SPECIAL INTERVIEW
Chris Skinner Banking on the Future

INDIAN POLITICS
One Year of Modi; Has He Kept His Word?

BRAZILIAN INDUSTRY
My Communist Business Partner

Emerging Markets Insight

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Q3 2015

COVER STORY

SPORTS: MORE THAN JUST AN EXPENSIVE HOBBY?

Soccer teams are new toys for the Chinese super rich. Why have they become soccer fans so suddenly?

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Q3 CONTENTS 2015

3 Special Interview
CHRIS SKINNER: BANKING ON THE FUTURE

10 Sports $ Money
MORE THAN JUST AN EXPENSIVE HOBBY?

16 Chinese Business
LETV'S JIA YUETING: THE SPIRIT OF A DISRUPTOR

22 Chinese Transportation
TRUCK GANG LEADER'S ENTREPRENEURIAL (AND WARRIOR) SPIRIT

28 One Year of Modi
HAS HE KEPT HIS WORD? OPTIMISM IS HERE TO STAY VS. CONFLICTING AGENDAS

32 Indian Manufacturing
THIS IS HOW IT'S DONE

38 Indonesian Investment
CREADOR'S INDONESIAN ATTRACTION

41 Brazilian Industry
MY COMMUNIST BUSINESS PARTNER

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BANKING ON THE FUTURE

FOR CHRIS SKINNER, IT'S SIMPLE: GO DIGITAL OR GO HOME, AND FIN TECH IS LEADING THE WAY

Profile

Author, commentator, and sought-after speaker Chris Skinner has been working in banking and insurance technology since the early 1980s, including stints at Wang Computer and NCR Corporation. Skinner has always looked to the future of banking and the opportunities and challenges new technologies bring. He has written 10 books on different aspects of banking, including *The Digital Bank: Strategies to Launch or Become a Digital Bank* (2013). Based in Great Britain, Skinner chairs the Financial Services Club, is chief executive of Balatro LTD and co-founded thefinanser.com, which regularly features his blogs. Skinner recently shared some of his views with EMI.

The global financial industry is experiencing new innovation and Fin Tech has recently been taking center stage. Could you define Fin Tech in your own words? It must be much more involved than simply saying "payment by mobile phone."

Fin Tech is the integration of finance and technology. For most, it means making the financial markets Internet-ready, as many bank and insurance systems were built before the Internet was invented or without a consideration of customers accessing those systems directly through the Internet 24/7.

IT companies used to be providers (or supporters) of technical methods for financial companies, such as e-banking and mobile-banking for banks. Now more IT companies are entering the financial business arena on their own to meet customers' needs directly. What triggers do you think have forced the IT companies to change? What differentiations and strengths do you think IT companies have in financial business in this new era? And could you give some examples of specific companies?

Financial companies are becoming IT companies and IT companies are becoming financial companies. This is exactly due to the previous answer—Fin Tech integrates finance and technology. But there's more to this than that basic statement, as two specific technologies are changing the game, and I call this the Internet of Value or the ValueWeb, if you prefer (the title of my next book). The ValueWeb allows anyone, anywhere, to exchange value with anyone else, anywhere else, in real-time for almost free.

Historically, banks have created systems that are slow. An international payment takes days to process for that reason. But mobile has changed all of this. Mobile technologies and specifically the mobile Internet, are allowing all of us to connect directly through the network one-to-one with each other. In other words, seven billion people living on Earth can create electronic connections with each other today. Once you do that, you can exchange information and build relationships and, most importantly, trade. However, you cannot trade if it is expensive to pay, and so the ValueWeb creates new ways to pay.

In particular, there needs to be a way to pay that is cheap and real-time, not expensive and slow. That is why the development of bitcoin and the blockchain has been transformational. The blockchain will allow anyone, anywhere, to transfer value global-

ly to someone else for almost free, in real-time, because it is an Internet ledger of transactions that is trusted and free. This technology is now being built into the banking system by companies like Ripple, Eris and Erethreum, and will soon be the de facto way to pay. This is why the two technologies of mobile and blockchain are the drivers of the Fin Tech revolution.

By way of example, in 2014 $13.2 billion was invested in Fin Tech startups by venture capital funds. In 2013, it was $4 billion and before that less than a billion. Why would VCs invest so much? Because they can see the returns. In 2014, there were 36 new Fin Tech startups like Lending Club, Stripe, Funding Circle and Square, with over a billion dollar valuations. The year before, only 12 and next year probably over 100. These new companies are using the mobile Internet to create new peer-to-peer connections for crowdfunding and lending and new payment systems through technologies from APIs (Application Program Interfaces) to the blockchain. In fact, a third of the Fin Tech firms are focused upon P2P (peer-to-peer) value connections like Zopa and TransferWise whilst a third are focused upon payments like Klarna and Traxpay. These firms are really changing the game and the result is that banks will lose money. A Goldman Sachs report on the future of finance published in the first quarter estimates that banks will lose over $10 billion of profitability—about 20% of the market—in the credit line of business alone over the next few years as customers defect to peer-to-peer lenders like Ppdai and Alibaba, so this is critical change to the financial system.

Then what kind of future are the traditional financial companies facing? As stated in your book *Digital Bank: Strategies to Launch or Become a Digital Bank*, it is not only a crisis but also opportunity for them. What differentiated strengths can they exert under the new circumstance that digitized financial services are pushing into our everyday lives? What new format of financial service can they provide to customers? Do you see any specific financial players who are successfully and innovatively adapting to this new circumstance?

Seven billion people living on Earth can create electronic connections with each other today.

Traditional financial firms have a problem, in that they were built in the last century and focused upon the physical distribution of paper through a localized network focused upon buildings and human hands; the new players are focused upon the digital distribution of data through a globalized network focused upon software and servers. The difference is that the new players can transact the same services—loans, mortgages, insurance, wealth management, investments, payments—at a fraction of the cost of the old. As a result, the old companies cannot compete with the new if their cost models are ten times more expensive because of their many buildings and staff structures. So they have to move rapidly from physical to digital.

Moving to digital is not simple however. For many financial firms it means ripping out their current systems that were built for physical operations and replacing them with digital structures that are Internet-enabled. Even if that is done, it means going one step further and changing management and leadership to get digital. I often say that banks are led by leaders who delegate digital to function or person—the Head of Digital. How can you delegate the future of the bank? So the leadership team must start with digital as their focal area, and the change management to become digital at their core.

That is tough, as it means a key understanding of building financial systems and structures where digital Internet services are the core of the firm and humans and buildings sit upon those digital foundations. Too often, I hear firms that talk about channels and functions, and realize that their thinking is that digital is being added to their buildings and humans as an overlay. It is completely wrong thinking, as digital firms think digital first and then work out what buildings and humans need to sit upon that digital structure.

This is the reason that I can only name a few firms that think this way. Digital titans are obvious—Alibaba, TenCent. Digital financial firms are not so obvious but a few are out there—mBank in Poland, Commonwealth Bank of Australia, ICICI Bank in India— but they are few and far between, and even these banks are not truly digital yet. In the digital age, customers expect and demand one-to-one personalized digital service.

For China, Eastern Europe and Africa, it is said that low rates in credit card use and underdevelopment of financial service infrastructure naturally lead to the successful development and growth of Fin Tech in the region. However, in Korea, the general public uses credit cards to pay and has easy access to ATMs and Internet banking, and

stock investments are more common. Do you believe the expansion of Fin Tech and digitized technology is still an inevitable path in countries like Korea, where the financial service infrastructure is already well established?

Fin Tech is going to adapt and change everything everywhere, based upon the mobile and value exchange technology of the blockchain I've described. In developed markets like Korea, you will see similar changes to those I see in Japan, Europe and America vis-à-vis direct peer-to-peer payments, funding and credit.

More intriguing, in some ways, are the developments we are seeing in China, Eastern Europe and Africa. These economies are still developing, and a key here is financial inclusion. There are five billion people who have no banking or are underbanked today. They have been excluded from the system in the past because to service them was too expensive. Building branches in areas where people are poor and there's no profit to be made didn't make sense. However, now through the mobile Internet and blockchain, seven billion people are being connected to an electronic system that is cheap, easy and real-time. That means that the whole planet will be able to communicate and trade one-to-one. Goat farmers in Ethiopia will be able to sell goat products – leather hides or crafts made from goat hide—to Korean buyers via QQ pages, Wechat photos, text messaged payments and Alipay logistics. That is an amazing new world and amazing new concept. Everyone on this planet can buy and sell anything with anyone, anywhere.

So the whole concept of how we live on this planet changes with it. That will be as transformational in Seoul, where people will

be connected to things they never thought of connecting with before, as it is in London, Paris, Mumbai, New York, Tokyo and Shanghai.

Welcoming gestures from individual customers and investors are triggering the popularity of Fin Tech. What factors and aspects of the Fin Tech do you think are attracting people? What merits and values can people expect from it, from the perspective of the customer, and investor?

There are three fundamental pieces to Fin Tech which the firms that are winning understand: connectivity, simplification and personalization.

Connectivity allows anyone to trade with anyone, anywhere. Simplification takes away the old complexities of markets and makes them easy by dealing with just a small part of that market. For example, for many Fin Tech companies they are just taking one process—lending, paying, buying, investing—and making that one piece simple. What is different is that they are simplifying the basics of finance, not trying to be all things to all people which is what traditional firms have been. It's a little like the Ubers or Alibabas who provide platforms to connect people who need to get from A to B or who need to buy something from people who have the car or the product you need. These middle-ground intermediaries act as the global or regional or national data hubs to connect the person who needs something with the person who has it, direct, one-to-one, through software and servers. That's what the simplification game is all about.

Finally, there's personalization which then becomes the differentiation. Personalization is all about making sure you remember what the individual did last time to make it easier for them to do it next time and, for the data intermediary, that's easy as they've got the data. Airbnb, Facebook, Google or whoever, know where you stayed, what you posted or searched for last time, and therefore just make it easier and easier each time you touch their service by repeated and simplifying that process on a personalized basis. That's what banks and insurers need to do: connect, simplify and repeat by making it personal. These are the basics of attracting and retaining the customer in the digital age.

There are worries about the bubble risks that Fin Tech might bring. Crowdfunding and P2P lending services, for example, could damage the participant's assets and security when regulation and supervision processes are incomplete and are not well-managed. What is your view on the side effects and the negative potential and risk that the digitized financial technology would bring?

There are three fundamental pieces to Fin Tech which the firms that are winning understand: connectivity, simplification and personalization.

Right now, there's a lot of downside to the Fin Tech bubble. People are starting to trust brands that are unregulated, and they are not aware of the risks. MtGox is a great example. MtGox was viewed as a store of value by many, and they assumed that their value store was guaranteed. It wasn't, and when MtGox went under, thousands of bitcoin investors went bust. MtGox lost $500 million in investments with no recourse, guarantee or reimbursement.

That's just plain wrong, and it's why financial markets are regulated. Banks and insurance companies work hard at compliance, audit and regulation because it is compliance, audit and regulation that give them their licence to provide a store of value. I find it hard to believe that consumers don't understand this, but maybe because it is not clear and underscored. If you store your savings in an Internet brand because you like that brand, you have zero guarantee of your money being safe.

This is critical in understanding the difference between the Fin Tech guys, who claim you don't need banks and insurers anymore. You need the financial system to provide stability and confidence. Without it, you have nothing.

For emerging countries, what kind of technology and business capability should be available for companies that plan to penetrate or do business in the region?

For emerging economies, the two technologies that are transformational are mobile and blockchain. Mobile provides inclusion for everyone cheaply and easily. Blockchain provides the transmittance of value cheaply and easily via mobile in real-time. This is why these two technologies will rapidly upscale these economies because suddenly those who have no access to financial transactions or markets can transact and play. A person who has an idea, a craft, an ability, anything can transact now with anyone and sell that idea, craft or ability. You could never do this before because that idea, craft or ability was limited to the locality of your community. Many people in that locality would know about that idea, craft or ability. They might even buy it once, but that was seriously limiting, as the idea, craft or ability could [not] be sold many times.

Right now, there's a lot of downside to the Fin Tech bubble. People are starting to trust brands that are unregulated, and they are not aware of the risks.

That is the transformation of mobile and blockchain. Anyone, anywhere now has the ability to sell any idea, craft or ability to anyone else, anywhere else on this planet. That is incredible and amazing and is unlimited by the banking system or even the governance system.

It is why Dee Hock, the founder of Visa, describes the blockchain as the future of not only payments, but of governance. It is here and now. We have connected the planet. This is amazing, so get with the program and work out how your institution, company, competency and capability can play a part in this transformation or be excluded and die.

Could you propose three keywords for the financial market player facing digital industrial revolution?

Core, humans and culture. Financial services institutions must first create a digital core. They then need to work out what role people play in supporting that core by, for example, engaging in customer relationships through remote digital outreach via social media. Then, if they are using social media, they must have a culture whereby the humans understand how to build relationships through digital outreach. Can you really be relevant to your target audience on their QQ page? That's the key. Core, humans and culture.

As a specialized analyst in financial markets, you have researched various cases of innovative companies that drove the digital transformation of today's financial industry. Could you describe which case has impressed you the most?

Well, the one I keep coming back to, because it showed commitment, is mBank in Poland. What is commitment? Most institutions participate and play with the idea of digital. They are not committed. They run pilot programs and tests. They don't bet the bank but mBank did just that.

mBank is actually a company called BRE Bank, a bank that had operated in Poland since 1985. BRE Bank launched the first Internet banking platform in 2000.

They were seen as the market leader for innovation back then and gained a lot of popularity. Then, in 2009, Alior Bank launched Alior Bank Sync, a cool social mobile app. BRE Bank looked old and slow, and lost customers to Alior Bank as a result, bearing in mind that BRE Bank had been the technology market leader as the first Internet bank in Poland. So the CEO took a really brave decision and decided to relaunch BRE Bank as a digital bank. He brought in a new digital leader from Microsoft, invested heavily in the development of a new mobile, social bank platform

and launched this platform in summer 2013.

