

CASE

Geely Motors: A Chinese Automaker Enters International Markets

Ilan Alon / Marc Fetscherin / Marc Sardy
Rollins College
Rollins China Center & International Business Department
1000 Holt Avenue
32789 Winter Park, FL

On January 22nd, 2006 Shufu Li, the director of international marketing for Geely Motors was rushing to the check-in counter at the Detroit Metropolitan Airport in order to travel back to Shanghai, China. He had just come from the Detroit International Auto Show where his company had presented its new car models. Geely (pronounced 'Gee-Lee') had been selling cars in China since 1997. In 2004 they had begun exporting cars to North Africa and Latin America. Geely had now set their sights on North America, the largest automobile market in the world. Geely's management was planning to sell cars in the US market for under USD 10,000 by late 2007. The International Auto Show in Detroit was crucial in order to get feedback and establish relationships to potential business partners, customers and the press. While he was boarding the plane, Mr. Li began to reflect on Geely's transition from a regional manufacturer focused on the domestic Chinese market to an international player. Would the last few years of their marketing effort turn Geely into a global player in the auto market? Would US consumers warm up to the cars Geely had shown at the auto show? How could Geely overcome the lack of brand name and negative country-of-origin quality image that Chinese manufacturers have?

Company Background

Geely Motors, from Zhejiang Province, is a large regional manufacturing conglomerate (**Exhibit 1**). Early in its history it produced primarily motorcycles, scooters, engines and vehicles. As it grew the company added an import-export trade company, a real estate management company, several hotels and a travel services company. In 1998 a motorcar division was built in collaboration with Jia Auto Works, Sichuan province. Two factories were used: one in Huzhou, the other in Quzhou, both in Zhejiang province. Among the

initial products were the Haoqing, a 4-door sedan, later the LG-1 station wagon and most recently the PS4 sports car. Geely Motors was the first Chinese private enterprise to build passenger cars. In 2000 the Haoqing, equipped with a 4-cylinder Toyota engine, was introduced. Geely presented the PS4 sports car at the Shanghai Automobile Show of 2005, and started to sell them in China during 2006 (**Exhibit 2**). By 2005 Geely Motors had four production facilities. One was a joint venture between Geely (53%) and the Quzhou Holding Co. (47%), an investment company listed in Hong Kong. Since 2003, Geely had also been working with Daewoo on a joint venture. In 2006 this venture had produced a new model of the PS4 sports car which had just been introduced at the 2006 Detroit International Auto Show. By 2006 overall production capacity for the four facilities were about 360,000 cars (**Exhibit 3**).

The Chinese Auto Market

The Chinese Automotive Industry celebrated its 50th anniversary in 2003. However, much of Chinese automotive production over the last four decades was for military and commercial vehicles. Private car production in China is relatively new and emerged largely in the mid-1990s. By the end of the 1990s, passenger automobile production in China was still below one million vehicles per year. When compared to global competitors such as Japan, Germany and the US in terms of quality, product features and R&D, the Chinese Auto industry is still in its infancy.

Throughout the last two decades China had become a haven for contract manufacturing. By the mid 90's many foreign companies had established joint ventures that brought needed expertise and exposure. In several industries ranging from toys to clothing and furniture, China had become the worlds largest manufacturer. With the 1999 handover of Hong Kong by Great Britian, China became the custodian of one of the worlds great captialist-economic centers. In 2001, as China entered the World Trade Organization (WTO), automobile production in China soared. In 2004, for the first time in history, a Chinese auto company appeared in the list of the Global 500. Shanghai Automobile Industry Corporation (SAIC) was ranked 461st on the list for its 2003 sales of 12.3 billion USD. By 2006, automobile production in China had risen to roughly 6 million vehicles almost all of which was consumed by the domestic market. This made China the third-

largest automobile market in the world, surpassing Germany and the UK. At its current rate of growth it will soon surpass Japan¹. This is quite an achievement considering less than 2.4% of the Chinese population have a car. The growth rate in automobile sales is expected to be between 8% and 10% per annum through 2010. Some estimates of growth suggest that the Chinese automobile market will exceed the US market by 2015.

