THE 1 HOUR CHINA BOOK
(2017 Edition)

TWO Peking University Professors Explain All of China Business in Six Short Stories

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Jonathan Woetzel
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One Hour China Consumer Book: Five Short Stories That Explain the Brutal Fight for One Billion Consumers, by Jeffrey Towson and Jonathan Woetzel (May 2015)


Operation China: From Strategy to Execution, by Jimmy Hexter and Jonathan Woetzel (December 18, 2007)

It has been three years since we published the *One Hour China* book. And three years is a really long time in China. For example, in this three year period:

- Over 30 million people moved into Chinese cities. By 2025, China will have ten New York-sized cities.

- 60 million people bought cars and over a thousand miles of metro lines (the distance from Dallas to Chicago) were built.

- Over 20 million people graduated from Chinese universities. Also during this period, China sent more than 1.4 million students to study overseas.

- Over 360 million Chinese tourists traveled out of the country.

- Chinese companies made over $400 billion in overseas acquisitions.
China’s foreign exchange reserves first grew by $800 billion and then shrank by $1 trillion to wind up at around $3 trillion.

Things move pretty fast in the PRC. We thought an updated edition of this book was definitely needed.

We also thought it was important to check how our main thesis has held up. We have argued that six mega-trends (urbanization, manufacturing, consumers, brainpower, capital and the Internet) drive most of China business. And that these trends explain most of the China stories you see in the news. We are pleased to see our thesis has held up over time.

However, in some cases, these mega-trends have begun growing even faster. For example, Chinese consumers are now a global force. Back in 2013, sales on the November 11 singles’ day holiday (in Chinese this translates to “me me me me”) outsold American Cyber Monday by 3:1. This ratio has now climbed to 5:1, with over $17 billion transacted in one day. McKinsey & Company has recently forecast that the working Chinese consumer will account for over a third of global consumption growth through 2030.

The intersection of the consumption and manufacturing trends is also becoming interesting. For example, technology’s richest woman globally is now Hong Kong-based Zhou Qunfei. Born in a poor, rural community in mainland China, Zhou was a factory worker in the glass industry before starting her own company, Lens Technol-
ogy. Today, Lens Technology is one of the world’s largest manufacturers of screens for mobile phones and tablets (and Chinese consumers are the biggest buyers of smartphones). Lens Technology went public in March 2015 and Qunfei now has an estimated net worth of $6.4 billion.

We found that the Internet chapter did need a serious update. This is not surprising as the Chinese Internet, and smartphones in particular, moves at a startling speed. It is also pretty unpredictable. As we are writing this, Chinese company Meitu is preparing for a Hong Kong IPO. Meitu offers a mobile photo editing application that lets you alter your appearance in your photos – such as by making your chin narrower, your eyes bigger, and so on. In the past two years, Chinese women have began using this app to “beautify” their selfies in stunning numbers. Over 440M Chinese women are now using the application. “Beautifying selfies” was a market virtually nobody saw coming. Even the CEO of Meitu has said it was a total surprise. These kinds of surprises are fairly common in the Chinese Internet.

Note: in September 2016, a woman was pulled over for drunk driving in Western Xinjiang. After a breathalyzer confirmed intoxication, the police began taking photos for evidence. The woman then demanded that they use Meitu for their photos, so she would look better.

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We wrote the *One Hour China* book for “smart but busy people”. We wrote it for people who wanted to know more about China business but who were not going to live in China. And who really didn’t have time to read 10-15 weighty books on China. We wrote this book based on what we would say to a smart but busy person if they gave us one hour of their time.

That turned out to be a pretty good idea. The book went to the top of the Amazon best-seller list (for China) and stayed there for over two years. It is now also being taught in business schools, foreign policy programs and undergraduate programs around the world. One reviewer described it as a “minor publishing sensation”, which we thought was a pretty apt summary for such a little book.

We hope this book helps you understand China a bit more. China’s impact on global markets is continuing to grow. This book is probably more relevant today than when we first wrote it. We are really just at the beginning of this phenomenon.

Thanks again for reading,
Jeff and Jonathan.
January 2017
China is big.

That’s our attention-grabbing opening. China is really, really big. It’s important to be provocative in publishing.

China is also really complicated. By economy, by industry, by population and by just about every other metric, the country keeps getting more and more complicated. China is now both really big and really complicated – not unlike, say, the United States and Europe.

So the idea of a one-hour China book is kind of ridiculous. How could you possibly explain such a big and sprawling topic in an hour?

But it’s not actually a theoretical question. We both do “China-to-the-world” thinking for a living. And more and more, we have found ourselves getting asked about China in places like Ohio, Brighton and Lima. Places that five years ago didn’t really care that much about this topic.
And the questions are not just coming from business people now. They are also coming from academics, concerned parents, policymakers and many other groups. China has become an important topic most everywhere. But most people don’t have the time to read lots of weighty China books. Some prominent American politicians know shockingly little about China by the way.

