View metadata, citation and similar papers at core.ac.uk

brought to you by CORE

provided by Research Papers in Economics

IPL instituto politécnico de leiria

working paper

China's challenge: The opportunities and risks that China's booming economy provides

Ronald Jean Degen
International School of Management Paris

2009

Working paper nº 36/2009

globADVANTAGE

Center of Research in International Business & Strategy

INDEA - *Campus 5*

Rua das Olhalvas

Instituto Politécnico de Leiria

2414 - 016 Leiria

PORTUGAL

Tel. (+351) 244 845 051

Fax. (+351) 244 845 059

E-mail: globadvantage@ipleiria.pt

Webpage: www.globadvantage.ipleiria.pt

WORKING PAPER Nº 36/2009

August 2009

Com o apoio da UNISUL Business School

China's challenge: The opportunities and risks that China's booming economy provides

Ronald Jean Degen
Ph.D. Candidate at the International School of Management Paris
Vice Chairman of Masisa Chile

Address:
E-mail: degen@lomasnegras.com
Phone: +55 41 9918 9000
Cabanha Orgânica Lomas Negras Ltda.
Caixa Postal 95
Campo Alegre, SC
89294-000 Brasil

Glob advantage

Ronald Jean Degen is in the Ph.D. Program of the International School of Management in Paris, and the Vice Chairman of Masisa in Chile. . He was a Professor at the Getúlio Vargas Graduate Business School of São Paulo where he pioneered the introduction of teaching entrepreneurship in 1980 and wrote the first textbook in Portuguese on entrepreneurship published in 1989 by McGraw-Hill. He just published a new textbook on entrepreneurship that was published in 2009 by Pearson Education

Glob advantage

China's challenge: The opportunities and risks that China's booming economy provides

ABSTRACT

The capability of designing to very low cost, and to compete successfully in the tough Chinese market can be transformed into a competitive advantage in other markets. On the other hand, MNCs that are not successfully in China will probably not acquire these capabilities. They will be in a cost disadvantage to compete against Chinese companies in their own markets. They run the risk of becoming secondary players to Chinese companies in the world market, as those competing in the microwave-ovens market against Galanz found out the hard way. MNCs have no choice; they have to accept 'China's challenge' to continue world players. They have to win in China or lose everywhere.

Keywords: China's challenge, win in China or lose everywhere, risks to China's future growth, China's entrepreneurs, China's disruptive innovation.

Glob advantage

China's challenge

China's amazing growth of ten percent a year over the last thirty years is without precedent. In these years, China has transformed itself from an economical and technological backward nation into one of the world's most dynamic economies. It has opened its doors to new ideas and techniques, introduced competition to all aspects of production, strengthened its commitment to widespread education, and taken advantage of the opportunities offered by its World Trade Organization (WTO) membership. In 2004, for the first time, China attracted more foreign direct investment than the United States. The world's fastest-growing economy is now the second largest behind only the United States, and by mid-century, it is expected to be number one. This means that any company that wants to be a key international payer has to be successful in the Chinese market (ALI, and GUO, 2005).

China's rapid and sustained growth created enormous profit opportunities and risks for foreign companies. They have to learn to win in the very competitive Chinese market. They have to learn to design 'products to cost'. Learn to develop the best cost-quality relationship in relation to their competitor. If they are successful in China they will be able to succeed in all other markets in the world. On the other hand if they are not successful in China, a Chinese competitor will probably in this decade beat them in their home markets.

Many multinational companies (MNCs) were very successful selling their global brands to the affluent Chinese, particularly luxury brands. According to the Time global luxury survey (2007, p. 108), 22% of affluent consumers in China own a Rolex, and the most owned luxury fashion brands in China are Lacoste, Valentino, Chanel, and Bally (Degen, 2009, p. 5). The international luxury brand market in China will be harder for Chinese companies to conquer because they first have to get international recognition for the Chinese affluent consumer to accept them (Degen, 2009, p. 18). But this is not true for most other branded products marketed in China by MNCs where Chinese consumers want affordable prices and comparable quality, and have no brand loyalty.

Glob advantage

An example is the microwave-ovens market. In 1991 the market was dominated by branded Japanese and European products that had a 5 percent penetration. This small penetration was way below the 80 percent in most developed markets. Galanz, a Chinese company, entered the market, matching the foreign brands in performance but beating them on price. Rather than pursue the obvious strategy of using inexpensive Chinese labor to make lower cost microwave-ovens for export, Galanz chose to compete against no-consumption in the domestic lower-end market. Galanz introduced a simple, energy-efficient product at a price that was affordable by China's emerging middle class, and small enough to fit in their kitchens (Hart, and Christensen, 2002, p 53).

