NOVEMBER–DECEMBER 2005 VOLUME 32 NUMBER 6

# THE CHINA BUSINESS REVIEW

THE MAGAZINE OF
THE US-CHINA BUSINESS COUNCIL

SPECIAL REPORT:

# RETAIL & DISTRIBUTION

The Beijing Market Modernizes
Distribution Opens Up
Point-of-Purchase Strategies
China's Young New Consumers

US$22/HK$220

THE CHINA BUSINESS REVIEW
THE MAGAZINE OF THE US-CHINA BUSINESS COUNCIL

NOVEMBER–DECEMBER 2005 VOLUME 32 NUMBER 6


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## SPECIAL REPORT: RETAIL & DISTRIBUTION



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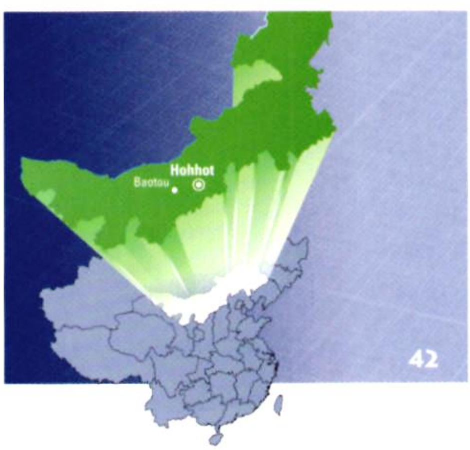

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THE MAGAZINE OF THE US-CHINA BUSINESS COUNCIL

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# Short Takes

## Advertisement Spending Soars in China

According to Nielsen Media Research, ad spending in 166 cities in China reached ¥143 billion ($17.3 billion) for the first half of 2005, marking 20 percent year-on-year growth. About 78 percent—or ¥112 billion ($13.5 billion)—was spent on television, the most popular medium. Newspapers and magazines had roughly 19 and 2 percent shares, respectively, of the total. Pharmaceutical, cosmetic, and retail companies were the top three spenders, all recording double-digit growth. Interestingly, advertising for men's cosmetics and men's fashion soared 64 and 75 percent, respectively, year-on-year, while ad spending for women's fashion fell 51 percent year-on-year. According to analysts, with ad spending amounting to 3 percent of GDP in the United States and Japan, China's 1 percent means much room for future growth.

## Pollution Costing Shanghai

Air pollution in Shanghai is costing the city more than ¥8 billion ($1 billion) in healthcare expenditures annually, according to a report from Fudan University's School of Public Health. While

*Continued on page 6*

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(Signed) Jesse Marth, Business Manager

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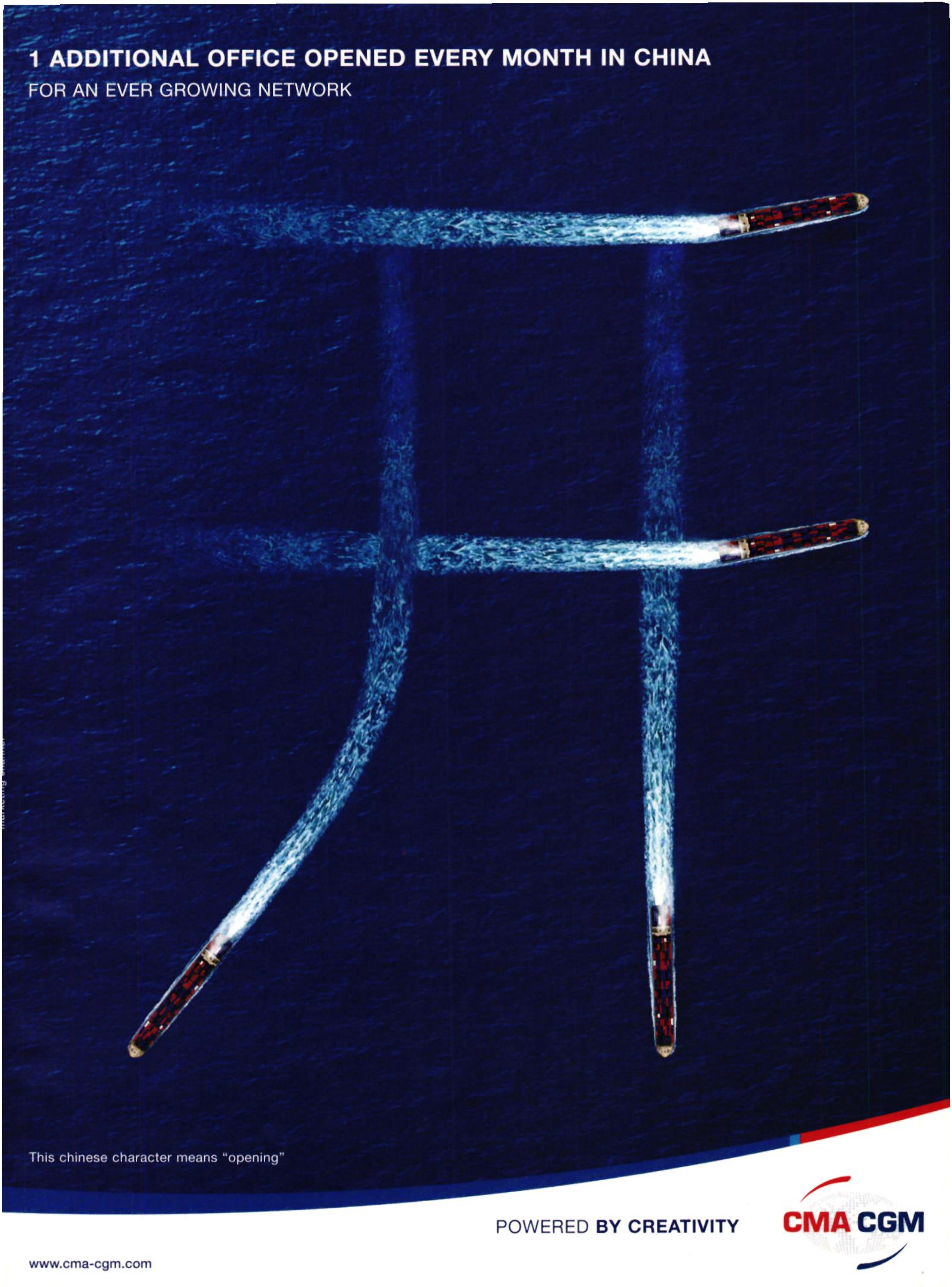
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# BULLETIN

## EVENT WRAP-UP

### Washington

**September**

**Issues Luncheon** Featured Undersecretary of the Treasury for International Affairs Tim Adams, who discussed China's exchange rate reforms.

**Roundtable Discussion on Key China Trade Issues** Featured Ira Belkin, senior trade compliance officer with the US Department of Commerce.

**October**

**Issues Luncheon** Featured Coordinator of International Intellectual Property Enforcement Chris Israel, who briefed members on the administration's newest initiative to increase IPR enforcement in China.

### Beijing

**October**

**Luncheon on Lessons from the Front Lines of Doing Business in China** Jointly sponsored by USCBC, the American Chamber of Commerce in China, and Ogilvy Public Relations Worldwide, the luncheon featured James L. McGregor, author of *One Billion Customers* (see p.44).

### Shanghai

**August**

**Luncheon on Best Practices: Selling to China** Featured Paul French of AccessAsia and Pablo Van of Caterpillar China.

**September**

**Luncheon on Best Practices: Establishing Shared Service Centers in China** Featured Rongxiang Chen, the managing director of BearingPoint China.

### Seattle and Minneapolis

**September**

**Roundtable Seminars on Investment Trends and China Trade Politics** Featured then-USCBC Chief Representative in Shanghai, Iain McDaniels, and Washington, DC-based USCBC Vice President Erin Ennis.

## UPCOMING EVENTS

### Washington

**Issues Luncheons**
November 17, 2005
December 15, 2005

**Forecast 2006**
January 24–25, 2006
For more information, see p.41.

**October**

**China Operations Conference** Featured experts from business and government discussing distribution, human resources, China's economy, and US-China relations, as well as best-practice sessions on cash management, customs compliance, and transfer pricing.

**Correction** In light of the aftermath of Hurricane Katrina, Presidents George W. Bush and Hu Jintao agreed to postpone President Hu's visit to the United States, originally scheduled for September. The dinner in his honor, which was listed in the previous issue of the *CBR*, thus was postponed.

## Short Takes

*Continued from page 4*

emissions of particulates and sulfur dioxide dropped over the last decade, nitrogen dioxide—which is mainly released by cars—jumped by 50 percent. The findings are consistent with figures released elsewhere. In a study by the Shanghai Environmental Sciences Institute, 16 of 18 road intersections tested in the city had "excessive" levels of nitrogen dioxide, and Shanghai city government statistics indicate that the level of nitrogen dioxide rose to 0.062 mg/m$^3$ in 2004 from 0.057 mg/m$^3$ in 2003. Analysts note that rapid economic growth has boosted the demand for cars and electricity, thereby worsening air pollution.

### NPC Holds First Public Hearing

The National People's Congress (NPC) held its first ever public hearing in September. Twenty pre-selected citizens spoke at a session that considered whether China should raise its individual income tax threshold from ¥800 ($99) per month to ¥1,500 ($185) per month. Chosen from a pool of nearly 5,000 applicants who were required to submit an outline of their views on the topic, the participants included migrant workers, civil servants, and teachers. Eight came from China's eastern provinces, with the remainder from China's central and western regions. According to Xinhua News Agency, the NPC Standing Committee will treat the opinions voiced by the participants at the session as an "important reference and basis" for its deliberations.








# What a Difference a Decade Makes

Patrick Powers

After many years of working in China, one of the most frequent comments I hear from visitors to our office in Beijing is, "You must have seen many changes since you first arrived." True, but at the same time it is becoming quite difficult to explain with any kind of reference point the myriad changes that have taken place in China's society and economy over the past 20 years. Around the world, local retail markets act as a bellwether not only of changes in consumer habits but also of the broader economy. Taking Beijing's retail sector as an example, then, may add some perspective to the question of what has changed in China and where it is heading commercially. (Following this article are statistics and brief snapshots of leading Beijing retailers—only one of which was a market leader a decade ago.)

**Patrick Powers** is vice president of the US-China Business Council in Beijing.

## The transformation of Beijing's retail sector

As the chief representative of a major European retailer in the early to mid-1990s, I was tasked with preparing market-entry feasibility studies on four major Chinese cities, including Beijing. The studies concluded, in short, that the retail sector in Beijing was ripe for an "extreme makeover" in terms of professional merchandising and operations.

Historically, a majority of foreign observers had considered Beijing a perennial underperformer in the retail sector: Total sales of consumer goods in 1992 Beijing were \$4.9 billion, compared to \$5.6 billion for Shanghai and \$11.9 billion for Guangdong. Shanghai and Guangdong were considered to be more open markets, with a

## The growing sophistication of Beijing's retail sector mirrors the increasing complexity of China's commercial environment

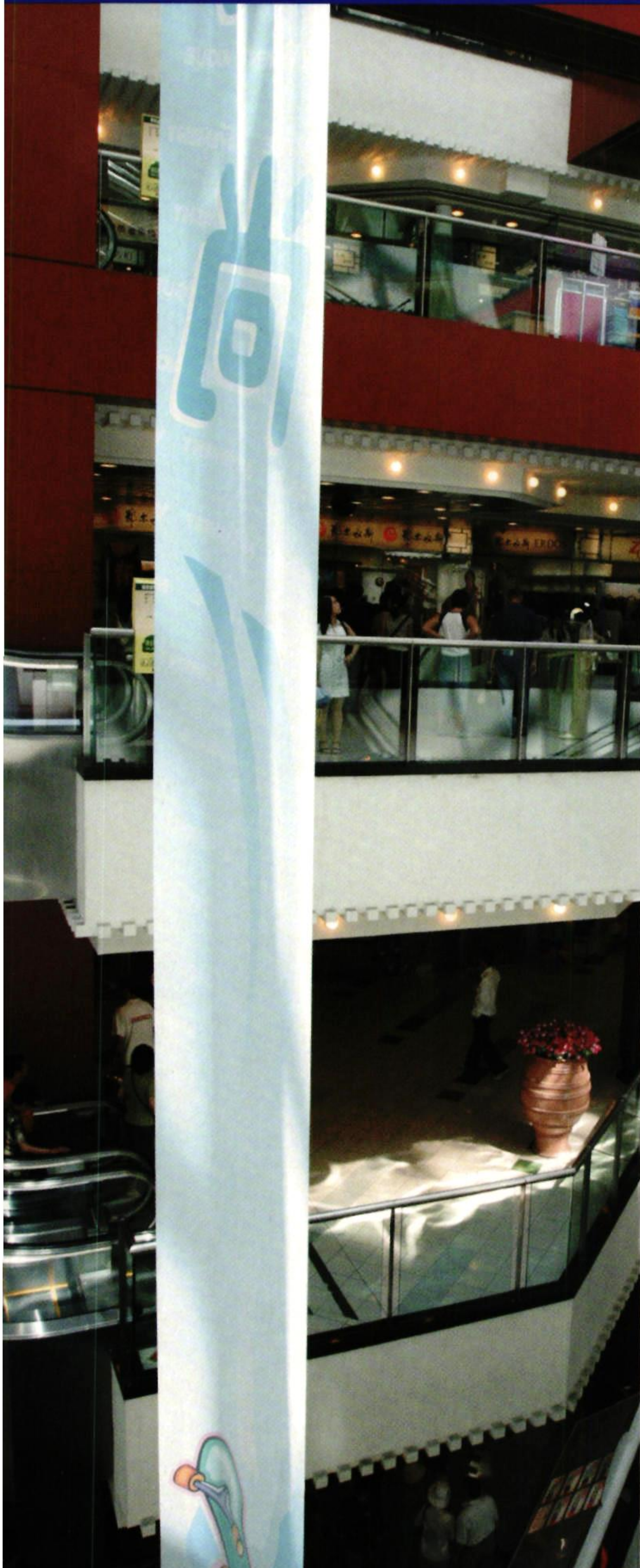
more diverse selection of available merchandise. Despite being dominated by plodding state-owned retailers that had no concept of customer service and merchandising compared to their southern cousins, however, Beijing was, and always has been, a primary shopping destination for travelers from the rest of China and has consistently had strong retail sales.

Back then, a typical Beijing resident would buy fresh products from large state-owned stores or local markets and dry goods from small shops. For bigger ticket purchases, the 10 most popular stores in Beijing were almost without exception large, state-owned department stores primarily located in and around the Xidan and Wangfujing shopping areas. The Lufthansa Center and Scitech department stores had just opened to large numbers of window-shoppers and sluggish sales, because of high prices and low consumer incomes. There were only a handful of chain stores at the time, notably Xifu and Jinghua, neither of which is in business today. The venerable Friendship Store and the former Lido Holiday Inn supermarket were virtually the only outlets for Western foodstuffs.

The market started to change in 1994–95 as city government-owned retailers, sensing a real threat to their traditional monopolistic position, started to copy the hypermarket format just prior to the opening of foreign operators SHV Makro and Carrefour Group. For the rest of the decade, the Beijing market racked up steady, solid retail growth. Operators gradually improved, in terms of merchandising and service, as disposable income levels and consumer demand rose. In 1992, as mentioned above, Beijing's retail sales were \$4.9 billion. Just 13 years later, total sales were \$27 billion.

But only in the past five years have Beijing retailers made great strides toward international levels of sophistication. Many of the changes have been in response to consumer demand, which encouraged the entry of smaller fashion and lifestyle retailers. On a more practical level, however, two primary market motivators have forced change: First, major foreign retailers aggressively expanded their operations and indirectly pressured local competitors to upgrade merchandising, store layout and fixtures, and service levels—or face closure. Second, strong homegrown retail chains have emerged, although one could


Photos: Dennis Chen



**Many domestic retailers are nevertheless still hindered by inefficient state-owned enterprise management structures.**

argue that they were protected from foreign competition via restrictive foreign investment policies that expired at the end of China's third year of World Trade Organization (WTO) membership.

Many domestic retailers are nevertheless still hindered by inefficient state-owned enterprise management structures. Others, such as Shanghai Bailian (Group) Co. Ltd., China Resources Vanguard Co., Ltd., and Gome Group, have made progress in adopting modern management systems, and in some cases, acquiring experienced managerial staff from foreign retailers.

One of the interesting features of the local retail landscape is that in the 1990s, China leapfrogged from being primarily serviced by small groceries and department stores, straight to hypermarket and warehouse formats, bypassing the traditional interim step of larger supermarkets. Now the market is looking back—one of the hot growth stories in recent years has been the development of quality supermarkets and convenience stores.

## Future outcomes

So what does all of this mean in the context of future retail development in Beijing and, more broadly, in China? It's all about the money. Back in the early 1990s, the main driver of consumer behavior was price. Supermarkets were considered to be expensive compared to local markets, so large hypermarkets became popular because foreign retailers adopted "EDLP," or "everyday low price" formats, on a wide range of consumer goods.

Recently, the market has matured, disposable income is significantly higher, and according to AC Nielsen, the primary motivators for retail shopping are now convenience, spaciousness, and layout. Price has fallen to sixth place. Oddly enough, the SARS epidemic—which banished people from all public gathering places, including public transportation—was a key driver in encouraging consumer spending for lifestyle items, such as home improvements, electronics, and automobiles. When people were cooped up at home for several weeks, they became bored and decided to spend on lifestyle purchases rather than on necessities.

Beijing's retail landscape is likely to eventually reach the level of sophistication found in Tokyo or Hong Kong, driven by the spending power of the middle class. Lifestyle, fashion, specialty retailing, franchising, and food and beverage operations can all look forward to positive growth opportunities.

**Growth in Beijing Income and Retail Sales, 2000–04**

| Year | 2000 | 2001 | 2002 | 2003 | 2004 | % Change, 2000–04 |
|---|---|---|---|---|---|---|
| Total GDP (¥billion) | 248 | 285 | 321 | 366 | 428 | 72.8 |
| Per Capita Total Income (¥) | 10,416 | 11,659 | 13,252 | 14,959 | 17,116 | 64.3 |
| Per Capita Disposable Income (¥) | 10,350 | 11,578 | 12,464 | 13,883 | 15,638 | 51.1 |
| Retail Sales (¥billion) | 144 | 159 | 174 | 192 | 219 | 51.9 |

Sources: PRC National Bureau of Statistics; Beijing Municipal Bureau of Statistics

But along the way, there will be commercial casualties, particularly among local retailers.

As is often the case in China, the market is oversupplied with local operators imitating other successful formats without differentiating their own brands. This makes market consolidation inevitable. In this regard, the government has been quietly pressuring the industry to strengthen itself via initial public offerings, mergers, and restructuring, with the ultimate goal being the formation of a number of genuine national and international retail conglomerates.

For historical reasons dating back before 1949, the PRC government is quite sensitive to the possibility that well-financed and -managed international operators could dominate the national retail sector. As a result, the government maintains an unstated policy that leading retailers should be local, not foreign. Smart foreign investors in the sector will factor that reality into their PRC development strategies.