However, unlike the Chinese market and its double-digit growth, the US market has faced, a slight decline of about 500,000 vehicles or 3% in total units sold between 2005 and 2006.²

Makers and Takers in Chinese Automotive Market

China's Automobile Industry is a largely home-grown, fragmented business, and is likely to undergo future consolidation. In 2006, there were more than 120 automobile manufacturers, with 12 national manufacturers. Sales are also concentrated amongst a few firms; the top 5 companies accounted for almost 70% of total domestic production. All of these companies have joint venture (JV) arrangements with foreign partners. Automobile companies in China fall into two categories: small local manufacturers and large national ones (**Exhibit 4 & 5**). Local manufacturers make and market mostly their cars within their region, often within their local community. Most of these small companies, are owned by their local government. However, from these local manufacturers a few private companies have emerged such as Geely Motors. The national players make and market cars in multiple regions within China. Many of them also have international manufacturing partners through joint ventures (JV). There are about 30 such partnership arrangements in place with foreigners. These partnerships are about access; where Chinese companies get access to international expertise and foreign auto manufacturers get access to the rapidly expanding Chinese market. Initially these JVs were tightly

¹ Ravenhill, J., 2006. The Growth of the Chinese Automobile Industry and its Impact on Production Networks.

² Jianhua, F., 2006. Getting out of First Gear, Chinese auto industry drives into a future featuring innovation and the will to take on the international market. Beijing Review Online.

N., N., 2006a. Can China Gear Up to Sell Its Cars to U.S. Consumers? Quality Is Key. In: Knowledge@wharton.

N., N., 2005a. Driving China: The New Automotive Frontier, Interview with Clarke, Troy E. and Mei, Wei Cheng. Georgetown Journal of International Affairs 6 (2), 61-71.

N., N., 2006. Future drivers of the China automobile industry. In: Special report for Boao Forum for Asia Annual Conference. Deloitte.

constrained by government regulation but China's compliance with the WTO has tempered some of these restrictions.

Growing Chinese Market

The growth in demand for Chinese automobiles within China can be attributed to many factors such as affluence, investment, infrastructure and liberalization of trade policies. Affluence in China an increase in per capita wealth has risen as a result of the boom in the Chinese economy; this has increased demand for luxury goods like cars. Heavy foreign direct investment (FDI) has contributed by improving expertise and product offerings. Massive infrastructure changes in cities and between major cities have created better places to use cars. Liberalization of trade policy such as reduction of import taxes have made it cheaper and easier to get components to build better vehicles (licenses or tariffs on imported vehicles went from 70% in 2001 down to 25% in 2006).³ The growth rate of automobile consumption has outpaced many of the developed more mature automotive markets in the last few years in China (**Exhibit 6**).

First Steps of Globalization of Chinese Automotive Manufacturers

While most of China's automobile production has been manufactured for the domestic market, most recently there has also been rapid growth in exporting automobiles to the international market. Some of the Chinese automotive firms are even building or purchasing manufacturing facilities abroad. Although, this has happened mainly in developing countries. But overall, the Chinese automobile export market is still in its infancy. Furthermore, most Chinese automobile manufacturers lack effective distribution and sales channels to connect with the international markets. Hence, the key challenges to overcome are quality improvement, meeting safety standards and emissions standards, sales and distribution networks, and establishing after sales service and maintenance networks. According to the China Association of Automobile Manufacturers, in 2005 the country exported about 170,000 vehicles to 179 countries, a small number of exports when compared to overall domestic sales. Destination regions ranked by volume were Asia, Africa, Europe, and South America. Of the 170,000 units, trucks made up nearly

³ Luo, J., 2005. The Growth of Independent Chinese Automotive Companies. In: International Motor Vehicle Program. MIT.