With a constant price reduction based on the company's ever-declining cost per unit, they made microwave ovens affordable to an ever increasing number of Chinese buyers. Based on its business model that could earn attractive profits at low prices, Galanz moved up-market against the established brands, manufacturing larger machines that had more sophisticated features. With this move Galanz began to disrupt the microwave-oven markets in developing countries. This strategy used by Galanz was christened by Hart and Christensen (2002) as 'disruptive innovation from the base of the pyramid.'

Glob advantage

Galanz with its disruptive innovation in 1995 already had 25 percent of the market in China; in 1998 it had 61.4 percent, and in 1999 in started to sell in the United States. Galanz used the route through becoming an Original Equipment Manufacturing (OEM) to companies all over the world to expand its international sales and so grow its production scale quickly. The fast growing large production scale made it possible for Galanz to use cost leadership and aggressive price-cutting strategies to capture market share (Ge and Ding, 2007, p. 668), and in 2002 its price were already 80 percent below the 1991 level. Galanz with its aggressive price strategy conquered 40 percent of the global market, with a 45 percent share in Europe, and more that 70 percent in South America and Africa. Building on this success Galanz started competing in the markets for air conditioners and rice cookers, aiming to be the world's largest manufacturer of these items in the near future (Hexter and Woetzel, 2007, p. 194-195).

Glob advantage

Another example is the Chinese appliance manufacturer Haier that became a global competitor based on an aggressive innovation strategy focused on three key capabilities: design, manufacture, and distribution. The aggressiveness of Haier's innovation plan can be seen in its objective: two successful intellectual patent applications for every work day. Today Haier is a dominant player in the appliance world market, selling in over 30 countries, with a product line of 96 appliance categories (DiPaola and Li, 2007, p. 3).

Some multinationals like Procter & Gamble (P&G) realized that the initial strategy to enter the market, by building market share for selected products in selected large cities, in what is called the upper-tier cities premium consumer market segment, was running out of growth opportunities. This strategy was leaving the door open for Chinese competitors to grown unchallenged in the lower-end consumer market. P&G saw the opportunities offered by fast changing and growing Chinese market, and in 2001 started its expansion into the mid-tier cities consumer market. This move put P&G in direct competition with Chinese companies that often had lower operating costs and a better understanding of the local markets. In some product categories the cost differences between P&G traditional products and those that the Chinese consumers in the lower-end market could afford was so wide that just making the product cheaper by changing some ingredients was not enough for P&G to become competitive (Hexter and Woetzel, 2007, p. 6-7).

P&G soon realized that to be able to compete against Chinese companies in the lower-end market it had to develop new capabilities to understand the needs of the new customers, and develop, market, and distribute competitive products to these markets. P&G started designing products in China from the outset to meet a target price point, controlling the cost required to meet the price. This approach, called 'design to cost', is a state-of-the-art practice followed in the world's top companies in developed markets. The twist is that competition in China is much tougher that in most other countries. P&G product developers in China spend much more time and attention on reducing product cost that in any other country (Hexter and Woetzel, 2007, p. 75). Today P&G is the most successful

Glob advantage

foreign marketer in China as measured by marked share, with leadership positions in most of the product categories in which the company competes. China is among its largest markets measured in sales volume (Hexter and Woetzel, 2007, p. 3).

This P&G capability of designing to very low cost and compete successfully in the tough Chinese market can certainly be transformed into a competitive advantage in the future in other markets. This capability is in essence the same that gave Galanz and Haier their competitive advantage to become dominant world players in their respective markets and beat well established traditional MNCs. In other words, MNCs that cannot compete successfully in China will probably not acquire the capabilities needed to compete against Chinese companies in their traditional markets, and become secondary players in the world market, as the manufacturers of microwave ovens and appliances competing against Galanz and Haier found out the hard way. MNCs seem to have no choice; they have to accept China's to challenge to defend their markets positions, and so continue being world players.