So this book is our answer to this situation. If we had the undivided attention of someone from Ohio, Brighton or Lima for just one hour, this little book is what we would say.

And we took it a bit farther. Not only is this book our one-hour explanation of China business, it is also written so that it can be read once, thrown away (please don’t) and remembered easily. That was our goal: a speed-read China book that explains most things and sticks in the brain.

If we have done our job well, you should be able to read this in 60-90 minutes. You can read the main points in an hour. If you read absolutely everything, it will take closer to 90 minutes. And after one reading, you should have a reliable framework for understanding China business. Most China headlines (say in the Wall Street Journal) should make sense. In fact, they should be fairly predictable.

ABOUT US: THE VIEW FROM THE LAOWAI TRENCHES

We both live and work with one foot in China and one foot out. We do China-to-the-world thinking for a living. Our main careers are in management consulting (Jona-
than) and private equity deals / advisory (Jeff). But we also write and teach at business schools.

Jonathan is a senior partner at McKinsey & Company in Shanghai and is co-Director of the McKinsey Global Institute. And he was the guy that opened their Shanghai office in 1994. If you want to know the answer to a ridiculously specific question like “what was Baosteel working on in 1995?”, Jonathan probably knows the answer. And there is a good chance that he was part of the team answering it. Jeff refers to him as the “national archive for China business”.

Jeff is an investor and advisor focused on US-China private equity deals. Jeff’s background was shaped by eight years working as an executive / slave to Prince Alwaleed. Alwaleed is usually known as the Saudi Prince who bought Citibank, News Corp and the Four Seasons. He is also occasionally known as the guy building the one-mile
skyscraper in Jeddah (Jeff’s old project.) and the Prince who turned an Airbus A380 into a private plane.

We both work in the trenches of China business. We spend our days digging into companies and industries. We are bottom-up analysts and our view of the world is based on studying and working with thousands of individual companies. Jonathan is also known for his ability to speak Mandarin so fluently that it shocks Chinese. Jeff has an accent that produces much the same effect.

As professors, our academic home is Peking University’s Guanghua School of Management in Beijing. Although it desperately needs a Starbucks, it is otherwise a great place to teach. Our students have come from virtually everywhere: China, South Korea, Singapore, Norway, Los Angeles, New York, Azerbaijan, Egypt, Germany and so on. Generally speaking, they are crazy ambitious, which
we respect. It is completely normal for MBA courses in China to run until 10pm on Friday night.

An important note: Some of our 2012 MBA students were involved in the first edition of this book. We have highlighted them at the end of this chapter.

THE ONLY 6 STORIES YOU NEED TO KNOW TO UNDERSTAND CHINA

A lot of China business can appear to have a mysterious quality. It can seem strange and far away. This is not uncommon for new industries or markets. Our first assertion is to relax. There is nothing mysterious or terribly difficult about Chinese companies or markets. In business, there is really nothing new under the sun. Consumers behave pretty much the same everywhere. Competition is pretty much the same everywhere. You just need to ignore the hype and hyperbole and stay focused on the basics.

And in China today, the basics are 6 big trends.

That’s it. There are six big trends that shape most of the industries. These six trends are also driving much of China’s impact on the world. They are like tectonic plates moving underneath the surface. If you can understand them, the chaotic flurry of activity on the surface becomes a lot more understandable – and even predictable.

However, we are talking about trends that move businesses on a monthly basis. These are revenue or cost drivers
that you can see in income statements. That is different than the high-level, “trends” that are typically discussed by economists, politicians and other macro analysts. Our trends are phenomena that are generating revenue, creating big companies and minting Chinese millionaires (and billionaires).

You will probably notice that we have little to say about Chinese politics or state capitalism. For some reason, Western business people who normally study customers and competitors shift their focus to politics and regulations when in China. Our experience is that these topics are wildly over-emphasized by Westerners in China. The business of China is mostly business.

Our big assertion is that six mega-trends are driving most of China’s business today – and its interaction with the rest of the world. The deals, the newspaper headlines, and the rising and falling wealth of companies are mostly manifestations of these six mega-trends – which we show below.
This is our simple framework. If you remember one thing from this book, it should be this chart. We will repeatedly come back to it throughout the book. In each of the following chapters, we will be talking about one of these six mega-trends. And we will be telling a story for each. We will tell the stories of six individuals that rode these trends to staggering wealth.

So you can look at business in China as either six mega-trends or as six short stories, depending on how your brain works. And this is our basic proposition. You give us 60-90 minutes and we will give you six stories and a chart that explain most of China business.

However, let us make an important caveat. These are powerful trends that are driving business activity today. It does not mean they are necessarily good things. Or that they are stable or sustainable. Most lead to profits, or at least revenue. Some may be stable. But some lead to bubbles that may or may not collapse. We are only arguing that they are big and are driving economic activity on a very large scale.

