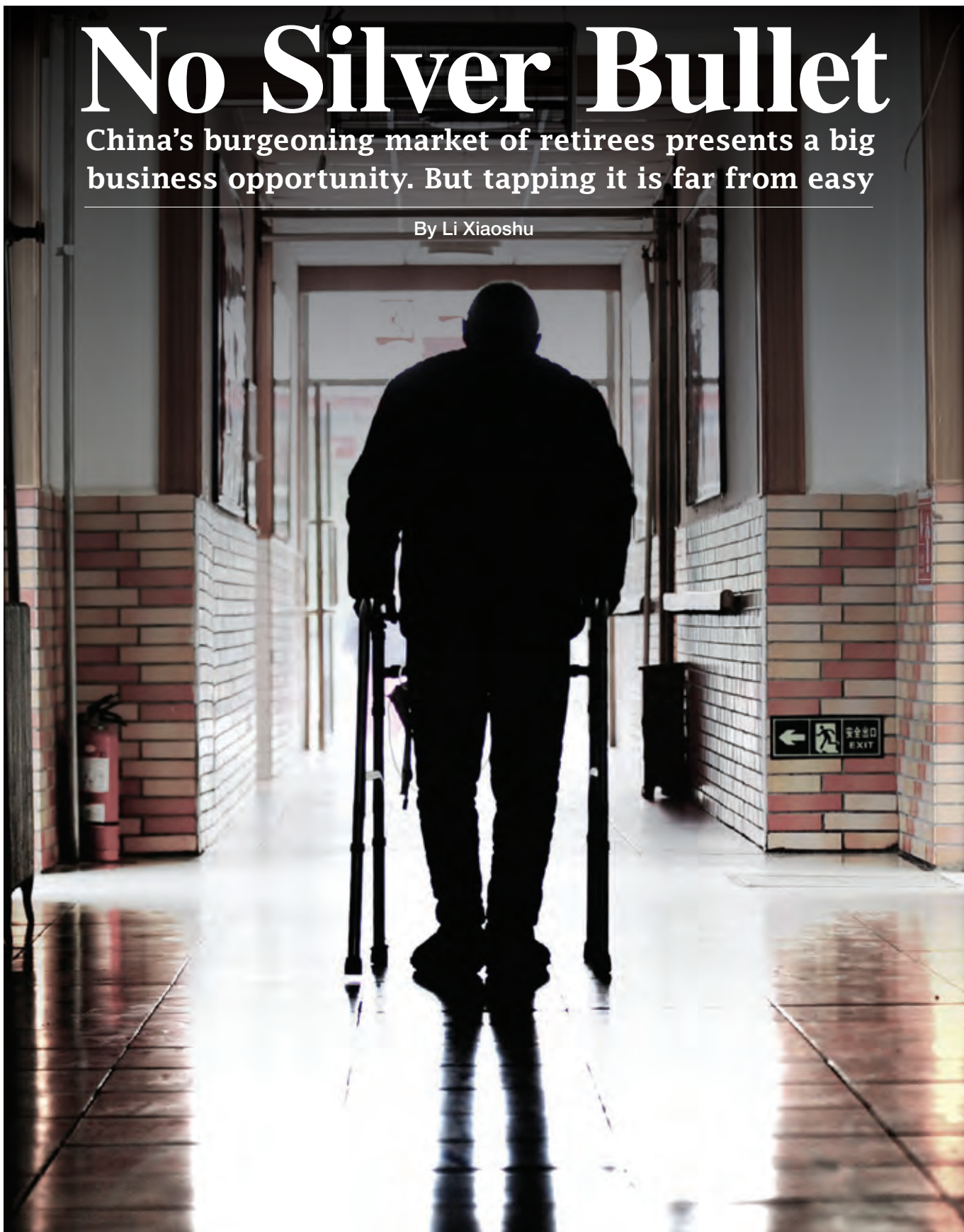


Photo:CFP

**L**iu Wen, a gray-haired 82-year-old, draws himself up from a deep Chinese-style sofa and shuffles to the door to answer the doorbell. It's lunchtime at Yanda International Health City, and Liu and his wife are among the senior residents getting their meals delivered—there's steamed bread, fried fish and pumpkin on the menu today.

Attracted by this kind of service Liu, a retired civil servant, moved here from Beijing which is a two-hour drive away. The couple pays RMB 7,600 a month (excluding utilities) for a 70-square meter apartment at Yanda.

“The rent is twice what you'd pay for an apartment of a similar size in Beijing's suburbs,” says Liu. “Many people our age can't afford to stay here, but the price is worth the medical care you get.” Liu's wife is paralyzed and she needs constant medical attention. With doctors, nursing attendants and dieticians on duty 24/7, Yanda seemed like a good fit for the couple. Beyond the bare basics, there are a few frills as well, such as a hot spring pool and a library.

Yanda, which opened in late 2010 as a high-end medical and nursing facility with capacity for 12,000 seniors, appears to be a perfect solution for many elderly people like the Lius, whose two sons are unable to give the time or care required by their paralyzed mother.

### End of the Demographic Dividend

There is another reason why senior-focused products and services—such as Yanda's retirement housing—are starting to sprout across China. These services are driven largely by China's population trends, which have been shaped by the country's one-child policy. The very high proportion of working-age citizens which delivered China a ‘demographic dividend’—fast economic growth driven by a huge working population—will end as a large proportion of its workforce moves toward retirement, says Cai Fang, director of the Institute of Population and Labor Economics under the Chinese Academy of Social Sciences.

The tide is slowly turning. According to statistics from the Ministry of Civil Affairs, in 2009 there were 167 million ‘over-60s’, about an eighth of the population. The most recent government census also found that around 185 million Chinese were over 60 years old in 2011. By 2050 the number of ‘over-60s’ will swell to 480 million, while the number of people in the “working-age” will have fallen in comparison, according to the census. The writing is on the wall. As Robert Wiest, head of China operations at Swiss Re, the world's second-largest reinsurer, commented in a company white paper published in April, “China by 2050 will become the most ‘aged’ among the emerging BRIC countries.”

In today's China, the pressures on the one-child generation are obvious. In what is commonly known as the ‘4-2-1 phenomenon’ (see adjoining illustration), the responsibility of caring for the elderly—the parents and



Wooing the Elderly: The serene environs of Yanda International Health City, located outside Beijing

two sets of grandparents—falls upon the single child who may not have the time or the resources to bear this burden. As Fung Global Institute Senior Fellow and Harvard professor Arthur Kleinman and fellow Harvard professor Hongtu Chen point out in an article titled ‘Looking after the Elderly—Asia's Next Big Challenge’, “...it is estimated that the elderly-support ratio is projected to decline drastically (in China). Right now, for every elderly person (aged 65 and above) there are nine working-age adults (ages 15 to 64); but by 2050, this ratio will be one elderly person per 2.5 working age adults.”

### Finding Out What Works

One would think that there would be many takers for a facility like Yanda. Apparently not. “We haven't sold as many residences as we were expecting,” explains Zhou Baiyun, deputy director of marketing.

When it launched the project in 2010, Yanda wanted to “seize the moment” and get the first-mover advantage. The company spent RMB 12.7 billion (\$2 billion) in building the complex. “We were a bit too early to test the water,” Zhou says in hindsight. “The apartments are not being filled up as fast as we expected.” Yanda reported RMB 40 million in revenue in 2011 and expects that figure to rise to RMB 200 million in 2012, according to Zhou. But despite the seemingly good growth figures, Zhou is reserved about future earnings. “It will be a long time [before we make back our investment],” he says.

A reason for underperformance is the reluctance among Chinese seniors to spend. Says Zhou, “Chinese seniors are much thriftier than their Western and



East Asia peers... they are less willing to pay for their sunset years than their children may eventually be.” While China is aging, it’s not clear that its elderly are willing or able to pay for elderly care. Only 11.3% of 19,986 seniors polled nationwide by the China Research Centre on Ageing said they’d prefer spending their twilight years in nursing homes. The average maximum that respondents would be willing to pay according to the poll, is RMB 1,016—hardly economical for ventures like Yanda.

Other developers have been finding out the hard way about what fits the current China seniors’ market. Among them is Greentown China Holdings, which lost several million on its Greentown Yi Le Academy, a nationwide chain offering recreational programs for the elderly, such as singing, painting, and Chinese calligraphy. Feng Yufeng, vice general manager at Greentown, explained that none of the 17 Yi Le academies has yet turned a profit, with only 1,500 seniors signing on for courses since January, 2011.

Greentown has had bad luck, too, with its retiree-focused Greentown Blue Patio, a premium category retirement community for the aged, in Hangzhou. Only 10 out of 86 high-end apartments were sold by late July. “Maybe it’s just the wrong time, wrong place and wrong people,” says Feng. “It takes time to figure out a path that really works in China.” He says the lesson for Greentown and others targeting the retirees market is simple: “Test the market with small projects that are niche, customer-centric and scalable.”

## A Better Route to Success?

That appears to be precisely the approach taken by a more successful venture, Singapore-controlled Pinetree Senior Care Services, which reported a 55% year-on-year growth in revenues in 2011. Set up in 2009, the firm’s 500 nurses provide in-home care to 20,000 seniors. Pinetree CEO Ninie Wang explains how the firm’s success is the result of lengthy market research into China’s elderly market.

Wang says that Pinetree had originally intended to set up care centers for seniors around China but abandoned the idea as “barely feasible” after three years of research. “It took three years to understand that Chinese old people prefer to stay at home rather than going to a care center in the Western sense, even if they’re seriously ill.”

Pinetree allows customers to choose from hourly rates between RMB 100 and RMB 260 depending on the experience of nurses, who are dispatched from 14 service units across Beijing. Customers typically spend between RMB 100 and RMB 800 per visit, explains Wang.

Having service centers in major residential areas across the city ensures efficiencies: nurses’ travel time to patient’s homes is capped at

## Niche Openings

China’s demographic transformation has generated a whole new raft of possibilities for makers of medical devices and insurance companies. Kang Fu Zhi Jia, a medical device chain, has 86 outlets across the nation. “Angel capital is very eager to invest into the medical device sector, especially professional hospital beds which are in strong demand,” founder Bai Yu says. Statistics from the General Office of China’s State Council show that the country only had 3.15 million senior nursing beds by the end of 2011, enough to cater to 1.77% of its over 60-year-old population, compared with 10% in developed countries like the US.

Christopher Kaye, partner and managing director in the Boston Consulting Group’s (BCG) Hong Kong office, expects 5% to 10% average growth in the retirement insurance sector and up to 40% increase over the next three years, provided the government encourages private participation in pension and healthcare plans.

An early example of this is Taikang Life Insurance Corp., China’s fifth-largest insurer by premium value, is coming out with offerings for China’s wealthier seniors. In April, Taikang launched a new commercial pension with a base premium at RMB 2 million that enables insureds to not only receive their annual fund, but also live in a senior community which Taikang is building in suburban Beijing with no additional payments required. Taikang said a total of 50 such pension policies were sold in the first 30 days since the product’s debut. “The model is innovative and could boost the number of life insurance products while also providing capital flow to the senior housing segment... It’s equivalent to issuing 30-50 year corporate bonds,” Taikang’s CEO Chen Dongsheng said to Xinhua News Agency.

15 minutes. Pinetree nurses are encouraged to walk or use bicycles and public transport. “Scheduling of staff and efficiency are key to profitability,” explains Wang. “Once you cut down travel time, nurses can visit more customers.”

Success in Beijing has encouraged Wang to go national: Pinetree is scheduled to open 1,000 franchises and hire 40,000 nurses nationally by 2015 to achieve a client base of five million patients.

Another success story, also in Beijing, is the Cun Cao Chun Hui Home for the Aged that offers round-the-clock nursing care to disabled elders. The facility in Beijing’s Chaoyang District broke even seven months after opening with a monthly turnover of RMB 500,000 on 100 beds. Company CEO Wang Xiaolong credits the firm’s success to research and “sustainable human resource strategy”—competitive pay, a clear system of training, career advancement opportunities and comfortable accommodation for employees to “encourage people into the sector”. Wang also narrowed the company’s target group from all seniors to disabled seniors.

## Policy Boost

Investors may be well advised to wait for government policy. China’s Ministry of Civil Affairs has encouraged private capital in senior services with taxation policies and land provision since 2007, but “it could take a couple of years before we see subsidies paid for elderly care,” says Cun Cao Chun Hui’s Wang Xiaolong.

Struggling to deal with the demographic shift, the Chinese government is currently mulling over its senior rights protection draft law which should guarantee that most of its elderly population should grow old at home and have sufficient care services, while public and private retirement homes are supposed to fill the gap when families aren’t available or capable to care for the elderly.

China’s local governments are also required to boost spending on service sectors for seniors. “Local governments are much quicker to give the green light for them,” says Zhu Fengbo, chief executive of Beijing Sun Cities Group, which develops retirement homes. Zhu signed three contracts to cooperate with second- and third-tier city governments to develop senior projects in the first six months of 2012. “Developing

provincial and national lobbying strategies will be critical, as will educating consumers and private investors to understand the public-private dichotomy to ensure that interests on both sides are met.”

Policy reform to encourage private sector participation will be vital for investors but they’ll be advised not to dive in head first without understanding this evolving market. China’s seniors are unique in their lifestyle choices and spending habits. Only companies that can understand their needs will succeed.



China's dominance of world seafood production is being challenged by weak exports, high costs and competition

By Mark Gao



**L**andy Chow plucks a shrimp and carefully checks the wriggling creature's body length and weight. The weight and the skin seem right, nods Chow before returning the gray-brown creature to the pond. The shrimp, one of millions he's bought from a farmer for an American supermarket chain, will be washed, cooked and frozen in a Guangzhou plant before being loaded into containers for the trans-Pacific voyage.

'Made in China' may not have appeared in their menus but seafood restaurants from Beijing to Boston have enjoyed low-cost seafood supplies over the past decade thanks to China's embrace of aquaculture. Siam Canadian, the multinational seafood trading house where Chow works as the head of the mainland China sourcing operations, is one of the many companies that source Chinese seafood for US retailers and restaurants. Given China's well-documented shortages of land and water it's surprising, perhaps, that China is the world's number one seafood exporter. China's annual exports account for almost 70% of global seafood production in terms of quantity and 55% in value terms, according to the latest data compiled by the Food & Agricultural Organization (FAO), a United Nations (UN) body.

China's seafood output clearly relies on aquaculture. In the period January to May 2012, China's seafood output totaled 18.9 million tons, according to data published by China's Ministry of Agriculture. Of that total figure, 13.5 million tons came from aquaculture compared to 5.39 million tons from non-farmed or wild catch. China exported around a quarter—3.3 million tons—of total January-May output. Over 90% of China's domestic seafood consumption is satisfied by aquaculture, according to the FAO.

China's rise as an aquaculture power was achieved by low-cost cultivation of commercially important finfish (such as catfish and tilapia) as well as mollusks (oysters, mussels and clams) and crustaceans (lobsters, shrimp and crabs) in onshore ponds as well as in coastal enclosures. Much of the produce is processed and packaged at plants clustered around coastal cities like Qingdao, Dalian and Yantai, which have also proven to be competitive in processing imported fish fillets for re-export.

China's rise in aquaculture has been dizzying. The country grew its seafood exports from \$3.6 billion in 2001 to \$13.2 billion in 2010, according to the FAO, while second-placed Norway grew its exports from \$3.5 billion to \$8.8 billion in the same time frame. China increased its exports further to \$17.1 billion in 2011.