Glob advantage

Risks to China's future growth

Before we consider the opportunities and risks of doing business in China for those that accept China's challenge, we have to evaluate the risks of China being able to maintain in the future its extraordinary economic growth. To evaluate these risks, we have to understand the key factors responsible for its extraordinary accomplishments of the last three decades. The study *China: The Balance Sheet* (2006, p. 19) conducted by C. Fred Bergsten and his colleagues under the auspice of the Center for Strategic and International Studies and the Institute for International Economics pointed to five factors as key to China's stunning transformation: "The embrace of marked forces, the opening of the economy to trade and inward direct investment, high level of savings and investments, the structural transformation of the labor force, and investment in primary school education." Of these key factors that promoted China's growth, none is really at risk if the Chinese government does not deviate from its present

economic policy and keeps up its refinement of its unique social-capitalist model. The real risks to China's future political stability and economic growth are the remaining poverty, the unbalanced and unsustainable economic growth model, and the bureaucracy and corruption of government officials.

Paradoxically, writes Johnston (2001, p.7), corruption may have helped Chinas economic development by helping to overcome some of the conflicts between state power, represented by its bureaucrats, and the forces promoting the economic reforms, represented by the fast emerging entrepreneurs. Corruption served as a kind of lubricant that motivated government bureaucrats to modify and adapt government policies that would have hindered the economic reforms by giving them extremely attractive opportunities for collusion with the entrepreneurs that promoted China's extraordinary growth.

Corruption may have helped lubricate the economic reforms but over the longer term it has potentially explosive consequences for China's economic and political future, as Johnston (2001, p. 8) and Minxin (2007, p. 1) points out. Illicit practices such as bribery, kickbacks, theft, and misspending of public money cost at least 3 percent of GDP, according to Minxin (2007, p. 1). It is also undermining the legitimacy of the ruling Chinese Communist Party, widening income inequalities between those that are benefiting from the economic reforms and those that are being marginalized, and so fueling social unrest by inciting popular resentment against the highly-visible new rich class of profiting bureaucrats and entrepreneurs.

China's government is aware of these risks, and is taking determined steps in raining in corruption, as demonstrated by the many crackdowns on corrupt government officials. The Chinese know that if they don't control corruption, the governing Communist Party will be lose its control over the country as did in the past the Imperial Qing Court, and the Kuomintang government of Chiang Kai-shek. The same determination by the government has been shown in alleviating income inequality, environmental degradation, and in encouraging the transition from an economy dependent

Glob advantage

on exports to one where internal consumers have a much more important role.

Most economists believe that the risks to China's future economic growth exist and are a real treats to China's future, but can be overcome by the pragmatic and determined Chinese government. The Chinese approach to political and economic development has been, and will probably continue being one of trial and error. Government officials describe this trial and error process as being similar to "crossing a river by feeling the stones underneath."

Accepting China's challenge

To win in the rapidly changing business environment of China, foreign companies need to learn the right ways to reach emerging customer segments with new products designed to very low cost, and how to beat local competitors in the cut-throat competitive markets. Most consumer product MNCs like P&G entered China in the late 80s or during the 90s through joint ventures with well-connected domestic partners and began to sell a wide range of products under global brands. These products were sold to the affluent Chinese consumers in the premium market of large coastal cities. Industrial companies selling raw materials, equipments and services to the emerging Chinese companies followed the same entrance route. The consumer products and industrial goods were bought by the Chinese at premium prices either because there were no substitutes, the affluent consumers wanted foreign brands, or the industrial company's required higher-end equipment. The higher prices attracted thousands of MNCs that flooded China.

The business environment is changing fast in the 21st century China and things will become a lot tougher for MNCs. The friendly business climate were customers paid premium prices for foreign goods, that attracted so many MNCs, is fast turning into the most competitive market in the world where only the most cost efficient will survive. The massive middle class of 250 million (Degen, 2009, p. 5) and over 400 million cell phone users that emerged in Chinese large and small cities have a different buying profile

Glob advantage

that the early affluent consumers that MNCs sold to in the 90s. At the same time competition between Chinese and foreign companies for the share of wallet in every consumer segment and business-to-business category is becoming ferocious.

The unique social-capitalism economic model developed by Deng Xiaoping, particularly the liberalization and promotion of the Chinese entrepreneurs, was extraordinary successful in transforming China from an economical and technological backward nation into one of the world's most dynamic nations (Yueh, 2008). Den Xiaoping clearly stated his support of Chinese entrepreneurs to fuel economic growth and progress in his historical 'Southern China Tour' of 1992 (Jin, 2003, p. 254) with the now anthological phrase: "To get rich is glorious" (Malkiel and Taylor, 2008, p. 38). He echoed in his way Schumpeter's (Schumpeter, 1942) thesis that without entrepreneurs acting as 'agents of creative destruction' there is no real economic growth and progress, and that the pure socials model was doomed because it did not promote entrepreneurship.