Retail is just one of many key industries, in fact, in which there is a bias for creating national champions via medium-term preferential treatment, directly or otherwise, from government institutions. A focus on the retail sector, then, provides not just a window into what has changed, but also into the elements of China's commercial environment that will be with us for years to come, regardless of WTO accession. 完

**China's Top 25 Retailers, First Half 2005**

| Enterprise Name | Sales: 1H 2005 Sales (¥ billion) | Sales: 1H 2004 Sales (¥ billion) | Sales: % Change | Stores: 1H 2005 Stores | Stores: 1H 2004 Stores | Stores: % Change |
|---|---|---|---|---|---|---|
| 1 Shanghai Bailian (Group) Co. Ltd. | 36.5 | 32.1 | 13.7 | 5,910 | 4,804 | 23.0 |
| 2 Gome Group | 19.6 | 14.8 | 32.0 | 309 | 162 | 90.7 |
| 3 Suning Appliance Chains Group Co. Ltd. | 17.8 | 10.6 | 69.0 | 255 | 185 | 37.8 |
| 4 Dalian Dashang Group | 13.0 | 9.1 | 42.3 | 120 | 96 | 25.0 |
| 5 Carrefour Group (China) | 10.2 | 7.8 | 31.9 | 69 | 50 | 38.0 |
| 6 Suguo Supermarket Co., Ltd. | 9.5 | 7.0 | 36.3 | 1,405 | 1,236 | 13.7 |
| 7 Shanghai Yongle Home Appliances Co. Ltd. | 9.3 | 6.5 | 43.1 | 135 | 74 | 82.4 |
| 8 Beijing Hualian Group | 9.2 | 7.3 | 25.3 | 70 | 53 | 32.1 |
| 9 Shanghai Nong Gong Shang Supermarket Co., Ltd. | 8.5 | 6.6 | 30.3 | 1,314 | 1,198 | 9.7 |
| 10 Shangdong Sanlian Group | 8.1 | 6.4 | 26.7 | 274 | 233 | 17.6 |
| 11 Chongqing General Trading Group | 7.4 | 6.7 | 9.9 | 175 | 167 | 4.8 |
| 12 Jiangsu Five Star Appliance Co. Ltd. | 7.3 | 4.3 | 69.6 | 148 | 110 | 34.5 |
| 13 Wumart Stores, Inc. | 7.1 | 4.8 | 48.7 | 650 | 564 | 15.2 |
| 14 Trust-Mart Co. Ltd. | 6.5 | 5.7 | 14.9 | 89 | 81 | 9.9 |
| 15 China Resources Vanguard Co., Ltd. | 5.6 | 5.4 | 4.6 | 491 | 450 | 9.1 |
| 16 Beijing Dazhong Electronics Co. Ltd. | 5.6 | 3.9 | 41.8 | 68 | 58 | 17.2 |
| 17 The Home World Group | 5.1 | 3.6 | 42.2 | 75 | 69 | 8.7 |
| 18 Jiangsu Wenfeng Great World Chain Development Co. | 4.8 | 3.8 | 26.8 | 543 | 453 | 19.9 |
| 19 Wal-Mart Stores, Inc. (China) | 4.7 | 3.7 | 26.8 | 47 | 39 | 20.5 |
| 20 Abest Supermarket Co., Ltd. | 4.6 | 3.3 | 38.9 | 62 | 49 | 26.5 |
| 21 Renrenle Chain Commercial Co. Ltd. | 4.3 | 2.0 | 115.9 | 33 | 16 | 106.3 |
| 22 Hefei Department Store Group Co., Ltd. | 4.3 | 3.6 | 20.2 | 42 | 19 | 121.1 |
| 23 Wushang Group | 4.1 | 4.1 | 1.0 | 40 | 36 | 11.1 |
| 24 Liqun Group | 4.0 | 2.2 | 76.2 | 555 | 389 | 42.7 |
| 25 Jinjiang Metro Cash & Carry Co., Ltd. | 3.8 | 3.3 | 14.6 | 24 | 20 | 20.0 |

Source: Department of Commercial Reform and Development, PRC Ministry of Commerce

### Beijing Chaoshifa Co., Ltd.

**Established:** 1997

**Number of Beijing stores:** 30

**2004 turnover:** ¥2.1 billion ($254 million)

**Largest Beijing store:** Shuangyushu, Haidian District

Beijing Chaoshifa Co., Ltd., established in 1997 under the auspices of the Beijing municipal government, operates 43 supermarkets and convenience stores, including one store in Austria. Most of its stores are in Beijing, concentrated in the Haidian area. Formerly one of the larger standalone retailers in Beijing, Chaoshifa is now controlled by rival chain Wumart, which became the majority shareholder in 2005.

### Beijing Hualian Group

**Established:** 1996

**Number of Beijing stores:** Not available (NA)

**2004 turnover:** ¥16 billion ($1.9 billion)

**Largest Beijing store:** NA

Beijing Hualian Group (BHG) operates more than 100 outlets across China, including 24 department stores, 70 supermarkets, and 7 shopping centers. Only a few of BHG's outlets are located in Beijing; the rest are located in other parts of eastern and central China. BHG recently entered a commercial venture with the China Mobile Group and plans to establish 100 information technology (IT) retail outlets by 2008. BHG is also focusing on shopping center development and plans to establish a strategic partnership with a major US-based shopping mall developer to enhance brand recognition and management skills. Because of its designation by the Ministry of Commerce (MOFCOM) as one of the top 20 "key and strategically important enterprises," BHG is eligible for government support, including project-related finance.

### Beijing Jingkelong Co., Ltd.

**Established:** 1994

**Number of Beijing stores:** 140

**2004 turnover:** ¥5.2 billion ($628 million)

**Largest Beijing store:** Jinglong Shopping Center, Chaoyang District

Jingkelong is a state-owned retailer that operates 140 stores, most of which are supermarkets between the Third and Fourth Ring Roads in Chaoyang District, Beijing. Two stores are located in Hebei. Jingkelong manages more than 200 of its own brands, primarily in household products. According to a company spokesperson, Jingkelong is likely to seek to expand outside of Chaoyang via mergers and acquisitions and franchising. It also plans to go public on the Hong Kong Stock Exchange in 2006 and expand its network of pharmacies and automobile distributors in Beijing. According to the corporate website, the company intends to operate 50 auto specialty stores and 50 pharmacies by 2008. Jinkelong started its operation by copying two-thirds of the Chinese name used by the Sino-Dutch cash-and-carry joint venture, CTA Makro Commercial Co.

### Beijing Wangfujing Department Store (Group) Co., Ltd.

**Established:** 1955

**2004 turnover:** ¥5.87 billion ($709 million)

**Number of Beijing stores:** 6

**Largest Beijing store:** Beijing Wangfujing Department Store, Dongcheng District

Beijing Wangfujing Department Store (Group) Co., Ltd. operates 14 stores in China. The Wangfujing department stores in Beijing focus on selling quality goods at low prices to middle-class customers. The name is well known in Beijing, and in 2004, Wangfujing made MOFCOM's list of 20 "key and strategically important enterprises." Wangfujing is a state-owned company, with, as of April 2005, 50.1 percent held by Beijing Enterprises Holdings Ltd., the investment vehicle of the Beijing municipal government. Wangfujing is listed on the Shanghai and Hong Kong stock exchanges.

### Carrefour Group

**Established:** 1959 in France

**First store opened in Beijing:** 1995

**Number of Beijing stores:** 6 hypermarkets

**2004 turnover:** ¥16.2 billion ($1.9 billion)

**Largest Beijing store:** Shuangjing, Chaoyang District

Global retailing giant Carrefour is currently the largest foreign chain in China with 61 hypermarkets nationwide, six of which are in Beijing. Carrefour originally had a highly questionable legal structure in China, which ultimately required the company to undergo significant restructuring. After 10 years of operation, Carrefour now employs more than 23,000 people in China and is generally considered the most aggressive of the foreign operators in terms of store development.

### China Resources Vanguard Co., Ltd.

**Established:** 1984

**Number of Beijing stores:** 6 superstores, 21 supermarkets

**2004 turnover:** ¥11 billion ($1.3 billion)

**Largest Beijing store:** NA

China Resources Vanguard Co., Ltd. (CR Vanguard), headquartered in Shenzhen, entered the Beijing market in 1998. It now operates 560 outlets across China under three business formats: hypermarkets, supermarkets, and smaller convenience stores. CR Vanguard was listed as one of the 20 "key and strategically important enterprises" by MOFCOM in 2004. It has historically been considered a market laggard, particularly in Beijing, given the resources of its parent company, China Resources (Holdings) Co., Ltd., which has total assets of about HK$70 billion ($9 billion). Beijing is considered an important market in the expansion plan of CR Vanguard's retail network in northern China, and the company has indicated that it will open 50 new supermarkets in Beijing's small and medium-sized residential communities before 2008. CR Vanguard sees the expansion of its superstores as a way of competing with hypermarkets like Wal-Mart Stores, Inc. and Carrefour in Beijing, Shanghai, and particularly in Southeast China. In 2004, CR Vanguard launched a new "own-brand" strategy using the Sunflower logo in all of its three types of stores.

### Golden Elephant Chain Pharmacy Co., Ltd.

**Established:** 2000

**Number of Beijing stores:** 213

**2004 turnover:** ¥516 million ($62 million)

**Largest Beijing store:** Xidan Store, Xicheng District

Golden Elephant Chain Pharmacy Co., Ltd. is a privately owned company with 311 pharmacy franchise outlets in China. Golden Elephant manages its brand reputation by emphasizing high-quality customer service. The retailer attracts customers through services such as phone orders, free delivery, 24-hour online service, and a customer-friendly return policy. According to its website, Golden Elephant plans to open 1,000 pharmacies in China before 2008.

### Gome Group

**Established:** 1987

**Number of Beijing stores:** 27

**2004 turnover:** ¥23.8 billion ($2.9 billion)

**Largest Beijing store:** Capital Palaestra Gome, Haidian District

Gome Group, the largest retailer of household appliances and consumer electronics in terms of sales turnover, operates almost 300 outlets across China. In 2004, it made the MOFCOM list of 20 "key and strategically important enterprises." In 2004, Gome Electrical Appliances Holding Ltd. listed on the Hong Kong Stock Exchange. The company is made up of eight large regional units, all of which share logistics and other resources in order to expand efficiently to second- and third-tier markets. By 2008, it aims to open more than 1,000 outlets across China and achieve an annual sales turnover of ¥120 billion ($14.5 billion). In Beijing, Gome mainly focuses on core commercial areas, such as the Xizhimen and Zhongguancun areas.

### Jian (Huapu) Hypermarket Co.

**Established:** 1997

**Number of Beijing stores:** 11

**2004 turnover:** ¥1.02 billion ($123 million)

**Largest Beijing store:** Chaoyangmen Supermarket, Chaoyang District

A subsidiary of Beijing Huapu Industry Group, Huapu is a privately owned company established in 1997. Huapu operates nine stores in Hebei, Hubei, Jilin, and Shandong and 11 stores in Beijing. Huapu's commercial focus is on the development of small and medium-sized stores less than 6,000 $m^2$. Huapu has recently retreated from its investments in Changchun, Jilin, where two of its three stores have closed. Currently, Huapu is exploring markets in Beijing, Hebei, and Shandong. According to a company spokesperson, Huapu has no plans to use franchising or alliances to enlarge its retail chain.

### Orient Home Co.

**Established:** 2000

**Number of Beijing stores:** 7

**2004 turnover:** ¥5.2 billion ($628 million)

**Largest Beijing store:** Lizeqiao Center, Fengtai District

Orient Home, a private firm founded in Beijing and a subsidiary of the Orient Group, operates 24 stores in 15 cities in China. Orient Home was a pioneer in China's do-it-yourself (DIY) retail market. All seven of its Beijing stores lie outside of the Fourth Ring Road. As is often the case with PRC retail outlets, Orient Home rents out premium shelf space within its stores and promotes its own brands in parallel. In the trade, Orient Home is considered to have a close relationship with central and local governments because its president is a member of the National Committee of the Chinese People's Political Consultative Conference. A spokesperson indicated that Orient Home plans to expand to 100 stores in China, including franchises, before the end of 2006 and that it is pursuing a joint venture with the Home Depot, Inc., the world's DIY leader.

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### Shanghai Lotus Supermarket Chain Store Co., Ltd.

**First entry in China:** 1997

**Number of Beijing stores:** 4 hypermarkets (another 3 under construction)

**2004 turnover:** ¥7.4 billion ($894 million)

**Largest Beijing store:** Lotus Supercenter in Golden Resources Shopping Mall, Haidian District

Back in the 1990s, Dhanin Chearavanont, chair of Thailand's CP Group, dreamed of being the "Sam Walton of China" after his successful experience in Thailand with the Makro chain of Holland-based SHV Holdings NV. After a number of strategic missteps in China, CP opened its first Lotus hypermarket in Shanghai in 1997. Lotus' retail format is derivative of European and American formulas. A corporate representative indicated that Lotus plans to open another three stores in Beijing and 100 more stores in other major cities in China by the end of 2005, although such a plan is unlikely to be feasible given local licensing requirements.

### Suning Appliance Chains Group Co. Ltd.

**Established:** 1990

**Number of Beijing stores:** 17

**2004 turnover:** ¥22.1 billion ($2.7 billion)

**Largest Beijing store:** Si Jiqing Qiao, Haidian District

Suning Appliance Chains Group Co. Ltd., one of China's largest home appliance retailers, is based in Nanjing, Jiangsu. Suning opened its first Beijing store in 1998. The company has interests in real estate, manufacturing, financial capital management, software development, and e-commerce ventures. In 2004, Suning was listed on the Small and Medium Enterprises Board of the Shenzhen Stock Exchange and raised ¥292.3 million ($35.3 million). Suning has been relatively aggressive in opening its own distribution centers, with about 20 currently in operation.

### Wal-Mart Stores, Inc.

**Established:** 1962 in the United States

**First store in China:** 1996

**Number of Beijing stores:** 2 (1 Supercenter, 1 Sam's Club)

**2004 turnover:** ¥7.63 billion ($921 million)

**Largest Beijing store:** Supercenter at Zhichun Road, Haidian District

Retailing titan Wal-Mart has been active in China since the early 1990s and now operates 49 stores in 23 cities in China, including 44 supercenters, 3 Sam's Clubs, and 2 smaller neighborhood outlets. Beijing's first Wal-Mart Supercenter opened in Haidian District in May 2005. With its Global Procurement Center located in Shenzhen, Wal-Mart is a major exporter from China. Its direct and indirect purchases from China have steadily increased annually, with $18 billion worth of exports reported in 2004. To date, it has relationships with about 20,000 suppliers in China. Wal-Mart plans to open 56 outlets by the end of 2005.

### Wumart Stores, Inc.

**Established:** 1994

**Number of Beijing stores:** 10 hypermarkets, 46 supermarkets, 405 convenience stores, and 8 chain drug stores

**2004 turnover:** ¥13.3 billion ($1.6 billion)

**Largest Beijing store:** Huixin hypermarket, Chaoyang District

Wumart Stores, Inc., a public company listed on the Hong Kong Stock Exchange, operates 650 outlets including hypermarkets, supermarkets, and convenience stores. After 10 years of operation, the company has become the leading retail chain operator in the Greater Beijing area. Wumart has also partnered with China Petrochemical (Group) Corp. (Sinopec) to establish convenience stores in gas stations. In 2003, Wumart obtained $6.5 million from the International Finance Corp., the private sector arm of the World Bank Group.

*—Research staff of the US-China Business Council's Beijing office*

# In-Store Strategies

## Operations management systems can help manufacturers and sales managers optimize sales, merchandising, and promotions in China

Yuan Li Chen

Globally, manufacturers of fast-moving consumer goods (FMCG) are faced with two major challenges. The first and larger challenge is execution: managing a large sales staff to get the right products in the right stores, merchandise the products well, and price them at just the right price point. The second challenge is promotional effectiveness. Because it is becoming increasingly difficult and expensive to reach target consumers through mass-market advertising, such as television ads, most companies are looking for more effective alternatives. They are spending more money "below-the-line," for example, on promotions in the supermarket, where shoppers make 70 percent of their purchasing decisions. To ensure that the promotion budget is well spent, it is critical to understand which promotions are most—and least—effective.

**Yuan Li Chen**
is operations director of Unisono Fieldmarketing (Shanghai) Co., Ltd. and director of the POP Monitor.

Unisono Fieldmarketing offers multinational and Chinese manufacturers outsourced sales, merchandising, brand activation, and information management solutions.

Both of these challenges are closely related to the "retail component" of a manufacturer's business. Many China-based companies, however, have not yet paid full attention to how, exactly, their brands and products are represented on the retail shop floor. This is in part because when the China market first opened, foreign companies had to focus on operational challenges and familiarize themselves with the local market.

Today, because companies have solved many basic business problems and have found that the point-of-purchase (POP) is increasingly the place where they need to convert shoppers into buyers, retail is coming back into focus. In China, as in Europe and the United States, many companies are exploring how best to address the retail component.

### Get the right products into the right stores

When it comes to execution, ensuring product availability is at the top of an FMCG manufacturer's priority list.

First, manufacturers must determine the different channels, such as hypermarkets or convenience stores, through which they will sell their products. Then they must develop a sales strategy for each channel. To get an overall picture of China's retail landscape, in 2002 the POP Monitor developed a web-based database that contains standardized profiles of around 100,000 POPs located in nearly 400 cities across China. In each of these cities, the POP Monitor's census teams regularly walk street by street to map the location and register detailed character-

**To get an overall picture of China's retail landscape, in 2002 the POP Monitor developed a web-based database that contains standardized profiles of around 100,000 POPs located in nearly 400 cities across China.**

istics of all cash-and-carry stores; hypermarkets; supermarkets; pharmacies; convenience, personal care, electronics, and department stores; and shopping malls. Clients can access the database online (www.thepopmonitor.com) to easily cluster POPs in different channels. Manufacturers then decide which products should be made available in each channel.

Second, manufacturers must get the products into the stores. In more mature markets, such as Europe and the United States, this can be achieved by negotiating with the head offices of major hypermarkets, supermarkets, and convenience-store chains. But in China an agreement reached with the retailers' head offices to take up a certain range of products in the assortment does not ensure that the products will be seen in all of the chains' stores. A second round of negotiations with each individual store is necessary to ensure that all stores in the chain indeed order the products and place them on shelf so that shoppers can buy them.

Once products get on shelf, sales staff should make further visits to maintain product availability—continuously suggesting and completing orders for all products.

## No management without measurement: A case study

The following is an example of how the POP Monitor's point-of-purchase database and reporting system work.

An FMCG manufacturer has 80 stock-keeping units (SKUs; 80 different products) and sells the SKUs in cash-and-carry stores, hypermarkets, supermarkets, and convenience stores. First, the manufacturer should define availability standards for each channel. In this case, the manufacturer identified 20 out of 80 products as "must-have SKUs" for convenience stores. Must-have SKUs are specific SKUs that must always be available. Then a target is set for each channel. In this case, 80 percent of the convenience stores must carry all 20 must-have SKUs.

