
Zejian Li

Abstract: Since 1955, when new China began to reconstruct its automotive industry, and for a long time after, Chinese car exports consisted mainly of commercial automobile products (chassis and finished vehicles, etc.) which were exported in small quantities by state-owned manufacturers. Since 2000, however, with the emergence of independent automobile manufacturers, the number of vehicles exported has increased rapidly, and the makeup of exports has shifted gradually from a focus on commercial vehicles to a focus on passenger vehicles. With regard to overseas expansion, manufacturers’ market access strategy has led to the rapid transition from parts trade to local knock-down manufacturing. However, despite the rapid progress of foreign expansion, problems have arisen due to insufficient risk management know-how with regard to foreign expansion on the part of independent Chinese manufacturers, and the fact that their experience acquired from domestic markets is not applicable to overseas markets. For these reasons, following a period of prosperous overseas expansion, some Chinese automobile manufacturers have been forced to withdraw from one market or have chosen to switch to another market. This entire process, from rapid prosperity to quick decline in Chinese automobile exports, is dramatically observed in the case of their overseas operations in the Russian market. This paper, then, focuses on the burst of growth in Chinese automobile exports around the year 2000, taking the Russian market (the most significant case with regard to the characteristics mentioned above) as a case study to analyse both the domestic and external reasons for this surge, and to investigate the mistakes in manufacturers’ overseas expansion strategies which led Chinese automobile exports from rapid prosperity to quick decline.

Keywords: international business strategy, Chinese automobile industry, overseas expansion, Chery, Russian market

Introduction

An overview of the history of the Chinese automotive industry reveals, as depicted in Figure 1, that following the Reform and Opening policy of 1978, which succeeded the planned economy period, the Chinese automotive industry experienced a period of takeoff in the 1980s and a period of stable growth in the 1990s. However, since the year 2000, the industry has undergone abrupt upheaval.

The market for China’s auto production from 2000 to 2007, as a whole, continued to expand at a double-digit growth rate. In the second half of 2008, due to the influence of the ‘Lehman shock’, many assumed that the automotive industry would enter a recession globally. Although the Chinese market decelerated quickly, it ultimately maintained...
positive growth of 5.02% over the previous year, passing the United States to become the world’s second biggest automobile manufacturing country. In 2009, the market dramatically recovered, recording sales of approximately 6,098,800 units in the first half of the year (a 25.62% increase over the previous year), and continuing to grow at such a fast pace that it is expected to replace Japan in 2009 as the number one automobile manufacturing country.

Another feature of the post-2000 Chinese automotive market is that, aside from its quantitative expansion, it has also exhibited structural changes. The indicator that demonstrates this is the number of exported automobiles. In 2000, the number of Chinese automobile exports topped 20,000 units for the first time, totalling 22,408 units. Following this, China’s participation in the WTO led to an increase in automobile imports; but at the same time, automobile exports proliferated at a rate exceeding that of imports. Finally, in 2005, as measured in unit base, China transitioned from an ‘excess of imports’ to an ‘excess of exports’ both in automobiles as a whole and in basic passenger vehicles (sedans), and became a purely automobile-exporting country.

In 2008, Chinese cars (including chassis) were exported to more than 190 countries (regions) around the world, reaching a record of 680,000 units. The so-called Independent Chinese Automobile Manufacturers took a leading role in the increase.\footnote{In addition to the independent manufacturers as exporters, there is also the foreign-financed, 100% export-only factory, Honda Motor (China) Co., Ltd. In September 2003, its financing was 55% from Honda Motor Co., Ltd.; 10% from Honda Motor (China) Investment Co., Ltd.; 25% from Guangzhou Automobile Industry Group Co., Ltd.; and 10% from Dongfeng Motor Group Co., Ltd. Operations began in 2005, with approximately 24,600 JAZZ units exported in 2006, 43,100 exported in 2007, and 45,600 exported in 2008. However, credit for the majority of exports belongs to the independent manufacturers.} Here, the term Independent Chinese Automobile Manufacturers (hereinafter abbreviated as
Table 1. The overseas manufacturing status of independent manufacturers (March 2007)