Now, the reason this impresses me most is not because the bank launched a digital bank service but because they threw away their 30-year-old bank brand. They got rid of the BRE Bank brand and launched anew as mBank. All the branches were rebranded— the ones they kept—and the new mBank became seriously cool. As a result, they've won global awards for innovation everywhere, but when it comes [down] to it, all they did is create a mobile, social bank fit for the Internet age. Every financial firm has to do this but, unlike mBank, most banks don't have the guts to make the change. That's the thing. Does the leader of the firm—the CEO—have the guts to commit to digital 100%? If they don't, does the firm have a future? I doubt it.

Anyone, anywhere now has the ability to sell any idea, craft or ability to anyone else, anywhere else on this planet.

SPORTS: MORE THAN JUST AN EXPENSIVE HOBBY?

Soccer teams are new toys for the Chinese super rich. Why have they become soccer fans so suddenly?

By Yaojuan

The Chinese love soccer. It's not uncommon to see a stadium full of soccer fans.

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Considering that Xu Jiayin, Wang Jianlin and Jack Ma all number among the wealthiest entrepreneurs in China and could have pretty much anything they want, just what is it about the sports industry that has grabbed their attention? Although China's sports industry is currently undergoing reform, looking at China's history and the current situation overseas, the industry poses no small risk to wealthy investors' businesses and reputation. Just look at the Glazer family, owners of Manchester United, the highest earning team in the world. Although they can be considered financial experts, their investment in the team 10 years ago has only brought them an approximately 60% return.

The money spent by these men has been considerable. First we have Xu Jiayin, who has spent an enormous amount recruiting domestic stars and foreign players and coaches to pave the way for Guangzhou Evergrande's AFC Champions League win in 2013 . Next we have Jack Ma's purchase of a 50% stake in Guangzhou Evergrande for $192 million in June of 2014. Then there's Wang Jianlin's trip overseas to acquire a 20% stake in Atletico Madrid and the huge amount invested in sports marketing leader Infront Sports & Media.

Next, we had rumors indicating that the Hangzhou Wahaha Group was looking to partner with Huawei, Alibaba and other companies to acquire Silvio Berlusconi's AC Milan, before Berlusconi has settled on Thai businessman Bee Taechaubol as a buyer.

Looking at the industry, it's clear that huge expenditures are nothing out of the ordinary, and yet China's wealthiest still remain entranced by sports.

Interception!

Although these wealthy men may appear to be laymen when it comes to sports, taking a closer look shows they may actually know what they are doing. Unlike most industries, people are the core of the sports industry, and if you want to get the right people, that takes money. When it comes to this, these men have been opening their wallets to recruit the right people without even blinking an eye. The money Guangzhou Evergrande used to ensure its path to success proves this point.

It seems that when it comes down to it, if you want to dance you'll have to be prepared to pay the band!

In 2010, the Evergrande Real Estate Group took over the Guangzhou Football Club for $16 million. Soon after, Xu Jiayin began implementing changes in a number of areas, first by hiring coaches and foreign players. Coaches, from Jose Antonio Camacho to Marcello Lippi, were some of the best in the world, while foreign players were setting new transfer records in the Chinese Super League. For instance, in 2011 the team spent $10 million in transfer fees and the promise of a $7 million annual salary to bring Dario Conca into the team.

For a player in the Super League, having Evergrande take an interest in you could change your fortunes overnight. The average annual salary for frontline players in the Super League is $240,000, whereas there are more than 10 Evergrande players who make more than $480,000 a year.

Another strategy that Xu implemented is offering high monetary rewards for matches, with rewards for a win or a tie at an away game being far higher than a home game. In 2012 alone, the total amount of rewards reached $23.7 million.

Xu Jiayin even ended up establishing a football training school, sending young players over to Europe for training. According to statistics, over these past five years Evergrande has invested no less than $480 million in football.

Although these expenditures may have seemed like the acts of a kid with a new toy, they had a huge impact on the club. Over the past several years, the Evergrande team has become increasingly more competitive, winning four league championships and the AFC Champions League in November of 2013. These wins earned the team a huge following in China. On the night of the AFC Champions match against FC Seoul, ticket sales reached $8.8 million, setting a new record for Chinese football and the AFC Champions League.

Does Xu Jiayin himself know how to play football? Not really. Although he may love the sport, he understands he is just an amateur. Although he may own the team, he doesn't enter the player's changing room nor does he decide who gets to play on the field, let alone interfere with the decisions of coaches. What he does understand, however, is human nature and how to manage and create encouragement. Commercial returns aside, as a lover of football, his investments

Unlike most industries, people are the core of the sports industry, and if you want to get the right people, that takes money.

For a player in the Super League, having Evergrande take an interest in you could change your fortunes overnight.

Alibaba bought a 50% stake of Guangzhou Evergrande soccer team.

have certainly not been a waste of money.

The huge success of the Evergrande team eventually caught the attention of Alibaba's Jack Ma. Although some might think, as a Hangzhou native, Ma may have a soft spot for the Hangzhou Greentown Football Club and its owner, real estate tycoon Song Weiping, when it comes to investments Jack Ma has always held to the idea, "If you can't be No.1, invest in No.1. If you can't do that, then cooperate with the No.1 in the field."

Jack Ma might as well be coming from another planet when it comes to understanding football. He has said that at the time Song Weiping told him, "Stay away from football. You don't understand it." Although this may seem like sound advice, Jack Ma has pointed out that he was never an expert on the Internet or computers either, and everyone knows how that turned out.

In June of 2014, Alibaba spent $192 million to purchase a 50% stake in Evergrande, changing the team's full name to Guangzhou Evergrande Taobao.

What's interesting is that although these entrepreneurs are involved in an industry not their own, this hasn't prevented them from enjoying taking swipes at each other.

Not long after Alibaba's acquisition, Wang Jianlin's Dalian Wanda Group announced that it would be acquiring a 20% stake in Spanish club Atletico Madrid for $50.85 million (the group ended up spending $56.27 million). While making this purchase, Wang Jianlin didn't forget to take a shot at Evergrande by pointing out that Jack Ma had spent the amount of money the entire Atletico team was worth to purchase only half of a domestic team. Xu Jiayin was of course not very happy when he heard this comment and followed with a barb of his own, "It would be meaningless for us to go to Europe or some other country to buy a top class team. What we want to do is make our [China's] teams become the best in the world."

Of course both sides have their own reasons for staying at home or going abroad. For Wanda, the purchase of Atletico goes beyond a love for football. Wanda has been looking to expand in Europe, for instance purchasing the Edificio España in 2014. Investing in one of the local football teams was most likely a quick way to create an emotional bond with locals and help maintain good community relations.

Also, in recent years, the cultural and sports industry has been one of Wanda's important development directions.

On Feb. 10 of this year, the Wanda Group announced that it had led three well-known organizations and Infront management in successfully purchasing Switzerland-based Infront Sports and Media for approximately $1.2 billion, with Wanda holding a 68.2% controlling stake.

This billion-dollar purchase set a new record for wealthy Chinese entrepreneurs getting involved in the sports industry. And quite a purchase it was: Infront is the second largest sports marketing company in the world, and one of the world's largest companies for sports services and related broadcasting. Covering 25 different sports, the company broadcasts more than 10 events every day. Its greatest value, however, probably lies with the marketing rights for the 2018 and 2022 World Cup matches.

While yachts and private planes and

On the night of the AFC Champions match against FC Seoul, ticket sales reached $8.8 million, setting a new record for Chinese football.

other luxury items many not be that popular after President Xi Jinping's anti-corruption movement, the wealthy's investment in football and sports has earned them overwhelmingly positive feedback from the public. In the end, these men's efforts in this industry have many in China feeling that the once impossible dream of winning the World Cup is one step closer than before.

A Hope for China

Xu Jiayin, Wang Jianlin and Jack Ma are all in the running to becoming the wealthiest person in China. The success they have achieved in their lives is a testament to their forward vision and ambition. If these three take an interest in something, there must be something about it that is worth their attention. So just why have they been willing to spend billions in in this area? Perhaps it has to do with predictions that the Chinese sports industry is about to undergo explosive growth.

Over the past 15 to 20 years, the global sports market has seen continued strong growth. In China, besides continued investment, government policy has also been helping this industry grow in the country. On Dec. 19, 2014, the central government released "Several Opinions of the State Council of the People's Republic of China on Accelerating the Development of the Sports Industry and Promoting Sports Consumption" in which it called the sports industry an important part of continued economic growth for the country and stated that its goal was to see the industry grow into an $800 billion industry by 2025. Even President Xi Jingping has high hopes for Chinese football. He once publicly stated he had three wishes, that "China would qualify for a World Cup, host a World Cup and win a World Cup." These same hopes are most likely the greatest wishes for most football fans in China.

Currently, the sports industry only accounts for 0.6% of China's GNP, whereas in Western developed countries this number is more than 3%. As Zhang Yidong, head strategic analyst for Industrial Securities, sees things, the current state of the sports industry is similar to that of the broadcasting industry in 2010. Over the short-term, policy and sports events will act as a catalyst, while over the long-term there is plenty of room for development. This "newness" is one of the main reasons he recommends the industry.

Looking at the general public, when GDP per capita in China passes the $6,000 mark, people's interest in sporting events is expected to explode. At the same time, the younger generation will have a more rational understanding when it comes to balancing work and life, and as more and more people begin to brag about the latest marathon they ran, running, tennis, badminton and cycling will become an everyday part of white-collar workers' daily lives.

Investors are already itching in their seats, just waiting to get in. Since the beginning of this year, a number of enterprises in traditional sectors have begun setting up sports investment funds or making moves into the industry. On Jan. 19, Guirenniao (603555:Shanghai) announced that it was cooperating with hupu.com to establish a $320 million sports industry fund that would focus on sports operations, training, media and other related sectors; China United Travel has announced that it will be registering $800,000 in capital to establish a subsidiary sports company; Toread Outdoor Products has announced that its subsidiary company in Tianjin would be working with an asset management company in Jiangxi to establish a sports investment fund worth $48 million.

This increase in industry capital has also spread into second-tier markets. In China's A-share market, sports industry funds like Guorenniao, club concept stocks of football clubs like Jiangsu Guoxin-Sainty and Beijing Guoan, sponsors like Ledman Optoelectronic and sports broadcast companies like Guangzhou Guangdong Daily Media have all seen increases in their stock prices since last year.

The rapid development of the industry is also expected to promote the growth of related indexes. On Feb. 9 of this year, the China Securities Index Company announced the establishment of its Chinese Securities Sports Industry Index, which will include more than 50 companies in sectors such as sports services, sports product manufacturing and sales, sports media, sports medicine and other related services.

Money or Fame?

It's worth being aware that the sports industry does have unique conditions that set it apart from other industries. This means that while success can come in the form of monetary reimbursement or fame, it is difficult to have both. A number of big names have tried and failed to successfully make their way into the industry.

"The football waters are too murky. I couldn't make it across…," famed comedian Zhao Benshan remarked about his experiences in the industry. In 2005, He took over as chairman of the Liaoning Football Club. Like Xu Jiayin, he had huge plans for the team, proposing that it establish a school at

Ben Shan Film Studios, work with domestic broadcasters and buy an online video site so it could establish its own sports channel. However, in just half a year's time Zhao's hopes fell flat.

"Football is a hard dish to eat." I used to hold my comrades in football circles in high esteem, but now I can see how dark football really is. Many things end up changing after they get involved in this sector." This is how Geely Automobile's Li Shufu described his time in the industry.

One of the reasons they weren't a good fit for the sports industry was because they were not prepared for the ever increasing expenses that came along with it. Just look at the Lifan Group's Yin Mingshan. He spent nearly $9 million in 2000 to acquire the Chongqing Qianwei Huandao Football Club, which he reorganized as Chongqing Lifan. Over the past 15 years, the Lifan team has suffered from long-term financial loss. Adding to this is the fact that since the team's listing, its expenses have come directly from Yin Mingshan's own pocket. In 2014, the team spent more than $11 million to get into the Chinese Super League, and it's estimated that they'll need to spend at least $32 million to stay there. At 77 years of age this may have been too much for Yin Mingshan. At the end of 2014, the team's legal representative and shareholders underwent some big changes, changing the team's name to the Chongqing Changsheng Football Club.

As it stands now, Chinese football seems to be a game reserved for real estate companies, as only these enterprises seem to have resources to keep their hobby going. And in many ways investing in football is a good hobby, as a team's success on the field can increase an investor's reputation. However, a successful team does not always equate to a successful business venture.

The night Evergrande won the AFC Champions League, the Evergrande Group introduced its Evergrande Spring brand of bottled water, making the bottled water brand nearly famous overnight. However, this boost was short-lived and was unable to help maintain long-term sales. At the beginning of 2014 Xu Jiayin announced that the group's sales goals for Evergrande Spring were $1.6 billion the first year, $3.2 billion the second year and $4.8 billion for the third year. However, looking at Evergrande's recently released annual report, sales of Evergrande Spring for 2014 only reached $174.44 million, while reported losses reached $368 million.

On the official webpage for the Evergrande Football Club, you can see that sales of Evergrande branded sports products are less than ideal. While low-priced products like T-shirts and calendars are fairly hot, the Nike brand jerseys that cost more than $50 are being left out in the cold. Also on the site are links to the group's cooking oil and rice products, but in reality the strategy to use the team's fame to promote the group's other business sectors isn't turning out to be very effective as these non-football related products on the site are barely selling.

Wang Jianlin's Dalian Wanda Group acquired a 20% stake in Spanish club Atletico Madrid for $56.27 million.

Before Wanda bought Infront, Wang Jianlin pointed out that sports should be an industry that does business, not a cause that needs supporting; only by making money could the sports industry truly achieve scaled development.

Looking at the current money-burning state of the sports industry, it seems that the money-making phase is still a ways off. Both Wanda and Evergrande's plans for the future include setting up schools and sending young players overseas for training, investment strategies that are sure to take quite a while to pay off.