To monitor product availability in each store, the POP Monitor's sales staff completes call cards (paper or digital forms for use on web-enabled mobile phones) to register, among other things, product availability during each store visit. After the sales staff submits the call cards to the POP Monitor, the firm then processes,

**Figure 1: Must-Have SKU Availability Target Compliance**

Target achieved | Target almost achieved | Far from target

| | Cash and Carry Store | | | Hypermarket | | | Big Supermarket | | | Small Supermarket | | | Convenience Store | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| City | Q3 2005 (%) | % change | | Q3 2005 (%) | % change | | Q3 2005 (%) | % change | | Q3 2005 (%) | % change | | Q3 2005 (%) | % change | |
| City 1 | 100.0 | 0.0 | → | 88.9 | -1.1 | ↓ | 71.4 | -12.9 | ↓ | 50.6 | 0.9 | ↑ | 45.0 | 4.3 | ↑ |
| City 2 | 100.0 | 0.0 | → | 88.9 | -11.1 | ↓ | 40.5 | -53.9 | ↓ | 25.8 | -8.2 | ↓ | 9.0 | -24.3 | ↓ |
| City 3 | 50.0 | -50.0 | ↓ | 92.0 | -8.0 | ↓ | 81.0 | -7.9 | ↓ | 44.9 | 19.9 | ↑ | 54.3 | 15.4 | ↑ |
| City 4 | 100.0 | 0.0 | → | 100.0 | 6.7 | ↑ | 66.7 | -3.7 | ↓ | 25.5 | 5.5 | ↑ | 36.4 | 19.9 | ↑ |
| City 5 | 100.0 | 0.0 | → | 100.0 | 0.0 | → | 88.9 | -4.9 | ↓ | 10.5 | -26.3 | ↓ | 0.0 | 0.0 | → |
| City 6 | 100.0 | 0.0 | → | 94.7 | -1.9 | ↓ | 86.7 | -6.7 | ↓ | 66.9 | -7.4 | ↓ | 48.4 | 1.0 | ↑ |
| City 7 | 100.0 | 0.0 | → | 95.2 | -4.8 | ↓ | 81.4 | -5.1 | ↓ | 57.7 | -7.9 | ↓ | 47.0 | 15.4 | ↑ |
| City 8 | 100.0 | 0.0 | → | 77.8 | -9.7 | ↓ | 63.6 | -13.6 | ↓ | 39.6 | 11.1 | ↑ | 18.2 | 18.2 | ↑ |
| City 9 | 100.0 | 0.0 | → | 92.3 | -.05 | ↓ | 66.7 | 4.8 | ↑ | 31.7 | 7.3 | ↑ | 47.4 | 14.0 | ↑ |
| City 10 | 100.0 | 0.0 | → | 100.0 | 20.0 | ↑ | 90.9 | 0.0 | → | 71.2 | 0.8 | ↑ | 100.0 | 50.0 | ↑ |
| City 11 | 100.0 | 0.0 | → | 81.5 | -4.2 | ↓ | 75.0 | 1.1 | ↑ | 33.2 | 4.3 | ↑ | 29.2 | 18.5 | ↑ |
| City 12 | 100.0 | 0.0 | → | 73.3 | -1.7 | ↓ | 50.0 | 1.5 | ↑ | 60.0 | 43.3 | ↑ | 38.2 | 31.9 | ↑ |

Note: Report is simplified for illustration purposes.
Source: The POP Monitor

**Figure 2: Must-Have SKU Availability**

■ SKU available ■ SKU out of stock ■ Void (SKU never reached shelf)

| | | | Must-Have SKUs | | | | | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Store** | **Address** | **Telephone** | **1** | **2** | **3** | **4** | **5** | **6** | **7** | **8** | **9** | **10** | **11** | **12** | **13** | **14** | **15** | **16** | **17** | **18** | **19** | **20** |
| Store 1 | Address 1 | Tel 1 | | | O | | | | | V | V | | | | O | O | O | O | | O | O | |
| Store 2 | Address 2 | Tel 2 | | | | | | | | | V | | | | | | | | | | | |
| Store 3 | Address 3 | Tel 3 | | O | | | O | | | | V | | | | | O | | | | | | |
| Store 4 | Address 4 | Tel 4 | | | | | | | | | V | | | O | | | | O | | | | |
| Store 5 | Address 5 | Tel 5 | | O | | | | | | V | V | | | | | | | | | | | |
| Store 6 | Address 6 | Tel 6 | | | | | | | | | V | | | | | | | | | | | |
| Store 7 | Address 7 | Tel 7 | | O | | V | V | | | | V | | | | O | | | O | O | O | O | |
| Store 8 | Address 8 | Tel 8 | | | | | | | | | V | | | | | | | | | | | |
| Store 9 | Address 9 | Tel 9 | | O | | | | | | | V | | | | | | | | | | | |
| Store 10 | Address 10 | Tel 10 | | O | | V | V | | | | V | | O | | | | | | | | | |
| Store 11 | Address 11 | Tel 11 | | O | | | | | | | V | | | | | | | O | | | | |
| Store 12 | Address 12 | Tel 12 | | | | | | | | | | | | | | | | | | | | |

Note: Report is simplified for illustration purposes.
Source: The POP Monitor

validates, and reports on the collected data within one week.

Figure 1 shows the contents of a report created for an FMCG regional sales manager. The report allows the manager to quickly identify in which cities and in which channels the must-have SKU availability target has been achieved (green cells) or has almost been achieved (orange cells)

**The system helps the sales team identify areas for improvement and prompts them to take corrective action.**

and where the target is still a long way off (red cells). The third-quarter 2005 percentages show the percentage of stores that meet the target.

As their first priority, managers should stop and analyze why targets were missed. In this case, the manager can see that in City 2, only 9 percent of the convenience stores comply with the target (a 24 percent decline compared to the previous quarter). It is time for the manager to take action.

The manager can "drill down" to see the results of each sales representative active in the city. The database ranks sales representatives by performance based on the percentage of stores that reached the required goal. (It is simple to quickly select the weakest performers and review the stores for which they are responsible.) According to managers, when combined with positive reinforcements for those that execute well, these rankings foster a healthy, competitive spirit among sales staff and their managers.

The report illustrated in Figure 2 lists all the stores for which a specific sales representative is accountable. In this case, the sales representative calls only on convenience stores, for which a total of 20 must-have SKUs are defined. The sales representative can quickly see the stores that require his or her attention. A green cell indicates that a specific SKU is available, and an orange cell indicates an out-of-stock SKU. The red cells indicate a manufacturer's worst-case scenario: A fee has been paid to "list" the SKU in the store—the SKU has been included in the store's computer system and its barcode can be scanned at the check-out counter—but the product has never reached the shelf.

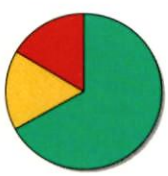
One weakness of the system is its reliance on the input of sales representatives. Recognizing this, auditors trained by the POP Monitor visit a large selection of the same stores to collect availability data as well. The POP Monitor then compares the data provided by the manufacturer's sales team with the POP Monitor's audit data. In some cases, differences of up to 200 percent have been found. (After the sales team realizes the system will be audited, the differences usually drop to less than 10 percent.) In this way, the system helps the sales team identify areas for improvement and prompts them to take corrective action.

**Figure 3: Promotion Effectiveness Analysis**

| | | | | Promotion Details | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| City | Chain | POP | Total sales value | Promotion duration in days | No. of promoters | Daily cost of promoter | Cost of commercial agreement | Total cost | Average cost per promoter day | Average sales value per promoter day | Total cost as % of sales |
| City 1 | Chain 1 | Store 1 | 1,887 | 6 | 1 | 100 | 950 | 1,550 | 258 | 314 | 82% |
| City 1 | Chain 1 | Store 2 | 5,616 | 3 | 1 | 100 | 950 | 1,250 | 417 | 1,872 | 22% |
| City 1 | Chain 1 | Store 3 | 5,160 | 6 | 1 | 100 | 950 | 1,550 | 258 | 860 | 30% |
| City 1 | Chain 1 | Store 4 | 6,124 | 6 | 1 | 100 | 950 | 1,550 | 258 | 1,021 | 25% |
| City 1 | Chain 1 | Store 5 | 10,973 | 9 | 1 | 100 | 950 | 1,850 | 206 | 1,219 | 17% |
| City 1 | Chain 1 | Store 6 | 7,822 | 6 | 1 | 100 | 950 | 1,550 | 258 | 1,304 | 20% |
| | | | 37,581 | | | | 5,700 | 9,300 | 276 | 1,098 | 25% |

| Overview | |
|---|---|
| No. of POPs | 6 |
| No. of POPs as % of total POPs | 9 |
| Commercial budget | 9,300 |
| % of total commercial budget | 11 |
| % of budget that is "money well-spent" | 67 |
| No. of POPs that achieve target | 4 |
| % of POPs that achieve target | 67 |
| % of POPs that almost achieve target | 17 |
| % of POPs that by far do not achieve target | 17 |

**% of POPs that achieve target**



■ % of POPs that achieve target
■ % of POPs that almost achieve target
■ % of POPs that by far do not achieve target

**Money well spent?**

■ Money well spent in the selected stores
■ Money spent in stores where the cost of the promotion as percentage of sales is higher than or equal to 30%
□ Money spent in stores other than those selected

Source: The POP Monitor

## Maximize promotional effectiveness

A common business process is to plan, execute, and review. The same routine is used for promotions. Unfortunately, however, the financial result of a promotion may be far from the expected result. This may occur because a promotion was delayed, incorrectly executed, or poorly communicated, or because items were out of stock. In many cases, companies look at the strategy behind the promotion and conclude that the strategy was wrong. Though the conclusion may be correct, it is reached after reviewing the plan—not the execution—which in many cases may be the true problem.

In Figure 3, a red cell indicates a POP that missed the target widely, raising a number of questions: Does the POP attract the target shoppers? Is the promotion displayed in an eye-catching section of the store? Does the promoter or promotion display meet the manufacturer's standards?

By further drilling down for information in the database on promotion periods, display, materials, pricing, promotion compliance cards, implementation checklists, and SKU availability, and by asking questions such as, "Were promotion SKUs available during promotion?" and "Were out-of-stock SKUs quickly replenished?" an overall picture emerges that enables the sales management team to identify problem areas and, most important, to act to improve the situation.

## Future POPs

The Chinese retail industry has developed rapidly within a short period. About 10 years ago, Carrefour Group and Wal-Mart Stores, Inc. outlets simply did not exist in China. Today, Paris-based Carrefour operates more than 60 hypermarkets in China and Wal-Mart about 50 stores (see p.8). China has lifted most restrictions on foreign retailers in accordance with its World Trade Organization commitments, so the number of foreign-invested stores will only increase. Chinese chains are also multiplying. Shanghai alone already counts thousands of Chinese-owned convenience stores. This expansion means that manufacturers must cover more stores to reach roughly the same number of consumers. The result: rising costs and falling revenues per store.

Most companies today focus their operations on a limited number of stores in first- and second-tier cities. If they reach a critical mass of sales, they can afford to operate sales forces in all of these cities and provide sufficient marketing support. But if their geographical coverage grows to 600 cities, manufacturers are unlikely to accomplish this task efficiently. At this level, outsourcing the sales force becomes more attractive—and the challenge of execution and promotional effectiveness looms even larger. 完

**The number of foreign-invested stores will only increase. Chinese chains are also multiplying. The result: rising costs and falling revenues per store.**


# Moving Forward on Distribution

## After nearly a year's delay, China opens the way for the expansion of foreign retail and wholesale operations

**Research staff of the US-China Business Council's Beijing and Shanghai offices**

December 11, 2004 was supposed to mark the date by which China would fully implement a system to grant trading and distribution rights to foreign investors, in accordance with its World Trade Organization (WTO) accession protocol. But it was not until mid-2005 that the PRC government fully clarified the application procedures for foreign investors to obtain such rights, thereby paving the way for an increase in the rate and number of approvals issued to foreign companies.

Trading rights refer to the ability to import into and export products out of China. Distribution rights denote the ability to sell—either retail or wholesale—products within China. Previously, companies were required to use domestic import-export agents and distributors for their imported products.

### Early delays

Although the PRC Ministry of Commerce (MOFCOM) issued regulations in April 2004 regarding foreign distribution operations, the measures did not clearly define the process by which noncommercial foreign-invested enterprises (FIEs) could expand their business scopes to include distribution. Moreover, various local authorities offered different interpretations of the Measures on the Management of Foreign Investment in the Commercial Sector. This, combined with insufficient interagency preparatory work and coordination, led to confusion and delay.

A survey by the US-China Business Council (USCBC) in March 2005 revealed that none of the surveyed companies had been able to secure trading and distribution rights unless the approvals were obtained under the Closer Economic Partnership Arrangement between the mainland and Hong Kong. Most companies, moreover, had withheld their applications pending clarifications from MOFCOM. Some local governments, including those in Beijing, Shanghai, and Shenzhen, had forwarded to MOFCOM applications to expand business scopes, but none of the local authorities had received responses from the central government. Other localities, meanwhile, were unable or unwilling to accept applications from companies because of the lack of guidance on the process from MOFCOM.

In April, MOFCOM clarified application procedures for noncommercial FIEs and holding companies to expand their business scopes. Shortly thereafter, MOFCOM officials and US companies indicated that the distribution rights application and approval channels seemed to be opening up.

There were several issues that still remained unresolved, however. At the top of the obstacle list was the question of whether FIEs in free-trade zones (FTZs), such as Waigaoqiao in

**Foreign companies may choose one of two ways to acquire trading and distribution rights. They can set up a new, standalone FICE or apply to expand the business scope of an existing FIE.**

Shanghai, could apply for distribution rights. The April 2004 measures made no specific mention of companies within FTZs. As a result, local foreign trade bureaus refused to forward distribution rights applications from companies with operations in bonded zones to MOFCOM, citing either a lack of regulatory authority to do so or the absence of appropriate channels.

In late July, the PRC government issued a notice indicating that foreign companies with operations in bonded zones may apply for distribution rights. And in August, MOFCOM issued three documents that fully clarified the application procedures for investors to establish new foreign-invested commercial enterprises (FICEs), for existing FICEs to open new stores, and for existing FIEs to expand their business scopes. The documents give provincial-level agencies the authority to review and approve applications and—if an FIE is registered in a province other than where it operates—to coordinate with other provincial authorities in the review process.

Thus, almost one year after the WTO implementation date, the process by which FIEs can obtain distribution rights finally came into place. The delay was not necessarily because of the desire to protect domestic companies, as has often been the case with delays in WTO implementation in other sectors. Rather, it appears to have resulted from the need for MOFCOM to coordinate with other ministries and departments, such as the General Administration of Customs and the State Administration of Taxation, to resolve various technical issues. For example, the distribution rights applications of bonded-zone companies were left in limbo in part because MOFCOM and Customs were still in the process of reaching an agreement on whether to treat goods that enter China from the bonded zones as imports or as domestically distributed products.

## The options

Foreign companies may choose one of two ways to acquire trading and distribution rights. They can set up a new, standalone FICE or apply to expand the business scope of an existing FIE. Existing manufacturing FIEs, free-trade zone trading FIEs, investment companies, and regional headquarters FIEs may all apply to expand their business scopes. Companies must specify in their applications the product categories they wish to trade in, based on Customs' Product Catalogue. Manufacturing FIEs may only deal in products that either they or their parent companies pro-

### Implementation of Select China WTO Distribution Commitments

| Commitment | Implementation Status |
|---|---|
| Allow wholly foreign-owned enterprises (WFOEs) in wholesale, retail, and commission agents' service | Done, late. In April and again in July 2005, the Ministry of Commerce (MOFCOM) issued clarifications on combining distribution and manufacturing activity. Manufacturing companies in China are eligible for distribution rights, but are expected to keep revenue from distribution below 30 percent of total revenue to continue to enjoy current preferential tax policies for manufacturing enterprises, although it is unclear how authorities will enforce this requirement. In July, MOFCOM issued a notice allowing foreign-invested enterprises (FIEs) in free-trade zones to apply for distribution rights. In August, MOFCOM clarified the application procedures for distribution rights. |
| Allow franchising | Done. FIEs can apply to franchise in China, although high capitalization and local presence requirements curtail new entrants. |
| Allow direct sales | Done, late. Regulations were issued in September 2005 and take effect December 1, nearly a year after the commitment due date. |
| Allow retailing and wholesaling of pharmaceuticals | Done, late. After initially saying that it would draft separate rules for foreign participation, MOFCOM now approves foreign pharmaceutical retail and wholesale WFOEs using the Measures on the Management of Foreign Investment in the Commercial Sector and the State Food and Drug Administration's Rules on the Management of Drug Business Licenses. |
| Allow retailing of refined fuel | Regulations allow WFOEs (Interim Measures on the Administration of the Oil Products Market), but as currently interpreted, the cap of 30 outlets permitted nationwide limits the value of this commitment. |
| Allow wholesaling of printed matter | Unclear. The 2003 Rule on Management of Foreign-Invested Book, Magazine, and Newspaper Distribution Enterprises opened up the sector early, but the 2005 Opinions on Attracting Foreign Investment in the Media Sector appear to roll back this commitment. |

Source: The US-China Business Council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**It also remains unclear how authorities will enforce the stipulation that manufacturers must earn no more than 30 percent of their revenue from sales of third-party produced goods, including imports, if they are to retain the various tax incentives enjoyed by foreign-invested manufacturers.**

duce; trading companies are generally limited to three product categories; investment companies may acquire up to five categories; and firms with regional headquarters status, as issued by the central government, have no category limitations on the products they may import and sell. Currently, companies with whom USCBC has consulted are generally satisfied with their new business scopes. Some, however, have expressed dissatisfaction with the narrowness of their product scope. There are also concerns that the product category restrictions are inconsistent with China's WTO commitments.

### Quicker approvals

Until the release of final clarifications, applying to set up a new FICE was the quickest method by which to acquire trading and distribution rights. In early fall, however, there was an across-the-board increase in the speed and number of both FICE and expanded-scope FIE application approvals. Manufacturing FIEs, FTZ companies based in Shanghai's Waigaoqiao, and regional headquarters or investment firms have all reported securing approval to expand their business scopes to include trading and distribution rights. Some companies applying to expand their business scopes have reported requests for additional increases in registered capital from local authorities; some firms have found that they can forestall this requirement by clearly explaining in their application's feasibility study report how they expect to finance distribution activities from existing cash flows.

Many of the companies acquiring approvals have used service companies affiliated with local or municipal government bodies, such as the

## At Last, Progress on Direct Selling

The PRC State Council issued the long-awaited direct selling rules in early September, reinstating the legitimacy of a business model that it had banned since 1998. Because of the large number of unscrupulous enterprises that used fraudulent pyramid schemes in the late 1990s to defraud hundreds, if not thousands, of Chinese, the PRC government banned all forms of direct selling and permitted only 10 foreign-invested direct selling companies to operate in China through retail outlets that employed sales representatives. Under its World Trade Organization (WTO) commitments, China agreed to reopen the market to legitimate direct sales firms by December 11, 2004. The regulations do so, but entry requirements are stringent. As with many PRC regulations, difficulties will lie in the interpretation, implementation, and enforcement of the rules.

The Administrative Measures on Direct Sales, which take effect December 1, 2005, indicate that direct sales companies may sell products of their parent and holding companies and may obtain foreign trade and distribution rights. Thus, foreign direct selling companies will be able to sell products without setting up production facilities in China, though they must establish local service networks with fixed locations. The measures impose various other requirements on direct sales companies, including rules for the recruitment and training of salespeople and direct sales trainers.

The Regulations on Prohibition of Pyramid Sales, which took effect November 1, attempt to eradicate illegal pyramid schemes. The regulations define pyramid sales and stipulate severe punishments for such activities. Companies and individuals that violate the rules may be fined up to ¥2 million ($247,179) or face criminal charges, depending on the type and seriousness of the transgression.

As the *CBR* went to press, MOFCOM was soliciting comments on a series of implementing measures that addressed issues including reporting requirements for direct sales companies; remittance and use of bank deposit required of direct sales companies; training for direct sellers; and product scope for the direct sales regulations. The draft measures left many questions unanswered. For example, they did not indicate how the 30 percent cap on commissions for direct sellers will be calculated or whether the multitiered marketing system will be permitted. Companies were hoping that their suggestions would be reflected in the final regulations.

—*Lin Jun* and *Rebecca Karnak*

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Foreign Enterprise Service Center set up by the Shanghai Municipal Foreign Economic Relations and Trade Commission, to assist in preparing applications. These entities are close to the approval bodies and know what is needed in the application to gain approval quickly. Companies that have submitted applications prepared on their own are also getting approvals, however. As the application process becomes clearer, it is likely that approvals will continue to accelerate; waiting times are now estimated at around three months.

## And now for the hard part

As FIEs acquire approval for trading and distribution within China, their focus is shifting to actually selling imported and third-party goods in China. Because relevant government bodies, particularly the customs and tax authorities, have yet to issue regulations governing the import and sale of products by foreign companies, it will likely take some time to develop routine processes and procedures. Firms trying to use trading and distribution rights will probably face new situations that cause uncertainty among local officials. As a result, municipal and local government bodies may delay processing transactions from FIEs with trading and distribution rights until receiving explicit clarification from their superiors—and until the regulations catch up. Ideally, under WTO national treatment principles, FIEs would follow the same procedures as domestic companies.