<table>
<thead>
<tr>
<th>Company</th>
<th>Year</th>
<th>Expansion (partner) Country</th>
<th>Vehicle type planned</th>
<th>Manufacturing configuration</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yutong Bus</td>
<td>2005</td>
<td>Iran</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Cuba</td>
<td></td>
<td></td>
</tr>
<tr>
<td>BYD</td>
<td>2005</td>
<td>Malaysia (ALADO)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Shaohua Auto</td>
<td>Unknown</td>
<td>Ukraine, Russia, Egypt</td>
<td>Shaohua CEO</td>
<td>SKD,CKD</td>
</tr>
<tr>
<td>Xiamen King Long</td>
<td>2002</td>
<td>India (JCBL)</td>
<td></td>
<td>Fifty–fifty joint venture</td>
</tr>
<tr>
<td>Beiqi Foton</td>
<td>2004</td>
<td>Ukraine, Pakistan</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Suzhou Foton</td>
<td>2006</td>
<td>Thailand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chang’an Auto</td>
<td>2004</td>
<td>Vietnam</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2005</td>
<td>Pakistan</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Geely Automobile</td>
<td>2005</td>
<td>Malaysia (IGC)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Ukraine</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Russia</td>
<td></td>
<td></td>
</tr>
<tr>
<td>JAC Motors</td>
<td>2004 – 2005</td>
<td>Vietnam, Malaysia, Indonesia</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dongfeng Motor</td>
<td>2003</td>
<td>Malaysia</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2005</td>
<td>Iran</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Ukraine (BOGDAN)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Great Wall Motor</td>
<td>2006</td>
<td>Russia</td>
<td></td>
<td>Fully owned *</td>
</tr>
<tr>
<td>FAW</td>
<td>2005</td>
<td>Ukraine (AIS)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Ukraine</td>
<td>Tianjin FAW Xiali Feizi</td>
<td>Unknown</td>
</tr>
<tr>
<td></td>
<td>2007</td>
<td>Russia (AMUR)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Zhongda Bus</td>
<td>2005</td>
<td>UAE (ICP)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Brilliance Auto</td>
<td>2005</td>
<td>Egypt (BAG) Middle East, North Africa</td>
<td>Zhonghua</td>
<td>CKD</td>
</tr>
<tr>
<td></td>
<td>2007</td>
<td>North Korea (joint venture with South Korea PMC)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chery Automobile</td>
<td>2002</td>
<td>Iran (SKT)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2004</td>
<td>Malaysia (ALADO)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Egypt, Indonesia, Ukraine</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Iran (IKCO)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Russia (AVTOTOR)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2007</td>
<td>Argentina (Chery Socma S.A.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Saic Motor</td>
<td>2002</td>
<td>South Korea GMDAT</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2004</td>
<td>South Korea SsangYang</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ZX Auto</td>
<td>2003</td>
<td>South America, North Africa</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Russia</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hafei Automobile</td>
<td>2006</td>
<td>Malaysia (NAZA)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lifan Automobile</td>
<td>2006</td>
<td>Vietnam</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Egypt</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2007</td>
<td>Russia</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sinotruk</td>
<td>2005</td>
<td>Mozambique</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>Mozambique</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: * indicates a plan to implement SKD manufacturing at the end of 2007 and CKD manufacturing at the end of 2009 with full ownership and capital of $70 million, which was rejected by the Russian government.


Independent manufacturers refers to the manufacturers of completed cars which have embraced independent management systems and independent brands by using Chinese capital, with the aim of making cars through independent research and development. With regard to the introduction of products, there are no products introduced by joint venture with foreign capital (Li, 2007b, 2008, 2009b). Chery Automobile and Geely Automobile are representative of such manufacturers. Following these two companies, Brilliance Auto, BYD Auto, Hafei Automobile, JAC Motors, Chongqing Lifan Automobile, Great Wall Motor, and Yutong Bus have also distinguished themselves in
recent years. Beginning with the establishment of Chery Automobile’s Iran KD manufacturing base in 2002, the overseas production of Chinese cars rapidly changed from finished car exports to onsite KD assembly, and as Table 1 shows, independent manufacturers led state-owned manufacturers with lengthy operational experience (such as FAW, Dongfeng Motor, SAIC Motor, and Sinotruk), assuming the vanguard in cultivating overseas markets for Chinese cars.

In comparison with the production of state-owned manufacturers, whose focus is on commercial vehicles, the foreign production of independent manufacturers, whose focus is on passenger vehicles, must be carefully analysed as a new trend indicating structural changes within the history of the Chinese automotive industry. Also, the emergence of independent manufacturers, along with the initiating of exports and overseas KD manufacture of passenger vehicle products, seems to suggest that China will compete in the future with the major manufacturers of the world on a global level (including Japanese manufacturers), and that they have a latent potential to battle for a foothold in the market. Therefore, to understand the current changes in the Chinese automotive industry, and to predict the forms it will take in the future, we must grasp the foreign expansion strategies of independent manufacturers.