Although the wealthy can afford such expenses, if sports is to be a business and not just a hobby, then the goal is still to make money.

Currently the global sports industry is a $113 billion industry shared among four main markets: Media and broadcasting accounts for 30% of that value, sponsorship revenue, 23%; ticket revenue, 32% and commercial development,14%. However, when it comes to China, the only ones who are striking it rich are the sports clothing sellers such as Li-Ning, Anata and Toread.

For Love of Money

Even in the Europe and US sports industries where sporting events, sponsorships and derived products are mature, most wealthy people invest mainly for the love of sports as they know it's only the lucky few that end up making money.

It seems that Internet and investment moguls are especially interested in sports teams. Before his retirement after working at Microsoft for 34 years, former Microsoft CEO Steve Ballmer gave himself a little retirement present buy buying the Los Angeles Clippers for $2 billion. His reasoning? "I love basketball," he said during an interview with CBS This Morning. "There's just no sport as great as basketball. There's poetry, the speed, the decision-making. I just love it. I love it. And for me to be involved is a heck of a lot of fun."

Looking at the general public, when GDP per capita in China passes the $6,000 mark, people's interest in sporting events is expected to explode.

If you attend an NBA game you also may have a chance to see Joshua Harris, co-founder and senior managing director of Apollo Global Management, and the Blackstone Group's David Blitzer. The two once came together to acquire the Philadelphia 76ers for $287 million; Platinum Equity's Tom Gores spent $325 million to own the Detroit Pistons; Paul Allen, co-founder of Microsoft alongside Bill Gates, owns the NFL's Seattle Seahawks and the Portland Trailblazers. The love of sports isn't just limited to buying teams. Oracle's Larry Elison is an enthusiastic promoter of the America's Cup.

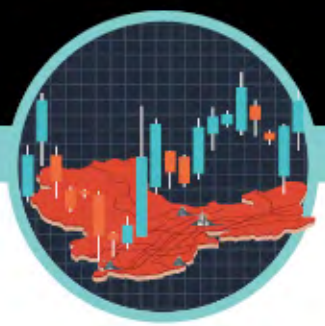
However, there are those that invest in teams to achieve other goals. After Russian oligarch Roman Abramovich took over the companies that controlled England's Chelsea Football Club in 2003, he used an enormous amount of money to quickly raise the team's performance. Although he has claimed his investment in the team was purely as a hobby, he probably cared more about mingling with the high class in English society and the political benefits. Some in the media have even said that he was using the team to launder money. Eventually other members of Russia's wealthy class followed suit. In 2007, an iron mogul acquired a partial stake in English team Arsenal, while potash king Dmitry Rybolovlev became owner of AS Monaco.

Of all these wealthy entrepreneurs to dive into the sports industry only a few have actually been able to make their teams profitable. One of the most successful examples is probably the Glazer family and Manchester United.

In 2005, with the backing of JP Morgan Chase Bank and the advisers the Rothschilds, the Glazer family managed to privatize the Manchester United in a highly leveraged deal for $1.47 billion. Holding the record for the most Premier League titles, the team's performance has turned the club into a world-class brand whose broadcast, ticket, sponsorship and derivative product revenue to continually climb over the years. However, despite this, due to the huge amount of interest on the acquisition loans and the high salaries of players, it took the Glazers five to six years before the team could begin turning a profit.

In order to bring in needed funds, Manchester United did all it could to commercialize operations, leading to it becoming the world's highest earning football club. It also went a long way toward controlling expenditures, lowering labor costs to 50% of all expenditures. In August of 2012, the Glazer family listed 10% of the club on the New York stock exchange (MANU.NYSE). Based on the stock's recent price of $17.67 (June 19, 2015), the total market value of Manchester United should be Is more than $2.6 billion, with the Glazers 90% share being worth more than $2.3 billion, roughly a 60% increase on their investment of10 years ago. Putting the love fans have for this world renowned team aside for a moment and looking at it from a business perspective; does this really qualify as a successful business deal?

LeTV'S JIA YUETING: THE SPIRIT OF A DISRUPTOR



The company makes not only TVs, but also provides video online contents and is looking to connect them all with its own smartphone. Is this grand plan achievable?

By Guyang

SYNDICATION / XIN CAI FU

After an eventful autumn, Jia Yueting, founder and chairman of LeTV, has begun leading his company to challenge not only Apple but also China's five major mobile Internet giants: Tencent, Alibaba, Baidu, Lei Jun's Xiaomi and Zhou Hongyi's Qihoo. However, although LeTV has been able to use the vast online services packed in its"Super" TVs to upset the TV manufacturing sector, when it comes to the mobile phone and automobile industries, it remains to be seen just how effective this strategy will be, especially considering Jia's Yueting recent call-to-arms for an "open system." As time marches on, it will be worth paying close attention to how Jia Yueting's LeTV empire fares as it continues pouring more resources and time into its battle for the mobile Internet.

On April 13, one day before the launch event for LeTV's "Superphones," Jia Yueting threw down the gauntlet by posting an open letter to Apple titled "Open system in the new age for connectivity" online. In the letter, while he recognized how Apple redefined the mobile phone industry with its App-based smartphone strategy, he challenged this very same "closed system" by saying it has held back innovation. Jia Yueting specifically pointed out how Apple has restricted the use of third-party Apps that block spam calls and e-mails—a type of App that is very popular in China—thereby negatively impacting customer experience. The letter went on to discuss how an "open system," and by extension LeTV, was the future of an era in which constant connectivity is fast becoming the norm.

According to LeTV, the company is going to establish a complete mobile Internet ecosystem, with its eUI operating system used on all its devices such as TVs, smartphones and cars. This ecosystem—based on the interaction of and connectivity among multiple devices—will be completely open to App makers and content providers.

There are quite a few unknowns when it comes to whether or not this strategy will succeed. If this ecosystem does manage to mature, then LeTV may very well be able to upset the current order of the mobile Internet in China to become a true powerhouse, and Jia Yueting may find his current net worth of $2.3 billion and 90th place on New Fortune's list of the top 500 wealthiest people in China rising to an all new level.

LETV'S BUSINESS SECTORS AND MAJOR COMPETITORS

	Structure	Major Competitors
Content	LeVision Pictures, DongyangHuaer Entertainment Media, LeTV Sports	Enlight Media, Huayi Bros, Beijing Galloping Horse Media
Platforms	Letv.com, eUI	YoukuTudou, Tencent, iQiyi
Terminals	LeTV Superphones	Xiaomi, OnePlus, Nubia, Huawei
	LeTV Super TVs	Xiaomi, Skyworth, Konka, Sony, Sharp
	LeTV Electric Cars	Alibaba, Tencent+Harmony+Foxconn

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Raising the Banner of Innovation

In his open letter, Jia Yueting described LeTV as possessing "the spirit of a disruptor." From a certain standpoint, "disruptor" is probably a fairly accurate description of the company. If the company's experiences in the TV manufacturing sector are any indication, its favorite weapon seems to be offering products packed with tons of features at low prices.

In May of 2013, after disrupting the set-top box sector by bundling a free smart TV box with the purchase of a year's subscription, LeTV went on to rock the TV manufacturing industry with its 60-inch X60 and 40-inch S40 "Super" TVs. LeTV's pride and joy, the X60, was not only considered a great combination of software and hardware from Sharp, Qualcomm, Foxconn and LeTV, it was priced at around $1,119, about half the price similar smart TVs sold for at the time.

It's clear this high price-performance ratio strategy had the desired effect. LeTV sold 1.5 million of its smart TVs in 2014. During a time when most color TV brands in China were showing different levels of sales decline, LeTV smart TVs bucked the trend by showing continuous growth. By October of that year, sales of LeTV smart TVs accounted for 7.73% of all sales, while the company's market share had quadrupled. It was also faring well in the Hong Kong market. When the company's TVs went on sale in the city on Oct. 9, 2014, it sold 1,000 X50Air TVs in just 9 minutes and 38 seconds.

Sticking to a single large screen is a recipe for disaster in the age of the mobile Internet as the future belongs to companies that can connect multiple screens in one ecosystem. Considering that mobile phones are one of the most commonly used mobile terminals in the world, it is only natural that LeTV would want to make a move into this market.

During LeTV's mobile phone launch event, Jia Yueting once again demonstrated his "disruptive" nature by stating that the hardware in LeTV's Superphone 1, 1 Pro and Max could take on any of the top manufacturers' best smartphones in a one-on-one fight.

Looking at price, the Superphone 1 sells for around $239 and the 1 Pro for $399. Looking at hardware, it's easy to see that the phones fit right in with the company's high price-performance ratio strategy. As for the company's flagship phone, the Superphone Max, LeTV released the phone's list of materials stating that it

would set a price after a round of crowd-sourced suggestions from users. Another of the company's secret weapons was that for a year subscription to LeTV's full-screen video Member Services, LeTV would take $48 off the price of the phone. In theory, so long as a customer subscribed to LeTV's services for long enough, they could walk home with a free Max phone. Looking at the way LeTV has handled its pricing, its message to consumers was clear: LeTV had no intention of trying to make money off of hardware.

High Cost of Success

Jia Yueting's understanding of "Internet thinking" is one of LeTV's chief sources of confidence in the TV and smartphone sectors. However, in the end, this type of thinking costs money. No matter if it's the company's TVs or its smartphones, its high price-performance ratio strategy means that it has had to take a hit on each piece of hardware sold in order to expand its user base. This of course means that funding is in high demand for the company.

For the time being at least, it seems that capital isn't a major problem for Jia Yueting. This is mainly the result of his depth of knowledge when it comes to the inner workings of the investment market and his ability to know the right time to make a friendly gesture toward stockholders.

Since LeTV.com's IPO, the company has issued high dividends every year. Prior to implementing its plans to carry out acquisitions through share issues and its share acquisition and fund-raising in October of 2013, LeTV managed to boost its stock prices by making six strategic moves (see Figure 1), resulting in a more than triple increase in stock prices in less than a year.

The lengths LeTV went to protect its share prices naturally came about because it needed investment. When LeTV announced its plans to carry out private issuance of shares to raise the $208 million needed to acquire a 100% stake in Dongyang Huaer Entertainment Media Co. Ltd and a 99.5% stake in LeTV New Media Culture, its share price had already experienced a notable increase, which allowed the company to raise the fund—more than the $116.8 million the company raised for its IPO—while only diluting its equity a relatively small amount.

This increase in share prices, not only helped LeTV with needed investment, but also helped Jia Yueting when it came to mobilizing funds to invest in subsidiaries in other industries.

According to public data, Jia Yueting put his own shares in the company up as collateral; at its peak this accounted for 77% of his shares in LeTV. In other words, if LeTV's share prices were to fall, Jia possibly would have to hand over his collateral or pay back the loan. Of course a situation like this posed a danger for investment into LeTV's subsidiaries. This in turn led the company to

> ***Its favorite weapon seems to be offering products packed with tons of features at low prices.***

becoming extremely sensitive to anything that could influence the company's stock prices. The year 2014 was a tough year for the company as it faced many challenges when it came to keeping the company's share prices steady (see Chart 1).

The first major hit came in July of 2014, when the State Administration of Press, Publication, Radio, Film and Television (SAPPRFT) tightened regulations on

FIGURE 1

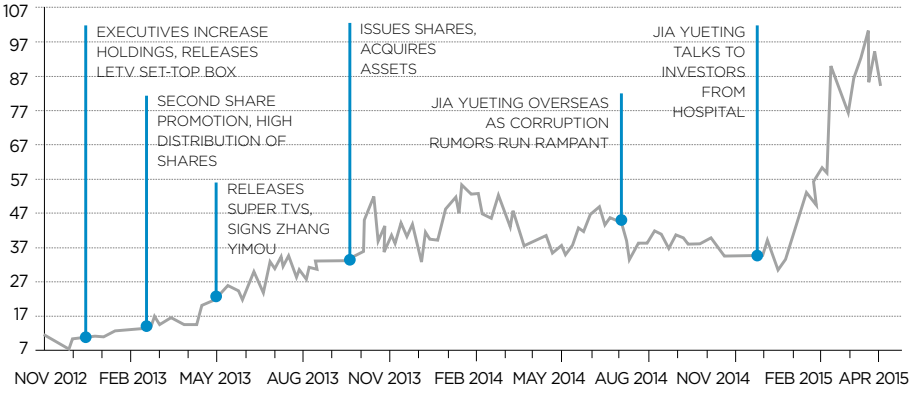
2012-2013 LETV'S MAJOR MOVES

December 2012	LeTV announces executives would raise funds over the following six months to increase share holdings
December 2012	LeTV releases C1 set-top box for 490 yuan; purchase includes 12 month free subscription worth 490 yuan (1yuan=$0.16)
February 2013	LeTV announces second plan to promote share prices, performance benchmark increases by 40% for the first time
March 2013	Announces plans for dividends of 0.5 yuan (including tax) for every 10 shares held and to distribute 9 shares to every 10
May 2013	Releases LeTV Super TVs
May 2013	LeVision Pictures signs director Zhang Yimou

Source LeTV

CHART 1

LETV'S SHARE PRICE AND MAJOR EVENTS



Source: New Fortune

Internet-connected TVs, smart TV boxes and related content. These regulations had a huge impact on LeTV's smart TV box business, and soon after headlines such as "LeTV's UI against regulations, partially shut down" and "LeTV ceases sales of smart TV boxes" could be seen everywhere in the media. This in turn hit the company's stocks hard, and its share prices fell for two straight trading days. To save the situation, LeTV applied for a temporary suspension of trading. In an advertisement that soon followed, the company did what it could to clear up rumors, while admitting that during cooperation with third-parties its smart TV boxes had violated regulations, but that the company had already taken steps to correct the situation and was preparing a report for investors that would outline the impact on its business. As a result, when trading on the company's stocks resumed, prices rebounded by 7.8%.