It also remains unclear how authorities will enforce the stipulation that manufacturers must earn no more than 30 percent of their revenue from sales of third-party produced goods, including imports, if they are to retain the various tax incentives enjoyed by foreign-invested manufacturers. Whether the loss of tax benefits would be permanent or temporary, and whether the new tax rate would be levied starting the next year or retroactively, remain unknown. The regulations also do not specify how the 30 percent would be calculated, an issue of particular concern to manufacturing FIEs that assemble products using a significant amount of imported components. At least one firm is keeping sales of such products to well below that level until this issue is clarified.

In short, China has come a long way in implementing distribution rights, but on several fronts, questions and uncertainties will be resolved only as companies start to exercise their new rights. 完

# China's "Workplace Tweens"

**A recent survey identifies the young drivers of China's consumer and fashion trends**


**Wu Qiong**

"Workplace tweens" in China—young adults with up to two years of work experience—are a driving force in China's consumer market. (The meaning of the term "tweens" in this case differs from its meaning in the United States, where it denotes children aged 8 to 12.) In contrast to young Chinese, such as university students who have not yet entered the workforce, workplace tweens are beginning to participate in society and lay the foundations of their professional careers. And, unlike experienced workers (defined as those with more than two years of work experience), workplace tweens have not yet firmly set their personal preferences and values. Workplace tweens thus boast their own unique culture and consumer characteristics.

An April 2005 survey conducted by Horizon presents a snapshot of these young people and shows, in particular, that workplace tweens have a considerable capacity to consume—in fact, compared to other groups, their purchase of personal consumer goods is explosively high. Strong consumer confidence, a longing for recognition, and the pursuit of individual distinction underpin this group's high consumption capacity. The Horizon survey involved multistage random sampling and door-to-door interviews of 3,515 permanent residents aged 18 to 60 in Beijing; Changsha, Hunan; Chengdu, Sichuan; Guangzhou; Shanghai; Shenyang, Liaoning; Taiyuan, Shanxi; Wuhan, Hubei; and Xi'an, Shaanxi. The data results were weighted to take into account the cities' different populations.

## Big spenders

Compared to experienced workers with comparable financial strength, China's workplace tweens, like their peers in other countries, have fewer responsibilities and more carefree lives. They also bear little resemblance to the older generation of Chinese, which tends to live frugally and simply. Workplace tweens are deeply affected by China's increasingly commercialized culture, as they grew up after China began its economic reform program. Guided by the philosophy of "live now, pay later"—a mantra far too familiar to American consumers—some workplace tweens spend all of their income and even accrue debt. (Indebtedness is a notable phenomenon in a country with a 40 percent average savings rate.) The survey shows that

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workplace tweens spend about ¥1,180 ($146) per month, more than any other group (see Table 1), and the group's consumer confidence index is similarly high. In the survey, workplace tweens were more inclined than any other group to believe that "now" is the right time to spend money.

## Fashion lovers

Unlike most people who enjoy shopping from time to time but wait until special occasions or sales to purchase goods, workplace tweens often turn their pent-up demand for fashionable consumer goods, which they could not afford during their school years, into high levels of spending in the short term. Take digital products, for example (see Figures 1-3). The percentage of workplace tweens who plan to purchase laptop computers is more than three times the average figure for all respondents combined. The percentage of workplace tweens who plan to buy a digital camera is similarly higher than the corresponding figures for other groups.

In the broader picture, the survey reveals that workplace tweens are far more fashion conscious than others and have a stronger desire for trendy products. Workplace tweens score 38 points on the "pursuit of fashion" index, which is much higher than other groups (experienced workers, 18 points; students, 28 points; other respondents, -22 points). The average number of 10 leading fashionable goods, including digital cameras, that workplace tweens own (2.8 sets) is higher than the average for all respondents (1.9 sets).

The workplace tweens' high consumption level and their pursuit of fashion may be a function of their overall outlook. In particular, the survey shows that workplace tweens value fame and achievement far more than do others in Chinese society. As workplace tweens seek

**Table 1: Consumer Outlook: Workplace Tweens vs. Others**

| | Workplace Tweens | Experienced Workers | Students | Other Respondents |
|---|---|---|---|---|
| Consumer confidence | 3.22 | 3.18 | 3.20 | 2.92 |
| Average monthly expenditure (¥) | 1,180 | 1,082 | 669 | 588 |

Source: Horizon Survey

**Figure 1: Popularity of MP3 Players**

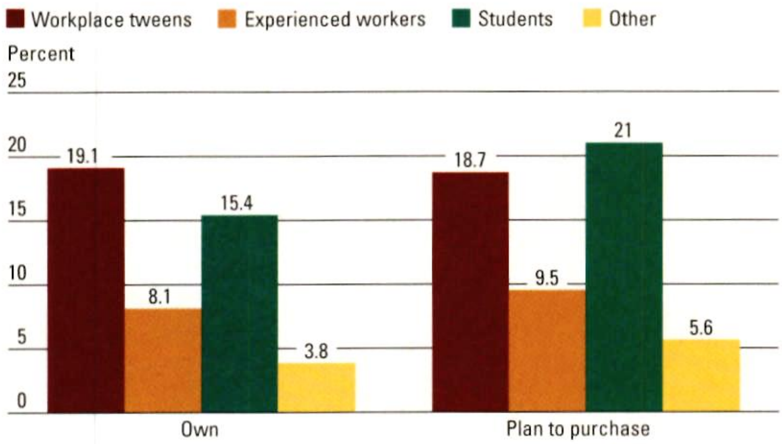



**Figure 2: Popularity of Digital Cameras**

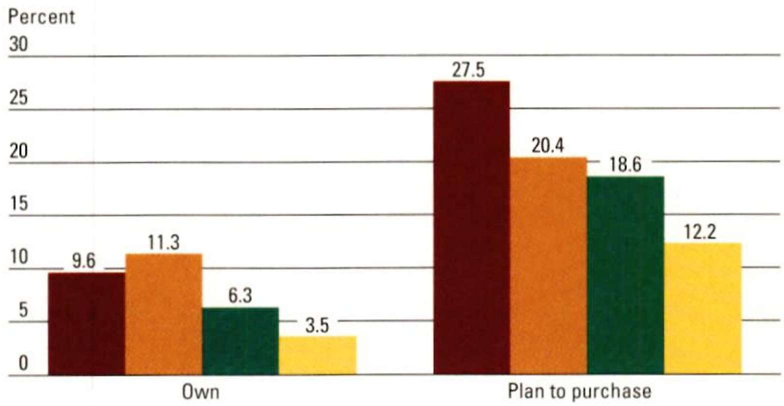
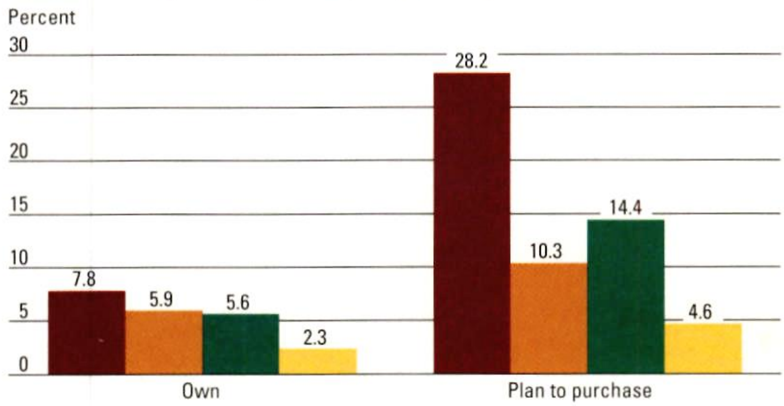



**Figure 3: Popularity of Laptop Computers**



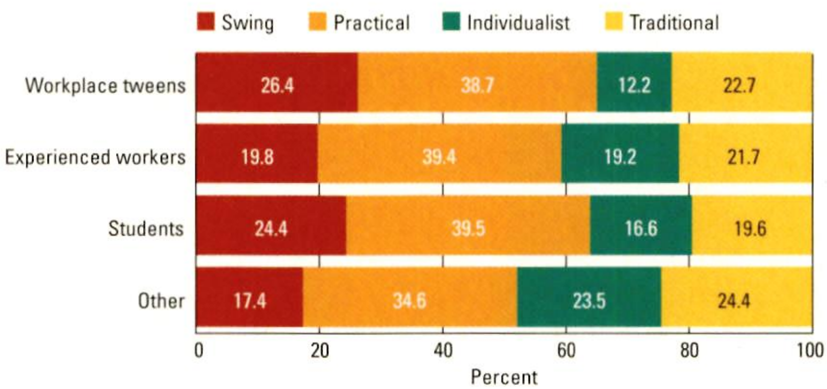

Source: Horizon Survey

**Table 2: Shopping Styles and Phone Brands**

| Brand | Fashion-Oriented Consumers | Enjoyment-Oriented Consumers |
|---|---|---|
| Motorola | 36.3 | 19.6 |
| Nokia | 15.5 | 26.2 |
| Sony-Ericsson | 15.1 | 9.0 |
| Samsung | 7.6 | 15.8 |
| Siemens | 1.3 | 10.2 |
| Others | 24.2 | 14.2 |

Note: Figures indicate percent of group members who own a brand's phone product.
Source: Horizon Survey

**Figure 4: Different Values**




Source: Horizon Survey

**Table 3: Values and Phone Brands**

| Brand | Swing-Type Consumers | Practical-Type Consumers |
|---|---|---|
| Motorola | 38.7 | 22.2 |
| Nokia | 22.4 | 17.2 |
| Sony-Ericsson | 12.7 | 12.1 |
| Samsung | 7.5 | 12.3 |
| Siemens | 1.0 | 11.4 |
| Others | 15.2 | 24.1 |

Note: Figures indicate percent of group members who own a brand's phone product.
Source: Horizon Survey

to join the elite, their ambition leads them to raise their demands for material goods. And, as newcomers to the workforce, workplace tweens tend to seek others' endorsement and recognition. The score of workplace tweens on the "seeking approval" index (9 points) is significantly higher than other groups (experienced workers, 3 points; students, 1 point; others, -1 point).

## Different shopping approaches

Marketing strategies that target workplace tweens should be formulated in accordance with the characteristics mentioned above but should also differentiate workplace tweens by their shopping orientation.

Workplace tweens exhibit two main approaches to shopping. Fashion-oriented consumers are easily attracted by a product's outer appearance, select products based on first impressions, and like to create and follow trends. Enjoyment-oriented consumers, meanwhile, prefer lengthy shopping trips and select their purchases carefully. Thus, for instance, mobile phones with attractive shells appeal more to fashion-oriented consumers, while enjoyment-oriented consumers tend to look for mobile phones that offer useful features and functions.

Products of Sony Ericsson Mobile Communications AB and Motorola, Inc. tend to be more physically attractive than other brands. As such, the ownership rates of these brands are higher among fashion-oriented workplace tweens than among enjoyment-oriented ones (see Table 2). On the other hand, enjoyment-oriented consumers prefer the mobile phone products of Nokia Corp. and Samsung Corp.

## Different values

Respondents were also divided into four categories based on their values: practical types, who emphasize concrete interests and materialistic pursuits; individualists, who put their own feelings first; traditionalists, who prefer routines and the status quo; and swing types, who are concerned with others' views and seek recognition from their peers.

Swing-type respondents appear more frequently among workplace tweens than in other groups (see Figure 4). The desire on the part of workplace tweens to win the recognition and approval of their peers is, in turn, reflected in their consumer behavior: They are ready to purchase goods that their peers believe reflect a high-status lifestyle. Practical types, in contrast, emphasize the usefulness and value of particular products and look closely at product functions.

These different outlooks may also lead to different mobile phone choices. Swing-type tweens tend to choose Motorola and Nokia phones. Siemens AG mobile phones appear to cater more to the needs of practical-type consumers (see Table 3).

## Crafting better marketing strategies

Studying the differences between shopping approaches and individual values not only helps distinguish among workplace tweens, but can also help to clarify the direction that targeted marketing strategies should take.

For example, among workplace tweens, *current* users of MP3 players are mostly swing-type consumers (54.3 percent). Boosting product recognition by engaging popular stars as product spokespersons has been effective in attracting this group of buyers. Most workplace tweens who *plan* to purchase MP3 players, however, are practical-type consumers (53.5 percent). These individuals favor products that offer practical benefits and good value for the price. Having famous stars as product spokespeople will not likely influence them much.

In addition, the choice of celebrity spokesperson should hinge on the different shopping orientations of workplace tweens. Tian Liang, an Olympic gold medalist in diving, is the most admired male athlete for fashion-oriented workplace tweens (20.8 percent), but he is not as highly regarded among enjoyment-oriented consumers (8.9 percent). Therefore, it may be effective to engage Tian Liang as a product spokesperson targeting fashion-oriented workplace tweens but not necessarily their enjoyment-oriented counterparts.

Workplace tweens like to be at the forefront of fashion trends. They are often the creators and promoters of fashion and play an important role in the transformation of a new fashion concept into a commercial trend. Thus, they are not only important consumers but also a key driving force in attracting the rest of the Chinese market to certain products.

Workplace tweens tend not to display much brand loyalty, however. A diverse range of brands is acceptable to this group, and their first impressions of a particular brand will help determine the likelihood that they will purchase products of the same brand in the future.

Grasping the defining characteristics of workplace tweens and taking them into account when shaping marketing strategies will help increase sales volume and revenue in the short term. It will also cement brand recognition and strength in the long run. 完

## China's Workplace Tweens and Leisure

**Leisure activities**

Compared to experienced workers, workplace tweens demonstrate a much greater interest in leisure activities that are relatively new to and unconventional in China. For example, yoga and rock climbing are three times more popular among workplace tweens than among experienced workers. Similarly, workplace tweens are three times more likely to go bungee jumping and skateboarding. Overall, the percentages of workplace tweens who currently, or plan to, participate in new or unconventional leisure activities (44.1 percent and 76.4 percent, respectively) are much higher than those of experienced workers (22.6 percent and 49 percent, respectively).

The entertainment quality of these activities often transcends their fitness value, and workplace tweens' interest in them is consistent with their perception of sports (see Table 1). In describing the value of athletics, workplace tweens tend to emphasize the dynamics, excitement, and vitality of physical activities. Experienced workers, on the other hand, view sports in more practical terms as a way to maintain health and a balanced lifestyle.

**Internet games and online shopping**

Although video games have been common in Chinese cities for more than a decade and many experienced workers were once fans of video games, Internet games—which are still novel—are far more popular among workplace tweens. The survey shows that 36.1 percent of workplace tweens play online games and spend an average of ¥160 ($19.80) per month on them. In contrast, only 13.1 percent of experienced workers report playing Internet games, spending an average of only ¥145 ($17.90) per month.

Workplace tweens shop online more often than older consumers. About 10 percent of them shop primarily through the Internet, compared to 6.5 percent of experienced workers. The percentage of workplace tweens who plan to use the Internet for most of their shopping in the future (14.6 percent) is also higher than the corresponding figure for experienced workers (8 percent).

In terms of goods purchased online, workplace tweens are more interested in buying leisure goods than are experienced workers (see Table 2). For instance, more than 55 percent of workplace tweens have purchased books and magazines online, while less than 45 percent of experienced workers have done so. Similarly, workplace tweens more frequently purchase flowers, gifts, and cosmetics over the Internet than do experienced workers.

—*Wu Qiong*

**Table 1: Perception of Sports: Workplace Tweens vs. Experienced Workers**

| Quality | Workplace Tweens | Experienced Workers |
|---|---|---|
| Youthfulness | 39.8 | 25.0 |
| Vitality | 52.8 | 42.0 |
| Fast-paced | 10.7 | 6.8 |
| Stimulation | 8.5 | 4.8 |
| Health | 58.5 | 74.6 |
| Relaxation | 16.7 | 20.8 |

Note: Figures indicate percentage of group members that associate a word with sports. Because multiple responses were accepted, the figures do not add up to 100 percent.
Source: Horizon Survey

**Table 2: Online Shopping: Workplace Tweens vs. Experienced Workers**

| Product | Workplace Tweens | Experienced Workers |
|---|---|---|
| CDs and VCDs | 56.9 | 52.1 |
| Books and magazines | 55.7 | 44.9 |
| Flowers and gifts | 37.2 | 28.7 |
| Software | 17.6 | 10.7 |
| Cosmetics | 24.3 | 15.6 |
| Home appliances | 5.8 | 11.6 |
| Computer and accessories | 3.6 | 9.3 |
| Clothes | 22.0 | 23.9 |
| Food and beverages | 5.8 | 14.0 |
| Online auction | 8.1 | 13.0 |
| Utility and phone payments | 5.8 | 11.0 |

Note: Figures indicate percentage of group members that purchased particular goods or used certain services on the Internet. Because multiple responses were accepted, the figures do not add up to 100 percent.
Source: Horizon Survey

# Sports Marketing in China: An IP Perspective

## Companies must protect their brands' IP to succeed in sports sponsorship deals

Rebecca Ordish

Yao Ming, a household name in China and the United States, has had an impressive career playing basketball in the Chinese Basketball Association (CBA) and for the Houston Rockets. In 2003, Yao filed suit against the Coca-Cola Co. in China for using his portrait, which was displayed together with the portraits of two other CBA players on commemorative cans. Coca-Cola argued that it had an agreement with the agent of the Chinese national men's basketball team, Chinese Sports Management Co., for sponsorship of the national team to which Yao belonged and therefore had the right to use Yao's image as part of the team. The case, which caused much debate among legal professionals, settled prior to a court decision. Coca-Cola agreed in the settlement to apologize publicly to Yao.

Many other international companies have already taken the plunge into sports marketing in China and are learning its rewards and risks. For example, Siemens AG sponsors the Chinese National Football Team. The company extended its sponsorship to the China Football Association's Super League in 2004, but terminated the relationship in early 2005 because of problems during the Super League's first season. (The season had ended in a near-boycott by sports clubs following widespread allegations of corruption and match fixing.)

Given the increasing popularity of sports among Chinese consumers and China's hosting of a number of international sporting events, it is no wonder that brand owners are seeking out sports marketing opportunities there. But brand owners must take note of the risks, particularly concerning intellectual property (IP) and brand management. Indeed, China's sports marketing environment is relatively new, and many players are inexperienced in the complexities of sponsorship arrangements. Moreover, the PRC regulatory environment is still developing, and IP rights remain difficult to enforce. Only companies that manage risks carefully will protect their brands and get the most from their sponsorship marketing dollars.

### Protect IP rights

The first step to a successful sports sponsorship deal in China is to identify the rights in the deal and to ensure that they are adequately protected. Copyright and design rights will protect certain IP elements, such as logos, athletes' uniforms, and stadium designs. But it is also particularly important to protect trademark and portrait rights in sports sponsorship arrangements.

- **Trademarks: The strongest protection**

A registered trademark is essential to protect IP rights in China, and the more elements a company registers to trademark, the stronger the

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**CHINESE ATHLETES ARE INCREASINGLY AWARE OF THE VALUE OF THEIR PORTRAIT RIGHTS, AND SEVERAL ATHLETES HAVE RECENTLY SOUGHT TO PROTECT THEIR PORTRAITS' COMMERCIAL VALUE.**

company's enforcement options will be and the greater the value of its sponsorship in China. Fortunately, China's enforcement mechanisms for registered trademarks are becoming increasingly effective, and public trust in civil litigation is growing (see the *CBR* November–December, 2004, p.24). In 1998, fewer than 4,000 trademark-related IP infringement cases were filed with Chinese courts. In 2004, the number surpassed 8,300.