A significant chunk of China's exports are, in fact, re-exported frozen fish (such as cod from Russia and the US and salmon from Europe), originally imported for processing. Figures for January to October 2011, published by the US Department of Agriculture (USDA), show that over 1.7 million tons of a total 2.2 million tons of seafood imported into China in that period were dominated by frozen fish, much of it likely for processing and re-export. China's value-add from processing is clear: China's total exports in the January-October 2011 period was 2.9 million tons valued at \$12.3 billion compared to imports of 2.2 million (value: \$4.2 billion).

China produced almost 55 million tons of seafood products valued at \$21.7 billion in 2011 (compared to \$17.2 billion in 2010) according to Cui He, secretary general, China Aquatic Products Processing Marketing Association (CAPPMA). In 2010 China shipped 540,000 of the 5.01 million tons of seafood imported into the EU (from non-



Fish farming or processing is dirty, hard work so finding workers has never been easy

Cui He, Secretary General of CAPPMA

EU states) in 2010, making it the bloc's second-placed supplier, behind Norway, according to EU statistics. Aquaculture has become a useful source of jobs and earnings for China, contributing over five million rural jobs and six million seasonal jobs in fisheries harvesting, according to Chinese government data.

### Weak Demand, Rising Costs

There are signs of weakening demand for China's key aquaculture export commodity, tilapia—shipments to the US, the largest market for Chinese tilapia exporters, shrunk to 85,173 tons from 111,436 tons in 2010. The EU, which imports 62% of its seafood, imported 23,000 tons of tilapia from China in 2010. Statistics from Eurostat, the EU's statistics agency, show shipments of tilapia from China slipped in 2011 to 22,000 tons.

Siam Canadian's shipment volumes have fallen by 20% in the first six months of 2012 compared to the same period in 2011, according to Chow, who blames weaker demand for China's top three indigenously produced export categories—tilapia,

shrimp and squid. Chow expects a 10-15% drop compared with last year in terms of container numbers. His figures are corroborated by CAPPMA's Cui He who reports that China's shipments have dropped by between 15% and 20% in the first half of 2012 but exact volume figures are not available.

While China remains dominant in key export markets like the US, Canada and Europe, the aquaculture trade is starting to feel pressures from rising wages in particular. Rising labor costs have rattled processors and fish farmers. "Fish farming or processing is dirty, hard work so finding workers has never been easy," says Cui, adding that Chinese seafood firms have been taking a 15% rise in wages each of the past two years. He points to one of China's seafood processing hubs, Guangzhou, which will increase its minimum monthly wage for the third consecutive year in 2012, to RMB 1,470 per month, up 13% from current wages.

### Competition from Vietnam

Beyond the cost challenges, there is the threat of lower-cost competitors. China's tilapia farmers have been facing competition from peers in Vietnam farming a similar species, basa (also known as pangassisus), a freshwater species of catfish which offers 40% meat yields compared to 35% yields for tilapia—an important consideration for seafood traders and restaurateurs seeking maximum value from a fish. Vietnam grew its exports from \$1.4 billion to \$5.1 billion between 2001 and 2010, putting it in fourth place in the FAO rankings of seafood exporters.

Simon Funge-Smith, Asia fisheries officer at the FAO, explains that Vietnam's success is based on "incredibly low prices" achieved through "very intensive farms with cheap labor and cheap feeds." However he also points to efforts by Vietnam's government to cap production due to land and water shortages.

The USDA's Foreign Agricultural Service in its report noted that a serious challenge for the tilapia industry lies in "the increased production and exports" of basa by Vietnam. Imports of Vietnamese basa into the EU have risen from 150,000 to 250,000 tons between 2007 and 2010, according to the EU Fish Processors and Traders Association. This figure may well rise further given aggressive plans (which may conflict with government efforts to cap production) by the Vietnam Association of Seafood Exporters and Producers (VASEP), an industry umbrella body representing



A dockside seafood market in Zhejiang province, one of China's key aquaculture hubs

Vietnamese seafood producers, to lift Vietnamese seafood exports from \$6.1 billion in 2011 to \$10 billion in 2020.

### Adding Value

Weaker export demand may prompt China's seafood sector to move up the value chain, improving product processing and marketing. Processors, aquaculture feed millers and industry associations like CAPPMA are talking about how to build the brand and quality of Chinese tilapia and other farmed species, notes Han Han, program manager at the Chinese Tilapia Aquaculture Improvement Project (AIP) run by the Sustainable Fisheries Partnership Foundation (SFPF), an NGO. "But it is taking a long time for the industry to reach agreement internally," she adds.

China's highly fragmented aquaculture sector is likewise seeing the emergence of large-scale players, among them fish farms such as the Dalian-based Homey Group and the Zhangzi Dao Fishery Group, also based in Dalian city on the country's northeast coast. Faced with tight export markets and falling prices, bigger players such as Homey and Zhangzi Dao have shifted to domestic markets and higher-margin products. A spokesman for Homey Group said the company was shifting its focus from cultivating shellfish to breeding sea cucumber (also known as *beche-mere*) for use in Chinese cooking and medicine. Homey has built a new seedling center and an 800-hectare farming project to raise production of sea cucumber. Gross margins of 25% on sea cucumbers compare favorably with shellfish, which yields less than 10% margins, said the spokesperson.

Qi Lu Securities, which analyzes the market and price of sea cucumber and shellfish, predicts that sea cucumber prices will rise from RMB 170/kg average in the first half of 2012 to RMB 200/kg in the latter half year of 2012. Zhangzi Dao claims it harvested 2,300 tons of sea cucumber worth RMB 500 million in 2011, a year-on-year rise of almost 70%.

The processing side of the sector is also seeing signs of a shift to higher margins. Fish farmers are shortsighted, says Han Han, looking no further than the latest prices. The same could be said of the country's seafood processing sector, haunted by an excess of capacity installed in better market conditions. Peter Redmayne, CEO of US-based Seafare

which co-organizes the annual Seafood Expo, the largest in mainland China, explains how Chinese players rushed into the sector, "ultimately building too many processing plants when a healthier EU economy supported stronger demand".

The larger seafood processors, however, have continued to invest, only this time on automation to save on labor costs while turning out more sophisticated products. Among the players moving aggressively to cut costs is Singapore-based Pacific Andes which this year completed a RMB 100-million renovation of its largest factory in Qingdao. A high-tech new production line at the plant, China's largest fish filleting and processing factory, will see electronic grading and trimming equipment replace workers. The new equipment will also allow processing of a wider range of fish species popular in Western export markets, including haddock and hake, according to a Pacific Andes statement which added the firm will "...launch new value-added and ready-meal products and develop other new businesses to further future growth".

### Rays of Hope

Redmayne believes the sector will remain subdued as long as European demand is weak. High unemployment rates in Spain, a key consumer country, "means they're chowing down a lot less fish". Slightly more hopeful, shipments of cod to the US rose to 11,000 tons in the first five months of 2012, compared to 8,000 tons in the same period last year. A bumper catch of Alaskan cod this season has led to demand in the US for cod processed in China, explains Redmayne.

CAPPMA head, Cui He, expects a slight rise of about 2% in locally-produced seafood volume in 2012. That suggests China will in the short-term remain a dominant player in volume terms, even as it copes with rising costs and falling demand. There remains the risk that China loses out to lower-waged Asian neighbors. However, Simon Funge-Smith believes China can ultimately hold onto its lead in seafood cultivation and processing, built up over the years. "Chinese production is still huge," says Funge-Smith, meaning any shift of production elsewhere is unlikely to significantly erode China's dominant position as the world's number one producing country.



# Charting a New Course

Vantone chairman Feng Lun on pioneering a new business model for China's real estate industry

By Wang Fanfan



**W**ith China's real estate market in cool-off mode after over a year of policy-driven credit restrictions, it's perhaps not surprising that one of the country's most high-profile developers has been looking at new territories and new business models. Vantone, a leading real estate developer in China, is changing its business model from property development to management with a long-term plan to concentrate on real estate fund management, says the company's chairman and founder, Feng Lun.

Vantone wants to move away from bricks and mortar to managing cash and properties for third-party investors. The company will move "upstream" to property management and financing, explains Feng, leaving it less reliant on building and selling properties, which he terms a "downstream" activity. "We want to move away from labor-oriented to skill-oriented services." Feng points to Tishman Speyer, a US firm, which as he explains, builds approximately \$150 million worth of developments in one year, but manages \$12 billion in real estate funds.

A closer look at company documents shows that Vantone is already attempting to emulate Tishman Speyer. Vantone's investment management wings include Beijing Vantone Zhengqi Investment Management Co. and Chengdu Wanxin Xinchuang Investment Management Co. (in which Vantone has a 60% stake). Both are listed as subsidiaries in Vantone's 2011 annual report, with registered capital of RMB 100 million and RMB 20 million respectively. The report also lists Singapore-based Vantone Investment as a wholly-owned subsidiary.

Given that Vantone hasn't released separate results for its investment vehicles, it is hard to judge their profitability. However there is some proof that Feng Lun is doing something right: profits at the company's Shanghai-listed arm, Beijing Vantone Real Estate Co., rose by 187% to RMB 20.6 million in the first half of 2012, according to company filings. By contrast another leading real estate developer, SOHO China, saw net profits dip 65% to RMB 613 million, a drop the company said was due to fewer project completions in the period.

Seated in a deep armchair at the glitzy Grand Hyatt hotel in Beijing, Feng Lun explains his fascination for what he calls the "American model". Feng believes China's real estate sector has much to learn from the US in terms of financing models. Due to the limited financing channels, he thinks Chinese developers should follow a US model of bundling properties into financial instruments like real estate investment trusts (REITs), a real estate investment structure similar to what mutual funds provide for



**Eye on the Big Apple:** Vantone has leased five floors of New York's One World Trade Center, slated to be the tallest building in the US upon completion

investment in stocks.

Feng admits that Vantone clients, shareholders and employees have been skeptical of the suitability of US models like REITs for China. "The biggest obstacle to moving to this kind of model in China is the immaturity of the financial markets here." While mainland Chinese properties have been packaged into REITs traded on the Hong Kong and Singapore stock exchanges, there

### Hong Kong Model vs US Model

The Hong Kong model which Vantone used to employ, puts emphasis on the appreciation of assets and land. On the other hand, the American model which Vantone is pursuing now seeks profits from management and operation of the properties.

Vantone's American model includes reducing the business in development, and focusing instead on value-added commercial real estate via world-class property management and operation, acquiring industrial properties and further turning the properties into financial products such as REITs. Vantone is also moving into real estate fund management, it now manages three funds: Vantone Shouzheng, Wanli Fund and American Black Lion Fund.

has been no such trading on the mainland exchanges. Property developers and investors have been eagerly awaiting the timeline and regulatory framework, promised by regulators, to allow REITs to list on mainland exchanges. Notably in 2011 the first renminbi-denominated REIT was launched on the Hong Kong exchange, allowing investors to invest mainland currency into REIT-packaged mainland properties.

Feng clearly sees long-term hope for the model in China. "Seventy percent of the US real estate development is financed by investors and 30% through other channels. America was able to build this kind of model because it has an advanced capital market. But if you look at China, bank loans account for about 90% of real estate financing."

"We have to wait for the maturity of our direct financing conditions if we want to follow the model. This is a challenge... but when more and more trust, pension and insurance funds flood the real estate market, our American model can be launched."

### New York Home

In the meantime Feng is studying the American system up close, as an investor.

In 2009 Vantone signed a 20-year lease on five-and-a-half floors of the first tower of the rebuilt World Trade Center (popularly known as One World Trade Center). After overcoming local sensitivities Feng opened a 190,000 square foot China Center with offices for Chinese corporations and exhibits on Chinese culture. He even incorporated a vertical Chinese garden designed by Japanese architect Kengo Kuma into the Center. Tenants include AVIC, China's state-owned aviation equipment maker, while others in the 104-floor glass tower include publishing giant Condé Nast.

Feng Lun became familiar with the World Trade Center project while completing a real estate lectures program at Columbia University in 2003. He was also among the Chinese developers who met with then New York governor, George Pataki, through an investor relations delegation to Beijing in 2005.

"I've flown to New York over 50 times since 2003," says Feng. "We want the 500 Chinese companies listed on the New York Stock Exchange and Nasdaq to move in... Our strategy is always to prioritize mainland Chinese clients and tailor our overseas products to their demands. If they want office space in Vancouver, we'll expand there and if they want to be in Hokkaido, we'll build there too."

Vantone doesn't deliberately seek American tenants for its US property. "We treat them as supplement. Everything we do is expected to be liked by both Chinese and Americans. Chinese clients are the basis [of our business], while

American ones are a bonus.”

Feng explains how expansion into the competitive New York real estate market is central to his ambition to make Vantone a global player. “People think we haven’t made much progress in recent years because they didn’t see us competing for land.” In reality, Vantone was competing for a slice of the Manhattan skyline.

Feng’s partner in the US is the Durst Organization Inc., the developer of the World Trade Center project which currently owns or manages 8.5 million square feet of prime Manhattan office space. Vantone invested \$11 million in Durst’s 855 Sixth Avenue, a mixed-use hotel and residential property. Durst has been an invaluable source of advice to Vantone on managing and operating green commercial high-rise, says Feng. “It’s been like going to college.” Vantone appears to have also advised Durst on investing in Asia. Durst invested a similar amount in Vantone’s Taipei 2011, a luxury serviced apartment complex in Taipei, Taiwan.

Feng says he will “certainly” make more investments in the US. “We will combine our American experience and resources with our strategy. This is a strategic consideration, through which we can improve and get to know new ways to run the real estate business.” Meanwhile, he is on the lookout for more opportunities. In August, *Bloomberg* reported that Vantone was in discussions with authorities in San Francisco to re-develop the city’s Pier 19, converting the 206,000 square foot warehouse near Fisherman’s Wharf for use as offices, meeting rooms, galleries or a hospitality center for Chinese business people.

Entering a mature market like the US has been a learning experience for Vantone. “In an unfamiliar market like New York you must have good partners, specific projects and good financial resources to control the risk,” says Feng.

Like Vantone, many Chinese developers appear increasingly keen on the US. The largest Chinese residential developer by sales, China Vanke, recently announced plans for its first overseas project in the US. Vanke’s President, Yu Liang recently said in a press conference in Hong Kong that “international expansion is going to be an important strategy”.

Feng has words of caution for Chinese developers thinking about the US. “None of the Chinese companies that go to the US to be developers are successful because they lack the experience in the mature market, but some who go there to acquire buildings have done well.”

### American Idol

American real estate mogul Sam Zell, a master of the REIT structure, is clearly a role model



Feng Lun is on a mission to reinvent Vantone

for Feng (see “Any Time You Don’t Sell, You Buy”, page 21). “Zell manages many people’s money. China Investment Corporation, for instance, gives Zell money. He utilizes both his own money and the money he manages. At present, Vantone also manages its own money and other people’s money, and gradually we are moving up the value chain. If we continue to move up the value chain, 10 years from now, we might be able to be like Sam.”

While Feng is clearly in awe of what he terms the American model, he also sees a model worth emulating closer to home. That’s Singapore-based CapitaLand, which Feng describes as having established a “complete real estate value chain in China”. He is referring to CapitaLand’s 10 real estate funds focused on mainland developments. “It took CapitaLand nine years to complete the transition; I think it will take Vantone 10 or 15 more years to make the transition from developer to real estate finance management firm.”