A few months later, media reported that Wang Cheng, the owner of one of LeTV's early major investors Huijin Lifang Capital, had familial ties to a former key lieutenant of former president Hu Jintao and was under investigation. This caused rumors that LeTV was involved in a political scandal to circulate throughout the industry. It wasn't until Jia Yueting, who had been overseas for five months, returned to China in November of 2014 and opened the company's books to investor investigation that the matter was finally put to rest.

Finally clear of the stormy weather that plagued the company that year, LeTV's share prices seemed more stable than ever. Even when the company made the huge announcement last December that it had ceased plans to acquire new assets to continue its expansion, its stock prices not only didn't fall but actually went up. This continued over the next quarter or so until the company's stocks had increased 170%.

In six years, revenue LeTV earned from redistribution of broadcast rights went from $8,000 to nearly $90 million a year.

Pieces on the Board

Internet thinking and funding are important if a company wants to become a major player in the Internet age, but even these are useless without the proper preparation beforehand. It's worth taking a moment out here to examine how Jia Yueting set up his chess board when he first began.

Although LeTV got an early start as a video site, it was never quite as well-known as its contemporaries such as Youku, Tudou, (now Youku Tudou), Ku6.com and iQiyi. If it weren't for the incredibly popular drama The Legend of Zhen Huan, the average consumer probably wouldn't have even

heard of LeTV. Incredibly enough, LeTV wasn't only able to turn a profit in this money-burning online streaming industry, but was also able to raise its profits to the level of a company listed on China's A-share market. This success has much to do with the long-term vision of Jia Yueting and his generational compatriot Liu Hong, the current vice-chairman of LeTV.

When LeTV was first growing, piracy was the norm in China as there existed little protection for intellectual property (IP) and there were few in the streaming industry willing to spend the money to establish proper protection mechanisms. However, LeTV insisted on buying the broadcast rights for the shows on its platform. Although some laughed at the company for its decision at the time , looking at things now, this move enabled LeTV to acquire quite a few IPs while prices for broadcast rights were still relatively low.

As China increased its protection of IP rights and entered into anti-piracy alliances, this created an incredible opportunity for LeTV. Needing to hold on to consumers as pirated content was being forced off streaming sites, these sites had no choice but to buy the broadcast rights to popular TV shows. This led to prices skyrocketing practically overnight. However, for LeTV and its vast IP resources this not only posed no problem; it was able to reap the benefits of its earlier purchases. In six years, revenue LeTV earned from redistribution of broadcast rights went from $8,000 to nearly $90 million a year . With this nearly geometric growth LeTV was soon able to become one of the biggest copyright distributors in China.

With Internet giants like Tencent and Xunlei counted among its top five clients, it's easy to see the huge advantages LeTV's early decision to grab broadcast rights brought about. One of the reasons why Chinese Internet companies such as Youku and Tudou went overseas to the US for their IPOs had a lot to do with domestic stock market requirements when it came to earning continuous profits. However, the move away from piracy in China allowed LeTV to get ahead when it came to turning a profit in the streaming industry and allowed it to become the only domestic streaming site to list on China's A-share market.

We've seen how LeTV's strategies in the streaming and TV manufacturing industry gave it a leg up on the competition. Looking at LeTV's current strategy, it certainly seems possible that it will once again win the initiative on the Internet battlefield. Currently LeTV has involved itself in the Internet, streaming, sports, TV and smartphone industries and is looking at the automotive industry. According to Jia Yueting's plans, each of these separate business sectors will be tied through the Internet using its eUI to create LeTV's own ecosystem.

It's worth noting that LeTV has spared no effort in each of these areas. LeVision Pictures CEO Zhang Zhao has quite a reputation as he was the former head of Enlight

LeVision Pictures CEO Zhang Zhao (left) has worked with the famous movie director Zhang Yimou (right).

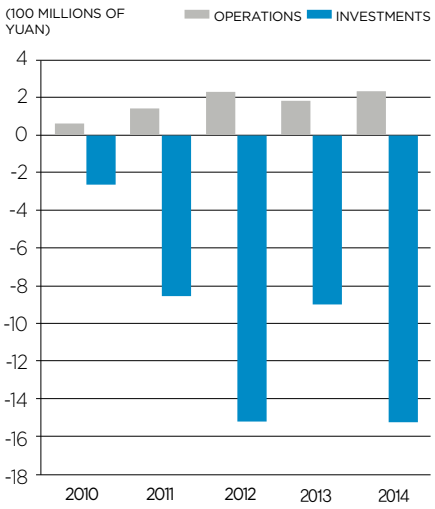
Pictures, the studio that distributed *Lost in Thailand* and *So Young*. After Zhang Zhao took the reins of LeVision Pictures, he demonstrated the studio's operating capabilities by distributing the *Expendables* franchise and Zhang Yimou's *Coming Home*, *Tiny Times 3* and other big films. In 2014 LeVision Pictures earned more than $480 million in box office revenue. During the third quarter of 2014, the company jumped to first place among China's five biggest private film companies.

As for the sports industry, LeTV Sports has already had a huge impact as an online sports platform, capturing the imaginations of investors. The company raised $50 million during its A-round of financing and currently has an estimated value of $270 million to $330 million. It has already made arrangements for its B-round of financing.

In March of 2015, LeTV Holdings and the Beijing Automotive Group signed a strategic cooperative agreement in Hong Kong to develop a connected smart car ecosystem. Once LeTV's automotive company establishes itself, LeTV's overall ecosystem will be close to completion. LeVision Pictures will produce content, letv.com will broadcast said content, while LeTV's TVs, smartphones and electric cars will use the eUI system to be connected to each other and allow consumers to access LeTV services no matter if they are at home, out and about, or going for a drive.

CHART 2

LETV OPERATIONS AND INVESTMENT CAPITAL



Source Wind

Bumpy Road Ahead

LeTV has made thorough preparations throughout its Internet industrial chain, but its methods at trying to revolutionize the current industry have been comparatively crude. Although using high-tech features to attract consumers and low-prices to put pressure on the competition worked in the TV manufacturing industry, it still remains to be seen whether the same strategy will pay off in the end when it comes to smartphones. The TV manufacturing industry still uses the same traditional manufacturing and sales model, but when it comes to the smartphone industry there are already a large amount of competitive domestic mobile phone companies like Xiaomi and Huawei fighting for their very lives when it comes to hardware and pricing. Add to this the signs that the smartphone industry is reaching saturation, and it looks like there might not be much room left for LeTV.

LeTV has involved itself in the Internet, streaming, sports, TV and smartphone industries and is looking at the automotive industry.

As for the electric car sector LeTV is looking to get into, not only has Tesla and its attention to detail and fair pricing entered the Chinese market, Foxconn, Tencent and the Changge Feng-controlled China Harmony Auto are preparing to ally together and enter the smart electric car sector at a level "on par with Tesla."

Alibaba is also looking to make a splash in this arena. Currently it has announced that it was integrating its automotive subsidiaries to establish a new Alibaba automotive division that will make use of Alibaba's big data services and automotive financing business to provide customers with a one-stop platform that can take care of all their automotive needs. Alibaba has even entered into a cooperative partnership with SAIC Motor and the duo's first model is expected to hit the market in the not-too-distant future.

Outside of the smartphone and automobile industries, it also looks like LeTV faces seemingly unbeatable foes in other areas of its Internet empire.

In addition to "external threats," LeTV also has to deal with internal issues. Since letv.com was listed on the stock market, its net profit has maintained a state of rapid growth, going from the $11.2 million earned its first year on the market to 2014's $57.6 million. Right alongside this has been the money spent on investments over the years. This amount has not decreased but has actually increased by nearly six times.

However, since outgoing investments have outpaced revenue and LeTV has not recently carried out share financing, capital has had to come by financing through debt. Since its IPO, LeTV's equity multiplier (The ratio of a company's total assets to its stockholder's equity; the higher the equity multiplier, the higher its debt ratio) has steadily risen (see Chart 2), indicating the company has continued to use debt for leverage.

From the current situation is seems only time will tell whether LeTV will be able to climb to the top of the Internet mountain. It will most definitely be worth watching to see if Jia Yueting's empire will end up being crushed under continued investment and high asset-liability ratios.

TRUCK GANG LEADER'S ENTREPRENEURIAL (AND WARRIOR) SPIRIT

Each time the Truck Gang has entered a city, it has faced a fight. It has even had to mediate with local underground forces. "You know what a VC values the most? My brute force!" said Dai Wenjian with a mysterious smile.

By Chenxi

Located in the northeastern part of Chengdu, Chuanhua Logistics Base is the biggest highway port and logistics center in the Sichuan province of southwestern China. Each day, several thousand vehicles and more than 10,000 drivers pass through here. Five showrooms are subdivided into several hundred compartment booths. Cargo owners provide their cargo information while drivers check in to find business. The surrounding area is both dirty and messy; there is a trace of an unpleasant odor floating in the air.

Dai Wenjian does not like it here; he only comes when escorting guests on a visit. Nevertheless, this obnoxious place has provided him opportunities.

Two years ago, Dai Wenjian rented an office and a small store in this area to promote his Apps: Logistics QQ and Truck Gang software which integrated cargo owners and drivers respectively. He wanted to reduce logistical costs and improve efficiency with the connection of vehicles and cargo through the Internet.

According to the "China Procurement Development Report (2014)," in 2013 the

total expenditure of China's social logistics topped $1.6 trillion, accounting for 18% of its GDP. This is more than twice that of the United States. In the age of the Internet, although there are many companies like the Truck Gang, it's far from easy to change this long-standing truck industry.

In the past when he found himself barely able to hold on, Dai Wenjian would come to the Chuanhua Base alone and sit in the densely packed parking lot, brooding all day.

In early April when this interview was held, Dai Wenjian was busy arranging Round A financing. His office, located in Chengdu's Hi-tech Industrial Development Zone, was bustling with activity. He shared that the financing was already in place and some financial auditing underway, but he was unwilling to volunteer any more details. It was rumored that the financing ran up to tens of millions of dollars.

"Do you know what a VC values most about me? My brute force." Dai Wenjian said with a mysterious smile while pointing to the Chuanhua Logistics Base. "When I first opened this store, many old men and women obstructed the gate with benches, smashed things, and blamed us for stealing their business."

This is merely a minor episode in the expansion process of the Truck Gang. According to Dai Wenjian, there are "truck scalpers" everywhere in China. They help cargo owners find vehicles and earn a certain commission. But cargo owners learned that they could find vehicles without paying any money if they posted their cargo source information on the App Logistics QQ. Cargo owners and drivers would then gradually detach themselves from their previous network. This inevitably challenged local cargo source networks. Each time the Truck Gang entered a city, it faced a fight. Smashed vehicles and disconnected Internet connections were commonplace incidents; the company even had to mediate with local underground forces.

"Right now we have already expanded through southern China and will soon enter northwest China. Many battles lie ahead." Dai Wenjian was eager to flex his muscle. Perhaps capital injection will provide him with more chips for negotiation.

"Right now we have already expanded through southern China and will soon enter northwest China. Many battles lie ahead."
—Dai Wenjian, Truck Gang

Out of the Shadows

In the logistics field, neither Dai Wenjian nor Truck Gang is very well-known. But two recent incidents have brought them into the limelight.

On Jan. 4 of this year, Premier Li Keqiang witnessed the first time that WeBank in Qianhai, Shenzhen issued a loan. Xu Jun, a driver using the Truck Gang platform, received a $5,600 loan. This loan business was introduced to drivers by the Truck Gang in cooperation with a third party. Dai Wenjian later told China Entrepreneur magazine that Tencen t played a significant role in this cooperation. It was reported that investment holding company Tencent is also one of the investors in Truck Gang's Round A financing.

Another incident occurred on March 16 when Jack Ma, founder of Alibaba, showed a Truck Gang App to German Chancellor Angela Merkel at the CeBIT (the annual exhibition and conference for IT and digital business in Hanover, Germany). This App was an entrepreneurial project based on the Ali cloud computing platform.

In the aftermath of these incidents, more people began to notice this previously little known company. In fact, "outsider" Dai Wenjian stumbled into the logistics industry totally unprepared.

Before founding the Truck Gang, he was one of the seven partners of NVC Lighting. In 1997 he was responsible for the design and marketing of NVC. During his time at there, he noticed the high cost of logistics. He realized it was due to repeated transit times, disorganized loading/unloading, and a high damage rate of light fixtures. Sometimes logistics expenses accounted for more than 30% of the total cost.

In March 2005, Dai Wenjian left NVC Lighting, wanting to enter the logistics field. Coincidentally, a former university classmate of his was chief of a highway project from Funing to Yanshan in Yunnan. Dai Wenjian undertook the transportation of steel products and cement for the project, which continued until February 2008.

Almost all of Dai Wenjian's friends looked down on his endeavor. One person told him that this section of the road was in a remote area between two provinces. It was far away from the supply site, and any vehicle could only return empty-handed after delivering the materials.

Perhaps it's because one is more unrestrained when changing fields, but Dai Wenjian led his team to tour the area and explore the landscape. They looked thoroughly for local products and mineral deposits. He found every possible kind of cargo along the route to the supply site. As it turned out, the project brought him very high profits. According to his description, the net profit back then ran around $11 million to $13 million, instead of the previously estimated $800,000.

Nevertheless, problems arose one after another. According to Dai Wenjian's concept, transportation could be outsourced to social transportation (using social media to conduct business) capacity. He only needed to provide payment in advance and guaran-

tee supply; in this way, within a matter of two years he could finish the project easily. In fact, the majority of social transportation capacity in China was scattered in the hands of private firms. He discovered that during off seasons, drivers were very willing to pick up delivery jobs. But when the peak season came, even if he gave them extra pay, many vehicle owners would leave him. He was deeply disappointed by the weakness of contracts within this segment.

"When a highway is under construction, one night it may need several thousand tons of cement. The supply cannot be delayed, otherwise it will affect the project schedule. Where can I find the money to make up for this kind of loss? But I needed to pay a higher cost if I wanted to regularly use social transportation capacity here. This would lead to a very low profit and could even incur loss. I had to buy my own vehicles if I wanted to solve the balance of transportation capacity." As far as Dai Wenjian was concerned, self-owned vehicles were in fact a trump card in his hands. When there was not enough transportation capacity, he would mobilize his own resources.