Glob advantage

China's disruptive innovation

The generation of Chinese entrepreneurs that emerged after the state eased the control over the Chinese economy are enthusiastically following Den Xiaoping's "to get rich is glorious", are relentlessly acting as Schumpeter's 'agents of creative destruction', and relentlessly obsolescing less more expensive or less efficient goods or services. But before the destruction of the industry leaders, as occurred in the microwave-oven industry with Galanz 'disruptive innovation from the base of the pyramid', a long period of 'creative creation' was developing in China's backyard (Hart, and Christensen, 2002, p. 52).

China provides its entrepreneurs, like Qingde Liang the founder of Galanz, and foreign companies doing business in China, like P&G, all the essential conditions for 'creative creation' that lead to successful 'disruptive innovation from the base of the pyramid'. Hart and Christensen (2002, p. 52) explain that the products and services available to Chinese customers of the lower-end market are deficient or not yet as good as those available to

Glob advantage

customers in the premium market of the large coastal cities, and especially to customers in developed economies. The lower-end market Chinese, permits companies to experiment with 'disruptive innovations', in less demanding applications, and among non-traditional customers. They can promote their 'creative creation', develop new 'disruptive innovations', and let them grow and mature with almost no competition, before taking them up-market to more sophisticated customers, and much tougher competition in the premium market of the large coastal cities. If successful in China, they then can then conquer the world markets, as Galanz and other Chinese companies did.

Most well managed MNCs are under pressure to pursue innovation in markets than can sustain corporate growth rate and enhance their profit margins. For them investing in 'disruptive innovation' seems irrational (Hart, and Christensen, 2002, p. 52). They prefer the 'incremental innovation' approach to improve their products or services so not to compromise their substantial investments in these products and their production technology and capacity. The idea of 'disruptive innovation' and having to obsolete their investments and start from scratch with a new technology scares them off. For this reason potential disrupters like Galanz are able to incubate their businesses in the safety of poor markets that their resource-rich competitors ignore. These upstarts, based on their success in these less sophisticated markets, will seek to grow up-market by attacking market tiers that are less attractive to industry leaders, and when they gained enough product savvy and production scale go after the main markets.

Gadiesh and Vestring (2006) point out that the MNCs that are accepting China's challenge are aware of the threat posed by Chinese entrepreneurs and the 'disruptive innovation'. They are doing more than just competing for the share of wallet of the rapid expanding lower-end market. They are using the Chinese lower-end market to warm up for the future worldwide competition. They are building the expertise, business capabilities and production scale to export their Chinese products and business know-how to other emerging markets, primarily India and Brazil, and then building on their success and production scale to developed

Glob advantage

markets. These MNCs know that China is the lead market in preparing them to pursue businesses in other developing markets, it is also clear to these companies that to continue succeeding globally they have to win in China first, as P&G is winning.

China's good-enough market

The Chinese market can be segmented into a small premium rapidly growing segment at the top of the consumer pyramid, mostly served by foreign companies with prestigious brands making good profits, and at the bottom a large lower-end segment served by local companies with cheap low-quality commodity type of products and services that are typically 40 to 90 percent cheaper than the premium offerings of foreign companies (Gadiesh, Leung and Vestring, 2007, p. 16). Between these two segments is rapidly expanding a new market that Gadiesh and Vestring (2006) called 'China's good-enough market', building on Christensen (1997) use of the phrase 'good enough' to suggest that start-up companies developing and releasing new products and services don't necessary need to aim for perfection to make inroads against established players.

China's cities are classified administratively into four municipalities directly under the Central Government - Beijing, Shanghai, Tianjin and Chongqing, 27 provincial capitals -Guangzhou, Hangzhou, Chengdu, etc., and 310 prefecture cities. Within the municipality, provincial capitals and prefecture cities' territory are 856 city associated districts, 369 county-level cities and 1,600 counties. A common approach is to prioritize these city markets in to four tiers: The four municipalities, 27 provincial capitals, and a handful prosperous prefecture cities such as Shenzhen, Dalian and Ningbo into a what is known as the first-tier cities, the more than 300 prefecture cities into second-tier cities, the 1,200 city associated districts and county-level cities into third-tier cities, and the 1,600 counties into fourth-tier cities (Lannes and Zhu, 2009).