100,000 units, with 90% of them being lightweight trucks. Most of these exports were privately owned Chinese domestic branded vehicles.⁴

Detroit International Auto Show

The Detroit International Auto Show is one of the most important windows into the direction of the automobile industry. Manufacturers feature their concept cars, their leading sellers and anything they plan to launch in the upcoming year. Geely Motors had a rather ordinary display featuring a small silver Haoqing and yellow PS4 model outside the main show room. But its presence in Detroit is by no means unimportant. “This is the first Chinese automobile company to participate in the Detroit Auto Show, so we are unique,” said John Humer COO and vice president of Geely-USA. Until recently, Chinese auto exports were limited to buses and trucks. However, China’s manufacturers have been busy upgrading their technology and production to compete overseas and are now ready to sell low-priced vehicles in the US automobile market. This is good news for price sensitive customers but bad news for existing auto makers struggling with sales. At the Detroit Auto Show Xu Gang CEO of Geely Motors, announced, “We have found a local partner that can facilitate distribution and we plan to enter the US market in late 2007”. Executives at established auto makers say they are not really concerned about the threat of competition from Chinese brands any time soon. The silver Haoqing sedan which was shown at the exhibition was about the size of a Honda Civic and gets 24 miles per gallon in the city and 34 miles on the highway. The marketing director, Mr. Li says “we are very competitive in pricing, this model will be available at a price below USD 10,000. We want to provide low-priced cars for American consumers”. Several Chinese automakers are carefully watching Geely’s progress in the United States as they are also considering entering this market. Malcolm Bricklin, American multi-millionaire, founder of the import company Visio Vehicles, and owner of 15 car franchise locations in major US cities is planning to import Geely’s cars by the end of 2007.⁵

⁴Ravenhill, J., 2006. The Growth of the Chinese Automobile Industry and its Impact on Production Networks
Jianhua, F., 2006. Getting out of First Gear, Chinese auto industry drives into a future featuring innovation and the will to take on the international market. Beijing Review Online;

⁵ Luo, J., 2005. The Growth of Independent Chinese Automotive Companies. In: International Motor Vehicle Program. MIT.

The open road ahead

While Mr. Li is exhilarated at the prospect of being the first Chinese auto manufacturer in the US he is also worried about the challenges his company will face in the coming months. He knows that going global with his company would provide enormous opportunities for future growth. However, there will be major organizational and resource challenges. Large financial resources will be necessary for manufacturing and establishing the distribution and sales network. To improve quality standards and meet US safety and emission standards, heavy investments in R&D will be necessary. They will also need to work closely with Malcolm Bricklin to develop international relationships, improve logistics, set up sales and distribution networks, build after-sales service and maintenance networks and manage currency risk. Malcolm Bricklin will need to work hard to build trust with consumers, and need to differentiate the brand in the US, one of the most competitive markets worldwide.

In a recent conversation with Mr. Li, John Humer expressed his concern that entering into the developed US market will be extremely costly. He believed that the firm might be better served by entering smaller, less competitive international markets and leveraging the logistics and expertise they develop to tackle the larger competitive markets. Mr. Humer also mentioned that, since Geely Motors has been declared as one of the top 100 firms the Chinese government would like to see as an industry leader, there might be an opportunity to raise needed capital from a Chinese government loan program that would lend Geely Motors money at below market rates. However it is not clear what autonomy this might cost Geely Motors or what perception a government partnership might create in a foreign market. Mr. Li wonders whether Geely Motors will be able to compete on price alone, especially when Japanese and Korean Automakers are entering international markets with their new “supercompacts” which are priced below USD 10,000 and provide a good value for money. And finally, he believes Geely must carefully consider the challenges of entering the international markets cheaply, quickly and safely, while providing customers the required sales and service network.

EXHIBITS

Exhibit 1 Profile Zhejiang Province

Map of China and the Zhejiang Province



Zhejiang province is also called the "the land of silk" and produces one third of China's raw silk, satin and brocade. The province has nine cities of regional level: Wenzhou, Jia, Huzhou, Shao, Jinhua, Zhoushan, Quzhou, Taizhou and Lishui, twenty-four county-level cities, thirty-eight counties and one autonomous county, with a total population of 47 million (2000). The main ethnic groups are Han, Hui, Manchu and Miao. Zhejiang province has a sub-tropical climate, warm, rainy and humid. Average temperature is between 16-19 C.