For over two years Dai Wenjian intermittently purchased over 60 vehicles. Nevertheless, he soon made a discovery: Without vehicles he could go nowhere, but with them also came many difficult experiences.

"When the phone rang at 11 o'clock at night, my back would be soaked with perspiration. Just imagine how big an accident would be if with an operation team of several hundred people the call had reached me," Dai Wenjian said. He recalled when a vehicle would slide into a mountain ditch, producing a disaster site several hundred feet long. He would agonize over such tragic scenes. For a certain period of time back then, he felt he himself was too frail to bear the stress.

Once, because the highway construction project was suspended for three months, several dozen vehicles were idle. They were forced to temporarily ship various social materials. However, once the vehicles were dispatched, they raced away like a flock of uncontrolled sheep. In the past it was easy to manage trips from point A to point B. Now the freight would come by chance and irregularly. Some drivers failed to return for half a month; some said the vehicle broke down, and others did some private jobs.

Dai Wenjian soon ordered GPS systems from Shenzhen and installed them in the trucks; this way he at least knew the whereabouts of his vehicles. GPS offered many advantages, but the ceiling was still easy to hit. He found it inconceivable to imagine having 100 or 200 vehicles.

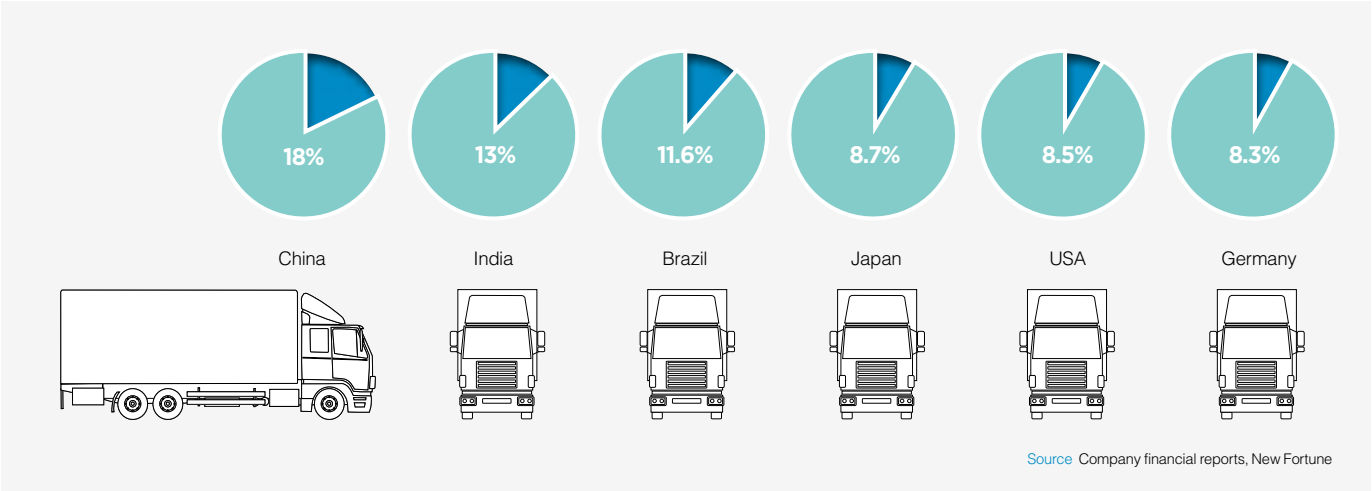
"I had to buy my own vehicles if I wanted to solve the balance of transportation capacity."
—Dai Wenjian

Painful Lessons

An unexpected experience jolted Dai, giving him a rude awakening. One truck was shipping cargo from Nanning, Guangxi to Leshan, Sichuan. It stayed in Leshan for two days without being able to find any cargo and in the end was driven empty 124 miles to Chengdu. After two days of looking everywhere, the driver found a delivery. However, it required him to first drive 106 miles with an empty truck to Jiajiang County, Leshan City in order to load the cargo. He calculated the costs. With fuel consumption, road and bridge tolls, insurance fees, parking fees, and driver's living expenses, the loss totaled over $400. This order ironically only brought a profit of $1,120.

This experience made Dai Wenjian realize a big problem within logistics. In April 2007 after returning from a survey tour to Europe, he became convinced that the

THE RATIO OF LOGISTICS COST TO GDP IN 2013



future of logistics would begin with the integration of transportation capacity. He discovered that the lack of a public transportation pool resulted in very high transportation costs in China. He wanted to become an integrator.

When GPS was installed in the vehicles, it could support the fleet's internal management. Meanwhile, it occurred to Dai Wenjian that if all social vehicles were installed with GPS, wouldn't he be able to obtain more transportation capacity resources?

In June 2008, Truck Gang spent $3.2 million and dispersed 20,000 GPS devices, trying to effectively integrate the already widely scattered transportation capacity. It did this by using GPS monitoring, developing a transportation capacity sharing platform, and then connecting with cargo owners.

However, Dai Wenjian didn't realize that GPS technology is one-directional. As a business manager, he could strictly track and control self-owned vehicles. But it was only after the 20,000 GPS devices were dispersed that he discovered he was basically unable to dispatch those 20,000 vehicles. Drivers were also unwilling to share their transport capacity.

In 2009, Dai Wenjian was unable to hold on. In order to minimize the loss, he transferred hardware and software technologies and disbanded the team, keeping only a few core members.

Originally he planned to give up completely, but at the end of that year China Unicom introduced 3G, which enabled him to see a glimmer of hope at the end of the tunnel. He decided to try once more. In 2010 he relocated his headquarters from Guangxi to Chengdu, and placed his operations center in Beijing, his call center in Guizhou, and his hardware team in Shenzhen.

Looking back at his first failure, Dai Wenjian used a philosophical expression to describe it: negative affirmation. It's wrong to use GPS in grassroots technology integration. This is due to high costs and poor interaction. However, the Internet is the right direction. More importantly, he became aware of a blind spot in the setup of his previous business model. He had overlooked cargo source, the drivers' most important demand.

"Our business is like a tree: Cargo owners constitute the roots and vehicle owners are the trunk. Only when the roots are deep can we have prosperous branches and leaves. Many people know Truck Gang, but they know nothing about Logistics QQ. In fact, without Logistics QQ to supply nutrients and water underneath, there is no way for this trunk to grow," Dai Wenjian said.

Through observation of the macro environment in the domestic logistics industry, Dai Wenjian discovered there was a wide difference between southern and northern China in terms of information integration. In northern China there were many regional cargo source integration platforms, but in southern China there was still a void. He decided to cultivate the market in southern China first.

Back then, few logistics workers in southern China owned computers. Software developed in northern China could not be installed on their computers. Truck Gang built 13 super QQ groups along 13 provinces south of the Yangtze River and attracted more cargo owners to be users through local promotion. Cargo owners posted information sources in the groups. They could recommend vehicles to one another and fulfill real-time interaction through mobile phone QQ.

The Big Switch

After cultivation for a year, Dai Wenjian accumulated over 6,000 cargo owners. But in September 2011, he made a tough decision: He disbanded Guangxi QQ group and

forced cargo owners to use Logistics QQ software, which caused a widespread negative reaction.

This risky action also reflected Dai's Wenjian's acumen as a businessman. He felt that dependence on other platforms was like building a house on the beach: Only by importing resources to his own platform could he bring about true connections. As it turned out, one week after Guangxi QQ group was disbanded, half of the people using it transferred to Logistics QQ.

After this, Dai Wenjian's team adopted more a conservative transferring method: It "kicked" people out region by region. Taking Hunan as an example, it kicked out cargo owners from Changsha, Yueyang, and Hengyang in batches. It took the team more than half a year to transfer all 13 QQ groups. Then, it began to integrate the drivers' end. In 2013 it introduced "Truck Gang," which was linked to Logistics QQ. In this way Dai Wenjian successfully matched vehicles with cargo information.

Dai Wenjian is against the order-grabbing model advocated by xiaojukeji.com transportation service. In his view, all processes on xiaojukeji.com are standardized. In contrast, his platform's vehicles, cargo, and even times are not standardized. Order transaction amounts can easily add up to $1,600, requiring negotiation on both sides.

From the platform supplier side, he lets both sides interact with each other. But the biggest obstacle was credibility.

One day, a driver saw that there was a cargo source in Zigong. He was eager to accept the order but was afraid the information would turn out to be false. Dai Wenjian guaranteed he would offer compensation if drivers ran into problems. "You must take care of his anxiety, otherwise he would not dare to go. How can the platform advance like this?" Last year he paid drivers $229,000 in compensation. Later he claimed $218,000 back from cargo owners who failed to keep promises. In order to remove cargo owners' misgivings, all drivers with Truck Gang have passed real name certification, and everyone pays a $19 certification fee each year.

According to data from Truck Gang, by the end of September 2014, Logistics QQ had assembled 167,000 cargo owners distributing in 13 provinces south of the Yangtze River and in seven provinces in northwest China. Certified driver users of Truck Gang reached 650,000; each day it released over 400,000 pieces of mid- to long-distance cargo source information.

The growth of drivers is clearly faster than that of cargo owners. Shaanxi truck driver Liu Chengping joined the Truck Gang earlier this year, saving him a lot of time and cost in hunting cargo. "Each evening after unloading the cargo at 8 or 9 o'clock, I can begin to load tomorrow's cargo. In the past it was different, I would stay overnight in a hotel at the logistics park and go there again the next day to find cargo."

"Our business is like a tree: Cargo owners constitute the roots and vehicle owners are the trunk."
—Dai Wenjian

Compared with drivers, cargo owners have more worries. Xu Kaiping, the chief of Huihai Logistics from Dongguan, Guangdong, has used Logistics QQ for two years. He said frankly that even though Logistics QQ has brought many conveniences when searching for vehicles, he still only found vehicles for about 30% of his cargo using this software. The remaining 70% of cargo is dispersed through large logistics parks in Guangdong.

"It is still a problem of trust. All drivers on the Truck Gang are certified, but they mostly have online certification. A vehicle owner's certificate may not be totally authentic. In fact, many vehicles driving on highways have a fake license. Some fellow colleagues discovered this situation when dispatching vehicles online.

Total dependence on this logistics network is not realistic. For instance, if I am in Dongguan and a batch of cargo needs to be delivered from Shanghai to Beijing, I will not be able to see the driver. In this case I will definitely entrust someone familiar to finish the job," Xu Kaiping told China Entrepreneur. They will have fixed companies to connect corresponding vehicles. Even if the expenses are constant and abundant, like wool coming from a sheep's back, the key thing here is security.

One logistics expert who wished to remain anonymous said that such a model to link vehicles with cargo is still in an observation period. Its success depends on the founder's genes and an understanding of logistics and its structure. In the end it requires the user to develop a close relationship with the platform. It is mainly concerned with four aspects: user numbers, activity degree, daily transaction volume, and transaction frequency.

Right now, Dai Wenjian is preparing to focus his energy on the cargo source side—only with sufficient cargo sources can he attract more drivers.

In the Trenches

Truck Gang has decided to march northward with an offer of complimentary incentives, slowly whittling away the regional cargo source network. By integrating resources on the Logistics QQ platform, it will inevitably touch other's territory of the regional cargo source network. In this rampantly growing field, disputes are unavoidable.

On the day of this interview, the Truck Gang team was "fighting" with a local network in Fuyang, Anhui. That local network platform included more than 1,000 cargo owners. Each cargo owner had been paying a $160-$320 yearly service fee. This model had continued for more than a decade, and

High transportation cost means a perfect opportunity for some startups.

the Truck Gang destroyed its business after its entry.

"Last year we had a dispute in the northwest. Our 300-person team connected the local network in seven provinces in northwest China in just one month. Several of our vehicles were smashed. I sat in the front seat of a Hummer and personally issued orders. This job cannot be done without brute force," Dai Wenjian said.

The expansion of Truck Gang smacked of military overtones. Each day his team would ask him: where will the next battle be? Sometimes he enjoyed the feeling that comes when conquering with overwhelming strength. Now, Truck Gang is making adequate preparations for expansion. It will also file reports in advance at the local police stations. Such aggressive methods will probably change after receiving capital. Dai Wenjian will also consider adopting an M&A method to finish integration.

One day after looking at the Truck Gang's model, an investor told Dai Wenjian, "Your business is not sexy." He then became obsessed with this idea of how to make it sexy. He later held an internal meeting on this subject. The result of the discussion was to "continue being unsexy." In his view, the industrial Internet ultimately must return to the real nature of the industry.

Maintaining a platform costs a lot of money. Over the past several years, Dai Wenjian's solution was to make money while developing the business. Wool comes from the back of sheep, but the bull pays the bill. He introduced different products at different times to create revenue. In one instance, he sold an electronic navigator exclusively for drivers. In 2012 its sales reached $11.2 million to $12.8 million.

Truck Gang also opened large restaurants in some logistics parks. These restaurants targeted cargo owners and drivers with the hopes of also promoting the Apps and building network. But it was later "asked" to leave by the logistics parks.

Presently, the driver certification fee has become an important source of Truck Gang's revenue. With 650,000 drivers each paying $19 each year, the annual revenue from this can reach over $12 million.

According to Dai Wenjian's plan, when the amount of the two base elements of cargo owners and vehicle owners is large enough, the business will generate many value-added services like finance, insurance, second-hand vehicle trading, etc. In fact, Truck Gang is making preparations for insurance. It has contacted Anbang Insurance. The premiums for nearly one million drivers may amount to billions of dollars.

In its next step, Truck Gang is cooperating with Ali Cloud on the technological side to create a system. Last year in the "Northwest battle," an opponent attacked its server, and Truck Gang narrowly escaped a system collapse. Fortunately Ali Cloud offered support and the attack was evaded. Truck Gang also works with Cainiao Logistics. Cooperation with Tencent is also under way.