The premium market in China was mainly concentrated in the first-tier cities and the lower-end market in the second-tier and lower cities. Aware of the rapidly expanding 'good-enough market', MNCs have started looking

Glob advantage

beyond the premium market to China's more than 300 second-tier cities, particularly to the 120 that have populations over one million, and approximately 1,200 county-level third-tier cities. The race is now on to sell in places like Yantai, Shaoxing, and Wuxi, writhe Lannes and Zhu (2009), where middle-class incomes is rising the same way they rose in first-tier cities earlier in the decade. China's second-tier cities now represent about 88 percent of the country's GNP. As a group, those cities experienced a twelve-fold increase in household disposable income per capita in the years between 2002 and 2006, while retail sales rose 79 percent. By comparison, in first-tier cities household disposable income rose 61 percent and retail sales increased by 80 percent in the same period.

There are many reasons for the rapid expansion of the 'good-enough market'. The main reason is obviously the rising income of Chinese consumer as a direct consequence of the extraordinary growth of the country over the last three decades. These consumers with rising income are trading up from the lower-end products they previously purchased. These new consumer are the driving forces for Galanz and Haier's rapid and successful growth, but also for the success of P&G, and specially the spectacular growth of Kentucky Fried Chicken (KFC) and Carrefour in China.

Glob advantage

The success of KFC is an interesting example of a MNC that took full advantage of the rapidly expanding Chinese middle market in the second-tier and lower cities. Liu (2008) explains KFC success by its product localization, the introduction of new products faster and more frequently than their competitors, and developing products that better fit the Chinese consumer's taste. The KFC highly localized menu includes congee or Chinese-style porridge for breakfast, Beijing chicken roll served with scallion and seafood sauce, spicy diced chicken resembling a popular Sichuan-style dish. Their latest creation is *you tiao* or Chinese dough fritters. All this adaptation to the Chinese consumer's taste let to two to one points of sales advantage over McDonalds in China, whereas outside China it's the other way round. Liu (2008) also warns that the success of KFC in China is already being challenged by fast rising Chinese fast food chains.

Curiously KFC could not duplicate its Chinese success formula to other large developing markets like Brazil, were with only four restaurants in Rio de Janeiro in 2009 it is struggling way behind McDonalds' 1,144 points of sale - 541 restaurants, 556 kiosks, and 47 McCafés - in 134 cities, of 21 states and the federal capital. According to Liu (2008) a vital ingredient in KFC's success was its leadership team. The team known as the 'Taiwan Gang', because most of the senior member came from Taiwan, had accumulated at least 10 years of fast-food industry prior to arriving in China, and though predominantly Western-educated, being ethnic Chinese, they inherently understood China. The experience and the understanding of the culture led to an intuitive knowledge of the market context, which then put KFC China on track to becoming a successful enterprise. Liu explains this point: "In order to be successful, especially for foreign companies or non-local companies, a deep and broad understanding of the market context is critical to success. To the extent that the understanding is even intuitive, meaning that you don't have to do the market research, you don't have to have multiple meetings to come to the best solution to a problem, or to point to a future strategic direction" (Cho, 2009). This means that KFC had the right team to succeed in China and probably did not in Brazil, were it has been struggling for decades.

The French hypermarket chain Carrefour, whose name means 'crossroads', also took advantage of the fast expanding middle market in China, and following essentially the same strategy of adapting to Chinese consumers as did KFC. Tanks of live fish, eels, bullfrogs and turtles dominate the fresh food sections, while vacuum-packed strips of bacon and slices of pepperoni lie in refrigerated cases a short distance away. Modern formats mix with local tastes in the French retailer's stores: Shoppers stroll down wide, brightly lit aisles, past displays of dried pork snouts and whole ducks hanging limply by the neck, as "Hotel California" plays on the speakers overhead (Child, 2006). Carrefour opened its first store in China in 1995, and shot to prominence very quickly in China's retail market with its strategy of adapting its hypermarkets to the taste of the new Chinese consumers. It beat its arch competitor Wal-Mart, taking a strong initial lead among the foreign retailers in the grocery market, lead that Wal-Mart won

Glob advantage

back in 2006 with the purchase of Trust-Mart the Taiwanese owned top retailer in China. However, Carrefour remains stronger than Wal-Mart in terms of revenue per outlet, and continues to lead the field in many innovations in the Chinese modern grocery market.

R&D in China

The success of P&G, KFC and Carrefour are based on designing the right products for the emerging Chinese consumer in the fast expanding middle market or 'good-enough market'. The implication is that any MNC that wants to succeed in this market needs to have the necessary product research and development (R&D) capability combined with a good understanding of the needs and aspirations of the emerging Chinese consumer. Besides doing R&D to serve the Chinese market, an ever increasing number of MNCs are betting that their product development capabilities in China will eventually become for their hub for their global R&D efforts, particularly in categories were competition is becoming increasingly ferocious like the pharmaceutical and chemical industries, and specially the high-tech consumer electronic area. The reason being that the costs of doing R&D in developing countries are increasing, and a Chinese R&D base could add up to substantial savings, particularly in products were R&D costs are important component in the final cost of the product (Hexter and Woetzel, 2007, p. 71).