OUR THANKS FOR READING OUR BOOK

This book is the result of the expertise of +30 people - including MBAs, McKinsey partners, China writers and many editors. While small, it represents a lot of expertise that we have tried to distill down to a speed-read that sticks in the brain.
We hope that our enthusiasm for this topic also comes across. The rise of China and its increasing collision with the world is a fascinating topic. And it is something we live on a daily basis. It’s a fascinating life. Dynamic. Fairly chaotic. Often anxious. May you live in interesting times...

Our thanks for reading our little (literally) book. We hope you find it helpful or at least a good way to kill a taxi ride home. We tried to keep it to one hour (and the price of a latte).

Also, if you would like to receive other reading recommendations, please sign up at www.onehourchina.com. The follow-up to this book, the One Hour China Consumer Book, is also now available.

Our thanks and cheers,
Jonathan and Jeff

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MBAS YOU SHOULD HAVE ON YOUR RADAR

Please take a moment to look at the 2012 MBAs who have worked on this project.

CHAPTER ON URBANIZATION:

Edan Kaplansky: Born in Manhattan and raised in Jerusalem, Edan holds an L.L.B. and an M.B.A. from Hebrew University, with studies at Peking University’s Guanghua School of Management. After his
MBA, he worked at Shibolet and Co., Advocates & Notaries, and was Managing Director of the ‘Brera Center’ Foundation, which provides free legal and educational services to underprivileged populations.

**Ron Klein.** Born in Chicago and raised in Israel, Ron holds an L.L.B. from Hebrew University Faculty of Law, where he served as Deputy-Editor of the Faculty Law Review. He also holds an M.B.A. from Hebrew University and Peking University, majoring in International Finance. After graduation, Ron worked at the Israeli Securities Authority, focusing on Corporate Governance and Securities Regulation Policy.

**Wang Xinran** holds an M.B.A. from Peking University and focuses on business operations and strategic management. After graduation, Xinran worked for SMIC (Semiconductor Manufacturing International Corporation) as an investment manager.

**Yinan Zhang.** Yinan focused on Strategy and Investment at Peking University. Prior to attending business school, Yinan worked for several multinational firms including Kraft Foods, Unilever and Nestle, focusing on supply chain management. Yinan earned a Bachelor’s degree in engineering from Beijing Normal University in 2005.

**CHAPTER ON RISING CHINESE CONSUMERS:**

**Scott Hicks.** Scott earned his MBA at the University of British Columbia, where he specialized in Finance, Strategic Management, and International Business. Holding a CFA charter, he has worked for the Canadian Federal Government and in the treasury department of Finning International.

**Denis Lenz** holds a Bachelor’s degree in Business Administration from the University of St. Gallen, Switzerland. Born and raised in
China, he has strong international exposure and a great interest in Asia’s dynamic societies.

CHAPTER ON MANUFACTURING:

Christopher L. Amador was a 2013 candidate in the Master of International Affairs program at the University of St. Gallen in Switzerland. He has experience in the automotive and consulting industry through internships with BMW Group and Bain & Company, where he worked on China-related topics.

Jangyoon (Johnny) Kim. A native of Seoul, Korea, Johnny is an established consultant and project manager. He is intrigued by China’s potential to shape the global economic landscape.

Maria Elena Kolesch earned her Bachelor of Science in Business Administration from Germany’s leading business university, Mannheim, in 2011. She completed her Master’s in Corporate Management and Economics at Germany’s “Zeppelin University.”

CHAPTER ON FINANCIAL SERVICES:

Juuso Makinen is an economics major from Helsinki intrigued by the challenges of emerging markets – particularly financial liberalization and asset pricing issues. As a student at Peking University, he gained insights into social and economic topics pertaining to China.

James Liu

Kexin Zheng was a part-time M.B.A. student at Peking University’s Guanghua School of Management. She holds a Bachelor’s degree in Economics and Sociology from Peking University. She served as a credit analyst at MetLife China and previously worked as a banking analyst at CCXI, the largest local credit rating company in China.
CHAPTER ON BRAINPOWER:

Theresa Gessner. With a background in corporate communications and management studies, her field of interest lies in cross-cultural management and international communication strategy. She earned her MSc from Stockholm University in 2013.

Spence Nichol was an associate with a global management consultancy, and a former strategic advisor to one of the world’s best performing school systems. He has studied at London Business School, the China-Europe International Business School in Shanghai, and the University of Alberta in his native Canada.

Xiaoyi (Fenny) Wang. A senior software engineer, Fenny has been working in a multinational telecom company for over eight years. She graduated from the University of Toronto with a Bachelor’s degree in Computer Science, and later studied in Peking University’s MBA program.