Exhibit 2 Example Geely Cars

Model Haoqing

In production since 2000. Technical Information:



- Engine type: 3, 4-cylinder
- Cylinder Capacity: 993 cc, 1046 cc, 1342 cc
- Engine power: 38 kW/ 5600 rpm, 40 kW/ 6000 rpm, 63 kW/ 6000 rpm
- Maximum torque: 77 Nm/ 3600 rpm, 85 Nm/ 3600 rpm, 110 Nm/ 5200 rpm
- Drive: 4 x 2
- Wheelbase: 2340 mm
- Length: 3900 mm
- Width: 1650 mm
- Height: 1420 mm
- Empty weight: 930 kg
- Tyre size: 175/ 65 R 14
- Maximum speed: 120- 145 km/h
- Fuel consumption: 6.3- 6.8 L/ 100 km
- Price in China: 35,000 – 48,000 Yuan (USD 4,500 – 6,200)

Model LG-1

In production since 2006. Technical Information:



- Engine type: 4-cylinder
- Cylinder Capacity: 1498 cc, 1587 cc, 1794 cc
- Engine power: 69 kW/ 6000 rpm, 79 kW/ 6000 rpm, 102 kW/ 6200 rpm
- Maximum torque: 128 Nm/ 3400 rpm, 137 Nm/ 5200 rpm, 172 Nm/ 4200 rpm
- Drive: 4 x 2
- Wheelbase: 2502 mm
- Length: 4342 mm
- Width: 1692 mm
- Height: 1435 mm
- Empty weight: 1040 kg
- Tyre size: 175/ 65 R 14, 185/ 60 R 15
- Maximum speed: 150- 170 km/h
- Fuel consumption: 4.7 L/ 100 km
- Price: 65,000 = 85,000 Yuan (USD 8,400 – 10,900)

Model PS4

In production since 2006. Technical Information:



- Engine type: 4-cylinder
- Cylinder Capacity: 1762 cc
- Engine power: 83 kW/ 5600 rpm
- Maximum torque: 157 Nm/ 3400 rpm
- Drive: 4 x 2
- Wheelbase: 2440 mm
- Length: 4160 mm
- Width: 1690 mm
- Height: 1325 mm
- Maximum speed: 190 km/h
- Price: 79,000 Yuan (USD 10,200)

Source: Company Website

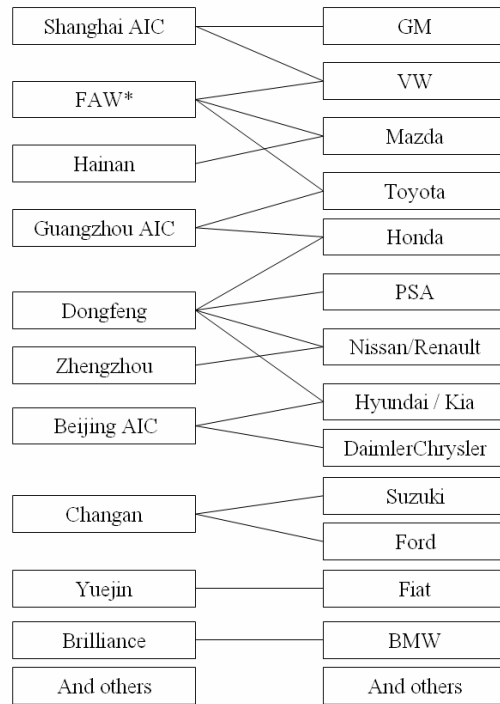
Exhibit 3 Geely Production and Capacity

Production 2005	127,950
Production 2004	86,535
Production 2003	71,555
Production capacity growth 2006	360,000

Source: Catalogue of the Present Chinese Motorcar Production, China Motor Vehicle Documentation Center. 2006.