Hexter and Woetzel (2007, p. 71-72) from McKinsey compared the cost of doing R&D for high-end telecommunication routers of an American and a Chinese manufacturer. The R&D costs for routers sold in the U.S. market were between 20 to 25 percent of the total costs. This means that a saving of 5 percent in R&D would generate a 1 percent margin improvement. Now considering that engineers in the U.S. earn roughly three to ten times more that their Chinese counterparts, and that the Chinese work nearly 20 percent longer on average. Even considering that the Chinese engineers were less efficient and so the Chinese operation needed more engineers, the American company was, in the end, spending five times more that its Chinese counterpart to develop similar products.

Glob advantage

This means that the Chinese company spends 80 percent less on R&D for their routers, and so have a cost advantage of 16 percent for R&D alone. The authors conclude: "A company needs extremely persuasive arguments for it to forgo that sort of advantage by keeping R&D in its developed home market". An interesting example of R&D in China is the chemical giant BASFs that has seven R&D sites in China, covering polyurethane, poly-THF, construction chemicals, dispersion, coating & specialties, textile auxiliaries, leather, pharmaceutical solutions, nutrition ingredients, personal care ingredients, care chemicals & formulators, engineering plastics, plasticizer, engineering unit, catalysts, electronic material and etc. (BASF, 2009).

Chinese companies are using the extraordinary growth of the Chinese economy to rapidly developing their own world class R&D capabilities as demonstrated by Galanz, Haier, and BYD. According to a recent article by Gunther (2009) in Fortune Magazine, last fall Warren Buffet's Berkshire Hathaway bought 10% of BYD for $230 million. The deal, which is awaiting final approval from the Chinese government, didn't get much notice at the time. It was announced in late September, as the global financial markets teetered on the abyss. But Buffett and is long time partners Charlie Munger and David Sokol think it is a very big deal indeed. They think BYD has a shot at becoming the world's largest automaker, primarily by selling electric cars, as well as a leader in the fast-growing solar power industry.

Buffet and his partners, according to the Fortune article, were fascinated by Wang Chuan Fu, the entrepreneur that started BYD in 1995 in Shenzhen, China. The letters BYD are the initials of the company's Chinese name. A chemist and government researcher, Wang raised some $300,000 from relatives, rented about 2,000 square meters of space, and set out to manufacture rechargeable batteries to compete with imports from Sony and Sanyo. By about 2000, BYD had become one of the world's largest manufacturers of cell phone batteries. The company went on to design and manufacture mobile-phone handsets and parts for Motorola, Nokia, Sony Ericsson, and Samsung.

Wang entered the automobile business in 2003 by buying a Chinese state-owned car company that was all but defunct. He knew very little

Glob advantage

about making cars but proved to be a quick study. In October a BYD sedan called the F3 became the bestselling sedan in China, topping well-known brands like the Volkswagen Jetta and Toyota Corolla. BYD has also begun selling a plug-in electric car with a backup gasoline engine, a move putting it ahead of GM, Nissan, and Toyota. BYD's plug-in, called the F3DM for 'dual mode', goes farther on a single charge - 62 miles - than other electric vehicles and sells for about $22,000, less than the plug-in Prius and much-hyped Chevy Volt are expected to cost when they hit the market in late 2010. Put simply, this little-known upstart has accelerated ahead of its much bigger rivals in the race to build an affordable electric car. Today BYD employs 130,000 people in 11 factories, eight in China and one each in India, Hungary, and Romania.

Deploying the armies of laborers at BYD is an officer corps of managers and engineers who invent and design the products. Today the company employs about 10,000 engineers who have graduated from the company's training programs - some 40% of those who enter either drop out or are dismissed - and another 7,000 new college graduates are being trained. Wang says the engineers come from China's best schools. "They are the top of the top," he says. "They are very hard-working, and they can compete with anyone." BYD can afford to hire lots of them because their salaries are only about $600 to $700 a month; they also get subsidized housing in company-owned apartment complexes and low-cost meals in BYD canteens. "They're basically breathing, eating, thinking, and working at the company 24/7," says a U.S. executive who has studied BYD (Gunther, 2009).