Though China recognizes trademarks not registered in China, the protection is limited to those classified as "well-known trademarks." As of 2004, China recognized 153 well-known trademarks including 28 foreign trademarks.

China maintains a "first-to-file" trademark registration system, which makes it crucial for companies to file trademark applications early. Companies should also consider whether to register a Chinese version of their trademark. Pfizer Inc. learned this lesson the hard way when the Chinese pharmaceutical company Shenyang Feilong Pharmaceutical Co., Ltd., registered its own version of Pfizer's brand Viagra, Weige, in China. The Chinese company's registration cost Pfizer a bundle (in legal fees while trying to recover the registration and in lost sales) and has made it harder for Pfizer to expand distribution of its Viagra brand in China.

To protect the value of their investment, sports sponsors should ensure that the rights holders of the sporting event have registered the relevant trademarks in China. In addition to registering more typical items, such as event names, team logos, and event logos, it is possible to trademark some less-common items in China for greater protection. For example, the underwear company Beijing Dani'aier Clothing Co. Ltd., registered the competitor number of a famous Chinese hurdler, Liu Xiang, "1363" for the Athens 2004 Olympics. Also, China allows registration of athletes' names as trademarks, which is impossible in many countries. Some requirements for this right were established when the family of the famous early twentieth-century Chinese author, Lu Xun, tried, but failed, to register his name as a trademark.

## Don't Forget the State

Negotiating sponsorship with a team or with athletes in China raises a unique challenge. Because nearly all athletes in China are supported by state-run sports organizations, the state has the right to manage athletes' commercial rights. Tian Liang, the 2000 and 2004 Olympic diving champion, and a Hong Kong entertainment group learned this lesson the hard way. After entering into a sponsorship arrangement with the Emperor Entertainment Group without state approval in early 2005, Tian was expelled from the Chinese National Diving Team and placed on a provincial squad. Not only were Tian's hopes of future Olympic glory shattered, but the sponsor lost its sponsorship and the money it had already paid under its agreement with the athlete. Sponsors should confirm that the relevant national or local authority, which is determined by the player's team, has approved the sponsorship arrangement and that the athlete has given his or her approval for use of the portrait. Companies should expect sports sponsorship agreements to involve the sponsor, the athlete, and the state.

*—Rebecca Ordish*

**MANY OF THE SPONSORSHIP STRATEGIES AND AGREEMENTS THAT ARE TRIED AND TESTED OVERSEAS WILL REQUIRE TWEAKING FOR SUCCESSFUL USE IN CHINA.**

The initial requirements to register a person's name as a trademark in China are basic: The person must give his or her consent, and the name must be distinctive as a trademark. But in the past (such as in the 2001 Lu Xun case), the state Trademark Office has also tried to keep the names of famous individuals available for public use; the government evidently believes that when a person is held in high moral, historical, or cultural esteem, that person's name is owned by society and should be available for public use. As the status of Chinese athletes increases and their names become ingrained in Chinese culture, the athletes will likely challenge this view.

- **Portrait rights protect the value of an image**

Internationally known Chinese athletes are quickly becoming the new pop stars of China. This year, the Laureus World Sports Awards named Liu Xiang its Newcomer of the Year, an award fellow compatriot Yao Ming won in 2003.

Unlike US law, PRC law provides for a portrait right rather than a separate right of publicity; use of a citizen's portrait for profit without consent is prohibited. Chinese athletes are increasingly aware of the value of their portrait rights, and several athletes have recently sought to protect their commercial value.

The Yao portrait case demonstrates that sport sponsors should confirm that they have the rights they are paying for and that the sports organizations with which they negotiate have the relevant rights regarding the athletes. In the future, sponsorship of individual athletes may well begin to conflict with team sponsorship. When sponsoring a team, sponsors should ensure that their agreement restricts individual athletes from entering into conflicting agreements with the sponsors' competitors.

The portrait right is not absolute. The Haidian District People's Court in Beijing considered its limitations in a recent case involving an image of Liu Xiang winning his gold medal at the Athens Olympics. The photo was placed on the front page of a newspaper above an advertisement for a local department store. Liu believed that the image's placement implied that he had endorsed the department store and therefore infringed his rights. The court divided portraits into two categories: a portrait that is independent of any special significant public event; and a portrait that is associated with a special significant public event. It decided that the portrait right for the former is absolute and the portrait right for the latter is subject to limitations. The court held that Liu's right of portrait, when associated with a major public event such as the Olympics, was subject to a fair use exception. In that case, the photo was used as the cover image for a newspaper article on major events in 2004, and the newspaper had obtained a license from Getty Images, Inc. to reprint the image for news reporting purposes. The court thus ruled in the newspaper's favor.

This case was significant for a number of reasons. First, it underlines athletes' expanding awareness of their portrait rights and the commercial value associated with them for sponsorship opportunities. Second, it shows the court's awareness of the importance of this issue. It seems likely that the district court sought input from the Supreme People's Court, as the judgment was thorough, well argued, and carefully established the reasoning for the decision and the boundaries of the portrait right. The district court likely realized that in the lead-up to the Beijing 2008 Olympics, more athlete sponsorship arrangements will be negotiated, and more companies will seek to benefit from athletes' fame.

## The sponsorship agreement: A critical tool

The sponsorship agreement is important for any sports sponsorship arrangement to succeed. In China, however, the role of the agreement is even more crucial. As sports marketing and event management are relatively new concepts in China, it is necessary to have a clear and detailed contract that specifies the parties' rights and obligations. PRC authorities are often unaccustomed to the types of rights and support international sponsors expect (for example, where logos should be placed at an event, how the "bundle of rights" is divided among sponsors, and how rights holders should promote official sponsors). Many of the sponsorship strategies and agreements that are tried and tested overseas will require tweaking for successful use in China. Though each sponsorship will vary, sponsors should check a few key issues:

- **Confirm the scope of your rights as a sponsor**

Modern sports sponsorships are complex, as brand owners fight for sponsorships and rights holders divide sponsorships into smaller and smaller pieces. Sponsors also try to squeeze as much value as possible from their sponsorship dollar through innovative logo placements. Problems with, for example, logo placement and co-marketing are likely to arise, particularly with venue operators and broadcasters. So it is important for sponsors to include these issues in the agreement to strengthen their future bargaining position. Companies should not assume that sports sponsorship in China will be as sophisticated as sponsorship overseas. In some countries with more developed sports sponsorship markets, vague language, such as "right to logo placement at the event," can work to a sponsor's advantage, as the sponsor bargains for greater coverage. In China, however, it is more likely to lead to frustration, as the expectation gap between the sponsor and the rights holder will often be wide.

- **Keep your sponsorship rights exclusive**

The core value of a sponsorship is derived from the extent of its exclusivity. This needs to be carefully negotiated; companies should make sure their sponsorship agreement contains no "gaps" that could allow competitors to reduce the value of the sponsorship through ambush marketing (when competitors of official sponsors associate their brand with the event without authorization). One of the best ways to prevent ambush marketing is through a strong sponsorship agreement that expressly covers the company's expectations of the rights holder and that addresses all appropriate sponsorship rights. Sponsors must not leave a form of media out of their agreement—such as the Internet, which is commonly forgotten—and risk finding their competitor sponsoring the official website. Examples of clever ambush marketing can be found in many past sporting events. For example, for the 2000 Sydney Olympics, which was officially sponsored by the now-defunct Ansett Australia, Qantas Airways Ltd. launched an intensive advertising campaign that featured a number of Olympic athletes. And Adidas-Solomon AG's official sponsorship of the 2002 World Cup was ambushed by Nike Corp.'s sponsorship of the Brazilian team, whose members all wore Nike uniforms.

Compared with their Chinese counterparts, many international sponsors have a distinct advantage: They understand how to get the most out of their sports sponsorships. For example, they do not merely slap a logo on a uniform, but create noise around their brands through associated events and marketing campaigns. On the other hand, Chinese companies' marketing strategies are becoming increasingly sophisticated, and more domestic companies are sponsoring overseas teams and athletes. For example, Haier Group Co. sponsored the Australian professional basketball team in 2004. And many high-profile Chinese firms, such as Lenovo Group Ltd. and Haier, will sponsor the 2008 Olympics.

One of the risks associated with sponsorship in China is ambush marketing by Chinese companies that use their relationships with authorities to target foreign brand owners' sponsorship of events. To minimize this risk, it is important to ensure that the sponsor address all appropriate rights and confirm in the agreement that the rights holder is obligated to prevent ambush marketing.

- **Confirm that the rights holder will also protect IP**

Unfortunately, a boost in a sponsor brand's global exposure and growth in China's sporting industry make infringement of related IP rights ever more likely. Brand owners must take steps to protect their own brands *and* must expressly place an obligation on the rights holder to protect the value of the IP in which the brand owner is investing. The rights holder should also assist and control infringements in a fast, effective manner (for example, by providing evidence of their rights to PRC authorities). The sponsorship agreement should expressly cover these expectations.

**ONE OF THE RISKS ASSOCIATED WITH SPONSORSHIP IN CHINA IS AMBUSH MARKETING BY CHINESE COMPANIES THAT USE THEIR RELATIONSHIPS WITH AUTHORITIES TO TARGET FOREIGN BRAND OWNERS' SPONSORSHIP OF EVENTS.**

## Learn the risks, aim for the rewards

As the disposable income of China's burgeoning middle class rises, so does the power of sports in China. Recent years have seen a significant shift in the sophistication and prestige of China's sporting events. Shanghai first hosted the Formula 1 Grand Prix in 2004. This year, the same Shanghai track hosted the Moto GP World Championship and the V8 Supercars from Australia, and China's second Formula 1 Grand Prix event was held in October. The Tennis Masters Cup, featuring the world's top eight male tennis players, will take place in Shanghai in November. Shanghai also played host to the Volkswagen 48th World Table Tennis Championships in May.

The opportunities are undeniable, but sports sponsors should be careful as they enter the Chinese market. Event management is still in its early stages in China, and local sports marketing skills are still thin on the ground. It is important for companies to plan carefully and to ensure that the investment they are making is protected, particularly from an IP perspective. Sports marketing is, after all, about the power of brands—the combined power of the sponsor's brand and the rights holder's brand to deliver value to both sides of the table. 完

# Foreign Investment Verification: Reform, Status Quo, or Bafflement?

**Recent measures that govern foreign investment project verifications are causing tremendous uncertainty**

**Amy L. Sommers**

In July 2004, the PRC State Council issued its Decision Regarding Reform of the Investment System, which appeared to mandate the National Development and Reform Commission (NDRC) to issue regulations that would promote more efficient investment in capital- or resource-intensive, or infrastructure-related, projects. But when NDRC unveiled the follow-up Provisional Measures for Verifying Foreign Investment Projects in October 2004, no one applauded. In fact, many commentators are still scratching their heads, puzzled about how to interpret the provisional measures and their place in the phalanx of existing regulations governing foreign investment in China.

### If it ain't broke...

NDRC has asserted both that nothing has really changed and that the provisional measures reflect the spirit of the July 2004 decision by placing approval jurisdiction lower in the bureaucracy, simplifying procedures, and raising the level of efficiency. An NDRC official interviewed by Xinhua News Agency in November 2004 stated, "Not only has there not been a change in China's methods of encouraging foreign investment, the measures have also made the environment for the system of foreign investment in China even more beneficial." How can one set of regulations both maintain the status quo and effect such seemingly sweeping changes?

Before evaluating whether the provisional measures have changed the process for approving foreign investments in China and, if so, the extent of the changes, it is helpful first to review the approval process. Since the early 1980s, all foreign investment has flowed through the Ministry of Commerce (MOFCOM) or its predecessors, either at the national level or at the provincial or municipal level, depending on the size and sector of the investment. MOFCOM's approval authority has been couched in terms of approval of entities rather than projects. But, as part of its review of the applicant's proposed constitutive documents, MOFCOM makes substantive comments on the bona fides of the prospective investors' business or projects. MOFCOM would probably tell anyone who bothered to inquire that this process has worked well for foreign investors and for MOFCOM itself. Foreign investors might be less sanguine but would probably concede that MOFCOM is at least a known quantity.

Until now (or, perhaps, even now), foreign investors that wish to invest in a business must establish a PRC legal entity or transfer ownership interests (through acquisition or merger) in an existing entity. The applicant would submit relevant documents, such as the articles of association, to the appropriate MOFCOM-affiliated agency for review, comment, and approval. MOFCOM has up to 90 days to decide whether to approve an application to form an equity joint venture (JV) or a wholly foreign-owned enterprise (WFOE). A shorter period applies to the approval of cooperative JVs.

If the investment falls into an area that is restricted for foreign investment, the investor must submit its application materials to the ministry charged with regulating investment in that sector. (The Catalogue Guiding Foreign Investment in Industry classifies every conceivable type of investment into one of three categories: encouraged, restricted, or prohibited.) If an investor wants to establish an educational

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venture, for example, it needs the approval of the Ministry of Education; if a logistics venture, the approval of the Ministry of Communications.

After MOFCOM or its local counterpart issues a certificate of approval, the applicant would then apply to the State Administration of Industry and Commerce (SAIC) or a local administration of industry and commerce (AIC) for a business license. That step has been largely administrative, with the strictest review occurring during the MOFCOM review stage. Though this process of foreign investment approval may not have been as simple as filing articles of incorporation in Delaware, at least it is well known and understood.

### Scope of the provisional measures

The provisional measures state that "projects" in the encouraged category that involve a total investment of at least $100 million or those in the restricted category with a total investment of at least $50 million should be submitted to NDRC for verification and approval (see Table). If a project in the encouraged category calls for total investment of $500 million or more, or if it is in the restricted category and involves $100 million or more, NDRC must also seek State Council approval. Thus, MOFCOM authorizes the formation of legal entities, though, according to the measures, NDRC vets the validity of the proposed projects.

For projects of less than $50 million in the restricted category or less than $100 million in the encouraged category, the decision about whether and how to verify such projects rests with local development and reform commissions (DRCs). The measures indicate that provincial-level DRCs must verify projects in the restricted category and that any local DRC may verify and approve projects in the encouraged category. But the measures grant significant leeway for local authorities to decide whether and how to exercise their verification powers. The last sentence of Article 4 of the provisional measures states, "If a local government has other stipulations on the verification of the projects listed in the preceding paragraph according to the relevant regulations, such stipulations shall prevail." Under this provision, DRCs could waive their opportunity to review foreign investors' projects by, for example, adopting regulations on verification and approval processes that do not call for verification or by electing not to adopt any regulations.

Local DRCs may, however, choose to exercise the verification authority and make an already-complex picture even more complicated. Indeed, certain municipalities have adopted rules that further delineate which local DRCs review certain projects. For example, Beijing and Chongqing require provincial-level DRCs to verify projects in the encouraged category with total investment of between $30 million and $100 million, as well as those in the restricted category of less than $50 million. But district- or county-level agencies verify encouraged projects in those two cities with a total investment of less than $30 million. Meanwhile, in Tianjin, which DRC is in charge of reviewing a particular project depends on the project's investment amount and category, whether the project is port-related, and whether the project is limited to one of Tianjin's special zones, crosses zones, or spans a zone and the rest of Tianjin. (As of October 10, Shanghai has not adopted local DRC verification regulations, but an official with the Shanghai DRC indicated that verification is nevertheless required. The lack of regulations suggests that verification can be very subjective.)

What all this means for foreign investors is that the investment approval process can become much more complex, as considerable discretion devolves to the local DRCs. Whether the step of seeking verification from DRCs—in addition to the existing MOFCOM approval process—is necessary depends on how active a local DRC wishes to be. The fact that investors may find considerable regional variation in DRC verification processes has already attracted considerable comment within China, especially from lawyers working with foreign investors.

Whether the step of seeking verification from DRCs (in addition to the existing MOFCOM approval process) is necessary depends on how active a local DRC wishes to be.

### Verification criteria: Potential concerns

The provisional measures set forth six criteria for evaluating and verifying applications submitted to NDRC. The criteria are interesting because they reflect concerns about the balance of foreign investment and protection of domestic business interests, including those of the government. The projects must

**Table: Verification of Foreign Investment Projects, Including Capital Increases***

| Investment Category | Amount ($) | Verification Agency |
|---|---|---|
| Encouraged | under 100 million | Local development and reform commission** |
| Encouraged | at least 100 million | NDRC |
| Encouraged | at least 500 million | NDRC and State Council |
| Restricted | under 50 million | Local development and reform commission** |
| Restricted | at least 50 million | NDRC |
| Restricted | at least 100 million | NDRC and State Council |

Notes: * Article 2 of the Provisional Measures for Verifying Foreign Investment Projects indicates that the measures apply to projects for Sino-foreign joint ventures and wholly foreign-owned enterprises, mergers and acquisitions of domestic enterprises by foreign investors, and capital increases by foreign-invested enterprises.

** The local development and reform commission has discretion over whether to exercise its verification authority and, if so, how.

Source: Provisional Measures for Verifying Foreign Investment Projects

**1** Comply with relevant PRC laws and regulations (including the investment catalogue);
**2** Comply with medium- and long-term national economic and social development and relevant industry plans and polices;
**3** Accord with public interest and conform to relevant provisions of PRC law governing antimonopolistic practices;
**4** Observe relevant land-use planning, macro urban planning, and environmental protection measures;
**5** Conform to national standards on technology and technical methods; and
**6** Comply with PRC law governing administration of capital accounts and foreign debt.

**The measures could be implemented in a way that would conflict with the WTO's national treatment principle.**

Clearly, these criteria provide considerable leeway for NDRC to limit the participation of foreign investors in the PRC market. For example, with regard to compliance with PRC measures that govern antimonopolistic practices, it is perhaps instructive to recall that in May 2004, SAIC issued a report that criticized alleged monopolistic practices by foreign multinational corporations. The new Antimonopoly Law, expected to be adopted in 2006, could open the door to the issuance of regulations that address those concerns (see the *CBR*, May–June 2005, p.30).

More important, as indicated above, Article 4 of the provisional measures allows and encourages the development of local standards for verification, which may differ from those of NDRC, vary widely across the country, and often limit participation by foreign investors in projects that are of interest to domestic firms that are well-connected in a particular locality. The PRC government might argue that this is no different than the division of power between MOFCOM and its local counterparts. But, as mentioned above, MOFCOM is a known quantity. In contrast, the measures, while enabling DRCs to erect administrative hurdles for foreign investors, do not provide (at least as of this writing) clear standards for all localities.

Thus, one might ask whether the provisional measures reflect an attempt by the PRC government (or, at least, a segment of it) to reclaim ground "lost" during the World Trade Organization (WTO) market-opening process. In particular, the measures could be implemented in a way that would conflict with the WTO's national treatment principle. Ultimately, these potential concerns could become significant in particular because the provisional measures apply not only to the formation of new projects, but also to increases in registered capital for *existing* investments. In other words, foreign investors already in China remain within the reach of these potential obstacles.

Growing concerns about depletion of raw materials, scarce energy resources, and burdens on the environment have certainly helped shape the provisional measures. The measures depart from previous ones, which required applicants to submit an environmental impact statement to the relevant land and resources administration bureau. The new rules mandate that applications to NDRC provide an environmental impact opinion from the provincial- or national-level environmental protection agency, an opinion on zoning issues for the project's prospective location from the provincial-level planning department, and an opinion on the preliminary examination of the proposed land use issued by the provincial- or national-level land and resources agency. Beijing, Chongqing, and Tianjin also require the same items, with variations on the agency to which they must be tendered, depending on the project.