Next, I would like to observe in detail the distribution of Chinese cars throughout the world. Figure 2 displays tallies of the total number of Chinese automobile manufacturers, which have expanded into a country’s markets by either manufacturing completed cars or conducting KD manufacturing. As shown in the graph, the three regions of the Near East (primarily Egypt), Southeast Asia (primarily the Philippines), and the Commonwealth of Independent States (CIS) (primarily Russia) are important expansion regions for Chinese automobiles. At a glance, activity seems to be flourishing, but in fact, only a small number of vehicles are sporadically exported to the majority of export destinations; one special characteristic of this situation is that markets, which truly make their presence felt, are few.

Other than the manufacturers of finished cars described above, there are also modified car (body) manufacturers which receive outside supplies of engines and chassis and perform body construction and assembly within the company, or which create unique vehicles through modifications. As they do not possess manufacturing rights for finished cars, these modified car (body) manufacturers are not treated as independent manufacturers in this paper. However, to better grasp the whole picture, we treat them as subjects for analysis together with independent manufacturers. Tianma Auto, Dadi Auto, and Hongxing/Shuanghuan Auto are representative examples.
The Russian market was expected to emerge as the single exception that would change the aforementioned state of affairs. The Chinese forces began entering the Russian market in 2003. In 2007, exports to Russia had increased 189% over the previous year (for a total record of approximately 107,700 units), suddenly putting Russia into the position of the most significant target of Chinese automobile exports. However, in 2008, the number of Chinese cars sold, which had until then continued to increase at a steady rate, suddenly began falling, and in 2009 showed a significant decline (see Table 2).

What exactly happened in the Russian market? In addition, what does the sudden change in exports to Russia tell us about the foreign expansion strategies of independent manufacturers? These questions define the starting point for this paper. As previously described, when seen from the viewpoint of either the number of foreign expansion enterprises or export achievements, the Russian market is the most significant site of Chinese automobile expansion, and when considering foreign expansion strategies, it is a representative market, which demands recognition. Therefore, the challenge undertaken by this paper is to shed light on one aspect of the role of enterprise management and on the strategies employed in the overseas expansion of Chinese automobile products. This paper also focuses on explaining the factors behind the sudden increase in Chinese automobile exports since 2001 through a case study of the expansion of independent manufacturers into Russia.

Firstly, this paper investigates the reasons for the sudden increase in exports to Russia on both the Chinese and Russian sides. Secondly, in order to understand the status of the expansion of independent manufacturers into Russia,

---

**Table 2. Top ten export records by country from 2000–2009 and exports to Russia (unit: vehicles)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Bangladesh</th>
<th>North Korea</th>
<th>Japan</th>
<th>America</th>
<th>Myanmar</th>
<th>Sudan</th>
<th>Hong Kong</th>
<th>Indonesia</th>
<th>Turkey</th>
<th>CR10</th>
<th>Russia (rank 60)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>22408</td>
<td>3830</td>
<td>2721</td>
<td>1894</td>
<td>1675</td>
<td>1564</td>
<td>1531</td>
<td>1366</td>
<td>630</td>
<td>412</td>
<td>80.23%</td>
<td>12</td>
</tr>
<tr>
<td>2001</td>
<td>15481</td>
<td>10431</td>
<td>2109</td>
<td>397</td>
<td>388</td>
<td>295</td>
<td>245</td>
<td>231</td>
<td>25</td>
<td>22</td>
<td>99.78%</td>
<td>Russia (rank 38)</td>
</tr>
<tr>
<td>2002</td>
<td>21914</td>
<td>3664</td>
<td>2079</td>
<td>1330</td>
<td>1172</td>
<td>1073</td>
<td>998</td>
<td>797</td>
<td>709</td>
<td>655</td>
<td>65.84%</td>
<td>Russia (rank 44)</td>
</tr>
<tr>
<td>2003</td>
<td>42224</td>
<td>7092</td>
<td>6064</td>
<td>3745</td>
<td>3291</td>
<td>1882</td>
<td>1515</td>
<td>1383</td>
<td>1045</td>
<td>966</td>
<td>73.74%</td>
<td>Russia (rank 23)</td>
</tr>
<tr>
<td>2004</td>
<td>75999</td>
<td>7092</td>
<td>11144</td>
<td>3275</td>
<td>3275</td>
<td>2435</td>
<td>2425</td>
<td>2148</td>
<td>1704</td>
<td>1686</td>
<td>70.41%</td>
<td>543</td>
</tr>
</tbody>
</table>

Note: Chassis are included in the total number of vehicles exported in each year; however, non-completed cars such as 'trailers and semi-trailers', 'tractors', off-road 'other passenger vehicles', and 'other' are not included.