Another example of how China moves fast in developing new technologies is China's lead over the U.S. in generating electricity from renewable sources. Bradsher (2009) in his article in the New York Times points out that as the U.S. is taking its first steps toward mandating that power companies generate more electricity from renewable sources, China already has a similar requirement almost two years ago, and is investing billions of dollars to remake itself into a green energy superpower. This year China is on track to pass the U.S. as the world's largest maker for wind turbines, after doubling wind power capacity in each of the last four years.

Glob advantage

Win in China or lose everywhere

The title of the last chapter of Hexter and Woetzel's (2007) book "win in China or lose everywhere" says it all. The examples of Galanz, Haier, and BYD clearly demonstrate that the new champions for every industry are being incubated in China. Companies, Chinese of MNCs, that learn to compete and win in the fast growing Chinese 'good-enough market', will build strong positions to win in the global market, especially in the large emerging markets of Brazil and India. The scale of the Chinese market will give companies that are successful in China a global structural advantage over companies that did not accept China's challenge.

REFERENCES

ALI, Shaukat, and GUO, Wei, Guo, 2005, **Determinants of FDI in China**, *Journal of Global Business and Technology,* Volume 1, Number 2, Fall

BASF, 2009, ***BASF Greater China R&D sites***, http://www.greater-china.basf.com (assessed June 2009)

BERGSTEN, C. Fred, GILL, Bates, LARDY, Nicholas R., and MITCHELL, Derek J., 2006, ***China: The balance sheet***, Public Affairs, New York

BRADSHER, Keith, 2009, **Green power takes root in China**, *The New York Times*, July 2, http://www.nytimes.com (assessed July 4)

CHILD, Peter, 2006, **Lessons from a global retailer: An interview with the president of Carrefour, China**, *McKinsey Quarterly*, (2006 Special Edition: Serving the new Chinese consumer), p. 70-81, www.mckinseyquarterly.com (assessed June 2009)

CHINA ECONOMIC REVIEW, 2009, ***China by Numbers 2009***, China Economic Review Publishing, Hong Kong

CHRISTENSEN, Clay, 1997, ***The innovator's dilemma: When new technologies cause great firms to fail***, Harvard Business School Press, Boston

CHO, Karen, 2009, ***KFC China's recipe for success***, ISEAD Knowledge, July 1, knowledge.insead.edu/KFCinChina090323.cfm?vid=195

CHOW, Gregory C., 2007, *China's economic transformation*, Blackwell Publishers, Oxford

CHOW, Gregory C., 2005, *Corruption and China's economic reform in the early 21st century*, CEPS Working Paper No. 116, Princeton University, October, www.princeton.edu/ceps/workingpapers/116chow.pdf (assessed June 2009)

Glob advantage

DEGEN, Ronald J., 2009 (1), ***Opportunity for luxury brands in China***, www.globadvantage.ipleiria.pt, Working Paper nº 31 (assesses June 2009)

DEGEN, Ronald J., 2009 (2), ***Understanding China's historical development: The profit and the risks that China's stock market provides investors***, www.globadvantage.ipleiria.pt, Working Paper nº 35 (assessed June 2009)

DiPAOLA, Paul, and LI, Jerry, 2007, ***From "Made in China" to "Invented in China"***, Bain & Company, p. 3

FARHOOMAN, Ali F., WOO, Claudia H.L., 2006, *Business corruption in China*, Asia Case Research Center, The University of Hong Kong, http://harvardbusinessonline.hbsp.harvard.edu (assessed June 2009)

FARRELL, Diana, GERSCH, Ulrich A., and STEPHENSON, Elisabeth, 2006, **The value of China's emerging middle class**, *McKinsey Quarterly*, (2006 Special Edition: Serving the new Chinese consumer), p. 60-69, www.mckinseyquarterly.com (assessed June 2009)

FERNANDES, Juan A., and UNDERWOOD, Laurie, 2009, ***China entrepreneur: Voices of experience***, John Wiley & Sons, Singapore

GADIEESH, Orit, and VESTRING, Till, 2006, **China's 'good-enough' market**, *The Wall Street Journal Asia*, September 5.