### Residential to Commercial

Feng Lun also wants to match CapitaLand’s success in commercial real estate. The Singaporean developer operates 53 commercial projects in mainland China, compared to Vantone’s two. Feng says government restrictions on the residential real estate market means Vantone will increasingly focus on commercial properties.

Chinese developers are hedging their bets with a presence in both the residential and commercial sectors since restrictions on

residential real estate were implemented in an effort to bring down prices. The government’s tightening measures, implemented in 2010 to bring home prices down, have included restrictions on home purchases in several cities, higher down payments and property taxes. Other property restrictions include a squeeze on credit to developers.

Potential for growth in the commercial real estate space is huge. “Chinese real estate companies started the transition from residential to commercial long before the policy enforcement,” says Joe Zhou, head of research at Jones Lang LaSalle in Shanghai. He explains that commercial property attracts investors as it’s “more closely related to the fundamental factors of the economy... For example, retail real estate is benefiting from the growth of incomes and consumer spending in China”.

A shortage of quality properties for sale, however, remains a challenge. Likewise capital and talent remain key challenges to developers tapping the commercial market. “The payback period is about 20 years for commercial real estate. Government is controlling the credit so real estate companies face great difficulties getting loans. China does not have REITs yet, and the scale of private equity funds is too small compared with the investment in development.” The other challenge facing developers is a lack of talent, particularly in the commercial real estate space. “It takes a long time to accumulate experience in office building and mall management for instance,” says Zhou.

While market conditions mature, Feng’s





Vantone Center in Beijing is the flagship commercial property of the company and the headquarters of Vantone Holdings

plan for Vantone's medium-term success goes like this: establish the Vantone brand name with quality commercial real estate projects which will ensure higher yields and longer-term occupancy with better management. Feng also sees a chance to increase the value (and thus occupancy) of a building by securing environmentally-friendly badges like Leadership in Energy and Environment Design (LEED), an international green building certification system which Vantone secured for its Vantone Center, a mixed-use building in downtown Beijing. "Once our rental yields exceed 6%, it will be possible to package these commercial properties in REITs," explains Feng.

### Dimensional Cities

Another one of Feng's notable innovations is what he terms the "dimensional city", which is Vantone's blueprint for sustainable cities as China continues its rapid urbanization.

Feng says Vantone has invested RMB 50 billion in realizing its first "dimensional city" in Chengdu, with work set to begin at the end of 2012 on a community that integrates commercial establishments and apartments. Vantone, he says, has also looked carefully at building similar developments in six second-

tier cities including Xi'an and Wenzhou.

"These settlements will deal with issues concerning the environment, industrial development and residential environment," says Feng, who adds that progress in individual cities will depend on local governments' "acceptance of our innovation". Feng explains, "In the traditional mindset, police stations are supposed to be in one-story buildings with a courtyard, but we will move them to the sixth floor. Likewise school playgrounds are on the ground, but we might move them to the fourth floor. This kind of innovation needs the cooperation and acceptance of local government." In these communities, 65% of the land will be dedicated to agriculture, commercial establishments, schools, hospitals and internet companies, while 35% will consist of green areas.

### Ideologue Turned Developer


Known for his colorful language and (often mixed) metaphors, Feng Lun compares his role as a fund manager to a diamond polisher: "You've got to be outstanding at making the diamond shine but you've also got to keep the diamond safe. You can increase the value of the properties 10 times but just like the man who polishes other people's diamonds you'll

only keep 5% of the profits that come from your skills as a manager, so you have to keep a level head."

Born in Xi'an in 1959, Feng Lun has cultivated an image as a "Renaissance man", authoring bestselling books and driving a jeep across Afghanistan in 2006. Feng, who earned a doctorate of law from the Chinese Academy of Social Sciences before a brief academic career at the Communist Party's Central School, has also styled himself as a philanthropist. He has been chair of the China-based Society of Entrepreneurs for Ecology and the Singapore-based World Future Fund which professes a goal of finding solutions to problems facing humanity, such as climate change and hunger.

Now a prolific author, Feng Lun still retains the worldly air of an academic. He keeps a portrait of Yasser Arafat in his office (apparently he admires Arafat's lifelong devotion to the singular goal of Palestinian statehood). His bestselling autobiography, *Full Fledged Ideals* (title loosely translated from Chinese), is a call to arms for young people to pursue their dreams. The book noticeably does not dwell on his relationship with former business partner and current rival, Pan Shiyi, Chairman of SOHO China, Beijing's biggest developer by land bank. The former business partners went their separate ways in 1994 in a dispute over the future direction of Vantone.

Feng's first book, *Rampant Growth* talks of Vantone's early days in Hainan's frothy real estate market in the early 1990s. Feng, as chairman and Pan overseeing sales, alongside Wang Gongquan, now the billionaire founder and chairman of venture capital firm CDH Investments. The trio established Vantone Industrial in 1993 with RMB 800 million in paid-in capital. Feng and Pan disagreed when Feng began to expand Vantone into other sectors like telecom and aviation. Keen to focus on real estate, Pan left to set up SOHO China, which is now a leading Chinese developer.

While Feng has a vision of an American model of doing business, it's unclear how soon he'll be able to transplant that model to China, given the restrictions on fund structures such as REITs. But Feng says he'll be busy for some time learning the way the US real estate market works. Reaching for yet another metaphor, he explains the process. "A farmer doesn't become a city slicker just by cleaning himself up and taking a shower. He first has to be educated. So it is with us, we have to learn how the system works." 

To read the full interview log on to: [knowledge.ckgb.edu.cn](http://knowledge.ckgb.edu.cn)



# The New Idea Factories

GE's past success in China hinged on localization. Its future, however, might be in reverse innovation

By Wang Jing

**R**ising oil prices and the global financial crisis have dealt a harsh blow to the global aviation sector. The Chinese aviation industry, however, is bucking the trend. It has become the second-largest aviation market in the world, second only to the US. If projections of the Civil Aviation Administration of China (CAAC) are to be believed, carriers have pledged to buy on average more than

300 planes a year till 2015. The country has an ambitious plan to build 70 new airports and expand 100 existing airports in the next few years.

GE Aviation, a unit of General Electric Company, has been in China for 27 years now and is well-poised to tap the opportunity in China's rapidly-expanding aviation sector. Among other things, the company has set up a systems

manufacturing facility in Suzhou and has inked a joint venture with Aviation Industry Corporation of China (AVIC) for avionics.

The parent company, GE, has made China a crucial centerpiece of its globalization plan. It is not hard to see why—the company's China revenue is growing at the rate of 20% a year, whereas it is facing declining revenues in its home market.

General Manager Xiang Weiming, a



veteran at GE Aviation, talks about the company's run in China so far, and elaborates on the lessons from GE's globalization journey as well as its more recent 'reverse innovation' strategy. Below are excerpts from an interview:

**Q: How is GE Aviation doing in Asia, especially in the Greater China region?**

**A:** GE Aviation entered the Chinese market in 1985, when China Southwest Airlines and Yunnan Airlines unveiled their first batch of Boeing 737 airliners, whose engines were provided by CFM [a joint venture between GE and Snecma].

The company has now been in China for 27 years, and holds an increasing share of the engine market. China has put more than 2,800 aircraft engines produced by GE and CFM into use, which accounts for around 60% of that market. In 2011, our turnover reached \$1.2 billion, double the figure for 2005.

In terms of business development, there have been many changes at GE Aviation. When we entered the Chinese market, our business was mainly focused on selling engines, providing outsourcing as well as after-sales and overhaul services. Later on, GE Aviation began to purchase components in China and gradually participated in local independent research and development programs, including providing a power plant for ARJ, a regional airliner developed and manufactured in China.

We participated in the C919 Large Airliner Program in 2011, provided engines for it, and established a joint venture with Aviation Industry Corporation of China (AVIC) specifically to provide avionics systems for the aircraft.

Due to our expansion, GE Aviation has developed unprecedentedly in terms of personnel. I joined GE Aviation in 1992. Back then, GE Aviation had little more than 10 employees in China, but now the number exceeds 700.

**Q: Your parent company GE's globalization strategy has been very successful. Are there any lessons from the GE experience that Chinese enterprises could use as they go global?**

**A:** GE's global business contributes 60% of its turnover, while North America [the home market] generates only 40%. It means that GE is no longer dependent on North America. GE's strategy is to attach great importance to emerging markets, because their fast pace of development offers more opportunities.

I believe that a successful global strategy should contain several elements. First, you need a thorough understanding of the local

“  
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.....  
market, then a good knowledge of how to obtain support from the local government, you need real localization, suitable partners, and finally, well-chosen local talent to manage the business.

Many Chinese companies send their Chinese staff—from upper management to lower management—to expand business in foreign countries. This approach has its advantages, but if they want long-term cooperation abroad, they have to train local talent and ensure localized development and operation. A global enterprise requires localization to deal with the market, government, local products and partners. I believe these elements are essential to a successful global enterprise.

**Q: During the process of globalization, enterprises may be prone to problems like poor adjustment and cultural conflicts. What has GE Aviation done to integrate the corporate culture with local culture?**

**A:** As far as I'm concerned, GE Aviation's practice of adopting a local management team has avoided maladjustment to a large extent, but of course, time is needed.

When we first entered the Chinese

market, it was impossible to give the most important work to inexperienced local managers. Over time, as local talent gathers experience, they gradually become qualified for key positions. Local managers have many advantages when it comes to cultural exchanges and communication, especially regarding the needs of clients.

**Q: Many multinational companies often have a communication barrier between the headquarters and the subsidiaries abroad. How does GE Aviation get around this issue?**

**A:** Each of our global business corporations keeps in contact with GE companies in China. We have a regular quarterly meeting where we discuss how to establish a better platform for each business department to develop in China. The topics can range from government relations and policy-making, to research and development. Many GE strategies for China were conceived via this approach, when we run into difficulties or challenges, especially with government relations, we seek help from the head office.

Take my position as an example. I visit the headquarters every month in the first quarter of each year to discuss our strategies for the coming year with the concerned people and departments. I also communicate with my superior at our headquarters on a weekly basis. We normally brief everyone on the global situation first, while I brief them on China's situation.

The briefings are normally done through teleconference, but seeing is believing. Since I took over GE Aviation, each year I invite our global vice-presidents to conduct field surveys in China during different seasons and at different times. During a typical field survey, they spend a week visiting clients and gathering feedback, including comments on our products and services, upcoming plans and the intentions of some airlines. After the survey, the senior officials from the headquarters tend to change their opinions about the Chinese market and our clients. Personally I believe it's the best way of communication, and one which can facilitate a better understanding of China.

**Q: GE is over a century-old. Again, are there any lessons from GE's experience that Chinese enterprises can emulate to achieve long-term sustainable development?**

**A:** I think enterprises should first promise to abide by the laws and policies made by the state and government, which are of great significance in the long run. GE has abandoned many businesses over



problems which arise from legislation. Many enterprises are financially ruined or even go bankrupt when they incur government fines for violating the law.

In order to become a company that can withstand the test of time, one should constantly change, discover and adjust to new markets, instead of adhering to old practices. Past success doesn't ensure future success. Kodak is the most telling example. Kodak was a pioneer of the analogue film industry, but became bankrupt with the onset of the digital era.

**Q:** *GE is famous for its 'reverse innovation' strategy (see 'The Business Imperative behind Reverse Innovation'). Can you elaborate a little more on this strategy, particularly on how it plays out in China?*

**A:** GE plans to establish at least three innovation centers in China, with a view to have a total of six in future. An innovation center in Chengdu has already been established, and centers in Xi'an and

Shenyang will be set up soon. Researchers and developers at the sites include not only engineers, but also marketers and managers, and even staff from our cooperating partners. They make a joint effort to develop products that satisfy local needs. Every market is different. We wish to develop products that will satisfy local needs and then promote them nationwide.


The 'reverse innovation' strategy aims to take new products developed in the Chinese market and promote them in the US and the rest of the world. For example, our low-cost CT scanner machine developed in China has been successfully launched in the American market.

**Q:** *What does GE do differently to fulfill its corporate social responsibility (CSR)?*

**A:** Every year we launch CSR-related programs. Last November we designed a course titled "Why Can Planes Fly" to be taught in a rural primary school in Yunnan province. We gave

lectures to the children and made some model planes for them to fly. After making the models and flying them around the playground, the children were holding on to us by our coattails, asking us to stay. I think happiness and inspiration of that kind can't be bought.

We have also designed a course for a primary school in Shunyi District of Beijing, asking the students to think about how classrooms should be divided, and to create their ideal school. We have also guided them to plan and imagine what a future city could be like, in order to inspire them to use their imagination.

GE Aviation establishes a special donation fund each year. But I still ask employees to donate money and time voluntarily, the more people we help, the more likely they will help someone else. 

*This is a translated version of an interview which originally appeared in Issue 36 of Chang Jiang Magazine, CKGSB Magazine's Chinese language counterpart.*

## The Business Imperative behind Reverse Innovation

**T**raditionally, MNCs have gone about globalization with the mentality of 'planting flags' across the world. They took products from their home markets and distributed them across the world, sometimes with minor adaptations to suit local conditions. With the rise of emerging markets and the slowing of the developed world economy, that strategy is becoming increasingly obsolete. And as MNCs are discovering, if they are to succeed in the long run, they need to be more responsive to the needs of the emerging market consumer and pay greater attention to local conditions. They also need to preempt local competition. That's why GE has started something which CEO Jeff Immelt calls 'reverse innovation'. The company is betting big on innovations in developing countries. For example, in 2009, GE created a portable ultrasound machine in China, and a handheld electrocardiogram device in India. Both products cater to local conditions without sacrificing quality, and are meant for price-conscious consumers—the ultrasound machine sells for just \$15,000, whereas the

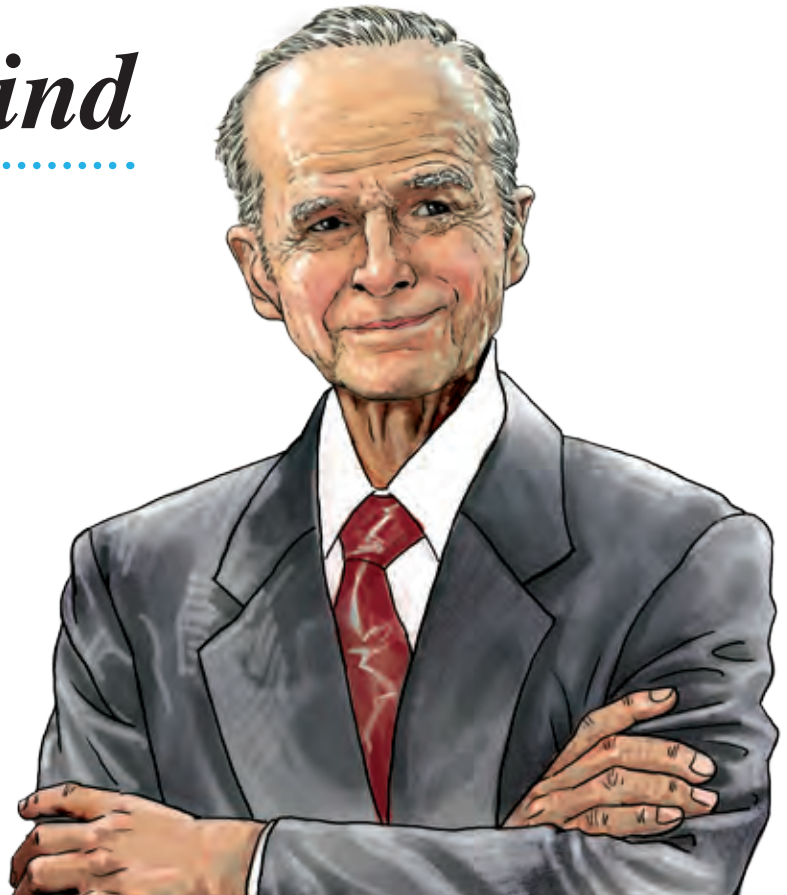


ECG machine comes at a price tag of \$1,000. These devices—innovations from the emerging market—are now also being sold in the US, something that was unheard of just 10 years ago. As Immelt wrote in a *Harvard Business Review* article titled 'How GE is Disrupting Itself' (co-authored with Vijay Govindarajan

and Chris Trimble), "To put it bluntly: If GE's businesses are to survive and prosper in the next decade, they must become as adept at reverse innovation as they are at glocalization. Success in developing countries is a prerequisite for continued vitality in developed ones."