Dai Wenjian does not like taking sides, nor is he willing to adopt exclusive cooperation. This proud young man aspires to building a shared platform with public transportation capacity. He wants to become the leader of the logistics industry. "[U]p until now there has not been a giant company. We are running directly to the throne."

HAS HE KEPT HIS WORD?

India
I

The Indian government led by Prime Minister Narendra Modi has completed its first year in office. We offer the views of some noted Indian commentators on what he has accomplished.

OPTIMISM IS HERE TO STAY

Despite some bumps, India is on the right track.

By Nirmani Jain Photo by Umesh Goswami

We are in a bull market; on that everybody would agree. The broader markets turned bullish when Narendra Modi took charge as the Prime Minister a year ago. Since then, there have been many hits and misses, but the undertone for medium to long term remains bullish. One of the most significant votes of confidence—not based on sentiment or liquidity—came from Moody's, which upgraded India's rating outlook. Remember, earlier there were threats of a downgrade. At the same time, one cannot ignore that corporate earnings and the Index of Industrial Production (IIP) still paint a dismal picture. Major policy reforms such as the land acquisition bill and the Goods and Services Tax (GST) Bill are getting stuck in political quagmire. I would summarize the situation as one where the juggernaut has started moving and changed gears as well. We cannot feel the speed yet as the journey

is still an uphill one. Every time the market falls, the criticism gets louder that things are not really moving and corporates are still reeling from low demand and margins, which lead to low investment and fewer new jobs. Let us take stock of the Modi government's first year in office.

The government has taken several positive steps. These include passage of the insurance, coal and minerals bills, successful and transparent coal and spectrum auctions that will yield $33 billion and $18 billion, respectively, to the exchequer. The auctioning of other minerals such as iron ore, bauxite and manganese will also happen in a similarly transparent manner. Out of 166 million LPG connections in the country, 124 million or 75% have been linked to bank accounts of the customers, allowing for direct benefit transfer (DBT). As a result, the government's subsidy bill could fall by 20% as these connections were earlier bogus/ commercial/duplicate or those that had opted out of the subsidy. LPG subsidy of $7.166 billion in FY14 is expected to fall to $4.05 billion in FY16, including an estimated $779 million saving due to better targeting of subsidy. DBT through Jan Dhan Yojana, Aadhaar and Mobile (JAM) will minimize leakages and ultimately benefit the needy. DBT is expected to be extended to other major subsidies and government's welfare schemes in the future.

Given that there was political fallout, initiatives on GST and land bills are steps in the right direction. The government's vision and roadmap for the renewable energy sector, affordable housing, railways and defense are pragmatic. Besides fiscal consolidation and expenditure reform in the budget, the government has not succumbed to vote bank politics. It has hiked railway passenger fares and gas prices, deregulated diesel prices and contained budgetary allocations to populist schemes like the MNREGA (Mahatma Gandi National Rural Employment Guarantee Act). New road projects have also picked up momentum.

With an increase in budgetary allocation, activity is set to pick up in infrastructure and transmission and distribution sectors. The government seems committed to improving the country's ranking on the ease of doing business through faster and fewer clearances. Building blocks for long-term structural reforms are underway, including the Make in India thrust, GST implementation, cordial foreign relations, rationalizing freight distances for natural resources and a pragmatic land acquisition policy

"The juggernaut has started moving and changed gears as well. We cannot feel the speed yet as the journey is still an uphill one."
—Nirmanl Jain, founder and chairman, IIFL Group

Crony capitalism is not encouraged anymore. Public sector undertaking (PSU) banks have stopped patronizing big industrialists, although bad loans of the past continue to bog them down. Coal and mineral auctions have raised the prices for the select few, who earlier had mines freely allotted to them. The proposed real estate regulator is expected to clamp down on unscrupulous builders and ensure fair deals and transparency.

A few significant disappointments of the Modi government are tardy progress on PSU reforms, including recapitalization of PSU banks and restructuring of state electricity boards. The government could have been bolder by sacrificing tax revenue from controversial provisions such as Minimum Alternative Tax (MAT) on foreign institutional investors' (FII) profits.

Corporate India is grumbling because sky-high expectations of a quick turnaround in economy have not been met yet. FY15 is turning out to be the worst in the last decade in terms of revenue, profit after tax (PAT) growth and margins and earnings before interest, tax, depreciation and amortization (Ebitda). Private sector balance sheets have been leveraged, preventing any meaningful capex. The government needs to kick-start the investment cycle by spending more on railways, defense, affordable housing and roads, but little has been done so far.

The market wants to see tangible and quick results. This explains the disenchantment and impatience among many investors. When this government came to power, the market euphoria was also fueled by falling commodity and global oil prices. The sharp correction now is on account of dismal corporate earnings growth, spike in crude prices from low levels, forecast of weaker monsoon, etc.

These factors will play out in the short term. For the long term, I recall Modi's quote: "I am a very optimistic man and only an optimistic man can bring optimism in the country." Like him, I am also optimistic about India and expect much better days for the economy and the markets in the future.

HAS HE KEPT HIS WORD?

India
2

CONFLICTING AGENDAS

Modi's ability to make good on the promises that won him the election is increasingly being questioned.

By Siddharth Varadarajan Photo by Sanjay Sakaria

By any conventional yardstick, Narendra Modi has had a great first year as Prime Minister, capping his spectacular electoral triumph in May 2014 with a string of victories in state elections from Maharashtra and Jharkhand to Haryancoa and Jammu and Kashmir. Inflation has fallen thanks to lower global crude prices and the investor community in India and around the world has applauded his every move. Though output and employment remain sluggish, a revised set of national income statistics has boosted the official growth rate. Within his own party, Modi's position is as secure as can be, and the media too has been wary of directly taking on the Prime Minister for his government's failings.

Despite this favorable political terrain,

however, Modi's ability to make good on the promises that won him the election is increasingly being questioned. This is largely because the politics he stood for and the campaign he ran generated a contradictory set of expectations among his supporters that, one year on, he is simply unable to resolve.

Consider the first contradiction: vikas vs. Hindutva. Modi's promise of "development for all" increased the BJP's (Bharatiya Janata Party) national vote share by more than 10 percentage points. These first-time BJP voters chose Modi not out of any love for the Sangh Parivar's (a collection of Hindu nationalist groups) Hindutva agenda but because they saw in him a leader who could fulfill their aspirations for employment and a better way of life. But the Modi victory was also the product of an efficient political machine operated by the RSS (a Hindi national volunteer organization), which flooded the country with activists to campaign for Modi and bring people to the booths on polling day. The operators of this machine have little interest in vikas (progress); for them, the BJP's massive victory has opened the door for the pursuit of their own religious nationalism. But the more they press ahead with this agenda—the campaigns against Muslims and Christians under the guise of "love jihad," "ghar wapsi" and other ridiculous slogans; against women's autonomy; against artistic, and cultural freedom—the harder it becomes for Modi to sustain the idea that he is a leader who stands for the development and progress of all citizens.

The second contradiction is equally serious. Modi won the election on the basis of the unprecedented financial support extended to him by the corporate sector of India. Indian businessmen backed the BJP because they see its prime ministerial candidate as someone who would not be squeamish about scrapping "business-unfriendly" rules and regulations on land acquisition, the retrenchment of labor and the protection of the environment, as well as what they considered fiscally profligate social expenditure. But millions of poor Indians backed Modi because they believed he would be willing to spend the government's money on housing, sanitation, job creation, healthcare and social security, and that their hard-won right to live in a clean environment and to use or sell their land as they saw fit would not be violated by his push for growth. One year on, it is clear that Modi's "suited-booted" supporters—the men who paid for his expensive election campaign—have the upper hand, while the poor who actually voted for him have nothing concrete to show other than the announcement of schemes for sanitation, financial inclusion and insurance with little or no dedicated expenditure to back them up with.

While Modi is counting on a higher growth rate to give him the fiscal headroom to resolve the second contradiction, his silence in the face of the provocative statements made by senior BJP and RSS leaders and the push for controversial laws like Maharastra's beef ban suggests he is unable or unwilling to deal with the first. Does this mean he is not as strong vis-à-vis the Sangh Parivar as has been commonly assumed and thus lacks the power to get them to stop their divisive politics? Or does he not think what they are doing is a violation of the mandate he won and is obliged to implement? Either way, the gap between the image and the reality is not particularly flattering to the Prime Minister.

The aggressiveness of the Sangh Parivar, the growing rural anxiety over land acquisition and the state of the farm economy, and the BJP's "take no prisoners" approach to the opposition, have all served to push Modi's political opponents to find ways of coming together. Some of them, like Mamata Banerjee in West Bengal, have demonstrated their capability of holding their ground in the face of the BJP's ambitious growth plans. In Bihar, the BJP now faces a reunited Janata Parivar (group of political parties) that has brought former rivals Nitish Kumar and Laloo Prasad on to the same platform. On the political front, what happens in Bihar later this year will be an important marker of the political challenges Narendra Modi might have to deal with, especially in Uttar Pradesh, which will hold assembly elections in 2017.

The politics he stood for and the campaign he ran generated a contradictory set of expectations among his supporters that, one year on, he is simply unable to resolve. —Siddharth Varadarajan, journalist

THIS IS HOW IT'S DONE

A handful of Indian companies have kept the Make in India flag flying high. Three notable ones are Bajaj Auto, Trident and DRL. A few lessons from their journey into Narendra Modi's pet project...

By Joe C. Mathew

Bajaj Auto, Dr Reddy's Laboratories (DRL) and Trident are among the leading foreign exchange earners in some key Make in India segments identified by the central government. In fact, these companies achieved an admirable global presence long before the launch of Prime Minister Narendra Modi's grandiose mission.

The industries they represent—automobiles, pharmaceuticals and textiles—have also done well. India ranks second in global textile exports, third in the volume of medicines produced, and sixth in terms of commercial and passenger vehicle manufacture.

Yet the growth opportunities provided by these industry segments are still quite large, as India's share in the $772 billion global textile trade is just 5.2%, while China, the leader, has a 36% market share. The Indian pharmaceutical industry is half the size of US pharmaceutical firm Pfizer, which registered $51.6 billion in sales in 2013.

In the case of automobiles, India's share is just 4.4% of global production. BusinessWorld recently talked with Bajaj, DRL and Trident to understand how they became leading exporters, and what Make In India means for their respective industries in times to come.

In The Fast Lane

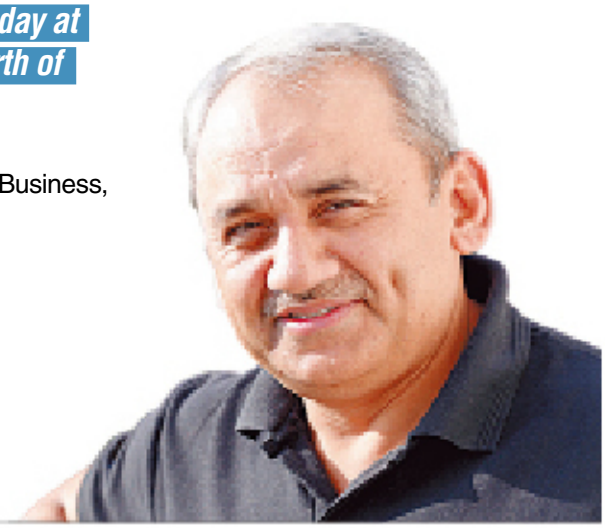
Bajaj is India's biggest two-wheeler exporter

Every 26 seconds, a motorcycle is made in Bajaj Auto's production facility at Chakan, near Pune. Over 60% of these are exported. Bajaj Auto, as a whole, accounts for 66% of India's motorcycle and 73.8% of three-wheeler exports. The company dwarfs almost every other Indian automobile maker, including larger players such as

Tata Motors, Mahindra & Mahindra and Maruti Suzuki India when it comes to foreign exchange earnings. "We are running today at [$1.558 billion] worth of exports. It has trebled in the past five years, and our ambition is to double it in the next four," said Rakesh Sharma, President, International Business, Bajaj Auto. India's share in the global two- and three-wheeler market is much bigger than it is in the commercial and passenger vehicles segment. India is, however, not the biggest player. The Chinese and the Japanese have 65%-70% share of the global market. While the Japanese are known for their quality, the Chinese have gained ground through commoditization. Bajaj has fought them both to create its own loyal customer base in Africa, South America and, to a lesser extent, in Southeast Asia.

"We are running today at [$1.558 billion] worth of exports."

—Rakesh Sharma
President, International Business, Bajaj Auto



The Price Is Right

In 2003, when Bajaj first participated in a motor show in Brazil with its 150 cc Pulsar motorcycle, that country was virtually a monopoly market for Japan's Honda. Bikes powered by 135 cc Honda engines enjoyed a 90% market share. But the minute Bajaj entered, Honda introduced bikes of higher power and also slashed prices. "That was the first time the Japanese faced real competition in the affordable commuter motorcycle space. We were able to make a desirable, good product and export it at an FOB (free on board) price of $500-$700, that is, an extra value of 30 to 40% compared to the Japanese bikes," said S. Ravikumar, President, Business Development, Bajaj Auto. If it was the pricing game that allowed Bajaj to counter the Japanese, quality helped the company check the Chinese advance, especially in Africa. "We did three things right. The first is R&D, the second is a long-term commitment to the market, and the third, the willingness to learn," said Sharma.

Premium Partner Bajaj's international business got a boost after it acquired a 14.7% stake in Austria's loss-making sports motorcycle manufacturer KTM in 2007. Bajaj went on to become its largest shareholder with a 48% stake and, in the process, turned KTM around. And how did Bajaj do that? Well, it started manufacturing KTM's low-end models at its Chakan facility. In 2013-14, Bajaj manufactured 36,047 units of KTM Duke, two-thirds of which found their way to the export market. The result was telling: Calendar year 2013 proved to be a record year for KTM, with sales and turnover touching the highest ever in its history. It sold 123,859 motorcycles, a growth of 15.6% and achieved a turnover of around $859 million, a growth of 17.1%. Profit after tax was more than $43 million, a growth rate of 44.3%. Like Bajaj, other Indian automobile companies have also made acquisitions overseas. Mahindra has acquired South Korean firm Ssangyong. Tata owns a majority stake in Europe's Jaguar Land Rover. But the synergy that Bajaj has achieved indicates the direction in which India's automobile sector is destined to grow.