Source: CATARC.
the status of the expansion of Chinese cars into Russia will be explained with regard to separate groups. Finally, those portions linked to the overseas expansion of independent manufacturers will be singled out from among the factors leading to the sudden drop in exports to Russia, followed by a conclusion of this assessment.

2. Analysis of the factors behind the sudden increase in automobile exports to Russia

(1) Factors on the demand side (Russia)

To analyse factors on the demand side, we will look into the special characteristics of the Russian market. Firstly, since 2001, in the wake of the 1998 financial crisis, the Russian economy has consistently maintained an economic growth rate of around 5%. The per-capita GDP (PPP) was $4,086 in 2004, but in just three years it approximately doubled, reaching $8,612. This sustained economic growth provided support for the increased demand for automobiles. Secondly, under the transitional economy which followed the collapse of the Soviet Union, the average age of cars increased due to the worsening economic situation and a drastic increase in used car imports, with the majority of cars more than ten years old still retained by owners. As of October 2008, in Vladivostok (the city with the highest number of retained passenger vehicles), vehicles more than ten years old comprised 80% of the total number of retained vehicles, with the statistic for Moscow and Saint Petersburg reaching a plateau at 37% and 38%, respectively. There was strong potential demand for replacements. Therefore, along with the gradual increase in personal incomes in recent years, motorisation made rapid progress in the Russian market, which came to be regarded as the most promising and the one in which automobile manufacturers worldwide planned to participate.

(2) Factors on the supply side (China)

Factors related to manufacturing—liquidation policies regarding overproduction caused by the cooling of the Chinese market

The scale, techniques, products, and sales networks of the independent manufacturers which emerged around 2001 are all inferior to those of the foreign capital joint-venture manufacturers which preceded them. Fortunately, motorisation began in China in 2002, and the country has been favoured by a rapidly expanding market (Figure 1) in which new car sales have increased by one million units each year. Thus, independent manufacturers were able to temporarily stabilise operational systems, and the scale of manufacturing continued to increase rapidly. However, the market cooled drastically in 2004 due to monetary tightening policies, and it suddenly became clear that those facilities enlarged during the boom period represented excessive capacity. As a result, independent manufacturers began paying serious attention to exports as a measure for stabilising operational systems. Also, foreign capital joint-venture automobile manufacturers had already included the Chinese market in their global strategies, and their focus lay mainly in responding to local needs. Consequently, there was a lack of incentive to export vehicles from China to Third World countries. Thus, the drastic increase in exports since 2004 was caused mainly by exports from independent manufacturers.

Above, I have explained the process by which the distress immediately following the emergence of independent manufacturers increased their motivation to export, but the question of why so many independent manufacturers were able to expand quickly into Russia still remains. To preview the conclusion, this occurred because powerful firms with wide-ranging personal connections in both China and Russia emerged, specialising in automobile exports and simultaneously bringing into play transactional functionality, transportation functionality, and information functionality, conforming well to the needs of both China and Russia.

---

3 IMF Database, Russia: Gross domestic product per capita, current prices (U.S. dollars). The figure for 2007 is a prediction. Incidentally, the figure was $6,897 for 2006.
6 Honda Motor (China) Co., Ltd., is an exception. For details, see Footnote 2.
Factors related to international exchange—the emergence of companies specialising in Chinese automobile exports

Firstly, we will examine the process by which these specialized export companies were established.

When Zhu Jingcheng, a Chinese diplomat stationed in Russia, became involved in the Russian expansion of a Chinese telecommunications company while in office in 2002, he received a proposal from the Russian side and began paying attention to the business of exporting automobiles to Russia. In the same year, he became aware of roughly 100,000 RMB pickup trucks manufactured by ZX Auto in Beijing, sensed the possibility of exporting them to Russia, and began seriously considering this. In 2004, he established a company specialising in automobile exports known as Siberian (Сибирь) Automobile Export (Beijing) Co., Ltd. (abbreviated below as ‘Siberian’), immediately appealed to a Russian dealer (Company A) which had been handling used Japanese and German-made cars for many years, and began working with them on exporting Chinese cars to Russia. In November 2004, a pickup truck by ZX Auto became the first Chinese car successfully exported to Russia.5

Secondly, we will examine the role played by Siberian.