# The Man Behind Marketing Science

The founding father of marketing science John Little talks about its evolution in this exclusive interview



**J**ohn Little, Institute Professor of Management Science at MIT's Sloan School of Management, is widely regarded as the founding father of marketing science. While he began his career in the field of operations research almost five decades ago, he eventually branched out into marketing and became known for his research on models of individual choice behavior, marketing mix models for consumer packaged goods, and adaptive control of promotional spending. In operations research he is best known for his proof of the queuing formula, commonly known as Little's Law.

Little has been at the forefront of many areas—even before the internet became popular, he had already created and implemented the idea of online marketing models. He was one of the pioneers in the use of scanner data, and predicting future buying behavior. He started companies such as Management Decisions Systems and Kana Software. The annual John D.C. Little Award is awarded by INFORMS in his name.

Even at the age of 84, Little is sprightly as ever. He works just as hard, and still goes for a run each morning. He showed no signs of jet-lag when he flew from Boston to Beijing where he spoke about his pet subject—marketing science—at CKGSB's Marketing Research Forum (see "Cutting Edge

Marketing Ideas", page 52).

Zhang Kaifu, Assistant Professor of Marketing at CKGSB, sat down with Little for a conversation on the evolution of marketing science in the US, and what Chinese companies can learn from it. Below are excerpts from the interview:

**Zhang Kaifu:** When you started working on this subject, marketing was not considered a science.

**John Little:** No, but everything has fundamentals. And they remain to be discovered and utilized [in practice]. In the 1960s, I worked on media models, for example, and there is a certain kind of data that exists and you can build models which will use [that data], but there are also judgments [that] have to be made. And one of the things people have been reluctant to do was to call it a science when you are using judgments.

**ZK:** So they consider science to be a hard, precise and mathematical process where there is no human judgment involved.

**JL:** Well... that's inappropriate in managerial conditions and in marketing conditions, usually. And therefore I wrote some papers which use judgments, and as time has gone by, we have understood processes better and better

and require less [judgment] in some sense. I have a paper called 'Managers and Models' (on how managers can use these models).

And for managers to be willing to use something, it has to be fairly simple, it has to include the important elements that he perceives as problems.

**ZK:** Not too complicated so they still can comprehend the essence...

**JL:** That's right. So a lot of people like that idea. Prior to that, you couldn't do any marketing science or management science without a very, very complete database, or they had a database so they analyzed it but they left out important things.

**ZK:** That is the beginning of marketing science. And as we know that after 40 years, many firms, in the US at least, have already adopted many tools from marketing science—conjoint analysis, optimization, etc.—and many of them have already proved to be quite successful. We want to get a little of that historical perspective from you. How did this adoption process first start?

**JL:** I founded a consulting company with some colleagues. The academics wanted to

solve new problems and publish them, but they then hired MBAs [to put this research into practice].

We were willing to do the methodology and see that it worked. And one of the interesting things that I was involved in was building a marketing mix model at Nabisco [which was then known as National Biscuit Company and is now owned by Kraft] for Oreo cookies and another one for Coca Cola.

**ZK:** *So it's like a measurement or optimization tool?*

**JL:** That's right. And perhaps the most well-modeled stuff—which I'm not so much involved in—is new products, because so many products fail. My colleague Glen Urban [David Austin Professor in Management, Emeritus at MIT] also worked out a measurement process that you can take into a mall, and get people to try the product, and also to view potential advertising for the product.

**ZK:** *This can be done before the product launches and it can help make some improvements...*

**JL:** That's right. And it used to be that the product launch cost a million dollars and this process cost maybe \$60,000, so the payoff was huge. And if you are going to kill it, kill it early.

**ZK:** *That's all for the better. You mentioned that companies like Nabisco and Coca Cola adopted some of the marketing science models early on. Did you see an impact after the companies made the adoption decision?*

**JL:** Well, interestingly enough, we had a built-in process of adaptation. It is [to see if] advertising effectiveness decreased or increased. Then you can shift the marketing mix and that sort of thing is very helpful. In fact, you can do experimentation.

**ZK:** *Counterfactual simulations before you actually carry it out in the real world...*

**JL:** That's correct. But you can also carry it out in the real world through a continuing re-measurement, because you introduce different advertising copy. The market changes, and you introduce different promotional techniques.

**ZK:** *Did some of these insights translate into actual managerial actions? Did Coca-Cola, for instance, change its advertising strategy after that?*

**JL:** Yes. Actually what one discovers when

one picks up and looks inside is that Coca-Cola does not sell soft drinks. They sell syrup.

**ZK:** *And the meaning attached to it.*

**JL:** That's right. So they are very seriously interested in advertising since their bottlers do most of the physical work and distribution.

**ZK:** *And your company for the first time quantified the effectiveness of advertising?*

**JL:** That's right. Anyway, it's grown from there. And one of the things where I hit a jackpot early from a marketing science point of view was discovering with a student of mine, Peter Guadagni, that the logit model, multinomial logit model [*Editor's note: these are models that predict market share based on product and consumer characteristics*], was remarkable. I've run millions of regressions and they always look bad, but these models look really nice. And this payoff would end in ways that can be used. For example, one of the promotional techniques frequently used in the US is to give coupons which you sometimes get in a store, sometimes get in the mail. And if you present them at the checkout, they entitle you some 10 cents off or a dollar off, depending on the kind of product you buy. And for those we use the logit model to predict ahead, to give a baseline as if the coupon had not been dropped. Then it was dropped and you can see a jump in the baseline.

One of the things about knowledge is that your first few [findings] are your maximum discovery. After that, they all seem to be almost predictable, in the same ballpark [range]. And so people lose their interest. Let's say they have a fancy new idea, in which case you can have a new "aha!" experience.

**ZK:** *But it is the major discoveries that you mentioned that are really pushing the boundaries of knowledge.*

**JL:** That's right.

**ZK:** *This is really one of the major issues that is attracting a lot of attention in China nowadays. Many managers are asking whether they can really apply marketing science tools and make their business processes more efficient. In a way, China today is a little bit like the US 30 years ago, in terms of the application of marketing science tools. And I think the examples that you've just given us provide a confirmative answer.*

**JL:** And you have to have somebody do the work who has the skills to do it now.

We found that many of our students—again we have mostly MIT people—but also a sizable number of them from Wharton, who understood what we were doing and could translate it. And you got to translate it.

**ZK:** *In a way, MBA students are really like a bridge between academics and practitioners.*

**JL:** Exactly. And we turned out a lot. If you think about the process of building a model or doing a project like this, first of all, you have to gain entry into the company. And you'd like to get it at a pretty high level because you frequently need a champion as it's not going to be done immediately. It's going to cost some money.

**ZK:** *At least, it's a one-of-a-kind problem, so you probably need a lot of communication between the company and the developers.*

**JL:** Absolutely. So you go in, and you go in with priors usually, a feeling, a hypothesis about what you might do. And then you do a lot to update that because you get the manager to articulate the problem. You go and talk to other people. Then you may come up with a model of some kind. But then you need data and you need to test the model and be sure you are doing it. And then one of my colleagues says that you should ask the manager, or discuss with the manager how he and you are going to evaluate the results, what is the success.

**ZK:** *I presume that by success, you mean both for the company and in terms of knowledge creation.*

**JL:** That's right. The company isn't to worry about that, which is okay. And I will say that the companies have very complicated objectives sometimes. But I usually say that if you can increase their profits, they can figure out what to do with them.

But then you go on. And you have to... You learn by trying to fit the model with the data, but the model is wrong, and the data is probably right. Or you mean you may need different kind of data. It's a circular process. ■

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Zhang Kaifu is Assistant Professor of Marketing at CKGSB. He holds a Ph.D in management from INSEAD. His most recent research explores both theoretical and empirical issues related to media, advertising and the Internet.

To watch the video of this interview, please log on to CKGSB Knowledge: [knowledge.ckgsb.edu.cn](http://knowledge.ckgsb.edu.cn)





# *Leadership's* ..... *Blue-Eyed Boy* .....

*By Neelima Mahajan*

**Marshall Goldsmith's brand of leadership appeals to everyone—from Fortune 500 CEOs to the layman. What makes him so popular?**

**A**t first glance, Marshall Goldsmith, a bald, sprightly man with icy blue eyes, a fringe of white hair and ears that stick out, looks like a pixie. He darts around the room with the energy of a two-year-old. It's fun to watch him walk—not an easy walk to imitate. When he teaches, he bounces from one end of the room to another, while his head stays stiffly in place and his arms straight. On most days, you'll find him wearing a green Polo shirt and khaki pants, his trademark attire somewhat akin to Steve Jobs' black turtleneck and blue jeans. His face breaks into an easy smile as he talks about his favorite subject, leadership and executive coaching. The words 'no', 'but' and 'however' do not exist in his vocabulary and if you make the grave mistake of uttering any of these words in front of him, he'll probably grab your hand mid-sentence and reprimand you.

When you meet him the first time, it's hard to take him seriously—and easy to dismiss his teachings as cloying, and him as just another self-help guru. But when you look deeper, you'll realize there is more to him than meets the eye. Goldsmith has the CEOs of many Fortune 500 companies eating out of his hands. People like Ford CEO Alan Mulally swear by him and pay through the nose to have some face time with him. He has worked as a consultant for companies like 3M, IBM, Philips and American Express. Over the years, Goldsmith, one of the world's foremost executive coaches and a "philosophical and psychological Buddhist" by his own admission, has built a stellar reputation in the leadership firmament and rubs shoulders with the likes of superstar coaches Ram Charan and Gary Ranker. He was ranked among the top five executive coaches according to *Forbes* magazine, and has consistently featured in the Thinkers 50, a ranking of business and management thought leaders.

At the heart of Goldsmith's success is his approach to coaching, which focuses squarely on the individual leveraging his or her own ability to bring about change. "The key variable for success in positive long-term change is not a coach or a teacher or a book, it's the person. My job is to really help people figure out what they want to change and then help them learn from everyone around them in the process to find, to facilitate and enhance this change," he says. "No one is better because they read a book or they have a coach or they go to a seminar. People get better because they work hard."

It is this approach that has earned Goldsmith his stripes. Back in the day, when companies were still trying to get their arms around the idea of coaching, Goldsmith introduced the concept of 360-degree feedback in leadership development. He went a step further and introduced customized 360-degree

## About Marshall Goldsmith

*Marshall Goldsmith is a leading executive coach and the author or editor of 31 books on leadership including the bestselling What Got You Here Won't Get You There; MOJO: How to Get It, How to Keep It, and How to Get It Back When You Lose It!; Succession: Are You Ready? and The Leader of the Future. In the bi-annual Thinkers 50 rankings, he was recognized as the number one leadership thinker in the world and the number seven business thinker in the world. He has been recognized as a leading executive coach by various publications including the Economist, Wall Street Journal and Forbes.*

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At the lower level, it's generally important to win, to prove you're right, prove your expertise, and show how smart you are. When you become a CEO, your job is no longer to prove you are smart and win—it's to make other people smart and help other people feel like winners

..... feedback as opposed to generic feedback. The experiment worked. "Our feedback process impacted probably millions of people over the years. Then I started measuring the 'before' and 'after' studies and tried to figure out, what are the keys to people really achieving positive long-term change?" says Goldsmith. That led to 'Leadership is a Contact Sport', a seminal article he co-authored for *Strategy+Business* magazine in August 2004. The premise of the article was simple: leaders who routinely reached out to co-workers for feedback and development made more positive impact on their organizations and themselves. Contact is the key word. "[The article was] a study of 86,000 people and it shows that the key variable for success is the ongoing follow-up of the leader with the coworkers, not so much to speak for the coach or the teacher," says Goldsmith. This article, which got on to the list of *Strategy+Business's* most popular articles,

catapulted Goldsmith to superstardom.

By some quirk of fate, Goldsmith ended up working with the high priest of management, Peter Drucker—he was a board member of the Peter Drucker Foundation for close to 10 years starting in 1996. He had the privilege of working closely with Drucker before his death in 2005. "One of his great comments was that we spend a lot of time teaching leaders what to do, but we do not spend enough time teaching leaders what to stop [doing]," says Goldsmith. That comment struck a chord. And as he pondered over it, he was struck by the power of that seemingly simple statement. As people climb up the organizational hierarchy, they develop some competencies—and habits—that they probably need to get up there. But when they reach the top and become leaders, these habits can become the proverbial millstones around their neck. Worse, they might be oblivious to it.

So what changes as you rise up the ranks? "At the lower level, it's generally important to win, to prove you're right, prove your expertise, and show how smart you are. When you become a CEO, your job is no longer to prove you are smart and win—it's to make other people smart and help other people feel like winners," says Goldsmith. As an example, he talks of Ford's Mulally who says, "Every time I come to work, I tell myself leadership is not about me, leadership is about *them*." That transition from a great achiever that is "all about me", to a great leader that is "all about them" is very difficult. And some of the behaviors that were fine when it's "all about me" do not work at all when it's "all about them".

As Goldsmith thought about it some more, he figured he had a few answers. The result was the *What Got You Here Won't Get You There: How Successful People Become Even More Successful*, a book that refused to get off the bestseller charts for years after its publication in 2007. The book—part leadership, part self-help—identifies 20 habits that can cause successful leaders to fail and offers practical solutions to counter them. So what might these habits be? The 20 that Goldsmith points out include habits like 'winning too much', 'adding too much value', 'not listening', etc. (See 'The 20 Bad Habits'.)

A lot of this is devastatingly simple, but

some are a little counter-intuitive. For example, a lot of us are brought up with the notion that we must focus on the goal and aim to win. When—and why—did that become a bad thing? “The classic problem with successful leaders is winning too much. It’s hard to break the addiction to winning,” says Goldsmith. “When it’s important, we want to win. [When it is] meaningful, we want to win. When it’s trivial and when it is not worth it, we want to win. We have to teach leaders that you don’t always have to be right and win—let others win.” Goldsmith talks about a CEO who was obsessed with winning, so much so that his people stopped challenging him. But one day he was wrong on a decision, and no one pointed that out. The company lost 50% of its market capital in one day. “He was not a bad man—he was brilliant. He was almost right so much that he was intimidating and people wouldn’t challenge him even when they thought that he was wrong,” says Goldsmith. Similarly, being obsessed with the goal can blind us, and distract us from the actual mission.