GADIEESH, Orit, LEUNG, Philip, and VESTRING, Till, 2007, The battle for China's good-enough market, *Harvard Business Review*, September, www.hbrreprint.org, Reprint R0709E (assessed June 2009)

GE, Gloria L., and DING, Daniel Z., 2007, ***A strategic analysis of surging Chinese manufacturers: The case of Galanz***, Published online: 10 November, Springer Science and Business Media,

GUNTHER, Marc, 2009, **Warren Buffett takes charge**, *Fortune Magazine*, April 13, http://money.cnn.com/2009/04/13/technology/gunther_electric.fortune (assessed June 2009)

HART, Stuart L., and CHRISTENSEN, Clayton M., 2002, The great leap: Driving innovation from the base of the pyramid, MIT Sloan Management Review, Fall, www.mit-smr.com, Reprint no 4415, (assessed June 2009)

HEXTER, James R., 2006, **Better manufacturing in China: An interview with two of PLP's executives**, *McKinsey Quarterly* 3, October, www.mckinseyquarterly.com (assessed June 2009)

HEXTER, Jimmy, and WOETZEL, Jonathan, 2007, ***Operation China: From strategy to execution***, Harvard Business School Press, Boston

HOOVER, William, 2006, **Making China your second home market: An interview with the CEO of Danfoss**, *McKinsey Quarterly* 1, p. 84-93, www.mckinseyquarterly.com (assessed June 2009)

INTERNATIONAL MONETARY FUND**Erro! A referência da hiperligação não é válida.**, www.imf.org/external/pubs/ft/weo/2009/01/weodata/weoselgr.aspx (assessed June 2009)

JIN, Yang, Planner, 2003, ***The history and civilization of China***, Central Party Literature Press, Beijing

JOHNSON, Roberta Ann, 2008, *Corruption: Dare we compare the United States and China*, Paper delivered at the Western Political Science Association meeting, March 20-22, San Diego, California, www.allacademic.com/meta/p238323_index.html (assessed June 2009)

JOHNSTON, Michael, 2001, ***Corruption in China: Old ways, new realities and a troubled future***, Department of Political Science Colgate University, people.colgate.edu/mjohnston/MJ%20papers%2001/currhist.pdf (assessed June 2009)

LANNES, Bruno, and ZHU, Larry Zhu, 2009, **The race for "small" town China**, *The Far Eastern Economic Review*, January 14th, http://www.profitfromthecore.com/bainweb/Publications, (assesses June 2009)

LEWIS, W. Arthur, 1954, *Economic Development with Unlimited Supplies of Labour*, The Manchester School, vol. 22, no. 2, pp. 139-191.

LIEBERTHAL, Kenneth, and LIEBERTHAL, Geoffrey, 2003, The great transition, *Harvard Business Review*, October, www.hbrreprint.org, Reprint R0310D (assessed June 2009)

LIU, Warren K., 2008, ***KFC in China: Secret recipe for success***, John Wiley & Sons, Singapore

MALKIEL, Burton G., and TAYLOR, Patricia A., MEI, Jianping, and YANG, Rui, 2008, ***From Wall Street to the Great Wall: How investors can profit from China's booming economy***, W. W. Norton & Company, New York

McEWEN, William, FANG, Xiaoguang, ZHANG, Chuanping, and BURKHOLDER, Richard, 2006, **Inside the mind of the Chinese Consumer**, *Harvard Business Review*, March, www.hbrreprint.org, Reprint R0603D (assessed June 2009)

McKINSEY GLOBAL INSTITUTE, 2006, ***From made in China to sold in China: The rise of the urban consumer***, November, www.mckinsey.com (assessed June 2009)

MINXIN, Pei, 2007, ***Corruption threatens China's** future*, Policy Brief 55, Carnegie Endowment for International Peace, October 2007, www.carnegieendowment.org (assessed June 2009)

MORISSET, Denis, and LEE, Lawrence, 2008, ***Welcome to the China luxury summit 2008***, http://www.chinaluxurysummit.com (accessed April 2009)

SCHUMPETER, Joseph A., 1942, ***Capitalism, socialism and demo**cracy*, Harper & Brothers, New York

TIMES global luxury survey: China, India, Russia, 2007, Time, September 17, pg. 108

UNITED NATIONS IN CHINA, 2008, *China's progress towards the millennium development goals 2008 Report*, Published Jointly by Ministry of Foreign

Glob advantage

Affairs of the People's Republic of China and the United Nations System in China, http://www.un.org.cn/index.htm (assessed June 2009)

YUEH, Linda, 2008, China’s entrepreneurs, University of Oxford, Department of Economics, Discussion Paper n° 324, www.economics.ox.ac.uk/Research/wp/pdf/paper324.pdf (assessed June 2009)

ZHANG, Z. John, 2006, ***How and why Chinese firms excel, in the art of price war***, Knowledge@Wharton, December, knowledge.wharton.upenn.edu/index.cfm?fa=viewarticle&rid=1625