CHAPTER ON THE INTERNET:

Peter Lehmann is a digital business professional with German roots and a global mindset. By following market trajectories and technology trends, he aims to build the products and services of the future. The insights he contributed to this book are the result of his studies at Peking University.

Stephan Maluck. Born 1986 in Germany, Stephan studied Management at universities in Germany, China, and Chile. He holds a Master’s degree and works as a management consultant in the financial services industry while pursuing his Ph.D. Prior to graduate school, Mr. Maluck completed an apprenticeship at Deutsche Bank and developed an entrepreneurial mind-set as an executive assistant of a German start-up.
Mathis Wilke holds an M.B.A. from CEIBS in Shanghai. During his studies he won the China Final of the CFA Institute Research Competition in Shanghai, and placed as a Semi-Finalist at the Asia-Pacific Regional Final in Hong Kong. Prior to business school, he worked as a Senior Associate in the Leveraged Finance departments of RBS and Mediobanca for five years, financing private equity transactions across Europe. He speaks German, English, Spanish and Mandarin Chinese.

Janet Yurasova. Originally from Russia, Janet graduated with an M.B.A. from the UCLA Anderson School of Management. Before attending Anderson, she ran a small web-development company and started three successful Internet endeavors. Janet has a diverse educational background in business, IT, law and social sciences from US, Russian, French, Cyprus and Chinese universities.

GENERAL RESEARCH:
Stian André Kvig holds an MSc. from Copenhagen Business School. Mr. Kvig has held several internships involving international capital markets during his studies, and he manages a private portfolio of investments. He has working proficiency in German and conversational ability in Mandarin.

Also thanks to Luke Masuda for his help with this project. Finally, a special thanks to Glenn Leibowitz of McKinsey. We are both greatly appreciative of his invaluable support and his generosity with his time.
MEGA-TREND #1: URBANIZATION

China is currently witnessing the largest migration in human history. Hundreds of millions of people are flooding from the countryside into the cities. And while over 300 million people have already migrated in the past 30 years, McKinsey predicts there are another 350 million yet on the way.

China’s urban population (M) over time

Source: China Statistical Yearbook
This urbanization phenomenon is adding an average of 18.5 million people to China’s cities every year. That is equivalent to adding the population of the Netherlands annually. Or the equivalent of adding the entire population of Japan every 8 years.

This process began in earnest in the 1980s when government controls on where people could live were loosened (to some degree). Prior to this, the Chinese population had been somewhat frozen in place. For example, in 1980, only 20 percent of the Chinese population was located in cities. In the US in 1980, it was 70 percent. So this massive urbanization process is a lot about China catching up. It is about transitioning from an agricultural to an urban industrial society.

Such a huge migration of people changes almost everything: cities, required infrastructure, environmental impact, required resources, the economy, etc. As cities contain virtually every aspect of life, such a migration changes virtually everything in China. However, this is not just an economic and demographic trend (which we will discuss). It is also a cultural phenomenon.

For many Chinese, the move from their home village to the city is a key moment in their lives. Workers, young college graduates and even entire families have strong memories of leaving their village for the first time and taking the train ride to Shenzhen or Shanghai. As in America’s great migration West in the 1800’s, this movement into the cities represents the search for opportunity and a better life.
On national holidays, workers return to their villages from the cities. Rain delays during these periods can cause massive congestion - as in the Guangzhou railway station in January 2008 (photo: Tan Qingiu / ChinaFotoPress)

Urbanization is our first China mega-trend. We have placed it as the starting point in our chart (below) - as it is the most important phenomenon shaping modern China. We will make just a few key points about this trend (helpfully noted as Key Points) and then we will tell a short story about its impact. This will be our process for each chapter - one story and a few Key Points.

The 6 China Megatrends
KEY POINT #1: THERE WILL SOON BE 1 BILLION CHINESE CITY DWELLERS

From 1980 to 2015, China’s urban population grew by approximately 450 million. That is more than the entire population of the USA. This brought the number of Chinese city-dwellers to about 750 million and the overall urbanization rate to 55 percent. However, this is still far below the 70-80 percent urbanization rate seen in Japan, the US and Europe. So we still have a long way to go.

In 2009, the McKinsey Global Institute (and Jonathan specifically) published a widely cited report, “Preparing for China’s Urban Billion.” It showed how by 2030, there will be over 1 billion Chinese city dwellers. That’s the number to remember: 1 billion city dwellers. Chinese urbanization is increasing at a fairly linear rate toward this big milestone.

When this happens, China’s cities will be more populous than the North and South American continents combined. The implications of this are profound. And 1 billion is a good number to keep in mind. It’s also pretty easy to remember.

KEY POINT #2: LOTS OF CITY DWELLERS MEANS LOTS OF CITIES

Not a big surprise. All these people moving into the cities have to live somewhere. So they need apartments. And they need buses and subways to get to work. And they
need water and electricity. And then they need things like police, parks, roads and sewage treatment. These are not little challenges.