India has the demand, the engineering talent, and proven capabilities in two-wheeler exports. Can it then become a global two-wheeler manufacturing hub? Not yet. "A shipment to Bangladesh today goes to Singapore first and gets re-routed to Dhaka," Sharma pointed out. Changes in the rules of origin, easing of visa rules, active engagement of embassies, risk funding—the list of trade facilitation measures the government can take to strengthen India's global prowess are many. Sharma says the ingredients for growth are all there. It's the ideal mix that is required. Given the strengths in two-wheeler manufacturing, this sector could perhaps be off to a great start. "But you will have to decide whether it should be a sprint or a hurdle race," he said.

TRIDENTGROUP

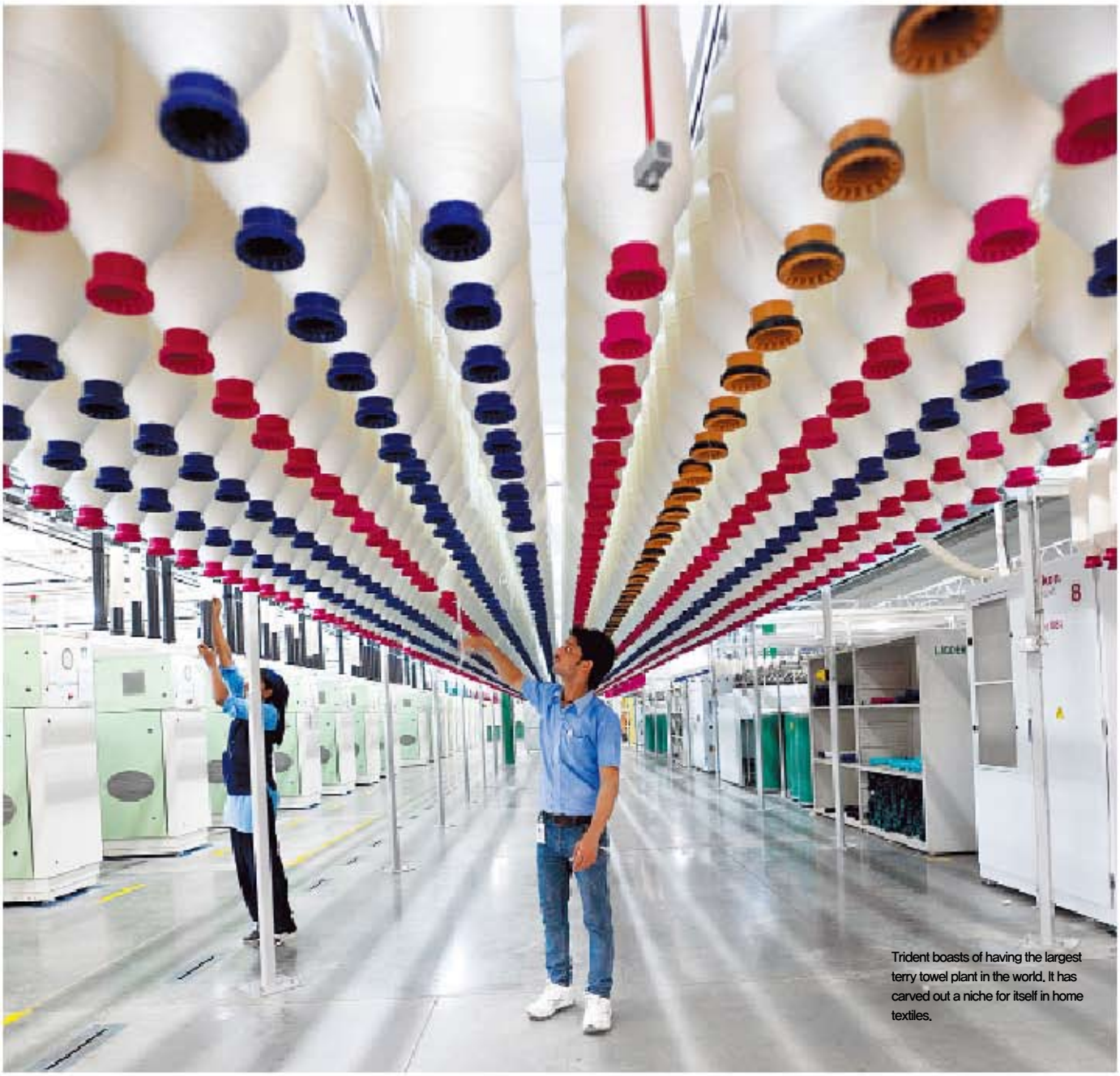
Weaving a Spell

Trident's terry towels are sold in 75 countries

Last October, Ludhiana-based Trident inaugurated the world's largest terry towel plant in Budni, Madhya Pradesh. It took 15 years for Trident to achieve the size and scale in terry towels it has today. The company started with only a spinning unit in 1993. Yarn, however, was not very profitable, which led the company to go beyond

making yarn and spinning. It created a niche business in home textiles. "Having invested money over a period of time, we understood the potential in home textiles. Hence the scale up," said Rajinder Gupta, Chairman, Trident Group. "When we entered the textile segment, 25,000 spindles was the highest size for a unit. Today, we have 125,000 spindles in one location. So, practically, we have gone from 10,000 spindleage to 200,000," he said.

Unlike several other sectors in Modi's priority list, textiles is a more traditional area where India's strengths are well known. The country is a net exporter of raw cotton, it has a manufacturing base for rayon and synthetic fibers, and technology and human skills are handy. But can India leverage these strengths? "If the world can, why not India" said Gupta. He said industries that are not very high-tech but can depend on local inputs can flourish in India. "We are net exporters of cotton. If China can buy cotton from us and be a world leader in textiles, why can't we? Textiles was an obvious choice for us. This industry does not have high technological barriers. Besides, the



Trident boasts of having the largest terry towel plant in the world. It has carved out a niche for itself in home textiles.

"When we entered the textile segment, 25,000 spindles was the highest size for a unit. Today, we have 125,000 spindles in one location."

— Rajinder Gupta
Chairman, Trident Group

capital expenditure is not a big constraint," he added.

Trident's customer base spans across over more than 75 countries and six continents and comprises global retail brands such as Ralph Lauren, Calvin Klein, JCPenney, IKEA, Target, Walmart, Macy's, Kohl's, Sears and Burlington. With the turnover from exports accounting for around 50% of total sales (nearly $525 million in 2013-14) of the company, Trident is looking at broadening its product portfolio in home textiles. "The right technology, scale and cost competitiveness, combined with innovation, have helped us grow. We have a research collaboration with the National Institute of Design," said Gupta. In addition to terry towels, the company is moving into the bedsheet segment. It is also widening its focus to other foreign markets besides the US. "One-third of our revenues comes from the US. We were overbooked in that geography till now. But with new capacity, we will be able to serve the European and Australian markets too," Gupta said.

The home textiles range is wide. In addition to towels, there are tremendous growth opportunities in bedsheets, floor covers, window and wall cover segments. It's not just Trident. Textile companies such as Vardhman, Welspun, Alok and Arvind have all gone international with world-class technology and global scale of production in India in recent years. That said, it will take more than individual efforts to turn India into a global hub of garment and home textile manufacturing. The biggest hurdle when it comes to capacity expansion of existing companies and the entry of new players is infrastructure. "If you go to tier-2 cities, capex goes up. If you go to tier-3 cities, holding talent becomes a problem. Industry cannot afford to invest more as margins are very thin in this industry," said Gupta. The success of textiles in the Make in India campaign thus depends wholly on the government's ability to set up integrated textile parks and the logistics and infrastructure support it can provide in the coming days.

DR. REDDY'S

Taking the Generics Route

US and EU account for 57% of DRL's revenue

Europe and North America accounted for 57% of the $2.2 billion in revenue generated by Hyderabad-based Dr Reddy's Laboratories (DRL) last year. Only 15% came from India. So DRL makes for a perfect case for Make in India. The company's revenue model, like most leading Indian drug makers, is to sell more pills, capsules and vials outside the country than within. "Export is in our DNA. We supply to the most discerning of customers globally," said Satish Reddy, chairman, DRL. "We were the third largest producer of ibuprofen in the world." The 30-year-old company started with manufacturing high blood pressure drug methyldopa for India and the world. It was the first bulk drug (active pharmaceutical ingredient or raw material) successfully launched by DRL.

In 1987, after the company got approval from the US Food and Drugs Administration to sell methyldopa in the US market, it ended up supplying the drug to the innovating company Merck Sharp & Dohme (MSD) to meet increasing global demand. What worked in DRL's favor? In the very year it started its manufacturing operations, came a US law that directly aided the growth of the generic drug industry in the country, which accounts for 40% of the global pharmaceutical market. Known as the Hatch-Waxman Act, it helped establish a drug regulatory system that rewarded early entry of low-cost generic medicines to supplement patented drugs.

DRL and Ranbaxy were among the Indian companies that utilized this opportunity to make in India and sell in the US and other markets. As a result, India has the largest number of FDA-approved drug manufacturing facilities outside the US. Forty-nine per cent of all drug master files, a detailed document for marketing approval of bulk drugs submitted in the US, are from India. According to Reddy, the focus of Indian companies should be on high-value complex products and acquiring partners and development houses. "We need to identify and develop alliances." "We give a significant push to ensure that more revenues come from overseas, through fewer mar-

"Export is in our DNA. We supply to the most discerning of customers globally."

—Satish Reddy
Chairman, DRL

kets and deeper penetration. Most of it comes through alliances. It has worked very well for us," said Reddy.

Even if more home-grown drug makers try to follow DRL's model, India will still find it impossible to catch up with the US in terms of the value of pharmaceutical sales, as the bulk of the latter's numbers are derived from the patented drug business—an area in which India is yet to make a mark. That said, it is already an established player in the low-value generics business and, with a Make in India push from the government, things will only improve for the generics segment. But some hurdles remain.

Perception Problem

The biggest threat to the Indian pharmaceutical industry today is the increasingly negative publicity around the questions raised by the US FDA regarding the regulatory compliance level of Indian drug companies. In addition to heightened FDA investigations—which resulted in product recalls and bans in a few cases—the smear campaigns carried out against India's intellectual property rights environment by global pharmaceutical majors and lobby groups is really beginning to hurt. The industry is also facing a problem of Chinese dependence as a majority of its production is based on the supply of raw materials from that country. "Especially when it concerns high-volume and low-value products, we are dependent on China [for bulk drugs]," said Reddy.

According to Reddy, the government can help revive the Indian bulk drug industry, especially the manufacture of those ingredients that are needed to make high-volume, low-revenue medicines. "A private company will not find it feasible to set up such facilities as margins are very thin. But if the government provides necessary infrastructure, the private sector can produce such bulk drugs here." India's pharmaceutical sector could perhaps be the easiest among the 25 priority sectors to boost. Strengthening of regulations and enforcement mechanisms within the country could play a key role in achieving this goal.

CREADOR'S INDONESIAN ATTRACTION

Global consulting firm Bain & Company sees the next decade as belonging to the US, with a new generation of big spenders maturing. But there's still room for emerging markets, with many investors putting aside some cash for longer-term plays in these potential growth markets. Creador, a private equity firm focused on long-term investment in growth-oriented businesses in Southeast and South Asia, believes Indonesia is still a good choice for investors.

By Dion Bisara

Cyril Noerhadi (left), senior managing director at Creador and Charlie Paulus (right), the president director of Bank Index Selindo.

SYNDICATION/GLOBE ASIA

As the US dollar has gained strength and with the Federal Reserve prepared to increase its federal funds rate, many private equity firms have taken the cue for a recovery of the world's largest economy to leave their bets in emerging markets, including Indonesia. One private equity firm, however, begs to differ.

It sees the largest economy in Southeast Asia as attractive as ever, with a bustling, burgeoning 80-million strong middle-income class that presents a huge opportunity for investors. "Indonesia is a developing country which still needs a significant amount of investment that in turn will create a lot of jobs," said Cyril Noerhadi, senior managing director at Creador.

The firm is betting on a positive cycle in Southeast Asian countries and India, as a young middle class emerges after years of rapidly growing economies, creating more demand for goods and services.

Creador first raised a $130 million fund in 2011 followed by a second fund of $331 million in 2013. The majority of the money came from North American and European investors, while the rest was from Asia and Australia.

The firm has invested in 15 consumer retail companies in Indonesia, Malaysia and India, businesses ranging from consumer finance to fashion and restaurant chains.

Creador was established in 2011 by seasoned private equity manager Brahmal Vasudevan, who already had 11 years of experience in India's private equity market. Cyril Noerhadi, himself a seasoned financial

executive with experience in Indonesia's bourse and energy companies, joined as a partner that same year.

Third Fund

Creador is now seeking to raise between $400 million and $500 million from investors in the second half of this year in order to expand its portfolio, according to a source familiar with the situation. That may be a tough sell to investors, particularly discriminating ones who prefer investment in places with strong legal protection, liquid capital markets and transparent corporate governance.

The report from private equity consultancy Bain & Company sees investors returning to the United States this year, after a massive exit from the Asia-Pacific region. "In striking contrast to trends elsewhere, macroeconomic signals are flashing green across North America," Bain wrote.

The consultancy noted that several major trends back a thesis of US economic expansion through and beyond this decade. First, US consumers are starting to spend again after seeing their wealth raised by the Fed's low interest-rate policies that have helped re-inflate the value of their main asset, their house.