Another bad habit he identifies is adding too much value. So if someone goes up to the leader with an idea and the leaders thinks

that it is a great idea, his tendency would be to say that this is a nice idea, why don’t you add this to it? “The quality of ideas may go up by 5% but their commitment to execute the ideas may go down to 60%—It’s no longer their idea, but the leader’s idea. It’s very hard for people to stop constantly adding value,” says Goldsmith. Of course, there is a very fine line between ‘adding value’ and ‘adding too much value’ where it is not needed, and that is something a leader has to be extremely careful about. Goldsmith cites the example of a coaching client, Jean-Pierre Garnier, former CEO of GlaxoSmithKline. Garnier had a very interesting observation of his times as CEO. He said, “My suggestions become orders. If they are smart, they are orders. If they are stupid, they are orders. If I want them to be orders, they are orders. If I do not want them to be orders, they are orders anyway.” Recognizing that this was a problem, Garnier decided to change his approach somewhat. As he told Goldsmith, “Before I speak, I stop and breathe and ask myself one question: is it worth it?”

If you look at all of Goldsmith’s work—whether it is through his coaching or his books

including *What Got You Here Won’t Get You There*, *Coaching for Leadership*, and the curiously titled *MOJO*—it is all about helping successful leaders achieve positive long-term changes, for themselves, their people and their teams. Goldsmith’s next book, tentatively titled *Ask What You Can Do*, focuses on the radical idea of teaching employees how to engage themselves. “I now see that the key to employee engagement is not the company or a program or a book, it’s the person and [we can] teach the person how to manage and lead their own engagement,” he says. This book has some parallels with Buddhism, which Goldsmith adopted 30-odd years ago. “It’s a very Buddhist idea—if you want to find the major source of your misery or happiness, just look into the mirror,” he says.

Talking of Buddhism, Goldsmith’s thinking has been influenced a lot by the Buddha’s teachings, earning him the epithet of “The Buddha of the Boardroom” (from *The New Yorker* magazine). “My Buddhism is not a metaphysical or religious Buddhism, but a philosophical or psychological Buddhism. Buddhism really has a lot of influence in terms of my work, my coaching and my teaching,” he says. Take for example, something Goldsmith calls “feedforward”. As opposed to feedback, which is focused on the past, feedforward is about getting inputs and suggestions for the future to help people get better. “In feedforward, you learn to ask for input, listen to the input, thank people [for it], and then use the input as a gift. Buddha said, ‘Only do what I teach if it works in the context of your own life. If it does not work for you, just don’t do it.’ To me that’s a great philosophy,” says Goldsmith.

Another very Buddhist idea is the belief that anyone can change. “Buddha did not believe in the necessity of a fixed identity over time. He believed that we can truly change. Well to me, I believe people can truly change,” he says.

Goldsmith warns against the great “Western disease” which has already razed countries like Singapore and Japan and is now sweeping across China and India. And pray, what is this disease? “I’ll be happy when I get the money and the status, the BMW, the condominium, when I build a big building, when I make a great achievement, when I make the next million dollars. Well, Buddhist philosophy says, ‘No, you won’t’. So in my school of Buddhism, I try to teach people of acceptance of *what is*,” says Goldsmith.

Goldsmith’s brand of leadership is simple and practical, and his solutions are commonsensical. It works for CEOs, and at some level, it works for everyday people in everyday jobs with everyday problems. And that is perhaps what makes him so popular. 📖

# —20 The Bad Habits



- 1 Winning too much
- 2 Adding too much value
- 3 Passing judgment
- 4 Making destructive comments
- 5 Starting with ‘no’, ‘but’, ‘however’
- 6 Telling the world how smart we are
- 7 Speaking when angry
- 8 Negativity, or “Let me explain why that won’t work”
- 9 Withholding information
- 10 Failing to give proper recognition
- 11 Claiming credit that we don’t deserve
- 12 Making excuses
- 13 Clinging to the past
- 14 Playing favorites
- 15 Refusing to express regret
- 16 Not listening
- 17 Failing to express gratitude
- 18 Punishing the messenger
- 19 Passing the buck
- 20 An excessive need to be “me”





# *Leadership is a Series of Acts*

By Neelima Mahajan

## Shalom Saada Saar on how to become a more well-rounded leader

**F**or several decades now, scholars have spent hours and hours agonizing over what true leadership is. But there is precious little on how to exercise leadership. Shalom Saada Saar, Professor of Managerial Practice at CKGSB and Senior Instructor at MIT, has been researching leadership for a long time now and has also coached several hundreds of senior executives and CEOs in the US, Europe and Asia. As he interacted with them over the years, Saar realized that it was high time he found that missing piece in the puzzle and help people exercise true leadership.

The result of this is *Leading with*

*Conviction* (Jossey Bass, upcoming), a book in which Saar and his long-time collaborator and co-author Michael J. Hargrove distill the wisdom that comes from three decades of experience as a professor teaching leadership as well as a leading executive coach. In this interview, Saar describes the contours of his new work:

**Q:** *What was the trigger for this book? What was the void you saw in leadership literature already out there that you wanted to fill?*

**A:** I don't think there is a void as much as the literature on leadership is scattered all over the place. If you look at the work

of Chris Argyris, Howard Gardner or Ronald Heifetz, all these books say what leadership is. And that is very subjective. What is missing, I believe, is how do we get there? The 'how' remains, in my view, an unknown. People say, "I know the seven habits of effective leaders, I know the seven mindsets or the 10 mindsets. What I don't know is that I am in a leadership position, and how do I [exercise leadership]?" This book accepts the literature that has been building up in the last two to three decades and helps the reader understand the 'how'—what one needs to do, almost step by step, to really understand and practice this idea of leadership.

**Q:** *Throughout the book, you lay a lot of emphasis on leadership with a small ‘I’ as opposed to the big ‘L’. Where are you coming from?*

**A:** Most books focus on leaders with the big ‘L’—the Gandhis, the Mandelas, the Churchills, the Kennedys and the Deng Xiaopings of the world. But the reality is that we cannot emulate those leaders. I don’t believe that leaders are born either. The time has come to look for leadership with the small ‘I’. When a receptionist picks up the phone and is very kind to the caller, at that particular moment, he or she actually exercises leadership with a small ‘I’. When a Chinese worker leaves his home for six months or one year in order to provide a living for his family so that his child has a better life, that particular moment to me is an act of leadership.

Leadership is a series of acts—when we accumulate them, we really begin to practice, demonstrate and experience the notion of leadership. So leadership with a small ‘I’ can be about the single parent who is trying to work and raise a child, a team leader who is trying to improve the performance of the team, a division leader, a CEO, a mayor... It is about those who really help life to move on.

I am interested in that small ‘I’. I think we have ignored it. We look at leadership with the big ‘L’ and we read about it, and it makes for fascinating biographies, but to be able to emulate it, I think, most of those books come short. They are great books. Don’t get me wrong, but I think there is a void, there is a missing piece in literature that can look at the average person in the course of the day and what acts he or she takes to exercise leadership because leadership, in my view, is an activity. We often look at leadership as “I want to be the leader”, but if you really dissect leaders, [you’ll find that leadership is] a battery of activities. I am interested in what those activities are.

**Q:** *You just touched upon the fact that you believe leaders are not born. For many decades now, that has been the subject of a constant debate—are leaders born or made. You seem to agree with the second statement.*

**A:** No one has proved yet that leaders are born. Look at the leaders you admire—if you want to look at leaders with the big ‘L’ like the Gandhis, Mandelas and Anwar Sadats of the world—they failed miserably, they met crises unsuccessfully. They were, in many ways, incomplete. But what distinguishes the leader from the non-leader is the ability to look at yourself and understand why you failed, why you went astray, what you did wrong, and whether you were on an ego



There is a common trait to those who are ineffective and the ineffectiveness is largely due to this idea of not knowing who they are. They have no idea of how they come across, what impact they make on others, how they carry themselves, and how they interact with each other

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trip? And as you look at it, you begin to understand yourself, and as you understand yourself, those ideas of leadership begin to evolve. Most of us don’t really exercise leadership, because we are not willing to look at the mirror to understand who we are, what we are, what makes us who we are and this refusal to analyze oneself becomes the Achilles heel that in many ways, deprives most of us from this idea of leadership.

**Q:** *The idea of knowing oneself is one of the key points of your book. However, knowing oneself is surprisingly not as easy as it sounds. What really comes between us and our understanding of ourselves?*

**A:** For so many years, I have coached hundreds and hundreds of executives, CEOs and people from all walks of life—

from governmental agencies, to not-for-profit business organizations. I have come to see that there is a common trait to those who are ineffective and the ineffectiveness is largely due to this idea of not knowing who they are. They have no idea of how they come across, what impact they make on others, how they carry themselves, and how they interact with each other. This lack of knowledge is the greatest barrier to leadership. Knowing oneself is not a new concept—2,400 years ago, Sun Tzu said that the general must know himself because if he does not know who he is, there is no way he can be successful. It really means that you must know your strengths and your weaknesses as those weaknesses can become your biggest derailers.

Let’s talk about Sun Tzu’s premise that the general must know himself and know their enemy. We understand what it means to know oneself and it is not easy to achieve. But the second part is to know your enemy. I ask my students, “Who is the enemy?” They say, “The competitors.” I say, “No.” They say, “The boss.” I say, “No.” That’s when I think of Pogo’s famous line, “All too often, the enemy is us.” We need to know ourselves because the enemy sometimes is inside us, and we need to understand that and how to manage it and correct ourselves.

We need to look deeper into ourselves. The process is painful—it is like peeling an onion in order to understand what our strengths and weaknesses are, what our dragons are, what is it in our way that can deprive us of being successful and, most importantly, being happy.

**Q:** *Your book is organized around different ‘pillars’ or dimensions of leadership such as self-awareness and balance (See ‘Pillars of Effective Leadership’). Do good leaders have to have all these dimensions?*

**A:** Often leaders might be very good at one dimension but not good at others. For example, I know many executives who have a very good vision and they can envision the future. But when it comes to the dimension of communicating that vision—not just talking, but listening, probing and asking—they come up short. So being good at one dimension is insufficient. You can communicate very well, but if you don’t have a clear vision, if you don’t know how to execute, if you don’t know how to work through others, it is incomplete. Most leaders are incomplete. The challenge is to have as many dimensions as possible, to have them embedded in you in order to really exercise leadership.

## Pillars of Effective Leadership



**Q:** *Have you ever come across someone who is truly an exemplary leader by these standards?*

**A:** I have not met individuals who, I would say, are complete on those dimensions. That is why I call it a 'leadership journey'—that we never actually get there. It is like one battle at a time to conquer a dimension and to embed it in us. I have not [come across] a person, [either] small 'I', or big 'L', who can actually serve as a role model. Think of any leader and I can tell you his or her flaws. As great a leader as he was, Gandhi was a terrible father. Nelson Mandela would perhaps be the closest [to being a great leader] just because of the suffering he had to encounter to understand himself and drive this incredible revolution. But even Mandela, in the last five to seven years has not been the role model we would like him to be. I believe that the human being is not a perfect machine, so I am wary of identifying a person as a role model because sooner or later, most role models disappoint us.


**Q:** *This also points to the whole question of balance or the lack thereof, which is also listed as one of the essential pillars of leadership in your book. Have you come across any example of leaders who are able to maintain balance, whether it is between the head and the heart, hard and soft skills, or stability and change?*

**A:** Balance is not accomplished by the way—like any balancing act, it is trial and error. I have seen people who want to be successful, so they put all their weight on their professional engagement. They work hard, they stay [in the office] for many hours, they go to school and get degrees, they sacrifice weekends, they don't see their spouses and kids. They do whatever it takes. And all of a sudden, they feel that something is missing. One of my observations—of Chinese executives in particular—is that even though they have reached everything in terms of material things, they are not happy. I ask them why. They say it's because something is missing in their lives. So it takes a long time to find a point of equilibrium, a lot of trial and error. Some people are better at it, they know how to balance between work and home, between being an individual and being a member of the team, between using the left brain and right brain, but I don't think it is a common practice.

Most books, especially in the last five years, have been encouraging people to be less of managers and more leaders, so less command-control, and more leader-facilitator or moving from a warrior to a diplomat. It is very misleading and dangerous. That's why we call for balance—we need to remain commanding and controlling in situations that require control. The earthquake in Japan did

not call so much for leadership. It called for managers to actually control the damage, to execute the orders, to provide emergency relief and in many ways, they came short. Leadership is a balancing act and it would mean being focused on the task and being people-oriented. One is not more important than the other. It is dangerous to say, "Let's walk away from management skills and embrace leadership skills." I believe, that let's hold the management skills, but add to the toolbox more leadership qualities. It's not either-or, but both. Adding more tools is the secret to effectiveness.

**Q:** *After this book, you are embarking on a new project on Chinese leadership. What is that about?*

**A:** China is the next most exciting laboratory for social scientists. In the next book I am going to take 15 to 20 Chinese executives and CEOs, and really shadow them, follow them and see what they have accomplished, what their strengths and weaknesses are. I would like to see what are the common patterns and common denominators of Chinese leaders and managers versus their Western equivalents. 

*To watch the video of this interview, please log on to CKGSB Knowledge: [knowledge.ckgsb.edu.cn](http://knowledge.ckgsb.edu.cn)*



# Getting Beijing's Taxis to Move, not Sit

How simple economics can make it easy for commuters to get a cab in Beijing

By Brian Viard

Some time back, I was standing outside a Beijing subway station desperately hoping to hail a cab for my friends visiting from out of town. Thirty minutes later, I was still there—my arm was tired from waving but no cab, even some that were empty, had stopped. So we opted for the much longer—and tiring—subway ride instead.

An *Economist* article titled 'All Hail: Dissent in the Capital's Taxi Ranks' (March 31, 2012) reported on the difficulty that Beijing residents have had finding cabs and the government's possible interim solution. Regulated taxi fares have barely increased over the last decade while a key cost for cabs—gasoline—has increased significantly. As the *Economist* article says, "Beijing's base fare of 10 yuan (\$1.60) has not changed in a decade. Charges for travelling farther than the minimum fare were adjusted in 2006, from 1.6 to 2 yuan per kilometre. Since 2009 drivers have added a small fuel surcharge for longer rides." In a city where the average income has increased so much, the increase in fares is hardly substantial. As a result, cab drivers often choose not to drive during heavily congested periods when the meter moves slowly. Increasing rates would fix the problem but the government is reportedly reluctant to do this for fear of increasing officially-reported inflation and because it wants to ensure taxis are readily available to the expanding Beijing middle class.

The government's proposed solution is to supplement cab drivers' incomes by RMB 300 per month. While these transfers would help partially restore the incomes of hard-working cab drivers who have seen their profits decline over the years, this won't help you the next time you are standing on the street waving frantically for a cab. Here's why: there is a simple principle of economics at work here that is deterring cab drivers from behaving the way the government wants them to. Cab drivers, like the rest of us, usually make decisions by comparing marginal benefits and marginal costs.



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There is a simple reason why cab drivers are not behaving the way the government wants them to. Cab drivers, like the rest of us, usually make decisions by comparing marginal benefits and marginal costs

A cab driver facing a traffic jam may take some comfort in his monthly salary having increased by RMB 300 but it will make him no more likely to pick up a ride. Here's why: in deciding whether to sit out the jam or pick up a fare, the driver's incentives remain the same. He will compare the marginal cost of the ride—primarily his time and the gasoline burned—to the marginal benefit, the fare he will receive. Since his time and gas prices remain unchanged and fares have not been adjusted, the calculation remains the same as before he received that month's extra RMB 300.