Obviously, a lot of Chinese cities just got bigger in response. Most added new districts. We can today count 160 Chinese cities with over 1 million people. In comparison, Europe has 35. And McKinsey predicts this number will increase to about 220 by 2025. So think 220 cities like Tucson, Arizona.

Some cities got a lot bigger. China currently has 16 cities with over 5 million people - and this will increase to 23 by 2025. So think 23 San Francisco’s (a scary thought for conservative America). And these will constitute 40 percent of the world’s cities with over 5 million people.

And finally, we are seeing the emergence of mega-cities. These cities, usually several cities linked closely together, contain 30-40 million people each. And many will reach 50-60 million people. These are fascinating and we will discuss them more in the key point on clusters.

Our point here is that there is a ton of building going on to handle the inflow of people. And it is not something that any country has ever attempted before. It also occasionally produces some unusual situations. An example is Shenzhen, often called a “city without memory”.

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Shenzhen is today, by any definition, a world-class, first-tier city. Located directly across the border from Hong Kong, it has several modern business districts, great parks, more than 10 million people, and a subway system that has grown from nothing to very large in about 10 years.

It is also a “city without memory”. It is a place where you always ask where someone is from, because nobody is from Shenzhen. The city was only a series of villages prior to 1980. The total population then was about 100,000. And as recently as 1995, the central business district Futian was empty fields. Building a thriving city from scratch in just over two decades is an impressive feat with some strange consequences.

If Shenzhen is a city without memory, Kangbashi in Inner Mongolia is often called a “ghost city”, another unusual situation created by urbanization. Mostly empty Kangbashi
MEGA-TREND #1: URBANIZATION

was built from scratch for an anticipated 1 million inhabitants by 2023. This population, by and large, did not show up and projections have been reduced to 300,000. So today it’s a big, impressive and empty city. There are communities of empty apartment blocks. Modern government buildings and retail spaces are deserted. Kangbashi and other ghost cities get a lot of media attention – especially when discussing China’s real estate bubbles.

Our point is that all of this is to be expected. If you are building cities at a breakneck pace against a huge urbanization inflow, sometimes your supply gets ahead of your demand. That, plus some real estate speculation and debt, gets you a ghost city. And sometimes your demand gets ahead of your supply and you get congestion (e.g., crowded Beijing). And sometimes you get it about right (e.g., Shenzhen). These things should be expected and are not as significant as newspaper headlines would have you believe.

KEY POINT #3: IN CHINA, URBANIZATION = WEALTH

Human beings are social animals. Putting us in close proximity to each other, such as in cities, changes us. And urbanization is fundamentally changing the Chinese people. How they act. How they shop. How they communicate. It is also changing their economic status.

In China, urbanization equals wealth. Going city-by-city across China, urbanization has directly coincided with approximately 350 million Chinese moving out of poverty since 1990. GDP per capita just goes up faster in cities.
And not only have 250 Chinese cities tripled their GDP per capita since 1990, but disposable income per capita is also up over 300%. So what you are seeing in Chinese cities is both an increase in the number of people in cities and an increase in spending power per person.

Facing massive urbanization, cities can easily vary between over-capacity (i.e., ghost cities) and congestion - as in the city of Shanghai (above)

© chuyu/123RF Stock Photo
This is not necessarily a causal relationship. And in most countries, urbanization does not directly lead to wealth (hello Latin America). More likely urbanization is necessary for wealth, even if by itself it is not sufficient. We make no claim for why this is happening in China. But the data is overwhelming. Note the chart below.

![Chinese urbanization (%)](chart.png)

That’s the end of the numbers for this chapter. Some people relate better to numbers (Jeff wants his obituary to be a PowerPoint presentation). But most people relate better to stories. And for Chinese urbanization, a good story to remember is that of Wang Shi and his company, China Vanke.
THE AWESOME STORY OF WANG SHI AND CHINA VANKE

China Vanke is a real estate company that has no equivalent in the West. The company’s revenues are greater than the top four American real estate developers combined. It has built more apartments than any other company in history. And Wang Shi, the founder, is now the world’s largest real estate developer. He is also the person who has provided a defining event for millions of rising Chinese: the purchase of their first home.

China Vanke is strictly a residential real estate developer. They make simple, clean apartments for China’s middle class. That’s it. This is a simple “value for money” proposition, which is a very common strategy among China’s first moguls. He did not really innovate. He did not offer luxury. He offered basic quality homes at a affordable price. And he did it in great volume very quickly. For example, in 2015 alone, China Vanke sold over 20 million square million in apartments across more than 25 Chinese cities.