Second, the US's 81 million young adults born after 1980 are entering prime household- and family-formation years and are set to create demand larger than the baby boomer generation, according to Bain & Company. Thirdly, innovation in energy has further pushed down costs, while advances in robotics, nanotechnology, genomics, artificial intelligence and ubiquitous connectivity have created a whole range of new markets.

Indonesia's Allure

Still, Cyril Noerhadi remains confident that Creador can attract investment to Indonesia, which accounts for a half of the firm's portfolio, as the country goes through its own stages of reform. "Our fundamentals are OK," he said, pointing to the country's narrowing current account deficit and growing trade surplus that should help the country bounce back from its slowest pace of growth in five years.

Indonesia's current account deficit improved to 2.81% of gross domestic product in the fourth quarter of 2014, down from 2.99% in the preceding quarter. Bank Indonesia sees the current account deficit at below 3% this year.

The investment firm is betting on a positive cycle in Southeast Asian countries and India, as a young middle class emerges after years of rapidly growing economies, creating more demand for goods and services.

The Indonesian government has implemented policies as part of an effort to narrow the persistent deficit in the current account, including waiving taxes for export-oriented and strategic industries, expanding visa-free short-term visits to citizens of 30 new countries, and providing tax allowances to export-oriented companies.

President Joko Widodo is pushing for infrastructure development and bureaucratic reform to support a boost in the country's economic expansion to more than 7% in the next five years.

Cyril Noerhadi noted that investors in Creador such as endowment funds, pension funds and family investment vehicles would like to retain some exposure in emerging markets and are committed to staying for the long term. "If they are mutual funds, with investment horizons of two to three years, they may not be suitable for us," he said. "But others such as endowment funds and pension funds with a longer investment horizon, would have set aside some money for this kind of investment."

A Regional Business Model

For Cyril Noerhadi, his focus now is to find companies that are a good match with Creador's vision and mission. "We decided our platform is regional; the focus sectors are consumer-based sectors with an investment size of between $10 million and $50 million, and we are predominantly minority shareholders," the former Medco chief finan-

cial officer said.

The regional platform means that Creador would invest in similar companies in a number of countries, allowing synergy within the firm's portfolio. "If we have a financial business in India and a financial business in Indonesia, we can synergize them, not in the sense of expanding the business, but in regard to sharing best practice and experience," said Cyril Noerhadi. The companies, meanwhile, would not be reluctant to share their trade secrets to another company as they operate in entirely different markets.

In Creador's portfolio are Simba, Indonesia's second largest cereal maker; Indian property developer Ashiana Housing Limited; Malaysian restaurant chain and coffee maker Old Town; Indian financing company Cholamandalam Investment & Finance Company Limited, and BFI Finance, a multi-finance firm in Indonesia.

Kiss the Frogs

Looking for a company that is just right, however, is tedious and labor-intensive, said Cyril Noerhadi. "It's like looking for frogs and kissing them one by one, hoping one will turn into a princess." That means a lot of socializing, meetings, conventions, cold calls and, at least in one instance, a cold fax.

"When I received a fax from Cyril one afternoon two years ago, I thought it was a mistake," recalled Charlie Paulus, the president director of Bank Index Selindo, a small Jakarta-based lender focused on small and medium enterprises.

"The East is different from the West, where business ownership is changing all the time."
—Cyril Noerhadi

"What on earth did a CFO of Indonesia's largest oil company want from a small bank like us? He must have dialed the wrong bank, I thought, but I decided to meet him anyway," said Charlie Paulus.

It turned out that it was a match made in heaven.

With an investment of less than $50 million, Cyril Noerhadi—who left Medco in 2011—knows that private equity must look for companies "where an added value other than money is important." Bank Index had been looking to list on the Indonesia Stock Exchange in order to raise enough capital to enable it to engage in Internet banking services. "It was a crucial step in our growth because in the future we saw that banks would go online," said Bank Index commissioner Joko Setiawan.

Creador came along with a unique offer, a commitment to help the lender expand its business while implementing the region's best corporate governance practices within a time scale of seven to eight years. "The family business owner can learn knowledge and skills on their own but the speed of acquiring such knowledge is different. And this is a practical learning experience," Cyril Noerhadi said.

Creador bought 20% of Bank Index for $24 million, bumping the lender's capital to close to $75.62 million, the minimum amount required by the central bank for conducting Internet banking. The deal made Joko Setiawan confident the lender could conduct a successful IPO by floating another 20% of shares in the next two or three years.

Another factor that Cyril Noerhadi believes is crucial in Creador's business model is that the equity firm is constantly looking for minority stakes, instead of going all out for a hostile takeover. "The East is different from the West, where business ownership is changing all the time. It's a sensitive issue if we say we want to become the majority shareholder," he said.

It's rare among family-owned businesses in Southeast Asia that a family wants to give up all of its business, Cyril Noerhadi said. When it happens, the sale may be due to a reformulated company strategy, changing interests within the founding family or owners, or the company just simply cannot survive on its own, which happened during the 1998-99 financial crisis.

"When we invest into a business, we are typically minority shareholders. So, for the business owner family, we are not a threat," Cyril Noerhadi said. "During our partnership and investment period, we will add value to their business, and help accelerate the business growth as well as help it evolve to a more modern and better-governed business."

MY COMMUNIST BUSINESS PARTNER

China seeks to expand its state-owned companies internationally. The example of Foton, which is building a truck plant in the Brazilian state of Rio Grande do Sul, shows that Brazil can benefit from that.

By Humberto Maia Junior

SYNDICATION/EXAME

Many Brazilian businessmen see the Chinese the way the Romans used to see the barbarians: foreign forces that should be kept outside the borders at any cost. No wonder. In past decades, China has become an exporting machine based in heavy investments and low costs—in 2014, the country sold the world goods worth a total of $2.3 trillion. In Brazil, Chinese imports went from $1 billion in 2000 to $37 billion last year. Trying to contain this expansion has proved to be wasted effort. Therefore, winning the Chinese as allies is probably better than fighting them.

An example of how such an alliance may work is the arrival of the state-owned company Foton to Brazil. It is one of the largest truck manufacturers in the world. Foton plants in China produce 650,000 vehicles per year, almost five times the truck pro-

duction of Brazilian manufacturers in 2014. At this size, Foton could take advantage of scale to export at competitive prices to Brazil. Instead, the company's management has chosen to invest in building a plant in Brazil, with the help of a Brazilian partner, Luiz Carlos Mendonça de Barros, an economist who and a former president of the Brazilian Development Bank (BNDES). Back in March he sold his 36% share of Quest, an investment management firm, and started to focus on Foton. In essence, he has become the capitalist partner of the Chinese government, led by the Communist Party and owner of Foton. "The Chinese plan on expanding their large state-owned company internationally, and Foton sees Brazil as an important market for that," said Mendonça de Barros.

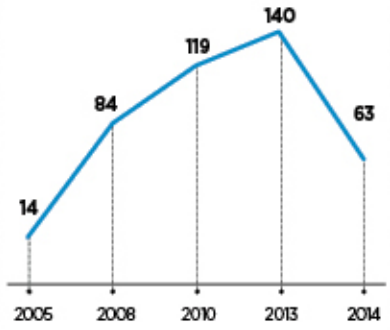
Foton's strategy for Brazil includes building a plant in Guaíba, Rio Grande do Sul. The site, which is still under construction, is planned to start operations in April 2016, with a production capacity of 24,000 trucks per year. For now, the Brazilian branch imports trucks from China. Four models with a 3.5-ton load capacity and a 10-ton model have been chosen for the country. The company sold 800 trucks of both models last year. An important step of the project is the creation of a dealership chain. Foton currently has 25 outlets (its main competitor, Mercedes-Benz, has around 150) managed by Brazilians. For the time being, the Chinese receive 2% of the sales prices.

Foton is investing around $66 million in its operations in Brazil. The money is welcome at a time of a deficit in foreign accounts. The balance of Brazilian assets and services transactions with foreign countries amounted to negative $90 billion in 2014. Attracting more international investments for manufacturers and other companies—what economists call foreign direct investment—not only helps decrease this deficit but also in increasing production capacity, resulting in more jobs and

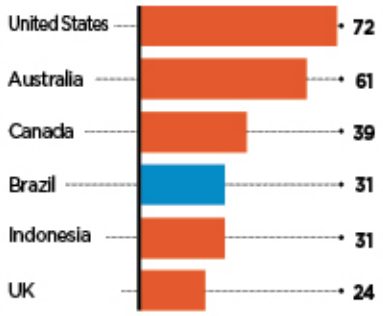
BUSINESS FROM CHINA

Since 2005, the Chinese have invested $870 billion abroad, and Brazil is one of the main destinations of this money

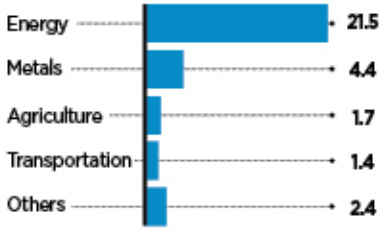
Chinese investments in the world peaked in 2013 but decreased last year(1)
(in billion dollars)



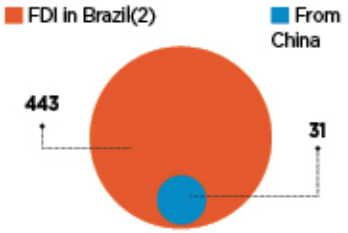
Brazil is one of the countries where China invests the most
(amount accumulated from 2005 and 2014, in billion dollars)



A great part of Chinese investments in the Brazilian market were in the energy sector
(amount accumulated from 2005 and 2014, in billion dollars)



Chinese participation is still small compared to the total of foreign investments in Brazil
(amount accumulated from 2005 and 2014, in billion dollars)



China is ruled by different values from Western ones. Professor Roberto Dumas Damas, from Insper, listed situations that may arise when Chinese and Westerners do business together

Respect for others

During negotiations, it is unlikely the Chinese will reject a proposal at an explicit way. Instead, they usually give signs that the deal will not be closed as proposed. They do so because they believe that negative answers are embarrassing to those on the other side of the table and disruptive to balance.

Importance of personal relations

Chinese tend to trust people more than contracts. This is what they call guanxi, which can be translated to contact. Gaining the trust of a Chinese is a slow process involving many protocols. But it is critical for a good negotiation.

Strict Hierarchy

Chinese society balance is based on hierarchy. At the workplace, projects are not discussed in groups, they are imposed top down. During professional conversations, hierarchy should also be respected. For example: during a meeting, you should always address the head of the team.

(1) For calculation purposes only amounts higher than $100 million were taken into account. Financial investments have not been included, such as bonds (2) Foreign direct investment
Sources: American Enterprise Institute and The Heritage Foundation

income. When operating, the Foton plant shall be responsible for 250 direct job posts and 650 indirect ones. "Foreign companies' investments usually bring new technologies along," stated Celso Toledo, an economist with LCA consulting company. "For this reason, this money may help the country to become more productive."

Friend of China

China does not lack capital to invest around the world. From 2005 to 2014, it invested $870 billion abroad, out of which $31 billion was in Brazil. During this period, the Chinese contribution was less than 10% of the capital injection in the country. However, increasing this figure requires adapting to the peculiar way the Chinese do business. "Chinese culture values long-term relationships, which they call guanxi, more than written contracts," explained Roberto Dumas Damas, Professor at Insper Business School and former Head of Banco Itaú BBA in Shanghai. "Wining Chinese trust is vital to having a successful partnership with them," he said. The difficulty in setting up this kind of relationship is one of the reasons they are known as extremely controlling in business relations. "When investing in other countries, many Chinese companies would rather [bring] their own workers to take over the work," said Reinaldo Ma, a lawyer at Tozzini Freire law firm. The latest case is State Grid, a state-owned company that won the bid to build the transmission lines connecting Belo Monte power plant to the Brazilian grid. State Grid is trying to get the Brazilian government to authorize bringing 11,000 Chinese workers to work on the construction.

The way Foton has approached Brazilians reveals how doing business with the Chinese follow a unique rationale. In the 90's, Mendonça de Barros was the President of the Brazilian Development Bank when he took a trip to China. The bank was financing the purchase of turbines manufactured by a Brazilian company for the Three Gorges Dam, the largest in the world today. It was the beginning of a trusting relationship. Because of this negotiation, Mendonça de Barros's name was included in a kind of list of friends of China abroad. Twenty years later, Foton reached out to him. "They had a project to enter Brazil and asked me to have a look at it," he explained. "I showed them how they could improve the project and I was asked to join them as a partner."

"Foreign companies' investments usually bring new technologies along."
—Celso Toledo, economist

The main weakness of Foton's initial plans was not taking the complexities of the Brazilian market into account. The company was planning on importing all its parts but did not consider the need to meet a minimum production requirement in Brazil, without which clients may not be granted access to financing by public banks with lower interest rates. Another mistake was to plan opening the plant without having a reselling network, which would leave the company behind its already established competitors. "Brazil is a complex country for foreign investment," stated José Othon de Almeida, partner of Deloitte. "It is vital to have a local partner to help dealing with tax and bureaucratic issues."

To compete with the traditional companies in the country, such as Ford and Mercedes-Benz, Foton is counting on the support of its China office, which employs 4,000 engineers. They help in adjusting the models to the laws and needs of the Brazilian market. "We also use Foton's size on our behalf when negotiating prices and conditions with global providers of truck parts," said Bernardo Hamacek, CEO of Foton in Brazil and former director of Iveco, a truck brand of the Fiat Group. With this advantage, Foton has been able to offer trucks at a price up to 15% lower than its competitors.

The downturn in the Brazilian economy is a challenge. Truck sales fell by 11% last year, and in the first two months of this year, sales registered 40% below the same period of 2014. Can the situation harm the plans? "Our partner has long-term plans for Brazil," Mendonça de Barros explained. "The current situation is bad but it should pass." Still, Foton has adopted a careful strategy: to start with the light trucks (up to 3.5 tons) and the medium trucks line (up to 24 tons) which are the ones that have the largest market participation. Anyhow, the famous Chinese patience will be tested in Brazil.