The same principle can be applied to address the particularly acute shortage of cabs during rush hour. During peak times congestion is worse and the cab driver cares relatively more about the waiting fare than the distance fare. Therefore, to stimulate a greater supply of cabs during rush hour, increasing the waiting fare is more important than increasing the moving fare. This increases the marginal benefit of driving during rush hour.

Let's return to one of the government's suspected goals—making taxis readily available to the middle-class. Rather than hindering the pursuit of this goal, raising fares will help. Higher fares increase effective supply because drivers are less likely to shut down during times of congestion. Unless potential riders are priced out of the market at the new rates (unlikely since as the *Economist* notes, taxi rides are a "rare bargain" in Beijing) this will increase availability to middle-class commuters. At the same time, the city can better utilize the cabs on the road and reward the cab drivers for what they do best—driving not sitting. ■

*Brian Viard, Associate Professor of Strategy and Economics at Cheung Kong Graduate School of Business, explores the workings of economics in everyday life and business in China through a column called Invisible Hand Revealed. It appears on CKGSB Knowledge every fortnight. Please log on to <http://bit.ly/NKczrW> for the full list of columns.*



# Snaring the Dragon

## What could stop growth in China and what can the country do about it?

By Bennett Voyles

**A**fter 30 years of strong growth, some observers worry that China won't be able to keep it up for much longer. Many countries, such as South Africa and the Philippines, have reached middle-income status only to hit a wall just when they seemed to be on the verge of becoming rich.

Various factors tend to bring promising economies down, but the most common is the difficulty in transitioning from a country that wins with low labor costs to one that wins because of its know-how. China is already on the cusp of such a transition. As rising labor and real estate costs, and a host of other factors erode competitiveness, China is struggling to find a new formula for growth.

In the long run, say 100 years or so, growth seems to correlate most strongly to institutional strength, says Dirk Willem te Velde, an analyst for British think tank, the Overseas Development Institute. In the short term, however, other factors play a role. In the case of China, some experts point to demographics, pollution and climate change, foreign financial crises and overinvestment as the key risks ahead.

### The Demographics Slump

Very gray and very male, the China of tomorrow faces demographic challenges that could have serious economic repercussions. A 2011 report by Swiss Re estimates that low fertility rates are leading to a steady decline in the working age population "as far as the demographer's eye can see". At the same time, it will be getting older (see 'No Silver Bullet', page 25). China's cohort of workers in their 20s is set to decline by 35%, 75 million, over the next 20 years. Also, the fraction of the population over 65 will swell.

Some analysts estimate that an imbalance in the sex ratios brought on by the one-child policy will create a large group of involuntarily unmarried men. In 2000, only 5% of men in their late 30s were never married. By 2030, this ratio could rise as high

as 25%. The consequences of this are not known yet, but Swiss Re notes "it is difficult to see how this could prove a plus for either economic performance or social cohesion".

### Hidden Costs

In a less densely populated country, environmental protection is often seen as an almost aesthetic concern. But with 1.3 billion people, it's about survival. Already, with an estimated 200,000-600,000 deaths a year due to air pollution, the costs of environmental degradation are high, but they could get worse.

Resource scarcity could also threaten growth. Energy and food are threats, of course, but in northern China, even water may be difficult to find. On a per capita basis, China has only 25% of the average water supply of other countries, and of its total supply, 80% is in the South, far away from the centers of agricultural production in the North, according to a Columbia University report. This is not a theoretical problem: already, over the last 50 years, 24,000 villages have been abandoned because of desertification, according to the report.

In the latest Five Year Plan, the government set ambitious goals to use its resources more efficiently. The government has earmarked \$680 billion over the next 10 years to water system improvements. But will they reach their targets?

In another report titled 'Drying Up: What to do about droughts in the People's Republic of China', the Asian Development Bank warned that, when it comes to water, there are a whole host of challenges, including "uneven distribution of water resources, uneven rainfall patterns, and a natural proclivity to droughts—all in addition to climate change and a degraded environment".

### Foreign Financial Crises

"China's growth model has done miracles to the Chinese economy but itself, it has brought weaknesses. Much of the growth is investment-driven so it relies on huge

domestic savings and in large part on the external economy," says Li Wei, Professor of Economics and Emerging Markets Finance and Director of the Case Center at CKGSB. The Eurozone crisis means that China can't count on Europe as a big consumer for its products. "We will not only see trade volume falling, but also a likely rise in disputes with Europe on the trade side," he says.

With the euro on the verge of a breakdown, Chinese companies and policymakers have had some time to plan their response to a crisis. However, if the situation worsens in Europe and in the US, particularly if there is an energy crisis at the same time, exports could be hit hard: the International Monetary Fund predicted in February that a severe downturn in Europe could cut Chinese growth by almost half.

One Asia-based venture capitalist says, on condition of anonymity, that there is no way China can avoid hitting the wall along with the US and Europe. The only way the country might have avoided it, he says, would be if it had a few more years to convert to an economy based on domestic consumption. However, he says, time is evil and the West is collapsing faster than China's strategy permits.

### Overinvestment Concerns

Perhaps the greatest immediate concern is the threat of overinvestment. Superhighways, high-speed trains, airports, housing—in almost every category, China is building a lot of it. Will the economy be strong enough to use all that capacity?

That's a crucial question. Development economist te Velde says the trick to avoiding the middle-income trap is to make sure that the investment leads to more productivity. Get it right and you end up with a rich country. Get it wrong and the country stops moving forward.

Some numbers suggest that at least a temporary rollback is already underway. In housing, for instance, Jack Rodman, a Seattle-based specialist in Chinese non-performing loans, points to bank analyst estimates that housing

prices fell by 20% in 2011. UBS forecasts another 5-20% drop of house prices in 2012.

Rodman, President of Global Distressed Solutions, thinks that real loan performance numbers are probably understated at this point. "It would be typical of China to warehouse inventories rather than report they did not meet municipal objectives and disappoint the party officials," he says.

Another complicating factor in estimating performance is the size of the informal banking sector. Such 'shadow banking' may be almost as large as the formal banking sector, which Rodman estimates loaned RMB 208 billion compared to RMB 211 billion by official banks in 2011.

That could be bad news in a crisis, he says, because informal loans tend to have shorter maturities and higher interest rates than formal loans.

Looking back on all the bubbles in the last 40 years of his career, Rodman says the common denominators were always the same: abundant and poorly priced liquidity, rapid loan growth in banks, a property bubble, a belief that property can

only go up, misallocation of state assets, weak regulation and lack of transparency. China has all these attributes and more, he says.

### Avoiding the Trap

How likely is it that the dragon will step into one of these snares?

Opinion is divided on whether China needs to brace itself for a big economic reversal, but Stephen Roach, the former chairman of Morgan Stanley Asia, and the bank's Chief Economist for nearly 30 years, remains bullish.

"I categorically reject the view of many that the Chinese economy is headed for a hard landing," says Roach, who is now a lecturer at Yale School of Management. "Unlike three to four years ago, when the global crisis pushed China to the brink of full-blown recession, the deceleration over the past year has been far more benign."

"In fact, the 3.8 percentage point slowing of GDP growth over the most recent four-quarter period is less than half the far more precipitous deceleration of 8.2 percentage

points that occurred in the depths of the Great Crisis of 2008-09," he adds. "Moreover, Chinese authorities have plenty of ammunition to stave off any further downside risks to the economy—short-term policy benchmark lending rates of 6.5% and a fiscal deficit of just 2% of GDP."

"Compared with the developed world's zero or near-zero policy interest rates and outsize budget deficits, China is in much better shape to deploy countercyclical stimulus in order to avoid the dreaded hard landing and get on with the heavy lifting of its all-important structural rebalancing," he says.

Longer term, Roach is also optimistic. "If (China) stays the course of the pro-consumption rebalancing that is laid out in the 12th Five Year Plan, I am confident that it will avoid the middle-income trap and all the other concerns of the China doomsday crowd," he says.

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Signing up stars like Didier Drogba won't catapult Chinese football into the big league  
<http://bit.ly/SuNZR2>



#### Customers aren't Biting

Prof Bing Jing on why Burger King's ambitious China expansion plan is flawed  
<http://bit.ly/SuvBGa>



#### World-Class in Beijing

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Is the Chinese economy strong enough to weather the Euro crisis?  
<http://bit.ly/R633im>



#### Two to Tango

What the Jaguar Land Rover-Chery joint venture might have in store  
<http://bit.ly/O7T8Ko>



# INSIDE CKGSB

50  
Betting on  
Innovation

51  
Emerging  
Markets Series

52  
Cutting Edge  
Marketing Ideas

54  
Global Events

56  
Clifford  
Chance's  
Boardroom  
China Briefing

## Steady Steps to a Promising Future



*Dear Friend of CKGSB,*

I hope you have enjoyed the thoughtful and insightful articles in this issue of *CKGSB Magazine*. Both this magazine and the *CKGSB Knowledge* website ([knowledge.ckgsb.edu.cn](http://knowledge.ckgsb.edu.cn)) strive to identify people, companies and trends that will shape not only the future of China's economy, but also the global business landscape.

This is tremendously important work. China's domestic consumption, the globalization of its companies, its nascent spirit of innovation—these are among many facets of the nation's culture and economy that will profoundly affect global business in coming years. Every business leader around the world needs to pay attention to China's ongoing economic and cultural renaissance, regardless of whether they do business in China—regardless, even, of whether they do business with Chinese companies.

In the following pages, you will read about some of CKGSB's recent global executive education programs and events, which are a natural extension of our scholarly research. In addition to offering tailored insights from CKGSB's faculty, these programs and events facilitate true two-way interaction and exchange of ideas between business leaders from China and the world. By leveraging CKGSB's highly influential alumni network and renown in China's business community we are truly putting the global business community into conversation with the people who are reshaping China and the world's business landscapes.

As you will read, some of the ways in which CKGSB has been facilitating top-level interaction between people from China and the world over the past several months include: inviting internet guru Kai-Fu Lee to speak to business leaders and members of the UK Parliament at London's Westminster Palace; bringing together successful businesspeople from among CKGSB's students and alumni to meet with their counterparts at the China-France Business Forum in Paris; and delivering a custom Boardroom China Briefing in Beijing to the global management committee of leading law firm Clifford Chance.

One of our next opportunities to bring together people from around the world to share knowledge and build personal connections will be CKGSB's 10th Anniversary celebrations in Beijing on the 22nd of November. Among distinguished guests from business, government, the non-profit sector and academia there will be one extremely special guest of honor: Mr. Li Ka-shing, to whose philanthropy we owe the existence and continuing success of CKGSB. I look forward to this special day and very much hope to see you there.

*Best Regards,*

A handwritten signature in black ink, appearing to read 'Xiang Bing'.

Xiang Bing  
Founding Dean, CKGSB

# Betting on Innovation

Tech evangelist Kai-Fu Lee on innovative business models seeded in China

By Neil Selby

**T**he latter half of the twentieth century has been defined by predominantly US-generated business models.

The geographically large, unified, predominantly single-language US market has led, over the last 50 years, to concepts of branding, mass marketing and category champions that have conquered developed markets around the world. These market conditions have provided aspirational business approaches to developing market entrepreneurs.

So, whilst the 1950s, 1960s and 1970s were defined by companies such as McDonald's, Wal-Mart, FedEx and Toys"R"Us, the 1980s were characterized by the likes of Blockbuster, Home Depot and Dell. The latest group to 'conquer the world' could arguably be the likes of Starbucks, eBay, Amazon, Google and Facebook.

These latest few companies, some of which were born in the heady entrepreneurial heartlands of Silicon Valley, display a technological prowess and invention capability that have enabled them to reach and connect huge numbers of customers with minimal cost and create enormous revenues through advertising and value-added services.

Kai-Fu Lee, China's internet guru, believes that the next group to 'conquer the world' will come from China. According to his address to the UK's Houses of Parliament in June 2012, courtesy of CKGSB, China's future dominance of the internet will be due to three main factors: size and market context; the emergence of new usage preferences driven by Chinese consumers and indigenous adaptive innovation, a process he intends to encourage and accelerate.

## China's Netizens

The size of the Chinese internet market is dazzling. By 2015, it is estimated that there will be more than 750 million internet users in China, with urban internet penetration reaching 66% and rural penetration 30% largely driven by mobile internet as cheaper



Kai-Fu Lee addressed the All Party Parliamentary Group (APPG) for East Asian Business in London on June 12

Kai-Fu Lee is a leading executive in the global technology sector, currently based in China. In September 2009, Lee founded Innovation Works, a \$115-million venture capital incubator which aims to foster Chinese start-ups in the mobile, internet and computing sectors.

and faster mobile devices proliferate.

Chinese consumers are on average 25 years old (compared to 42 in the US) and spend on average about 19 hours a week on the internet: four hours streaming video or music (twice as much as the US); four hours chatting and instant messaging (10 times as much as in the US); four hours online shopping; three hours on gaming; 2.5 hours on social media; 1.5 hours reading news and less than half an hour on e-mailing (compared to five hours in the US).

To the young Chinese consumer, starting out in life, the internet represents a world to be explored in which everything is possible—money, fame and even, increasingly, justice through the connecting power of microblogs. More than 33 million follow Lee on Sina Weibo (the equivalent of Twitter) and eight million people in China follow his own microblog. "Microblogging leverages the wisdom of the crowds," he says. "The good things get forwarded and bubble up to the top."

This makes the internet a very powerful tool that attracts the attention of the leaders of all societies, whatever social models they represent. Lee believes that progress in harnessing the potential of the internet is dependent upon working with society's leaders and understanding their contextual concerns. "I, as an individual," he says, "want to bring the most advanced technologies and the greatest legal access to information that I can. If accepting some law is a requirement to make that goal possible, I have no issues with accepting that law. Activities such as microblogging will accelerate thinking about dissemination of information and cause our leadership to reflect. Whether such reflection causes change is not for me to speculate."

## New Usage Preferences

According to Lee, usage preferences that are particular to the Chinese market have repeatedly undermined the one-size-fits-all American model. eBay, for instance, introduced the PayPal payment system that bore no account of the fact that most Chinese do not own credit cards and was, therefore, doomed to failure. Taobao's Alipay system resolved the issue by introducing an escrow account that only releases funds once a transaction is completed. Alipay is, therefore, now by far the dominant payment system in China.

Indeed, Lee is critical of US companies that aim to impose global models without assembling sufficient local knowledge. Local insight teams, he maintains, can bring enormous value by capturing the enthusiastic

engagement Chinese internet users' display. Two such examples are Master Kong and Budweiser. In partnership with Tudou, China's biggest video-sharing website, Master Kong—the leading beverage and noodles brand—asked consumers to shoot videos with romantic stories about its new jasmine tea. Within a month, 300,000 consumers participated and 3 million users watched the videos—which Master Kong used for additional conventional advertising. In a further collaboration with Tudou, Budweiser invited users to edit its 'innovative ants' (similar in sound to creative ideas) commercials. More than 2,000 edits were submitted which attracted 10 million visits.

Unique Chinese creativity can also be brought to bear on revenue generation, says Lee, citing the example of QQ's avatars. Each QQ user is assigned a free standard avatar which owners are invited to dress more individually after three months for a small consideration. Those who ignore the call to improve the avatar tread dangerous ground. Failure to respond results in

an avatar stripped of all but undergarments and potential loss of online 'face'.