Cynics might observe, however, that under the provisional measures, localities do not have to require these documents at all. Moreover, although the July 2004 decision requires all kinds of enterprises to comply strictly with laws and regulations regarding resources and land use, zoning, and environmental protection, NDRC has taken a less rigorous approach in addressing activities by domestic enterprises. Regulations for domestic enterprises cover only overseas investments and domestic fixed-asset or infrastructure-type projects that do not include any public funding—in other words, a relatively narrow class of projects. The provisional measures, on the other hand, apply essentially to *all* foreign-invested projects. Thus, foreign investors are far more heavily affected than domestic enterprises.

## Reactions from MOFCOM and foreign investors

In response to a query about whether projects must pass through the NDRC process before a foreign investor can apply to MOFCOM to establish or amend the structure of an entity, a MOFCOM official provided a suitably tautological reply: Projects needing verification (note: he did not say "approval") from NDRC or its local counterparts, as stated in the July 2004 decision, should follow the procedures as stipulated in the provisional measures to acquire verification from NDRC or its local counterparts. Investors then should file with MOFCOM or its local counterpart to establish the foreign-invested enterprise. So that settles that. Or does it?

The normal practice to form a WFOE in Beijing has been to file a name reservation with the local AIC, file the documents to form the WFOE with the municipal or the applicable district bureau of commerce, obtain a business license from the AIC, and then complete the post-licensing registrations, such as with the tax bureau. Beijing's AIC has taken the position that it does not need verification from the local DRC to issue the business license of a WFOE. If the foreign investor seeks to establish a JV, however, the AIC will not issue the business license unless

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**—Vaughn Koshkarian**
**President, Ford Asia Pacific Operations and Vice President**
**Ford Motor Company**

it has received confirmation that the local DRC has verified the new JV's proposed projects.

There appears to be no basis, though, in either the provisional measures or any local law or regulation for making such a distinction between WFOEs and JVs. The practice of Beijing's AIC thus indicates that the actual extent to which local DRCs will play an important role in the foreign investment project approval process depends on the willingness of other agencies to condition their own actions and procedures on the local DRC's approval. (It is also interesting to note that the Beijing AIC's practice has existed for some time, even prior to the adoption of the provisional measures, which suggests that the measures may be irrelevant in particular localities.)

Because local authorities could delay projects using the leeway granted by the provisional measures, however, some investors are simply acting as if the measures do not exist and are sticking with the MOFCOM approval process. Others are contacting local DRCs to inquire whether a particular project must be vetted by a DRC. In many cases, the answer is "no," but, as discussed above, the legal basis for declining to exercise jurisdiction is not entirely clear. It is the piecemeal nature of responses by local agencies and the lack of certainty that are most troubling to investors who seek predictability in both the timing and the steps necessary to get their ventures off the ground.

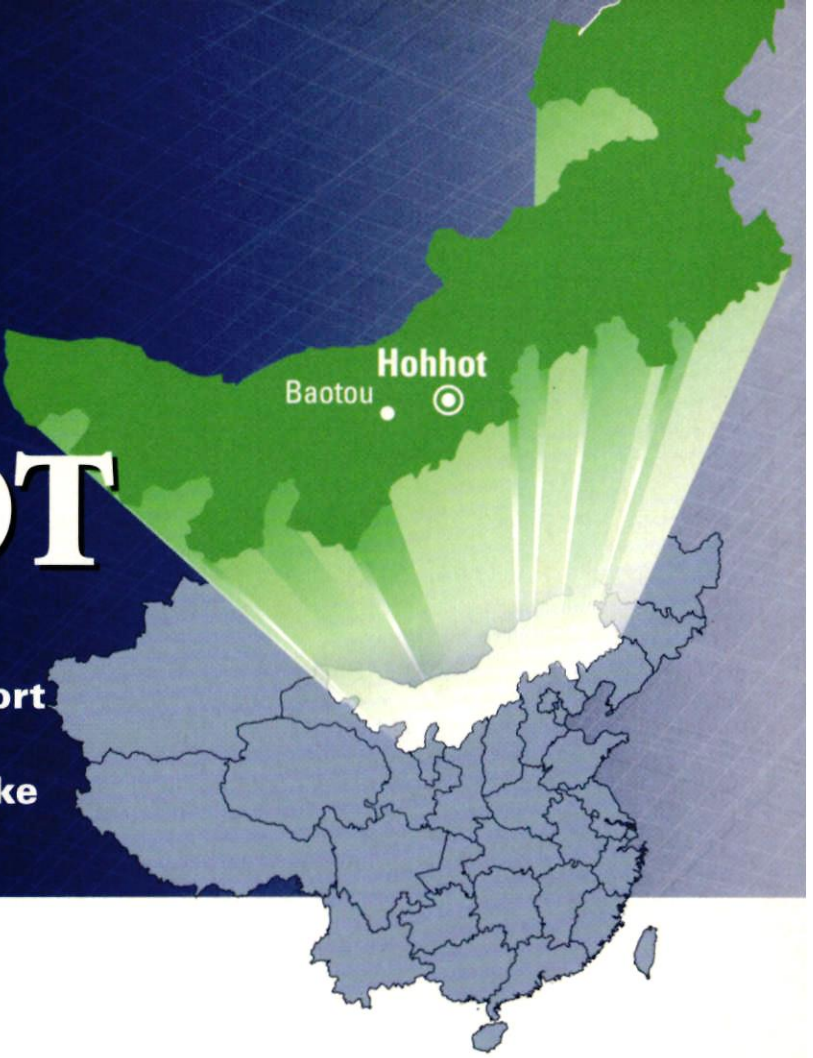
## Will the fog clear?

The provisional measures clearly suggest that the aim of NDRC (but not necessarily of MOFCOM) is to provide room for further checks on the bona fides of foreign-invested projects in China. NDRC's claim that the provisional measures do not reflect a significant change in the investment climate seems rather unfounded, at least on the face of the measures. Beijing, Chongqing, Shanghai, and Tianjin have already staked out territory for local-level DRCs to vet foreign investment projects.

More troubling, though, is that the measures leave room for local authorities to craft standards and procedures that could treat domestic and foreign investors differently and that could make it harder for foreign investment projects to receive a green light. As with so much in China, only time will tell how the story plays out. 完

# CRITICAL EYE ON HOHHOT

**Ample raw materials, energy sources, and investment support make Inner Mongolia's capital ripe for investors willing to take the road less traveled**




**Lisa M. Hoff and Victor Hou**

In the early thirteenth century, when the Mongol conqueror Genghis Khan and his sons ruled Asia from the Pacific Ocean to the borders of Eastern Europe and from Siberia to the Sea of Bombay, the area now known as Hohhot served as the capital of the Mongolian Empire. The capital was the region's center of commerce, law, religion, arts, and culture.

Today Hohhot, which means "blue city" in Mongolian, is the capital of Inner Mongolia, one of China's ethnic-minority autonomous regions. Reflecting its past as a cultural crossroad, Hohhot is a diverse city of roughly 2.5 million people that is once again becoming a trade nexus in northwestern China.

Excluding China's four directly administered municipalities, Hohhot has grown faster than any other Chinese city in the last four years. The city's GDP rose 33.3 percent from 2003 to 2004, jumping from $4.9 billion to $7.2 billion. According to 2004 statistics, the key industries that drove this growth are electronic information systems (40 percent of growth), dairy (30 percent), and electric power (20 percent) generated by coal, solar energy, and wind. Other important industries include real estate, construction, general manufacturing, services, and retail.

Hohhot's economic growth is the result of a confluence of factors, including its strategic geographic location, valuable and abundant natural resources, government support, and competitive workforce.

## Frontier town

Inner Mongolia stretches across China's northern frontier. It borders nine Chinese provinces and two countries—Russia and the Republic of Mongolia.

Trains, trucks, and airplanes arriving and departing from Hohhot carried nearly $4 billion in natural resources and manufactured goods to western China, Mongolia, Russia, and Europe in 2004. The recently completed trans-Asian railroad links Hohhot to Frankfurt, Germany, by rail in 18 days. (Prior to the container rail line's completion in March, shippers sent containers by sea through the Port of Tianjin, which could take roughly 40 days.)

Beijing and Tianjin lie about 600 km and 710 km southeast of Hohhot, respectively—making Hohhot only a 45-minute flight or a 5-hour

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**Victor Hou**
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## Hohhot at a Glance

### By the Numbers

| | |
|---|---|
| GDP (2005 estimate) | $8 billion |
| Population (2005 estimate) | 2.58 million |
| Urban | 1.5 million |
| Rural | 1.08 million |
| Urban per capita disposable income (2004) | $1,228 |
| Rural per capita disposable income (2004) | $490 |
| Total foreign trade (2003) | $488 million |
| Exports | $362 million |
| Import | $126 million |
| Foreign investment (2004) | $239.4 million |

Sources: Hohhot Development and Reform Commission; Hohhot City Government; *Hohhot Statistical Yearbook, 2005*

### Contacts

**City Government**
Mayor: Tang Aijun
Director of Regional Trade: Sun Qingshan
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Fax: 86-0471-460-5568
www.huhhot.gov.cn

**Hohhot Bureau of Commerce**
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E-mail: info@hhboftec.com
www.hhboftec.com

**Inner Mongolia Administration of Industry and Commerce**
Tel: 86-0471-662-8490
Fax: 86-0471-662-8475
E-mail: wjf_gsj@nmg.gov.cn
www.nmgs.gov.cn

### National-Level Development Zones

**Hohhot Economic and Technical Development Zone, Ruyi District**
Vice Director of Investment Promotion: Ma Qing
Tel: 86-0471-462-7630
Fax: 86-0471-462-7630
E-mail: maqing2004@126.com
www.hetdz.com.cn/zw.php

**Hohhot Economic and Technical Development Zone, Jinchuan District**
Chief of Foreign Investment Promotion Bureau: Lan Changqing
Tel: 86-0471-360-1229
Fax: 86-0471-360-1223
E-mail: lcq7225@163.net
www.hhjcq.gov.cn/home/index.asp

drive from the nation's capital. For corporations with offices in Beijing, Hohhot provides a convenient manufacturing base. Trains from Hohhot arrive at the Port of Tianjin in 12 hours.

In preparation for the 2008 Beijing Olympics, China is upgrading Hohhot's transport infrastructure. The PRC central government earmarked $70 million to build a new international airport there, scheduled for completion in 2007. It will serve as backup for Beijing Capital International Airport in case of weather disruption or overcapacity. The superhighway between Hohhot and Beijing was completed in September 2005.

### Powering Hohhot industries

The natural resources found just outside the city supply energy to locations across China and provide raw materials for Hohhot's factories. Roughly 140 rare-earth minerals, including gold deposits, iron ore, granite, and graphite, are available within 100 km of Hohhot. Twenty percent of Beijing's electricity is generated by coal mined in Inner Mongolia. One of the largest natural gas reserves in Asia lies to the west of Hohhot—the Sulige natural gas field in the Ordos Basin. Alternative energy sources, namely solar and wind, dot the villages that surround Hohhot and offer a secondary energy source for the city's factories, businesses, and residents. Each year, while factories in southern China endure brownouts, blackouts, and reduced operating hours, factories in Hohhot work around the clock to drive the regional economy.

Eighty percent of the wool used for cashmere fabric in China is sourced from Inner Mongolia. China's top two dairy companies—China MengNiu Dairy Co., Ltd. and Inner Mongolia Yili Industrial Co., Ltd.—are headquartered in Hohhot and operate state-of-the-art processing plants that produce milk and dairy products for China and abroad. One of China's top consumer electronics manufacturers, TCL Corp., operates two factories in Hohhot that produce cell phones and TVs for domestic and international markets.

Although Hohhot can supply a variety of raw materials, some foreign companies encounter procurement problems. Because Hohhot is home to few foreign suppliers, foreign companies may need to import some components and semi-finished assemblies from overseas or from other provinces.

### Government support

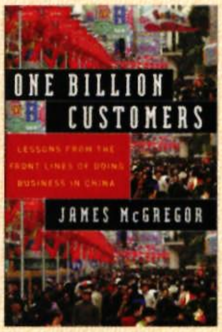
As part of the PRC central government's preferential economic policies for minority areas and its 2000 Great Western Development Strategy, Hohhot enjoys special financial and tax incentives and some relaxed government policies. The two economic development initiatives provide companies that invest in the area certain advantages, such as lower land and natural resource costs and some freedom from central government restrictions.

The central government has also commissioned two national-level economic and technological development zones (ETDZs) in Hohhot: the Ruyi ETDZ, which is located in eastern Hohhot, near Baita Airport and the city and provincial government complexes; and Jinchuan ETDZ, which is located in the western part of the city and includes the Hohhot Export Processing Zone. The Ruyi and Jinchuan zones make up the Hohhot Economic and Technological Development Zone. Jinchuan's export processing zone contains bonded warehouses and a dedicated customs processing office; factories that export at least 51 percent of their production enjoy value-added tax exemptions and logistics support.

The city government also hopes to steer development and investment toward many provincial and local-level zones that do not yet have national-level status or administrative operations. The Inner Mongolia Administration of Industry and Commerce handles investments in these zones.

*Continued on page 46*

# Reviews




## One Billion Customers: Lessons from the Front Lines of Doing Business in China

**By James McGregor. New York, NY: The Free Press (Simon & Schuster, Inc.), 2005. 336 pp. $27.00 hardcover**

Anyone involved for any length of time in commercial transactions with China has read his or her share of the many books that claim to explain all and reveal the secrets that will make the difference between success and failure. *One Billion Customers* stands out from this crowd in a few important ways.

James McGregor, former head of Dow Jones & Co.'s China office, started out in China as a journalist. He is now a businessperson in China and has thoughtfully structured the book with this audience in mind. Each chapter contains an overview, an often-riveting story broken up into short subsections, and a wrap-up section entitled "What This Means for You." Each chapter closes with McGregor's "Little Red Book of Business" that lifts the most important lessons of each chapter and places them in the businessperson's favorite format, the bulleted list.

It is the carefully chosen stories, and the descriptions of the characters that bring these stories to life, that are the heart of the book. Many of the stories have become legends in the history of China business and are familiar to those of us who have watched the events unfold. But McGregor zeroes in on the details that are most likely to provide lessons for a foreign company operating in China.

Many of these lessons arise out of the face-to-face interactions between Chinese and foreign managers and between Chinese or foreign businesspeople and PRC bureaucrats. For instance, in the chapter on Morgan Stanley's joint-venture investment bank, China International Capital Corp., McGregor discusses the different styles and perceptions of the venture's two leaders—Jack Wadsworth of Morgan Stanley and Wang Qishan, now mayor of Beijing but then head of China Construction Bank. McGregor points out not only the cultural differences that were partly responsible for the problems between the two, but also the fact that the two men used interpreters from within their respective organizations who filtered the communication according to the interpreters' own agendas. The lesson: Hire independent translators.

In a chapter on corruption, McGregor recounts the rise and fall of smuggler Lai Changxing, who ran a phenomenally successful operation in the southern port city of Xiamen, Fujian. Lai's superior ability to form personal relationships with PRC officials propelled him to the top, but it was not enough to prevent his downfall when leaders in Beijing needed a high-profile case to demonstrate their commitment to eliminating corruption. The lesson for foreign businesspeople: "[R]elationships and personal power reign supreme" in China. But, McGregor states firmly, "Don't Bribe. Nobody stays bought and the Chinese know it is against American law. Instead, invest in long-term, mutually beneficial relationships with customers including training, travel, and recreation opportunities."

McGregor also uses his experience as chief China representative for Dow Jones to suggest ways to solve problems that arise with PRC government officials who will inevitably interfere in the day-to-day operations of a foreign company in China and may even attack the very existence of the foreign operation. This was the case for Dow Jones and Reuters, when Xinhua News Agency, acting as both regulator and competitor, tried to use its authority to move in on the lucrative financial news market by demanding that the two companies pay heavy fees and turn over their proprietary technology to Xinhua. McGregor's success at beating back this attempt provides another set of important lessons for foreign companies facing such issues today: Establish government relations functions to anticipate, and deal with, such inevitable issues. These experts will be crucial to deciding how high up to take your dispute, how hard to push the bureaucracy, and when to take a deal, McGregor says.

His concluding chapter provides some insights—and perhaps solace—for foreign companies fearing the rise of new Chinese multinationals. McGregor points to thousand-year-old traditions that are likely to stand in the way of Chinese corporations' growth. Among these are the "stuffed-duck-style" educational system in which "[s]ubjects are taught in isolation and rarely does anyone make a link between two subjects, like statistics and marketing." Another is the fact that internal cooperation is largely absent from most Chinese organizations, which tend to develop from the top down under a "benevolent dictator." This is why, according to McGregor, "Long term mentoring is the single most effective technique for foreign companies to build an effective Chinese executive corps."

The book boils down such lessons particularly well. In this way it succeeds where a wordier narrative, or a more academic management textbook, would not. China experts may take issue with some of his generalizations about the Chinese psyche. Others may quibble with the solutions he proposes. These objections do not detract from the book's value as an important tool for foreign businesspeople in China. In short, McGregor has written a book about doing business in China that seems destined to become a classic.

—*Catherine Gelb*

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Catherine Gelb is editor of the *CBR*.


## The Business of Lobbying in China

**By Scott Kennedy. Cambridge, MA: Harvard University Press, 2005. pp.278. $49.95 hardcover.**

During a recent taxi ride in Washington, DC, a lobbyist estimated that $1 billion per month was being spent in the nation's capital on lobbying activities. Though the Washington lobbying scene may seem mysterious to many, even less is known about the level of interaction between business groups and the central government in China. Scott Kennedy's groundbreaking work, *The Business of Lobbying in China*, which was based on his doctoral dissertation, attempts to navigate these uncharted waters.

Formalized associations of business groups did not exist in China until recently, in part, because of central-government worries about organized activity and also because of the "free-rider" effect—essentially, Mancur Olson's theory that groups generally rely on the collective action of others to derive benefits rather than expending valuable resources. Unlike in the United States, where officials are banned from holding other positions, China permits sitting officials to preside over trade groups, thus diminishing some of the autonomy that a business association might otherwise enjoy. These dual-hat officials may unduly influence or hinder the national coordination of industry-specific policy. At the same time, however, lobbying efforts may be facilitated when an official who is tasked with the regulation of an industry also presides over its trade association. As Kennedy writes, "The limited autonomy of business associations—due to a government role in their creation, affiliation with government agencies and the frequent presence of government officials on the staff, and limited overlap among some associations originally organized by ownership—is still commonplace."

Through a series of case studies, Kennedy, an assistant professor at Indiana University, closely examines three industries that illustrate the larger lobbying picture in China: steel, consumer electronics, and software. Steel is predominantly state owned, while consumer electronics is dominated by the private sector. The software industry falls somewhere in the middle and includes a balance of foreign and domestic players. Kennedy documents, analyzes, and tracks how far China's business groups have come in asserting their places at China's policy tables. He concludes that, "while small firms are occasionally aided by associations, one economic factor in particular, size, has decisively shaped companies' relative ability to influence policy."

The large state-owned enterprises (SOEs) that operate China's steel mills have long enjoyed regular access to bureaucrats, notes Kennedy, reducing the need for trade associations in the steel industry. Kennedy raises an important observation about the future trajectory of China's policy process: Lobbying will pit trade associations and large SOEs against the newly created bureaucracies that have limited, but growing, influence in policy circles. For example, Kennedy cites environmental regulators, who had, until recently, been effectively sidelined by China's steel industry. As concern has grown over environmental protection, and as, Kennedy argues, statistics increasingly demonstrate the adverse impact of pollution and other environmental hazards on China's GDP, the balance of power has been shifting toward the environmental regulators and away from the metallurgy bureaucrats that protect steel interests.