Wang Shi, Chairman of China Vanke (Photo: Imaginechina)
MEGA-TREND #1: URBANIZATION

A PRETTY INSPIRING RAGS-TO-RICHES STORY
Wang Shi was born in 1951 in a military family in Liu-zhou, Guangxi. Even today, this is a world away from Shanghai and Beijing. But back in the 1950s, it was deep in the wilderness of China. It was an isolated and poor city that was just recovering from its occupation by Japan in World War II.

Shi graduated from junior high school in 1968 at the height of the Cultural Revolution, a time when urban youth and other groups were being relocated to the countryside. Coming of age during this difficult period of China’s history is a common theme for many of the successful business people we will discuss in this book.

Following his parents’ advice, Shi joined the army and headed off to Xuzhou, Jiangsu (near Shanghai). However after just 6 months, he was transferred to the Turpan Basin in Xinjiang. This is just about as far northwest as you can go in China. It was literally the end of the world at that time. And for 5 years, Shi worked there within a military logistics group. Finally in 1973, he left the army and found a job as a furnace worker in the Zhengzhou Railway Bureau in Henan in central China.

The now 23-year-old Shi eventually enrolled in the Department of Water Supply and Drainage Engineering at the Lanzhou College of Transportation, capturing one of the only two entrance opportunities available. After graduation, he returned to southern China and began work in the engineering section of the Guangzhou Railway Bureau.
In terms of rags to super riches stories, it is difficult to find a more humble beginning for a billionaire than Wang Shi’s story. To come of age in rural China during the Cultural Revolution meant a focus on survival. And Shi’s early movements between colleges, military positions and government jobs were not uncommon. These were largely the only career options available in China at that time.

By 27, Shi had settled down. He worked on several civil engineering projects as a technician, got married to Wang Jianghui, the daughter of a retired deputy party secretary of Guangdong Province, and started a family. There was virtually no indication of the capitalist heights to which he would soon rise.

However, in 1980, Shi took and passed the recruitment examination for the Department of Foreign Trade and Economic Cooperation of Guangdong Province. This would turn out to be the move that would change everything for him. For Guangdong, just across the border from Hong Kong, was about to become the first part of China to open to the world. Another common theme of the success stories in this book is being in Guangdong and Shenzhen in the early 1980s.

Shi became a liaison for Guangdong’s Foreign Trade and Economic Relationship Committee. Whether by strategy or luck, he had found himself in the epicenter of newly capitalist China. As China opened to the world, foreign trade through Shenzhen and Guangdong was the first big economic activity. And as liaison for the foreign trade
committee, he likely had a bird’s eye view into the business opportunities being created at that time.

In 1983, Shi quit his job and struck out on his own. He went right to Shenzhen, which had by that time been designated China’s first Special Economic Zone. He was not alone in this move. Government officials from all over China were jumping into business and heading to Shenzhen. But as mentioned, while Shenzhen is a first tier city today, it was not much more than a series of villages in the early 1980s.

Shi struck gold fairly quickly. At that time, China needed basically everything and those bringing goods across the Shenzhen border were extracting large profits. Shi made his first 3 million renminbi (about US$1 million at that time) by bringing in corn and reselling it to an animal feed company. He used this first windfall to jump into consumer electronics, importing electronic equipment from Japan and then selling them to the local market. He also started up several manufacturing plants for garments, watches, beverages and printing. Shenzhen had become a boomtown for just about every type of product. Shi would later say, “Except for pornography, gambling, drugs, and weapons, Vanke (his company) did almost everything.” His company Vanke, in Chinese, basically means diversification.

What Shi was doing was deal-making. He was trading, buying and selling – basically cutting deals amid the frenzy of China’s opening to the world. According to China Daily, he was at one point the biggest importer in Shenzhen.
However, this chapter is about the urbanization mega-trend. And while Shi was successful, so were many others. He had not yet caught the mega-trend that would rocket him upwards above the rest.

That changed in November 1988 when Shi participated in a land auction for the first time. He made an astonishingly high bid for the “Vuitton Villa” land plot in Shenzhen. His bid was so high it surprised everyone, including the auction officer. But it got him into the real estate game. And with his first real estate project acquired, his company began to transform from a trading house (called the “Modern Educational Equipment Exhibit Center”) into a real estate developer. He also raised 28 million renminbi in funds (about US$7.6 million at that time).

From there, his rise was meteoric. The massive migration of Chinese into cities - as well as the movement of current urban residents into nicer apartments - created a huge demand for modern residential housing. In 1991, just three years after its first real estate deal, China Vanke went public on the Shenzhen Stock Exchange. It was the second company to list on the new exchange.