### Adaptive Innovation

Chinese companies, he stresses, are constantly innovating in the internet space. Clever, resourceful, fast, scrappy—and often unscrupulous, “the Chinese internet is like a gladiatorial, no-holds barred, fight to the death”. New ideas are constantly surfacing driven by imitation, localization, iteration and innovation where the speed of iterative trial and error is exponentially fast. Sina Weibo, he says, is a perfect example. Only three years old, it has 200 million users, is valued at \$2 billion and now has features that its original source of inspiration, Twitter, is beginning to emulate.

This is why Lee has created Innovation Works, an internet venture incubator. As the new growth drivers of mobile internet, e-commerce, social networking and gaming redefine the internet space, the new global game changers, he believes, will be found in China.

In Innovation Works, he has brought together Chinese entrepreneurs who are hungry for success, have grown up with the internet, know the local market and are willing to iterate quickly. He speaks of companies such as Diandian, XingCloud, Buding, Tapas, AppChina and Nevel as the big names of the future and how Innovation Works helps them to build prototypes, iterate and improve, market, promote and prepare for funding and growth. Now undoubtedly the number one brand in seeding tech start-ups in China, Innovation Works, he believes, is creating the future—not only in China, but also on a global scale.

“China's growth will continue to outpace that of the rest of the world,” he says. “And it will become a technology giant—well, you can bet on it. It's a bet I can guarantee you will win.”

*Neil Selby is Director of Executive Education at CKGSB.*

## Emerging Markets Series

CKGSB works with Oxford University's budding entrepreneurs to explore emerging market opportunities

In 2011, CKGSB joined the Oxford Entrepreneurs Society as Knowledge Partner of the Emerging Markets Series to provide budding student entrepreneurs with the opportunity to learn about the business and entrepreneurial culture of emerging markets such as China, India and Russia. CKGSB assists in coordinating the series of keynote speeches given by some of the world's most successful businesspersons.

Founded in 2002, the Oxford Entrepreneurs Society is now the world's largest student entrepreneur society, with over 7,000 members, and was recognized by the Department of Trade and Industry as one of the top three organizations promoting entrepreneurship and innovation in the United Kingdom. With a mission to inspire entrepreneurship in the student community, the society organizes speaker events, professional development programs and a mentorship scheme.

In May of 2012, Lord Nat Wei was invited to address the society at an intimate Emerging Markets Series event. As a previous advisor to the UK government and one of the founders of the Shaftesbury Partnership and Teach First, he has a wealth of experience to call upon and



share with promising young entrepreneurs. Lord Wei discussed the entrepreneurial opportunities that arose with the creation of the internet and explained what led him to work with social enterprises. He used his own experiences and achievements to inspire the audience. Lord Wei is one of the co-founders of Teach First, a UK-based social enterprise, which addresses educational disadvantage

by transforming exceptional graduates into effective, inspirational teachers and leaders in all fields. The organization is placed 7th in *The Times* Top 100 Graduate Employers in the UK, and the model has now been applied in 20 countries worldwide, including China, Brazil and India.

In addition to his achievements in the social entrepreneurship space, Lord Wei was appointed as Chairman of the All Party Parliamentary Group (APPG) for East Asian Businesses, established earlier this year. CKGSB serves as the APPG's secretariat.

Other distinguished speakers featured in the Emerging Market Series include Vladimir Yakunin (President, Russian Railways), John Porter (Chairman, Sinopec), Ian Scott (former Director, World Bank and Executive Director, Emerging Markets Symposium), Peggy Liu (Chairperson, JUCCE) and Frank Tang (CEO and Managing Partner, FountainVest Partners and CKGSB alum).

Through the speaker events, a range of inspirational entrepreneurs of today met with some of the promising business minds of the future, sparking inspiration and connecting with the future business leaders of tomorrow.



# Cutting Edge Marketing Ideas

Leading global marketing academics share their ideas at CKGSB

## David Bell

Xinmei Zhang and Yongge Dai Professor of Marketing, Wharton School, University of Pennsylvania

Why the key to successful e-commerce, as with brick-and-mortar retail, is still location, location, location.

*“The two lessons [of a successful e-commerce strategy] are: number one, find the customer’s pain-point [under-served need], and number two, don’t give everything away, retain some value for the firm. You’re going to need that value to grow in the future and, in fact, to build the company, to build better products and services going forward.”*

## Jean-Pierre Dubé

Sigmund E. Edelstone Professor of Marketing, Robert King Steel Faculty Fellow Booth School of Business, University of Chicago

How brick-and-mortar retail can compete with e-commerce without devaluing products in a “race to the bottom”.

*“Show-rooming is putting price pressure on traditional retailers and making it very difficult to sustain a network of physical stores. Also from the manufacturers’ point of view, it is also becoming harder to sustain a selling environment where the intermediary is actually adding value to the channel by helping you with point-of-purchase marketing.”*

The CKGSB Distinguished Speakers Series is an elite series of forums, panel discussions and speaker events which feature global thought leaders in conversation with CKGSB’s accomplished faculty. On June 26, CKGSB Dean’s Distinguished Chair Professor of Marketing, Associate Dean of Global Programs and Director of Social Media and Customer Information Management Center, Sun Baohong and Visiting Associate Professor of Marketing, Jack Xinlei Chen, invited five global thought leaders in the field of marketing from leading international business schools to CKGSB’s Beijing campus to discuss new marketing trends.

The forum addressed new tools, new strategies and new opportunities across the field of marketing with Prof. David Bell (Wharton School), Prof. Darren Dahl (Sauder School of Business), Prof. Jean-Pierre Dubé (Booth School of Business), Prof. John Little (Sloan School of Management) and Prof. Karunakaran Sudhir (Yale School of Management), who shared their recent research and related their findings to the Chinese market.



### John Little

Institute Professor of Management Science  
Professor of Marketing, Sloan School of  
Management, MIT

Why developing a marketing science community in China is essential to encouraging sophisticated marketing practices.

“There has been marketing in China for a very long time; it’s a nation of channels of distribution, skillful marketing practice and probably some scurrilous marketing practice—but no marketing science. What marketing science tries to do is to use models and data to describe marketing activities and improve them.

### Karunakaran Sudhir

Professor of Marketing  
Yale School of Management, Yale University

Why leveraging social media is an effective alternative to traditional advertising.

“Social media is a serious alternative to advertising because of the scale and efficiency you can have. You can listen, see and record. Message control is something people worry about but by and large, for most companies it turns out not to be much of a problem.

### Darren Dahl

Fred H. Siller Professor in Applied  
Marketing Research, Professor and Chair,  
Marketing Division  
Sauder School of Business, University of  
British Columbia

Why developing creativity skills is essential to becoming a true business leader.

“The number one thing leaders of the future need is creativity. You can develop creativity by focusing on four things; learning how to play, learning how to think differently, learning how to be curious and observe, and learning how to experiment and fail. When you can do these things, you will develop the creativity you need.





## APEC China CEO Forum—Deepening Sino-US trade relations

**June 8, Beijing**

Political and business leaders from around the world came together in Beijing for the 2012 Asia-Pacific Economic Cooperation (APEC) China CEO Forum. At the forum, CKGSB Dean Xiang Bing chaired a plenary discussion session on ‘The future of China-US economic and trade relations: collaboration and cooperation’, which focused on the hot topic of Sino-US trade. The session included in-depth exchanges from a political, economic and commercial perspective. Sitting on the discussion panel were: US Ambassador to China Gary Locke; former Vice Minister of Foreign Trade and Economic Cooperation, and the chief negotiator for China’s WTO accession, Long Yongtu; and Nick Reilly, former President of General Motors Corporation Europe. With such prestigious global business leaders present, the APEC CEO Forum involved discussions of major political and economic issues such as promoting trade liberalization and economic cooperation. Commenting on the importance of the China-US relationship Dean Xiang Bing said, “A good bilateral economic and trade relationship is not only beneficial to both countries, it is also crucial in terms of global development.”



*CKGSB strives to facilitate two-way knowledge exchanges between China and the global community. Through the school’s organization of and participation in global events, CKGSB drives a global conversation of business excellence and leadership. CKGSB’s events provide a platform for ideas, inspiration and innovation throughout the school’s influential community.*



## CKGSB’s China-France Business Forum—New Ways of Engaging

**June 26, Paris**

The first China-France Business Forum, co-organized by CKGSB with HEC Paris and the Chamber of Commerce and Industry of Paris, gave Chinese and French business people an opportunity to consider how France and China can benefit further from mutual co-operation. The forum encouraged the gathered French and Chinese business leaders (including a large cohort senior Chinese business leaders who are students and alumni of CKGSB’s EMBA and Executive Education programs) to visualize the steps needed to strengthen the business and economic relations between France and China. Participants discussed the ties that already bind the two countries and the tools needed to further deepen business cooperation in the future.

## Harvard Kennedy School Globalization Forum—Exploring the Global Forays of Chinese Companies

**June 19, Cambridge**  
CKGSB Dean Xiang Bing shared his insights on the globalization of Chinese companies at the fourth Harvard Kennedy School (HKS) Globalization Forum. The forum, hosted at the HKS campus, gathered scholars, advisors and policymakers for “candid conversation and meaningful collaboration on key topics related to United States-China relations”, according to organizers. The globalization forum’s focus on China-US issues was timely and it provided an opportune moment for Xiang to share CKGSB’s unique on-the-ground insights on the vital role that Chinese firms will play in the globalization process in coming years.



### CKGSB Distinguished Speaker Series—Practicing Local to Global Business Strategies for Success

**July 17, Beijing**

CKGSB Professor of Strategy Cho Dong-Sung invited Moon Kook-Hyun (pictured on the bottom right), former CEO of Yuhan-Kimberly and former South Korean presidential candidate, to talk about his fascinating career in international business, environmental management, politics and academia and how he has helped an international company flourish in East Asia. Moon also discussed the importance of considering both the local and global markets in the business world. Cho Dong-Sung, who specializes in the development and implementation of business strategies, competitive strategies, business culture and philosophy gave a presentation on “Localization” (a combination of two words of “localization” and “globalization”), a concept he has researched extensively.



### Global Business Strategy: China (North America Edition)

**August 8-10, New York City**

CKGSB's Global Business Strategy: China program is held in partnership with Columbia University's Columbia Business School (CBS) in New York and provides a platform for North American executives to develop crucial insights and understanding of best practises that will help their organizations succeed in China. The program offered insights from CBS and CKGSB's leading faculty with Founding Dean and Professor of Accounting Xiang Bing, Assistant Dean and Professor of Marketing Sun Baohong (pictured on the top left), Assistant Dean and Professor of Strategy and Innovation Liao Jianwen, and Professor of Economics Leslie Young each delivering keynote speeches and moderating panel discussions across the three-day program.

### Upcoming Event: CKGSB 10th Anniversary Celebrations



**November 22, Beijing**

On November the 22nd in Beijing CKGSB will celebrate the 10th anniversary of its founding. The day's events will kick off with the CKGSB 10th Anniversary Business Forum, held under the theme *China and the World*. In the afternoon, the CKGSB 10th Anniversary Ceremony will provide an opportunity for CKGSB to look back at the school's accomplishments and look forward to the next decade. Speakers at the Anniversary Ceremony will include CKGSB alumni, leading scholars, prominent government officials and one singularly esteemed guest: Mr. Li Ka-shing, whose philanthropic foundation has provided CKGSB with the financial support indispensable to the school's mission of generating world-class original research, delivering the highest standard of teaching quality and remaining independent and not-for-profit.

### CKGSB Summer Forum—New Asia, New Opportunity

**July 20, Kunming**

Held in cooperation with the Yunnan Provincial Government, the CKGSB Summer Forum brought together business and government leaders of East Asia to discuss opportunities within the region. The annual forum endeavors to promote localized cooperation between East Asian nations. In this year's forum, distinguished speakers included CKGSB Dean Xiang Bing, Secretary of the CPC Yunnan Provincial Committee and Provincial People's Congress Director Qin Guangrong, former CEO of Yuhan-Kimberly and South-Korean politician Moon Kook-Hyun, Research Fellow at the Department of Foreign Economic Research of the Development Research Center of the State Council (Director of the Department of International Economic Research at the State Council Development Research Commission) Long Guoqiang, CKGSB Professor of Finance Zhou Chunsheng, and TCL Corporation Chairman and CEO Li Dongsheng (pictured on left).



# Clifford Chance's Boardroom China Briefing

Senior leaders from the global top 10 law firm update their knowledge about China with a CKGSB Executive Education custom program



CKGSB Dean Xiang Bing addresses Clifford Chance's Global Management Committee in Beijing

**C**CKGSB believes that with the right insight, global executives can close their China knowledge gaps and greatly improve their effectiveness in doing business in China and with China, as well as understanding the implications of the next wave of globalizing Chinese firms. Such knowledge will be a vital tool for successful businesses to stay ahead of the curve as China drives economic growth in coming years.

Global law firm Clifford Chance is one such business that has already achieved extraordinary success and has recently chosen to go “back to school” with CKGSB to upgrade its China knowledge. The firm’s Global Management Committee gathered at CKGSB’s downtown Beijing campus on May 17 to take part in a CKGSB Boardroom China Briefing.

“China is important to us for three reasons,” says Clifford Chance Managing Partner David Childs. “It’s important because

as Chinese companies begin to invest overseas, they are clients of ours. It’s also important as we act for our clients investing in China—many, many multinationals are investing in and will continue to invest in China. The third reason is because China’s overseas investment has also helped open new markets.”

The half-day session supported Clifford Chance’s goals by providing senior decision makers with the freshest thinking on China’s economic growth and globalization, as well as an overview of China’s global cultural impact from renowned New Confucian scholar and CKGSB Honorary Professor Tu Weiming.


The idea for Boardroom China Briefings arose from CKGSB’s pioneering work in executive education within China. “Our original idea in establishing CKGSB in 2002 was that the school should integrate the best business and economic insights from China and abroad,” says CKGSB Dean Xiang Bing. “But we very quickly discovered that the top

of the Chinese business leadership pyramid was not being served with access to world-class business education, so we moved to provide them with such education.” After establishing CKGSB as the authority on executive education for Chinese business leaders, CKGSB quickly realized that our students’ Western counterparts were also underserved in their need for China executive-level knowledge.

Thus Boardroom China Briefings were born. The programs deliver unique insight and interaction opportunities to the senior leadership teams of companies from around the globe and from all manner of industries.

“The session today at CKGSB is terribly important,” said Stephen Harder, the Managing Partner for Clifford Chance’s China operations. “We have our Global Management Committee here. There are individuals who manage six different global groups, whether it be corporate, or capital markets or litigation. There are also members who manage regions—the Americas, Southeast Asia, Europe, Central Europe, the Middle East, Africa.

“Many of them are highly sophisticated businesspeople and lawyers,” continued Harder. “But they don’t spend a lot of time understanding China. China is such an important part of our strategy. For them to come here and experience really great experts gives an opportunity for them to feel they profoundly understand the changes here, and that they’re not just relying on yesterday’s newspaper headlines.”

The briefing for Harder and more than 20 senior Clifford Chance team members included lectures and debates covering business, economic, political and cultural issues. The briefing was built around the expertise of CKGSB faculty members such as Xiang, who spoke on the global impact of Chinese firms, and Professor of Finance and Accounting and Associate Dean Liu Jing, who spoke on China’s financial system. 