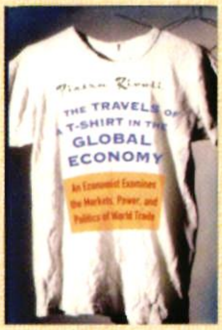
In a case from the consumer electronics industry that Kennedy highlights, Premier Zhu Rongji in January 1998 ordered the Ministry of Finance to impose a tax on the domestic consumption of VCD and DVD players throughout China. Industry made its intense opposition known through various channels, including National People's Congress deputies, noting that such a tax would contribute to unemployment. Three months later, Zhu rescinded his order.

The software industry is peculiar in that it has characteristics, according to Kennedy, that propel "government-business ties further in the direction of pluralism" compared to the steel and consumer electronics industries in China. These traits include a knowledge-intensive industry with an extremely young, highly educated workforce and low economies of scale, compelling executives and bureaucrats to listen more closely to employees in this sector or risk losing workers or companies to a competing company or jurisdiction that will listen. Perhaps because of their independence, voluntary nature, and flat organizational structures, Kennedy argues that the software trade associations are the least aggressive in China, have less access to high officials, and are thus less effective.

Through a series of well-documented case studies, Kennedy presents an intelligent and accessible analysis of "the business of lobbying in China." He does a superb job of focusing on industries that are national in scope and that command the attention of senior policymakers in China. For business leaders, academics, and graduate students alike, *The Business of Lobbying in China* illuminates the nuances associated with the complex political and business cultures in China.

—*Mark T. Fung*

Mark T. Fung recently completed his dissertation, "Bonds and Bureaucrats: The Politics of Finance in China: 1953–2003," at the Johns Hopkins University School of Advanced International Studies.




## The Travels of a T-Shirt in the Global Economy

**By Pietra Rivoli. Hoboken, NJ: John Wiley & Sons, Inc., 2005. 215 pp. $29.95 hardcover**

*The Travels of a T-Shirt in the Global Economy* presents an engaging account of globalization through the life of a $6 T-shirt. Pietra Rivoli traces the life of her T-shirt from a cotton production plant in Texas to a factory in Shanghai to a used T-shirt market in Tanzania. She explains the economic and political factors involved in globalization through the personal accounts of different characters involved in the life of her shirt. The author also provides solid economic data to support her arguments. Drawing on her background as a professor of international business at Georgetown University's McDonough School of Business and on her travels to the locations discussed in the book, Rivoli combines an academic study with illustrative examples.

*Travels of a T-Shirt* is divided into four parts, each devoted to different stages in a T-shirt's life. Each chapter could be read separately, depending on the reader's particular interest. For instance, a "China reader" might skim the sections on the history of American cotton and pay closer attention to chapters devoted to China. Here the author discusses her T-shirt's assembly and the factory conditions surrounding it. She argues that the drudgery at the factories is a necessary step in the development of any industrializing country, citing factories in Manchester, England, and the United States as some examples. Docile women working in poor conditions were at the heart of every industrial revolution, she writes, and China is no exception. Factory work, though often dangerous, has served as a route to freedom and further development in much of the developed world. Rivoli also explores China's rise as an apparel exporter, noting that "Americans purchase approximately 1 billion garments made in China each year, four for every U.S. citizen."

One of her more interesting arguments is her critique of US cotton subsidies. Rivoli argues that US cotton farmers have developed such strong commercial infrastructure and reached such a high technological level that the subsidies' removal would do little to reduce their competitiveness in global markets. She also suggests that low labor costs could impinge on scientific and economic progress because it could encourage hiring instead of developing new technology. This applies to China, where abundant, cheap labor has discouraged investment in cotton-production technology.

Rivoli also presents interesting insights about the global clothing market. For instance, most writing on globalization focuses on production and retail; discussion of what happens after an item is sold is rare. She goes a step further, exploring the afterlife of a T-shirt, and discovering that the United States dominates the world's clothing recycling industry.

The author wrote *Travels of a T-Shirt* in response to student-organized anti-globalization protests at Georgetown University, hoping to find a way to reconcile the two extremes of the globalization debate. Her goal was not to convince the reader of a certain argument, but rather to tell a story that reveals the complexities involved in the debate. This she does admirably, all the while giving readers a well-rounded understanding of globalization.

Rivoli's conversational approach, along with the charts, graphs, and photographs scattered throughout the book, make *Travels of a T-Shirt* an easy and enjoyable read, worthwhile for anyone interested in deepening their understanding of globalization and international business. Since the book explores both political and economic implications, it should be useful to political leaders and businesspeople alike.

—*Maria Repnikova*

Maria Repnikova is a research assistant at the *CBR*.

# Critical Eye on Hohhot

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The national-level ETDZs have attracted companies in electronics, high-tech, power, textiles, dairy and food processing, and pharmaceuticals. The zones host more than 50 domestic and international companies, including leading Chinese firms such as China MengNiu Dairy and Inner Mongolia Yili Industrial Co.; TCL Corp.; Inner Mongolia Lantai Industrial Co., Ltd.; the Inner Mongolia Sanbao Kaolin Co., Ltd.; and the North China Power Group. Outside of mainland investors, Hohhot's top investors include Hong Kong, Taiwan, and Mongolian companies. Of American firms, LW Packard is strong in manufacturing, while Yum Brands, Inc. (parent company of KFC Corp. and Pizza Hut, Inc.) and McDonald's Corp. are strong in the service sector.

## Competitive workforce

As the region's educational hub, Hohhot boasts 17 universities and colleges, graduating more than 14,500 students each year. The Inner Mongolia University and Inner Mongolia Polytechnic University offer MBA programs that draw students and employees from across China. The city's location also gives companies in Beijing, Tianjin, and the local area the ability to recruit easily within the autonomous region.

Hohhot's educational system produces skilled employees who, because of the city's comparatively low costs of living, work for lower salaries than their coastal counterparts. In 2005, average salaries have ranged from ¥420–¥500 per month for unskilled laborers to ¥1,000–¥1,500 per month for mid- and senior-level managers ($52–$62 and $123–$185 per month, respectively).

Nevertheless, management and staff in Hohhot have less experience with Western business and management practices than their counterparts in China's large, coastal cities. According to Pacific Resources International, the English reading and writing proficiency of the region's college graduates—particularly in business, finance, management, and engineering—is generally high, but only 10 to 20 percent of college graduates have sufficient English oral communications skills to work on a day-to-day basis in that language. Government officials have also had few opportunities to assist foreign companies with long-term investment and development, though there is a strong willingness to expand and improve services as more companies move to the area.

## Hot for Hohhot?

As China's economy grows, companies across China are racing to acquire the necessary resources to power their expansion, secure coveted raw materials, hire qualified employees at competitive wages, and find supportive infrastructure and government policies. Because Hohhot can help companies fulfill these goals, the city presents an attractive alternative for companies seeking to invest in China's rapid growth.

家易得

# Oxford & Associates

## Property Consultants

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*International Expertise. Local Knowledge*

## *Shanghai Real Estate Experts*

Oxford & Associaes Property Consultants delivers comprehensive real estate solution to our clients by providing effcient professional services.

To achieve these solutions, Oxford & Associates utilizes our international experiences combined with local knowledge to provide professional services to and on behalf of landlords,tenants and investors of all levels.

Oxford & Associates was established in the year 2000, Our leadership team is comprised of managers with over 20 years of experience in such diverse fields as real estate, law and banking to provide a wide range of solutions to suite different needs.

### SCOPE OF SERVICES

#### RESIDENTIAL LEASING AND SALES:

**Residential Leasing**

Oxford & Associates represents a diverse number of residential properties from new to second-hand for lease. Our properties range from apartments, villas to historical homes. With a database that includes private landlords and developers. We offer clients the widest choices when selecting a home. Oxford & Associates will then negotiate the best possible rental rate on behalf of our clients.

**Residential Sales**

Oxford & Associates takes our clients from start to finish during the home purchase process. From selecting the right property to negotiating the price and administering the closing process. Oxford & Associates will be there to handle virtually any issues. Our Residential Sales Department works closely with the Mortgage Services Department to ensure the financial considerations are taken care of as well.

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- Grade A and B Office
- Lease Review Negotiations
- Acquisitions and Disposals
- Tenant Representation

#### CORPORATE RESIDENTIAL SERVICES:

Oxford & Associates assists multinational companies in relocating expatriate employees to China to ensure they receive all the information they require to settle down into a new city and lifestyle. The aim of the Corporate Residential Services Department is to assist the client company's human resources / administration department to reducing time and expenses in relocating overseas staff. Our After Sales Department will be there to solve any problems for the duration of the lease. This program includes.

**Customized Orientation**--From pick-ups at the airport and hotel arrangements to tours of the city, school introductory visits, etc.

**Home Search and Lease Negotiations**--With our extensive property database , we will conduct the entire home search process from property inspections to negotiating the lowest price on the rental rate.

**Tenancy Management**--Oxford & Associates will oversee the lease management process prior to move-in , duration of the lease and the expiry of the lease from extension to expiry.

**Payment Management**--A payment management system will be established to handle all financial accounting from debit notes to chasing outstanding payments and offcial receipts.

#### INVESTMENT CONSULTING:

Our track record of projects over the past several years make us well qualified to consult on areas from retail mortgage services to developmental finance consulting. For companies or investors who maintain a dynamic property portfolio, Oxford & Associates can dispose of assets through our extensive network of associates in china and internationally.

#### MARKET RESERCH:

Information is power and the Market Research Department verifies and validates information provided by local sources to offer useful property information to our clients. The information provided will be crucial in making sound real estate decisions.

#### MORTGAGE SERVICES:

Oxford & Associates understands different clients will have different needs. We will work with a range of local Chinese and foreign banks to source the most competitive financing available for our clients, making the home buying process flexible and fast while reducing the overall cost of transaction.

**Downtown Apertments For Lease**

**The Summit**--3Br 147sqm brand-new USD3,000-3,500
4Br 295sqm,high flr, furnished USD8,800-9,000
**The Edifice**-- 2Br 123sqm,2 baths,high flr USD2,100-2,500
3Br 160sqm,great layouts USD2,500-2,800
**Yanlord Gardens**--4Br 215-220sqm, various layous USD3,500-4,000
5Br 302sqm high flr, furnished USD6,800

**Villas For Lease**

Tomson Golf Villas--4-5Br 351-410sqm,fully furnished USD6,000-7,000
6Br 500sqm,newly renovated USD6,500

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## Sales and Investment

August 16–October 15, 2005

Compiled by Maria Repnikova

The following tables contain recent press reports of business contracts and negotiations exclusive of those listed in previous issues. For the most part, the accuracy of these reports is not independently confirmed by the *CBR*.

Firms whose sales and other business arrangements with China do not normally appear in press reports may have them published in the *CBR* by sending the information to the attention of the editor at publications@uschina.org.

### Advertising, Marketing & PR

#### INVESTMENTS IN CHINA

**European Marketing Group (the Netherlands), USA Strategies, Inc. (US)**
Formed joint venture, EMG China, to assist North American and European clients with in-country research, market development projects, advertising, and public relations. 08/05.

**SIMS Trading Co. Ltd., a division of CITIC Pacific Ltd. (Hong Kong), SPAR Group, Inc. (US)**
Will establish a WFOE, SPAR (Shanghai) Field Marketing Co. Ltd., to provide specialized marketing services for retailers and manufacturers in China. (US:50%-Hong Kong:50%). 08/05.

**Trader Classified Media NV (the Netherlands)**
Bought 15% stake in Beijing-based SouFun Holdings Ltd. $22.5 million. 07/05.

#### OTHER

**Avis Europe plc (UK)/China Southern Airlines Co. Ltd. (Guangdong)**
Developed a joint frequent flier promotion plan for China Southern Airlines' Sky Pearl Club members. 07/05.

### Architecture, Construction & Engineering

#### INVESTMENTS IN CHINA

**URS Corp. (US)**
Bought Shanghai-based Austin Ausino Engineering Co. Ltd. 09/05.

### Automotive

#### CHINA'S INVESTMENTS ABROAD

**ASIMCO Technologies Ltd. (Beijing)**
Bought US-based NVH Concepts LLC 08/05.

**Nanjing Automobile (Group) Corp.**
Bought UK-based MG Rover Group Ltd. 08/05.

**Shanghai Baosteel Group Corp.**
Bought 50% stake in Canada-based Court Group unit. $15.41 million. 07/05.

#### INVESTMENTS IN CHINA

**DaimlerChrysler AG (Germany)**
Will establish a financing company, DaimlerChrysler (China) Finance Ltd., in Beijing. 09/05.

**Isuzu Motors Ltd. (Japan)/Qingling Motors Co. Ltd. (Chongqing)**
Will form joint venture to manufacture engines and parts. 09/05.

**Valeo (France)/Hangshen Electronics (Guangdong)**
Formed joint venture to produce ultrasonic products and switches in Shenzhen, Guangdong. (France:75%-PRC:25%). 09/05.

**DaimlerChrysler AG (Germany)**
Will increase stake in Beijing Benz DaimlerChrysler Automotive from 42% to 50%. 08/05.

**Ford Motor Co. (US)**
Increased stake in Shenzhen-based Jiangling Motors Corp. Ltd. by 0.04%, bringing it to 30%. $128,200. 08/05.

**Visteon Corp. (US)/Chang'an Automobile (Group) Co., Ltd. (Chongqing)**
Formed joint venture, Chongqing Chang'an Visteon Engine Control Systems, to develop automobile engine management systems in Chongqing. (US:50%-PRC:50%). 08/05.

**Nissan Diesel Motor Co. (Japan)**
Will acquire additional 25% stake in Dongfeng Nissan Diesel Motor Co., bringing Nissan's stake to 50%. 07/05.

#### OTHER

**Toyota Motor Corp. (Japan)**
Will build Prius hybrid passenger vehicles at Sichuan FAW Toyota Motor plant, a joint venture with FAW Group, in Changchun, Jilin. 08/05.

**Abbreviations used throughout text:** **ABC:** Agricultural Bank of China; **ADB:** Asian Development Bank; **ASEAN:** Association of Southeast Asian Nations; **AVIC I and II:** China Aviation Industry Corp. I and II; **BOC:** Bank of China; **CAAC:** General Administration of Civil Aviation of China; **CATV:** cable television; **CBRC:** China Banking Regulatory Commision; **CCB:** China Construction Bank; **CCTV:** China Central Television; **CDB:** China Development Bank; **CDMA:** code division multiple access; **CEIEC:** China National Electronics Import and Export Corp.; **China Mobile:** China Mobile Communications Corp.; **China Netcom:** China Netcom Corp. Ltd.; **China Railcom:** China Railway Communications Co., Ltd.; **China Telecom:** China Telecommunications Group Corp.; **China Unicom:** China United Telecommunications Corp.; **CIRC:** China Insurance Regulatory Commission; **CITIC:** China International Trust and Investment Corp.; **CITS:** China International Travel Service; **CNOOC:** China National Offshore Oil Corp.; **CNPC:** China National Petroleum & Gas Corp.; **COFCO:** China National Cereals, Oils, and Foodstuffs Import and Export Corp.; **COSCO:** China Ocean Shipping Co.; **CSRC:** China Securities Regulatory Commission; **DSL:** digital subscriber line; **ETDZ:** economic and technological development zone; **GSM:** global system for mobile communication; **ICBC:** Industrial and Commercial Bank of China; **IT:** information technology; **LNG:** liquified natural gas; **MII:** Ministry of Information Industry; **MOFCOM:** Ministry of Commerce; **MOU:** memorandum of understanding; **NA:** not available; **NDRC:** National Development and Reform Commission; **NORINCO:** China North Industries Corp.; **PAS:** personal access system; **PBOC:** People's Bank of China; **PetroChina:** PetroChina Co., Ltd.; **RMB:** renminbi; **SARFT:** State Administration of Radio, Film, and Television; **SEZ:** special economic zone; **SINOPEC:** China National Petrochemical Corp.; **SINOTRANS:** China National Foreign Trade Transportation Corp.; **UNDP:** United Nations Development Program; **SME:** small and medium-sized enterprise; **WFOE:** wholly foreign-owned enterprise

**Honda Motor Co., Ltd. (Japan)**
Will introduce Acura model to China next spring. 07/05.

## Aviation/Aerospace

### CHINA'S IMPORTS

**Airbus SAS (France)**
Will provide 10 A330 carriers to China Southern Airlines Co. Ltd. $1.5 billion. 09/05.

**The Boeing Co. (US)**
Will provide 42 B787 aircraft to Air China Ltd., China Eastern Airlines Co., Ltd., Shanghai Airlines Co., Ltd., and Xiamen Airlines Co., Ltd. $5.04 billion. 08/05.

**The Boeing Co. (US)**
Will provide 10 B787 aircraft to China Southern Airlines Co. Ltd. 08/05.

**Airbus SAS (France)**
Will provide 20 A330 carriers to Air China Ltd. $3.1 billion. 07/05.

**The Boeing Co. (US)**
Will provide 50 B747 jetliners to Air China Ltd., China Eastern Airlines Co., Ltd., Hainan Airlines Co., Ltd., Xiamen Airlines Co., Ltd., and Shanghai Airlines Co., Ltd.
$6 billion. 07/05.

### INVESTMENTS IN CHINA

**China Airlines, Ltd. (Taiwan)**
Will buy 25% stake in Yangtze River Express Airlines Co., a unit of Hainan Airlines Co., Ltd. $39 million. 09/05.

**Korean Air Lines Co., Ltd. (South Korea)**
Will invest in Tianjin-based Okay Airways Co. 08/05.

### OTHER

**The Sukhoi Co. (Russia)**
Will open an office in China. 09/05.

## Banking & Finance

### INVESTMENTS IN CHINA

**Asia Financial Holdings Pte Ltd. (Singapore)**
Bought 5.1% stake in CCB. $1.5 billion. 09/05.

**Bank of America Corp. (US)**
Bought 9% stake in CCB. $2.5 billion. 09/05.

**Citigroup Inc. (US)**
Increased its stake in Shanghai Pudong Development Bank Co., Ltd. from 5% to 19.9%. 09/05.

**Refco Group, Ltd., LLC, a subsidiary of Refco Inc. (US)/Jingyi Futures Co., Ltd. (Beijing)**
Formed the first futures brokerage joint venture in China. 09/05.

**DBS Group Holdings Ltd. (Singapore), Deutsche Bank AG (Germany)**
Bought 10 billion shares in Guangdong Development Bank. $2.18 billion. 08/05.

**Deutsche Bank AG (Germany)**
Bought 5% stake in Beijing-based Huaxia Bank Co., Ltd. $110 million. 08/05.

**Principal Financial Group, Inc. (US)/CCB, China Huadian Corp. (Beijing)**
Formed joint venture, CCB-Principal Asset Management Co., Ltd., to market mutual funds. (US:25%-PRC:75%). 08/05.

**The Royal Bank of Scotland Group plc (UK)**
Bought 10% stake in BOC. $3.1 billion. 08/05.

**Schroder Investment Management Ltd. (UK)/Bank of Communications Co., Ltd. (Shanghai), China International Marine Containers (Group) Co., Ltd. (Guangdong)**
Formed mutual fund management company in Shanghai. (UK:30%-PRC:70%). $24.7 million. 08/05.

**Standard Chartered plc (UK)**
Bought 19.99% stake in Tianjin-based Bohai Bank. 08/05.

**Bangkok Bank Public Co., Ltd. (Thailand)**
Bought 10% stake in Beijing-based PICC Life Insurance Co. 07/05.

### OTHER

**Citibank, a subsidiary of Citigroup Inc. (US)**
Opened a branch in Chengdu, Sichuan. 09/05.

**Citibank, a subsidiary of Citigroup Inc. (US)/China Union Pay (Shanghai)**
Formed strategic alliance to allow China Union Pay cardholders to obtain foreign currency from Citibank's ATMs. 09/05.

## Chemicals, Petrochemicals & Related Equipment

### INVESTMENTS IN CHINA

**Degussa AG (Germany)/Yingkou Sanzheng Fine Chemicals Co., Ltd. (Liaoning)**
Formed joint venture, Degussa Sanzheng (Yingkou) Fine Chemicals Co. Ltd., to manufacture cyanuric chloride and derivatives. (Germany:65%-PRC:35%). 07/05.