As mentioned, China Vanke focused on basic residential units for the middle class. And they turned them out in great numbers. China Vanke quickly became the largest residential real estate developer in China, with operating income and net profits growing annually at approximately 30 percent and 35 percent.
In 2015, China Vanke’s annual sales exceeded 260 billion renminbi (US$38 billion). Its total sales area reached 20 million square meters. And Vanke’s business covered 55 Chinese cities, with its national market share at 3%. It is dominant in China’s mega-clusters of the Pearl River Delta, the Yangtze River Delta and the Bohai Rim Economic Circle. Today, China Vanke is the world’s largest real estate company, employing approximately 16,000 employees in 28 locations.

However, all of this success has now had an interesting development. As of this writing in 2016, Vanke is fighting against China’s first major takeover battle. Financial speculators, Chinese red chips and other real estate players are all in the mix. Vanke’s success, its listed status and the low shareholding of Wang Shi himself has put the company in play.
But the story of Vanke is one we will see again and again in this book: an entrepreneur was in the right place at the right time, caught one of the six mega-trends and then rocketed upwards at astonishing speeds.

Today, at 65, Shi remains Chairman of China Vanke and is one of China’s most famous businessmen. He is also a philanthropist and a noted environmentalist. And he is a particularly well-known mountain-climbing enthusiast, having conquered the highest peaks of all seven continents.

**Wang Shi – Chairman, mountain climber, philanthropist, environmentalist**
*(Photo: Imaginechina)*

**THE SECRET OF HIS SUCCESS**
We have argued that China Vanke’s meteoric rise followed from catching the urbanization mega-trend. That means being in the right place at the right time – which 1988 Shenzhen absolutely was. However, they were certainly
not the only ones there doing real estate. So how did they become number one?

The secret to Vanke’s success was cost-efficiency and speed. While many developers focused on building landmark real estate projects or on projects with outsized financial returns (say, 100 percent), China Vanke focused on speed. Shi has said he focused on projects with 25% returns and would drop any project over 40%. This reflects a core concept of Vanke’s operating strategy: expediting turnover while driving trading volume, even if it means passing on higher return projects.

Vanke has a business model it calls “5-9-8-6.” Start construction within five months of land purchase. Kick-off sales in the ninth month. Achieve 80% of the target in the first month. And sell out 60% once the project has opened up for sales. This enables the company to retrieve cash faster than its competitors. It can then re-invest to acquire more land for construction and development.

We argue that their focus on speed, turnover and covering a large network of cities enabled them to ride the urbanization wave more effectively than others. They also chose to focus exclusively on real estate. Early-on, they sold 10 other promising businesses so they could focus entirely on residential real estate.
That’s most of our point for this chapter. We’ve given you a big trend. We’ve given you a story. And we’ve made a few key points. But there are some fascinating aspects to urbanization. And we have detailed six more of them below. These can be skimmed if you are trying to keep this book to one hour.

KEY POINT #4: CHINA IS A SERIES OF CLUSTERS, NOT A CONTINENT

Looking at China today, what you don’t see is an integrated continental economy. You don’t see infrastructure connecting each part of the country, like say in the United States and Europe. That is likely the future but not yet the present.

If you look at the population and the existing infrastructure, what you actually see is a series of “clusters”. You see
clusters of cities with over 60 million people. For example, Beijing / Tianjin in the North is actually a cluster of 28 cities – all tightly interconnected by roads, rail and other infrastructure. Qingdao, well known for its beer, is actually part of a 35-city cluster.

China has more than 20 of these clusters (shown below), and each of these clusters is about the size of a European country. According to government plans, China’s main clusters will cover 80 percent of GDP and 60 percent of the population.

If you think about China as a series of clusters, and not as a continent, a lot of things make more sense – especially urbanization and infrastructure. Much of the highly publicized high speed rail and other infrastructure projects are about creating clusters. It is about making it possible for people and goods to travel cheaply and quickly within a cluster.
And these clusters do vary by income, demographics and social structure. Shenzhen, the original migrant megacity, is markedly younger than Guangzhou, its cousin 2 hours away. Shanghai has more rich people than nearly all of the inland clusters combined. And in Beijing, household sizes are shrinking faster than in any other cluster. It is an interesting phenomenon to keep track of.

Much of the new infrastructure, such as high-speed rail, is about building clusters
(Photo: redstone / iStockphoto)

KEY POINT #5: URBANIZATION = BIG PROBLEMS = BIG OPPORTUNITIES

As mentioned, urbanization is creating a need for housing and infrastructure that is ongoing. But infrastructure is only part of the problem. These new urban populations are creating increasing pressure on government for security (e.g., police), for public services (e.g., sanitation, buses,
Imagine being a government city official facing such an inflow of people every year. How many roads will you build this year? How many new subway lines? How will you deal with rising pollution levels and crime? How will you grow the GDP? How do you plan for rapid growth across virtually every aspect of urban life? It’s a daunting job.