At the corporate level, Siberian acted as a bridge and provided many opportunities for interaction between Chinese and Russian automobile manufacturers and related businesses (see Table 3). Although China and Russia have the benefit of geographical proximity, few independent manufacturers saw the latent attraction and possibilities of the Russian market. In general, the effects of the ideological conflict which occurred between the two countries during the Soviet period still lingered; further, Russian language education had been declining in China since the reform and opening policy, so it would seem that these two countries which were so close geographically were, in fact, psychologically distant. This state of affairs can also be seen in the low number of automobile exports to Russia until 2003 (see Table 2). However, this state of affairs suddenly changed with the establishment of Siberian. As well as the exports to Russia by ZX Auto, reports from the Russian mass media about the expansion of Chinese cars and information about the Russian market reached China en masse through the window of Siberian, at once arousing the interest of independent manufacturers.

In addition, at the industrial level, Siberian enjoyed a favorable position because of founder Zhu Jingcheng’s personal connections with the political world and with individuals in the business world in both China and Russia. Other factors favoring it were its familiarity with Russian culture/business customs as well as its numerous employees proficient in Russian, and, as described later, its having established the certification system for Chinese cars in the Russian market.9 When Siberian facilitated the export of ZX Auto pickup trucks to Russia, the number one barrier was model certification. As there was no precedent, creating associated rules was the largest obstacle. With regard to the model certification of imported automobiles, Russia continues to use a multinational agreement approved in 1958, the ‘Agreement on Uniform Technical Prescriptions for Vehicles’ from the United Nations/Economic Commission for Europe (UN/ECE). However, as China is not affiliated with this ‘1958 agreement’, as it is popularly called, the Russian side refused to accept the automobile inspection test approval certificates issued by China, insisting that when Chinese cars were imported, all certification inspections had to be conducted at the Russian National Automobile Standards Certification Centre (ГУП НИЦИАМТ). In addition, in Russia, the image of Chinese industrial development had not changed for decades, and Zhu Jingcheng said that this outdated notion was another main cause of the obstacles. In Russia, the Chinese continued to be ridiculed with statements such as, ‘The Chinese are going to the moon on a bicycle (since all they can make is bicycles, they have no choice but to use bikes no matter where they go).’ For this reason, Russians mistrusted not only the quality of Chinese cars, but also the testing and certification capacity of the Chinese. In order for the pickup trucks made by ZX Auto to receive export certification inspections, Siberian went to great trouble, providing translated documents, explaining manufacturing conditions and so on, and because of the exertion of actually going to Russia a number of times, the certification was received after 18 months. Based on the ZX example, Zhu Jingcheng realized that fully following the process insisted upon by Russia and translating submitted

---

7 This company has established five divisions, exporting Chinese cars to Russia and the CIS countries as well as North Africa.
8 Before ZX Auto pickup trucks were exported to Russia, sales and purchases of Chinese cars were performed by individuals in the form of a border trade, but these are not counted because the quantities were extremely small.
9 Except in cases of a specific refusal, the description of Siberian here is based on interviews conducted by the author in August 2007 and April 2008.
documents, transporting vehicles for testing, and so on, required enormous time and expense. In addition, the outdated notions made it necessary to spend an unforeseen amount of effort explaining the situation on the Chinese side, so he concluded that it would be difficult to change the state of affairs unless he could dissolve the Russians’ mistrust. In July 2004, Zhu Jingcheng extended an invitation for personnel from the Russian National Automobile Standards Certification Centre to visit ZX Auto and the Chinese National Automobile Quality Supervision and Inspection Testing Centre. In other words, he began devising tactics to get rid of the outdated notions held by the Russians. As a result, the Russian National Automobile Standards Certification Centre accepted the inspection certification results from the Chinese National Automobile Quality Supervision and Inspection Testing Centre, and consented to proxy applications by Siberian. These efforts by Siberian reduced the time required for the certification procedure from the original 18 months to 2–4 months, breaking through the most difficult barrier to exporting Chinese cars to Russia. Also, as a trading company, Siberian not only mediated transactions but acted as a window for disseminating information, becoming involved in the Russian domestic distribution business, and performing the inventory and transport functions needed by independent manufacturers when exporting to Russia. In addition, Siberian made use of the advantageous position described above, established two assembly bases of its own in the European and Asian regions, and began conducting KD manufacturing of SUVs branded ‘Siberian-Dadi’.