### OTHER

**Loyal Chemical Industrial Corp. (Taiwan), NOVA Chemicals Corp. (Canada)**
Will jointly manufacture ARCEL moldable foam resin near Shanghai. 09/05.

**JMD GHG Reduction Co., Ltd. (Japan)/Zhejiang Juhua Co. Ltd.**
Signed agreement to establish a clean development mechanism project. 08/05.

## Distribution, Logistics & Related Services

### OTHER

**DHL International GmbH (Germany)**
Opened quality control center in Beijing. 07/05.

**UPS, Inc. (US)**
Will start new flight service from Qingdao, Shandong, to Incheon, South Korea. 07/05.

## Education

### OTHER

**Columbia University (US)**
Partnered with Fudan University School of Management in Shanghai to establish an executive education program. 08/05.

## Electronics, Hardware & Software

INVESTMENTS IN CHINA

**Kimball Electronics Group, a subsidiary of Kimball International Inc. (US)**
Will establish manufacturing facility in Nanjing, Jiangsu. 08/05.

**NewMarket Technology Inc. (US)/Huali Computer Co. Ltd. (Zhejiang)**
Will form joint venture to provide core systems integration services to Zhejiang clients. 07/05.

**United Test and Assembly Center Ltd. (Singapore)/Semiconductor Manufacturing International Corp. (Shanghai)**
Will establish joint venture semiconductor assembly and testing facility in Chengdu, Sichuan. (Singapore:30%-PRC:51%-Financial investors and employees:19%). $81 million. 07/05.

OTHER

**Intel Corp. (US)**
Will establish global headquarters of its Channel Platforms Group in Shanghai. 08/05.

**LG Philips LCD (South Korea)/Xiamen Overseas Chinese Electronic Co., Ltd. (Shanghai)**
Signed strategic cooperative partnership agreement to jointly market flat panel TVs internationally. 07/05.

## Energy & Electric Power

CHINA'S EXPORTS

**China National Heavy Machinery Corp. (Beijing)**
Signed contracts with the Department of Hydroelectric Power of Myanmar to supply 230 kv transmission lines and substations for Yewa hydropower project. $45.8 million. 09/05.

CHINA'S INVESTMENTS ABROAD

**China Huaneng Group (Beijing)**
Bought 25.5% stake in the Monto coal project of Australia-based Macarthur Coal Ltd. $22 million. 07/05.

INVESTMENTS IN CHINA

**Larsen & Toubro Ltd. (India)**
Will build manufacturing plant in Wuxi New District, Jiangsu, to produce high-end air circuit breakers. 08/05.

**Vestas Wind Systems A/S (Denmark)**
Will establish wind turbine factory in Tianjin Economic-Technological Development Area. 07/05.

## Environmental Equipment & Technology

CHINA'S IMPORTS

**Fuel-Tech NV (the Netherlands)**
Won a contract from Nanjiang Longyuan Environmental Engineering Co., to install NOxOUT selective non-catalytic reduction technology at Ligang Electric Power Co. Ltd., in Jiangyin, Jiangsu. $9.3 million. 09/05.

**United Envirotech Ltd. (Singapore)**
Won a 30-year transfer-operate-transfer contract to treat wastewater in Xintai, Shandong. 09/05.

**Veolia Water, a subsidiary of Veolia Environment SA (France)**
Won a 23-year management contract for water services in Urumqi, Xinjiang Uyghur Autonomous Region. $337.8 million. 09/05

**Veolia Water Asia, a subsidiary of Veolia Environment SA (France)**
Won a 25-year water services management contract in Handan, Hebei. $74.6 million. 09/05.

**Bio-Treat Technology Ltd. (Singapore)**
Won a build-operate-transfer wastewater treatment contract in Nanjing, Jiangsu. $10 million. 08/05.

**Onyx, a division of Veolia Environment SA (France)**
Signed a 30-year concession agreement with Foshan Municipality to invest, construct, and operate a municipal waste landfill in Guangdong. $323.8 million. 07/05.

INVESTMENTS IN CHINA

**Biosphere Development Corp., a subsidiary of Global Environment Energy Corp. (US)/Yankuang Group Co. (Shandong), Shenzhen Rayes Group**
Will form joint venture to build about 1,300 waste treatment systems in China. 08/05.

## Forestry, Timber & Paper

INVESTMENTS IN CHINA

**ArjoWiggins, a subsidiary of Worms & Cie Group (France)/Shandong Chenming Paper Holdings Co.**
Will form a joint venture to produce "special-use" paper. (France:70%-PRC:30%). $24.7 million. 07/05.

**Schweitzer-Mauduit International, Inc. (US)/China National Tobacco Corp. (Beijing)**
Will form joint venture to produce cigarette paper in Jiangmen, Guangdong. (US:50%-PRC:50%). $100 million. 07/05.

## Insurance

INVESTMENTS IN CHINA

**The Carlyle Group (US)**
Will buy 24.9% stake in Shanghai-based China Pacific Life Insurance Co. $400 million. 09/05.

**Great Eastern Holdings Ltd. (Singapore)/Chongqing Land Properties Group**
Will form joint venture life insurance company. $37 million. 08/05.

**British Royal & Sun Alliance Insurance Co. (UK)**
Will change its China branch into a WFOE, Sun Alliance Insurance (China) Co. Ltd. 08/05.

## Internet/E-Commerce

INVESTMENTS IN CHINA

**Skype Technologies SA (Luxembourg)/TOM Online Inc. (Beijing)**
Will form a joint venture to develop, customize, and distribute a simplified Chinese version of the Skype software and premium services to Internet users and service providers in China. (Luxembourg:51%-PRC:49%). 09/05.

**Yahoo Inc. (US)**

Bought 40% stake in Hangzhou-based Alibaba.com Corp. $1 billion. 08/05.

**Anatomy Corp. plc (UK)/China Netcom Broadband Corp. Ltd. (Beijing)**

Will form joint venture to bring next-generation technology to China's Internet consumer market. 07/05.

### OTHER

**China Digital Media Corp. (Hong Kong)/Shenzhen Coship Electronics Co. Ltd.**

Will launch a trial for a new IP-based set-top-box in Nanhai, Guangdong. 08/05.

**FeedBurner Inc. (US)**

Signed partnership agreement with Beijing-based Bokee Ltd. to extend its services to Bokee's network consumers. 07/05.

## Light Industry & Manufacturing

### INVESTMENTS IN CHINA

**JK Yaming International Holdings Ltd. (Singapore)**

Will buy 65% stake in Fujian Connex Metal Industries Co. Ltd. $1.37 million. 09/05.

## Media, Publishing & Entertainment

### INVESTMENTS IN CHINA

**Eastman Kodak Co. (US)**

Will establish a WFOE, Kodak Graphic Communications (China) Co. Ltd., in Xiamen, Fujian, for operations related to computer-based digital graphic communications products, equipment, systems, and materials. $100 million. 09/05.

**Lingo Media Inc. (Canada)/Liaoning Dianya Culture Book Distribution Co., Ltd., a subsidiary of Liaoning Publishing Group**

Will form joint venture in Shenyang, Liaoning, to develop and co-publish educational products that will be sold through LPG's distribution network. (Canada:51%-PRC:49%). 08/05.

**Sega Corp. (Japan)/Shanghai New World Co. Ltd.**

Will form joint venture, Shanghai New World Sega Recreation Co. Ltd., to manage indoor amusement park in Shanghai. (Japan:50%-PRC:50%). $20 million. 08/05.

## Metals, Minerals & Mining

### CHINA'S IMPORTS

**Palladon Venture Ltd. (US)**

Will sell 1 million tons of iron to China over a 12-month period. 08/05.

### INVESTMENTS IN CHINA

**Mittal Steel Group Co. NV (the Netherlands)**

Will buy 36.7% stake in Shenzhen-based Hunan Valin Steel Tube & Wire Co. 07/05.

### OTHER

**PT Aneka Tambang (Indonesia)/Aluminum Corp. of China Ltd. (Beijing)**

Signed MOU to develop a smelter-grade alumina project in Indonesia. 08/05.

## Petroleum, Natural Gas & Related Equipment

### CHINA'S IMPORTS

**EnCana Corp. (Canada)**

Sold oil assets in Ecuador to Chinese consortium led by CNPC. $1.42 billion. 09/05.

### CHINA'S INVESTMENTS ABROAD

**China State-Owned Enterprise Investment Co. Ltd. (Beijing), Beijing Jingdeshun Materials Co. Ltd.**

Will invest $200 million to build Mongolia's first oil refinery in Ulan Bator. 09/05.

**CNPC (Beijing)**

Will buy Canada-based PetroKazakhstan Inc. $4.2 billion. 08/05.

### INVESTMENTS IN CHINA

**Exxon Mobil Corp. (US), Saudi Arabian Oil Co./Fujian Refining & Chemical Co. Ltd., a subsidiary of China Petroleum & Chemical Corp. (Beijing)**

Formed oil refinery joint venture in Quanzhou, Fujian. (US:25%-Saudi Arabia:25%-PRC:50%). 07/05.

**SK Networks Co., trading and oil distribution arm of SK Group (South Korea)/Guangsheng Electronic Ltd. (Jiangsu)**

Will form joint venture to build fuel-oil processing plant in Taizhou, Jiangsu. 07/05.

### OTHER

**BP (Shanghai) LPG Co. Ltd., a subsidiary of BP plc (UK)**

Launched sales of bottled liquefied petroleum in Shanghai. 09/05.

**Enviro Voraxial Technology Inc. (US)/CNOOC (Beijing)**

Signed a contract to deploy a Voraxial Separator on an offshore oil production platform. 09/05.

**Petroleos de Venezuela SA**

Set up an office in Beijing. 08/05.

**Petroles de Venezuela SA/CNPC (Beijing)**

Signed agreement to develop and manage Venezuela's Zumano oilfields. 08/05.

## Pharmaceuticals

### INVESTMENTS IN CHINA

**Coremed, Inc. (US)/Shanghai Fosun High Technology (Group) Co., Ltd., Wanbang Biochemical Pharmaceutical Co., Ltd. (Jiangsu)**

Formed joint venture to develop Alveair inhalable insulin through all phases of clinical trials and product commercialization. 08/05.

### OTHER

**Alltracel Pharmaceuticals plc (Ireland)/Yunnan Baiyao Group**

Signed partnership agreement to develop and co-market Alltracel's m•doc stops-bleeding technology in China and other international markets. 08/05.

## Ports & Shipping

### INVESTMENTS IN CHINA

**Paul Y-ITC Construction Holdings Ltd. (Hong Kong)**

Will invest $590 million in Yangkou Port in Nantong, Jiangsu. 07/05.

## Rail

CHINA'S IMPORTS

**Jilin Midas Aluminum Industries Co., a subsidiary of Midas Holdings Ltd. (Singapore)**
Won a $12.7 million contract for the regional line project with Changchun Railway Vehicles Co., Ltd., in collaboration with France-based Alstom Transport SA, to supply aluminum alloy profiles for electrical multiple-unit high-speed train car bodies. 07/05.

**Jilin Midas Aluminum Industries Co., a subsidiary of Midas Holdings Ltd. (Singapore)**
Won a $3.5 million Shanghai MRT Line 1 extension contract from CSR Nanjing Puzhen Rolling Stock Works, in collaboration with Alstom Transport SA, to supply aluminium alloy profiles for MRT car bodies. 07/05.

**Implant Sciences Corp. (US)**
Will deliver 101 Quantum Sniffer handheld explosive detection units to Beijing Ritchie's Time Co., Ltd. to sell to the Chinese Railway Administration for use in a large railway security project. 07/05.

## Raw Materials

INVESTMENTS IN CHINA

**Tino Stone Group (Spain)**
Will build a production center and logistics platform in Zhangjiagang, Jiangsu. $28.6 million. 07/05.

## Real Estate & Land

INVESTMENTS IN CHINA

**The Carlyle Group (US)**
Will buy 7.5% stake in Tianjin-based China Real Estate Network Ltd. $10 million. 08/05.

**Softbank Asia Investment Fund, a subsidiary of SOFTBANK Corp. (Japan)**
Will buy 15% stake in Tianjin-based China Real Estate Network Ltd. $30 million. 08/05.

**Simon Property Group, Inc., Morgan Stanley Real Estate Funds (US)/ SZITIC Commercial Property, a subsidiary of Shenzhen International Trust and Investment Corp.**
Formed joint venture to build shopping malls in Shanghai; Nanjing, Jiangsu; and Hangzhou, Zhejiang. (US:65%-PRC:35%). 07/05.

**Wharf (Holdings) Ltd. (Hong Kong)**
Bought 70,000 $m^2$ site in Chengdu, Sichuan. $96.1 million. 07/05.

## Research & Development

INVESTMENTS IN CHINA

**Alcatel SA (France)**
Will open R&D center in Chengdu, Sichuan, focused on mobile network technologies. 09/05.

**Google Inc. (US)**
Will open R&D center in China. 07/05.

## Retail/Wholesale

INVESTMENTS IN CHINA

**Chlitina International Trading Corp. (Taiwan)**
Will build production facility in Shanghai. $11 million. 09/05.

OTHER

**Chlitina International Trading Corp. (Taiwan)**
Established mainland headquarters in Shanghai. 09/05.

## Telecommunications

CHINA'S EXPORTS

**ZTE Corp. (Guangdong)**
Signed agreement with Mundo Startel SARL (Angola) to install fixed-line networks in eight Angolan states. 07/05.

**ZTE Corp. (Guangdong)**
Signed agreement with Tajiktelecom to build first-generation network in Tajikistan. 07/05.

CHINA'S IMPORTS

**Teradata, a division of NCR Corp. (US)**
Will provide Yunnan Telecom Co. Ltd. with an enterprise data warehouse system. 08/05.

**UTStarcom, Inc. (US)**
Will provide China Telecom and China Netcom Group Corp. (Hong Kong) Ltd. roughly 500,000 lines of its AN-2000 IP-based digital subscriber line access multiplexer solutions in 18 provinces in China. 07/05.

**UTStarcom, Inc. (US)**
Will provide China Unicom Corp. Ltd. 250,000 CDMA handsets. 07/05.

**Redback Network Inc. (US)**
Will provide Redback SmartEdge 800 Service Gateways to China Netcom Heilongjiang Communications Corp. 07/05.

INVESTMENTS IN CHINA

**NewMarket Technology Inc. (US)/Huali Group (Zhejiang)**
Will form joint venture to expand services offered by NewMarket Technology Inc. to Huali Group's client base. 08/05.

OTHER

**Avaya Inc. (US)/G-NET Integrated Services Co., Ltd. (Beijing)**
Formed strategic partnership to jointly provide communications services. 09/05.

**AT&T Corp. (US)**
Will move its China headquarters from Hong Kong to Shanghai. 08/05.

# Beijing's Mega Mall


Dennis Chen

**Rebecca Karnak**

I do not usually enjoy shopping. In China—with the crowds, the multiple steps needed to check out, and the infinite choices of things to buy—I dread it even more. But when I heard that Beijing had opened the largest standalone shopping structure in the world, I had to investigate.

Until recently, Beijing's 6 million sq ft Golden Resources Shopping Mall was the world's largest. (Guangdong's 6.5 million sq ft South China Mall opened this spring.) Opened in October 2004, Golden Resources still easily tops the largest mall in the United States—Minnesota's 4.2 million sq ft Mall of America—as well as the largest mall in North America, the 5.3 million sq ft West Edmonton Mall in Canada. Today, China has more than 400 malls. Deloitte Research estimates that 7 of the world's 10 largest malls will be in China by 2010.

At the start of my investigation, I hopped in a cab near Beijing's Jianguomenwai subway station, and the driver sped up the Second Ring Road toward Golden Resources in Haidian District. After almost half an hour, the driver wound his way through the narrow, tree-lined streets near Beijing Foreign Studies University and entered a wide street lined with new apartments and office buildings. Approaching the mall as the driver did, I was not as overwhelmed by its size as I thought I would be. Golden Resources is a compact, five-story building with neatly arranged shops that run east-to-west. I paid my ¥40 ($5) cab fare and stepped inside.

My first stop was a jewelry counter, an island between rows of shops. I looked at a few mid-priced gray pearls and braced myself to be greeted by an overenthusiastic sales assistant. When no one approached me, I looked up to see a young female sales assistant at the opposite counter talking to her friends, presumably the sales assistants selling silver bracelets next door. Being ignored by the sales assistant was a refreshing switch from being accosted by pushy vendors at Beijing's Silk Market and elsewhere. The scene felt familiar, as if it could happen at a mall in Cleveland, my hometown.

But as I walked past watch shops, cafés, women's clothing stores, and plenty of advertisements for brands such as Gucci, DKNY, and Fendi, I realized that most of the other sales assistants weren't jumping up to greet the few customers strolling by on this late Sunday afternoon either. In a city of roughly 14 million residents, I expect crowds at most public places on Sunday afternoons. But after more than a half year in operation, Golden Resources has yet to attract the number of customers it will need to stay profitable. In fact, I turned one corner of the mall to discover two people playing badminton. The stores in that section of the mall had not opened yet, and the couple was taking advantage of the open space.

Once I hit Toysmart on the fourth floor, though, I found signs of commercial life. Kids were running around, testing out scooters their parents had yet to purchase. Down the hall were two different playgrounds for children and their families that charged by the hour for jungle gym access.

The adult playgrounds are on the mall's fifth floor: Stellar International Cinema, which has seven screens, and the Century Club, a health and fitness center. Making my way back down through each level, I came across shops neatly arranged by product sold. I passed three consecutive shops selling treadmills, wondering which one would go out of business first, before entering an area of sporting goods stores. For the first time in Beijing, I found authentic North Face gear, and the Nike and Adidas stores also carried the real deal. Many of the products I saw, though, including the treadmills and the ¥32 ($4) fruit smoothie I purchased at a kiosk, are luxury items for the average Beijinger.

Golden Resources' 1,000 stores, 230 escalators, and 10,000 free parking spaces seem like nothing in comparison to its rival's facilities. Guangdong's South China Mall boasts theme parks, pyramids, giant windmills, a 1.3-mile river, and an 85-foot replica of the Paris Arc de Triomphe. These large, high-end malls might not be the most profitable model for China, however. Even though China's middle class is growing, and urbanites have more money to spend than ever, China is generally a country of savers. According to the *People's Daily*, Chinese citizens have spent, on average, only 60 percent of their incomes over the past 10 years, while the world average has been 78 percent. Walking through Golden Resources makes clear that China either has too many malls or that prices are still too high for many customers. Most likely it is a combination of both.

Golden Resources has not attracted a large foreign crowd yet either, mostly because of the mall's location in northwestern Beijing outside of Third Ring Road—far from the city's foreign enclaves. I did not see a single foreign face or hear a foreign language in the hour and a half I spent shopping that Sunday afternoon. Moreover, none of the stores I visited accepted foreign credit cards. In contrast, in many stores at the Oriental Plaza and China World malls in the center of the city, no one bats an eye when a customer hands over a Visa card from a foreign bank.

But once the newly built apartments and office centers around the mall are occupied, Golden Resources will have plenty of Haidian residents to serve, including the many wealthy employees of China's Silicon Valley, Zhongguancun, and other Beijing districts. Currently, many bus lines run to and from Golden Resources, but the subway gets customers only part way there (shoppers must take a bus from the Gongzhufen subway stop). Under Beijing's 2008 subway plan, the nearest subway stop will be Wanliu, less than a mile away. When the new subway lines are completed, all of Beijing might flock to Golden Resources on a hot summer day, even if only for the air conditioning—or perhaps to show support for one more record-breaking Chinese achievement. 完

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