There is some fascinating work by McKinsey on strategies for city development (we are obviously biased here). One interesting project is the Urban China Initiative, which is a joint project between McKinsey, Tsinghua University’s School of Public Policy and Management and Columbia University. Central to this project is the question of how do you balance economic development, resource needs, environmental impact and social well-being. You can find the research at www.urbanchinainitiative.org.

WATER IS THE BIGGEST PROBLEM
A good example of how urbanization creates both big problems and big opportunities is the water situation.

China is one of the world’s thirstiest countries. There is limited water supply in general and agriculture uses the majority of fresh water today (about 62 percent). And as China grows wealthier, this agricultural usage is increasing (wealthier countries eat more). And what’s more, industrial and municipal uses are actually growing faster than agricultural uses. So across the board, we are seeing increasing demand for a fairly small water supply.
Exacerbating this supply problem is the deteriorating water quality in China. By most estimates, 60 percent of underground water and 40 percent of rivers are seriously polluted and unfit for use. This is largely due to the 75 billion tons of sewage and wastewater that has been discharged into them. One extreme example of this river dumping phenomenon was the surprising appearance of 2,800 dead pigs in Shanghai’s main river in the summer of 2013. The pigs had been dumped upstream into the river and floated into downtown Shanghai one Monday morning.

Overall, approximately 300 million rural dwellers have no access to safe drinking water. And when you combine this water situation with the urbanization mega-trend, it is not surprising that two-thirds of Chinese cities today are short of water.
The government’s response to this problem thus far has been to increase the water supply. In particular, they have been building large projects such as the South-North Water Transfer Project. This is a multi-decade, multi-billion dollar infrastructure project that creates Western, Central and Eastern water routes. All three routes aim to divert water from the Yangtze River to the Yellow River and Hai River. The project was originally expected to cost $62 billion – more than twice as much as the Three Gorges Dam - but over $80 billion had been spent by 2014. But supply alone cannot solve the problem. Next on the agenda is water conservation and treatment. And the government is openly supporting innovation in this area.

The Three Gorges Dam (Photo: Thomas Barrat / Shutterstock)
All this creates big business opportunities. According to Chen Lei, Minister of Water Resources, China plans to invest $636 billion on water-related projects through 2020. These projects will be geared toward treating heavily polluted rivers and lakes and toward improving water ecosystems in ecologically fragile areas. For example, China currently accounts for about 90 percent of the annual global investment in forests, wetlands and other ecosystems that help keep human water supplies clean.

KEY POINT #6: IT’S MOSTLY ABOUT THE CONSTRUCTION

Urbanization, real estate and infrastructure all get mixed together as topics. The numbers can get confusing. When this happens, just check the construction spending. It’s mostly about the construction. Real estate accounts for about 20-22 percent of the total national investment in fixed assets. And construction employs over 100 million people directly or indirectly.

Construction also ties to other industries. Real estate is a factor in the sale of consumer appliances, furnishings, and anything else that can be put in an apartment, house, office or warehouse. And obviously, construction and real estate play a decisive role in the building material industries. Each year in China, 25 percent of steel, 70 percent of cement, 40 percent of wood, 70 percent of plate glass and 25 percent of plastics are used in real estate development and construction.
Economically, it’s still mostly about construction
(© Zhang Yongxin/123RF Stock Photo)

Basically, it’s all about construction. It doesn’t mean it is sustainable or even necessarily a good idea. But it is where the biggest dollars from urbanization are located.

**FINAL POINT: URBANIZATION IS A SOCIAL PHENOMENON**

Cities have all aspects of human life: family, culture, health, politics, work, art, environment, and just about everything else. So urbanization affects almost everything. And it is putting the majority of the Chinese population into close contact with each other for the first time. Such close contact will change everyone. Ultimately, Chinese urbanization is the largest social experiment ever seen.
The long-term implications of this on Chinese social, cultural and lifestyle norms are anyone’s guess. Alongside the many positive outcomes of urbanization (such as increasing incomes) are some that may challenge the fabric of Chinese society. There is without question a widening income gap between rural and urban populations— and between urban professionals and migrant workers (the unofficial urban lower class). Pollution has very quickly become a major priority for urban residents. And urban life is very different than the slow-moving, family-centric village lifestyle that dominated China for centuries. And all these changes are happening very quickly.

So it is worth keeping in mind that when people talk about 1 billion Chinese city dwellers, nobody really knows what that means.

Is it all too much too fast? A 13-story building falls over in Shanghai in 2009
(Photo: Imaginechina)
MEGA-TREND #2: HUGE MANUFACTURING SCALE

Our second mega-trend is Chinese manufacturing scale. And this is likely the most well-known trend to Western observers. Consumers around the world are long accustomed to things being “Made in China.” Shoes, bicycles, toys, tables, and so on. China is the “world’s workshop”. It is also sometimes known as “the place where underwear comes from.”

Chinese manufactured products outbound to the world at Qingdao port
(Photo: Imaginechina)