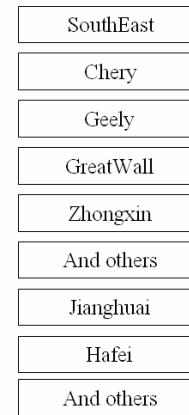
Exhibit 4 Foreign and Chinese Joint Ventures

National government support



* Tiating

Local government support



Source: Case writers

Exhibit 5 Major Chinese Automotive Manufacturers

	Total Sales (unit)	Passenger Car Sales (units)
Companies	2005	2005
FAW	1,013,300	620,886
SAIC	848,542	617,257
Dongfeng	503,308	212,383
BAIC	530,993	173,924
Changan	504,805	157,171
GAIC	209,551	202,066
Chery	105,879	105,879
Brilliance	99,572	19,690
Geely	86,568	86,568
Southeast	60,069	28,693
Yuejing	95,275	26,553
Great Wall	55,091	55,091
ZhongHAOQING	28,114	0
Others
TOTAL	5,070,000	2,320,000

Source: Ravenhill, J., 2006. The Growth of the Chinese Automobile Industry and its Impact on Production Networks; Jianhua, F., 2006. Getting out of First Gear, Chinese auto industry drives into a future featuring innovation and the will to take on the international market. Beijing Review Online; Luo, J., 2005. The Growth of Independent Chinese Automotive Companies. In: International Motor Vehicle Program. MIT.

Exhibit 6 Number of Vehicles per segment (in millions)

Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Truck	0.60	0.63	0.57	0.74	0.84	0.86	0.89	1.09	1.12	1.51
Bus	0.22	0.19	0.27	0.32	0.42	0.58	0.72	0.86	1.00	1.24
Cars	0.34	0.38	0.49	0.51	0.57	0.61	0.70	1.09	2.07	2.32
Total	1.15	1.20	1.33	1.56	1.84	2.05	2.31	3.05	4.19	5.07

Source: Luo, J., 2005. The Growth of Independent Chinese Automotive Companies. In: International Motor Vehicle Program. MIT.

TEACHING NOTE

Geely Motors: A Chinese Automaker Enters International Markets

Detailed teaching notes (TN) will be provided upon acceptance of this case

Case Summary

In 2006, Geely Motors, a Chinese Automotive manufacturer, was the first Chinese company to participate in the International Auto Show in Detroit. This case outlines the Chinese automotive market, compares it to the global market, describes opportunities and threats faced by the Chinese automotive company when it enters competitive international markets. The case also discusses the potential impact of the new entry on the global automotive industry.

Possible Frameworks

The case can be discussed with framework like PEST analysis, Porter 5-forces, SWOT analysis, BCG Matrix, Ansoffs-Matrix, Market Entry Modes, Marketing Mix, Product Life cycle, etc.,

Suggested Student Assignment Questions

Broad Questions (Industry Level)

- How does the entry of Chinese auto makers in the US compare with those in the 1970's for Japanese and in the 1980's for South Korean auto makers?
- How does the competitive landscape change with the entry of Chinese auto makers?
- Should Chinese automotive manufacturers enter smaller, less competitive developing markets, or enter larger more competitive developed markets? Or should they focus on their growing domestic market?

Narrow Questions (Company Level)

- How should Geely Motors enter its chosen market? Provide **quantitative** answers for the market screening and selection (ranking or Likert scale rating). What is the most suitable entry mode for Geely Motors to enter international markets?
- How can Geely Motors compete against existing auto manufacturers? Can they establish a brand in international markets? Which competitive advantage(s) should be their focus?
- What are the opportunities and the challenges facing Geely Motors when entering the US market?

- If Geely Motors were to export their LG-1 or PS4 model, how much would it cost to export each from China to the US? Provide a **quantitative** answer (transportation costs in China, shipment, VAT, insurance, freight, tariffs and taxes, etc.) as well as a description of the type of documents required. At what price might these models be sold in other markets (developed or developing)? How should their product be positioned? How distributed and promoted? (4P's)