# The Homes of Huizhou

Bai Shiyuan and his curious collection

By Matthew Jukes

Enter any of the countless, brown-brick factory warehouses of Haidian district, on Beijing's northwestern outskirts, and you're likely to be greeted by sweaty workers, hoards of crates and scowling overseers. Pass the threshold of entrepreneur and compulsive collector Bai Shiyuan's warehouse, however, and you'll walk straight into a breathtaking imperial gateway, flanked by restored wooden pillars, ornate carvings and huge gold-embossed characters on every surface.

Surrounded by construction work and dilapidated pathways, the monochrome building looks like any other in the area. But inside is a cavernous temple to wealth and decadence, akin to the Ming Dynasty which ruled between 1368 and 1644. Stepped gray brickwork adorned with wooden carving trim rises up to the ceiling, in the center, the Chinese-style slanted slate roofs give way to the courtyard's trademark skylight encased in glass, the only reminder that this is a building within a building, a ship in a bottle.

Collecting is Bai's greatest passion, and for the last 30 years, he's obsessively hunted down and restored the merchant houses of Huizhou, assembly halls built several centuries ago by wealthy southern Chinese traders to mimic the emperor's affluence. The soft-spoken 50-year-old businessman painstakingly moved his latest find, an old Huizhou courtyard, into his factory block-by-block and pillar-by-pillar, reconstructing the relic within a warehouse in northern Beijing.

## The Huizhou Style

Huizhou's ornate and extravagant traditional dwellings—with their southern Chinese architectural stylings such as upturned eaves, elaborate woodcarvings and pillars—were built in the Ming and Qing dynasties (1644–1911). The houses were constructed in the Huizhou region of Anhui province by ambitious merchants of the time who had made small fortunes trading in commodities such as bamboo, wood, lacquer, tea and salt.

The Huizhou mansions are renowned for fabulously ornate pillars, corbels and doors carved with intricate details, often incorporating local or family fables from the time. Antique window screens from traditional Huizhou homes which have already been demolished have, in some cases, been salvaged and sold as decorative items to luxurious restaurants, business clubs and homes in China and worldwide.

Bai believes that by collecting he preserves rather than disrupts Chinese cultural relics. He acquired his warehouse-bound dwelling from the Jixi area of Anhui province. "I believe it belonged to the family of a high-ranking noble heiress and was used



as a temple by the family. My priority was to preserve the building before it was torn down,” he says.

In a rush to preserve the structure from demolition, the businessman paid RMB 2 million for the 300 square meter property, and went to work on the relocation. Starting with the roof, Bai hired a team of technicians to take each slate off and wrap it carefully for transportation to Beijing. Damaged or rotten wood was replaced using the same material from the local area. Carvings were even restored by the few remaining Huizhou experts of the craft, who Bai encourages to pass on their expertise to other members of his team.

Bai is not alone in his passion for the old houses. More recently, modern-day Chinese tycoons have begun to buy whole antique wooden homes in Anhui to be dismantled and rebuilt for display in villa gardens. The trend has prompted worries among conservationists that a unique form of Chinese culture is being lost forever.

The trend prompted Chen Rongjun, director of Dongyang Relic Protection Office, in Anhui province, to tell local media that while the houses are not listed as protected buildings, they lose their unique cultural value once removed from their original sites. His concerns focused on wealthy businessmen in Yiwu, a wealthy city in Zhejiang province, who had developed a penchant for buying up the old homes from Anhui and reestablishing them in their home city.

But not all collectors are cashed up businessmen looking for a new garden ornament. There are some in the Yiwu area, who share Bai's vision of preserving the antique structures for future generations. Yang Handong, a textile tycoon in Yiwu has turned his collection of antique Huizhou-style antique houses into a public exhibition. Yiwu locals can view seven

exquisitely restored structures in a park next to the headquarters of Yang's Hujiang Group, China's biggest thread producer. Likewise, Zhu Youfu, a retired local official in the city, has created a dining and tourist complex around his collection of Anhui houses, with guests paying to feast in some of the restored buildings.

Bai won't confirm if he'll invest his own funds in a similar open-doors museum for the public appreciation of a unique form of Chinese cultural heritage. For now, it appears, Bai's exquisite Huizhou homes are for private viewing only.

### Long Time Collector

Since the 1980s, Bai has bought around 200 similarly exquisite decorated courtyards. When he first purchased one of the properties, at around 300 square meters, it cost him between RMB 7,000 and RMB 8,000, he recalls. In the 1990s, just before he stopped buying the houses, his last property cost RMB 7 million. By this time an awareness of cultural heritage had driven the prices so high that he had to stop.

“The living standards and education of people in the Huizhou area was on the rise,” said Bai. “Their understanding about the nature of cultural heritage and relics had increased, and while they were still looking to move, the price of the buildings had increased.”

The traditional houses are now Bai's proudest possessions and have a history of decadence. In imitation of the imperial style, the merchants became lavish in the design of their own homes, temples and assembly halls, utilizing the unique talents and materials of the local area for stonemasonry, wood carving and brickwork. It was this excessive attention to quality



*The courtyard of a Huizhou-style mansion preserved inside a glass house. Collector Bai Shiyuan sees art and architecture as the next big investment market*



and decoration that first attracted Bai, who still believes that the Huizhou houses are the very best in Chinese civil architecture. Originally, he had begun collecting inspired by the Ming Dynasty paintings which appreciated rapidly in value, but later found himself driven by a desire to preserve China's cultural heritage.

The buildings had just about weathered the test of time, and somehow managed to survive China's Cultural Revolution. By the 1980s however, the original occupants of the old buildings were keen to move into more modern buildings with better amenities and had been tearing down the structures in favor of China's passion for faceless apartment complexes. Bai, struck by the beauty of the buildings, and well aware of the potential



value of collectibles, rescued them.

"I actually didn't start this with the idea of cultural heritage preservation in mind," he remarks. "My collection of art has undergone three phases. Firstly as an investment for my future, then collecting, organizing and appreciating, but finally I realized that we were taking these things out of society's grasp. They are still precious to society, and it's about giving them back for people to appreciate them as well."

In the future, he hopes, there will be 10 Huizhou-style villages around the world, reconstructed as they were as a testament to and an avenue for spreading Chinese culture. With no concrete plans yet, Bai hopes to start in China, but is waiting for the right time to contact the Chinese government to approve a property or piece of land for his planned museum, before he moves further afield.

His true vision is to recreate entire villages in the same state that he found them in various locations around the world, as a place for tourists or locals to appreciate Chinese culture and learn about China's history. Meanwhile, the relics are sitting in a 100 acre warehouse on land belonging to Bai in Beijing, waiting for their rebirth.

The urge to preserve China's ancient culture now appears to drive Bai as much as the thrill of collecting. "I think this can only happen in China," he says, referring to the Cultural Revolution. Between 1966 and 1977, the Red Guard, a militant youth group established by Chairman Mao Zedong, was encouraged to root out bourgeois elements within society. Artworks associated with imperial China were targeted and destroyed across the country and many artists were subject to public criticism or at worst, torture.

"At that time, families who owned great calligraphy and paintings didn't even burn them, in case it attracted the attention of informers or the authorities. Instead, they would submerge them in water until they just turned to pulp. So many great works were lost," he says sadly.

### Appreciating in Value

Bai's hobby for collecting old works of art soon became his main occupation, and he has now accumulated not only a healthy collection of ancient courtyards, but also stacks of carefully archived boxes, kept in an air-conditioned storeroom, each of which contains pieces of Chinese calligraphy by different artists along with ink wash paintings, sculptures and historical relics.

Bai says that his wife and four-year-old son have given their somewhat tacit approval of his compulsive collecting, making space in the family apartment in Yayuncun, near Beijing's Olympic stadiums, for Huizhou carvings and other relics.

Pointing to a Qing Dynasty (1644-1911) bed, he casually mentions that it's worth somewhere in the region of RMB 30 million, and a scroll that was once in the care of the Manchu Emperor Qianlong (1711-1799), is thought to be priceless. Paintings hanging on the walls of his warehouse by younger contemporary artists, still working in traditional styles, are valued in the thousands. He insists he is not collecting with a view to profit, but rather out of his own desire to possess elegant things.

Bai spends much of his time with promising traditionalist artists, collecting their work before it appreciates in value. "Chinese collectors who go to the auctions don't buy a collection; they focus solely on a single expensive piece. I'm not like that at all," says Bai. "I never compete in the auctions. I always collect things that other

people overlook. I'm looking for things that will appreciate in value over the next 20 years."

Certainly China's fine arts market doesn't want for eager buyers. The European Fine Art Foundation (TEFAF), based in Maastricht, The Netherlands, has calculated that China now accounts for 30% of the world's arts and antique sales, surpassing more stagnant markets in the UK and US, which now account for 22% (unchanged) and 29% (down five percentage points from last year) respectively. The country's fine arts market was estimated at \$3 billion in 2010 according to the TEFAF.

Wealthy Chinese buyers have turned the global arts market on its head, with former top sellers like Spanish artist Pablo Picasso and American pop-culture icon Andy Warhol being eclipsed by Zhang Daqian and Qi Baishi, both Chinese traditionalist painters born in the late 19th century.

Chinese collectors have opted for local artifacts. A single scroll by ancient calligrapher Huang Tingjian sold for RMB 436 million on June 23, 2010, at Beijing's Poly auction house, smashing the previous record of RMB 169 million held by *Handscroll of the Eighteen Arhats* by Wu Bin from the year before, according to a press release from the auction house.

### In for the Long Haul

As a lowly radio mechanic in Beijing in the late 1970s, a young Bai bought three vases from a street side antiques market for RMB 15, two months-worth of wages at the time. Raised in an educated family, Bai could see that the vases were of some value, but it was only when he sold two of them to pay outstanding debts in the late 1990s for RMB 1 million, that he realized what he had on his hands. Eleven years later, he sold the remaining vase for nearly RMB 20 million.

"My businesses have never done very well," he chuckles. "I've always spent all my money on collecting. I had hoped to gather as much of value as I possibly could by the time I was 50. Afterwards I can stand back and work on other things."

Despite accumulating an Aladdin's Cave in a grubby Beijing suburb, Bai says he has no intention of selling it all off for a quick buck. Participating in the Olympic Fine Arts project—an event established alongside the Beijing 2008 Olympics to promote culture with sports—Bai took a series of paintings and scrolls to London this year, to show off Chinese antiques to a wider audience. While keeping his Huizhou dreams alive, he's waiting for government support to allow him to share the structures with the public. In the meantime, he's doing what he does best—watching, waiting and collecting. ■





# Connecting the Dots

**Jennifer Li, CFO of search engine giant Baidu, on her eclectic reading habits**

I have very wide interests in reading. For leisure business people don't always read business-related stuff. They read all kinds of things. Most recently, I was reading *Boomerang: Travels in the New Third World* (by Michael Lewis), which is about the financial crisis. I particularly enjoyed that book because it really helped me understand the source of the crisis. And those are more about the macro issues, it's not about managing internet companies (which is something I do as a professional). But those macro issues are very interesting. I love to put all the information together. And when you read that kind of book, you think about what happens in China in the real estate market, and what can happen, and what works and what won't work. We all know that we are under macro challenges here in China, and that real estate was a big contributor, so what to do there? I think reading that kind of stuff is very enjoyable because you can relate it to many other things.

I also like to read biographies and learn about the lives of interesting people. I have read the biographies of Margaret Thatcher, Bill Clinton, and, of course, like everybody, Steve Jobs. These are just fascinating people and make for very interesting reading.

I have been a big fan of the biography genre for a long time. I like to read about how people go through their lives. When you read of their experiences, you often think that if you were put in that situation, how you would deal with it. When you are little, reading is often done for reading's sake. But when you experience more, you can relate to these things and think about the kind of questions they face. This just inspires you. Even very, very old figures can be very inspiring. And you learn history along the way—what it was like when they were growing up, etc. And then you look elsewhere in the world, and wonder, 'Can history ever repeat itself?'

It's hard to say what my all-time favorite book is. But I do have a tendency to go back to the same books again and again. Years pass and every time I read them, they give me a different learning. I would put something like *Romance of the Three Kingdoms* by Luo Guanzhong in that category. Every time I read it, it gives me new wisdom.

*Jennifer Li, CFO of Baidu, is often heralded as the 'Sheryl Sandberg of China'. She worked with General Motors in various capacities and across geographies before joining Baidu in 2008. She is an independent director on the board of tobacco giant Philip Morris International and has been nominated by Forbes magazine in the list of Women to Watch in Asia.*

## BUSINESS BESTSELLERS

China

US



**Influence: The Psychology of Persuasion**

by **Robert Cialdini**  
(Wanjuan Publishing Company, 2010)  
How to influence others

**The Effective Executive**

by **Peter Drucker**  
(China Machine Press, 2009)  
Classic from the master of management

**Hai Di Lao—It Cannot be taught**

by **Huang Tieying**  
(CITIC Press Corporation, 2011)  
The story of Haidilao, China's most successful hot-pot chain

**The Essence of Sales—Human Relationships**

by **Ni Jianwei**  
(Yunnan People's Publishing House, 2011)  
Sales with Chinese characteristics

**Positioning: The Battle for Your Mind**

by **Al Ries, Jack Trout**  
(China Machine Press, 2011)  
The Bible for marketing strategists

**The Minto Pyramid Principle**

by **Barbara Minto**  
(Nanhai Publishing House, 2010)  
How to write clearly

**Our Entrepreneurial Stories**

**CCTV Business Channel**  
(Beijing Publishing Group, 2011)  
The luminaries of Chinese business tell all

**The Full-Fledged Ideals**

by **Feng Lun**  
(Culture and Art Publishing House, 2012)  
Vantone Chairman on vision, society and real estate

**How to be the most effective HR?**

by **Pan Xinmin**  
(Chemical Industry Press, 2011)  
Notes from a Fortune 500 HR Director

**Xiao Ai's Accountbook**

by **Chen Yanhong**  
(Northeastern Finance and Economics University Press, 2011)  
Accounting for dummies

(Source: Dangdang.com)



**Steve Jobs**

by **Walter Isaacson**  
(Simon & Schuster, 2011)  
Biography of the tech visionary

**The Power of Habit**

by **Charles Duhigg**  
(Random House, 2012)  
How companies can harness our love of routine

**Imagine**

by **Jonah Lehrer**  
(Houghton Mifflin Harcourt, 2012)  
How we can all be more creative

**Thinking, Fast And Slow**

by **Daniel Kahneman**  
(Farrar, Straus & Giroux, 2011)  
Understand how the two thinking systems prejudice your decisions

**Mobile Wave**

by **Michael Saylor**  
(Vanguard, 2012)  
Mobile computing is about to turn the world upside down

**The Price of Inequality**

by **Joseph E. Stiglitz**  
(W.W. Norton, 2012)  
The rich are getting richer, the poor poorer—that could mean the end of America

**Unintended Consequences**

by **Edward Conard**  
(Portfolio/Penguin, 2012)  
A spirited defense of the One Percent

**The Total Money Makeover**

by **Dave Ramsey**  
(Thomas Nelson, 2009)  
Get out of debt and build wealth

**\$100 Startup**

by **Chris Guillebeau**  
(Crown Business, 2012)  
Do what you love—and make money from it

**The 4-Hour Workweek**

by **Timothy Ferriss**  
(Crown Archetype, 2009)  
Work less, earn more

(Source: The New York Times)



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