In general, Siberian overcame the factors behind the information-related, language-related, and distribution-related obstacles, achieved congruence between Russian needs and independent automakers’ motivation to expand abroad, and initiated the export of Chinese cars to Russia. The same company’s efforts made it possible for numerous independent manufacturers to enter the Russian market all at once.10

### Table 3. Projects by SAEC

<table>
<thead>
<tr>
<th>Year</th>
<th>Cooperative enterprise</th>
<th>Activity details</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>ZX Auto</td>
<td>Exports to Russia</td>
</tr>
<tr>
<td>2004</td>
<td>Zhongtong Bus</td>
<td>Pioneering the Russian market</td>
</tr>
<tr>
<td></td>
<td>Tianma/Dadi</td>
<td>CDK assembly/provision of parts in joint venture with Derways Company</td>
</tr>
<tr>
<td></td>
<td>Chery Automobile</td>
<td>Mediating a CKD assembly project in Siberia</td>
</tr>
<tr>
<td>2005</td>
<td>Avtotor</td>
<td>Introducing Beijing Automobile and Nanjing Automobile as candidates for cooperation</td>
</tr>
<tr>
<td>2007</td>
<td>AMUR</td>
<td>Promoting exports by ZX</td>
</tr>
<tr>
<td>2008</td>
<td>Rolf and Geely Automobile</td>
<td>Mediating/promoting five-year contract to export 200,000 vehicles</td>
</tr>
<tr>
<td></td>
<td>Wuzhoulong/Changzheng</td>
<td>Exporting Wuzhoulong buses/Changzheng trucks to Russia</td>
</tr>
</tbody>
</table>

Source: Based upon interviews conducted from 2007 to 2008 with Siberian Automobile Export (Beijing) Co., Ltd.

3. Independent manufacturers’ expansion into Russia

In 2003, efforts by Siberian opened the Russian market to Chinese cars, and so far, some twenty manufacturers of passenger (commercial) vehicles have expanded into Russia (see Table 4). However, as the abilities, entrance timing, and positioning of products within the Russian market differ for each manufacturer, Russian expansion has taken many diverse forms. Below, manufacturers are separated into four groups: the early lower ranked group, the early top group, the late top group, and the late lower ranked group (see Table 5), based on entrance timing and manufacturer scale (see the number of cars manufactured in 2007 in Table 4). The focus is placed on representative businesses from each group, and the differences in the expansion strategies and special characteristics of each group are presented in order.11

---

10 Even a manufacturer like Great Wall Motor, which had no direct point of contact with Siberian, certainly indirectly benefited from Siberian’s activities, such as introductions into the Russian market and the model certification system.

11 Of course, it is difficult to draw absolute lines, and there is much scope for investigation. Here, as is popularly recognized, the question of whether a manufacturer has a manufacturing record of 100,000 vehicles a year is used as the standard for recognising its scale. Similarly, 2006 (the year when the route for expansion into Russia became fairly clear) is used as the standard for
Table 4. Sales records for Chinese cars in the Russian market (unit: vehicles)

<table>
<thead>
<tr>
<th>Company</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>Total of left</th>
<th>Total production in 2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chery</td>
<td>476</td>
<td>12,242</td>
<td>3,7120</td>
<td>15,728</td>
<td>4,914</td>
<td>70,480</td>
<td></td>
<td>387,880</td>
</tr>
<tr>
<td>Great Wall</td>
<td>4070</td>
<td>4,788</td>
<td>6,238</td>
<td>8,324</td>
<td>2,490</td>
<td>25,910</td>
<td></td>
<td>122,605</td>
</tr>
<tr>
<td>BYD</td>
<td>152</td>
<td>1,694</td>
<td>2,566</td>
<td>5,341</td>
<td>1,001</td>
<td>10,754</td>
<td></td>
<td>100,376</td>
</tr>
<tr>
<td>Hafei</td>
<td>1,523</td>
<td>2,246</td>
<td>512</td>
<td>-</td>
<td>-</td>
<td>4,011</td>
<td></td>
<td>198,776</td>
</tr>
<tr>
<td>Geely</td>
<td>3,721</td>
<td>3,780</td>
<td>7,681</td>
<td>15,182</td>
<td>2,16774</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Brilliance</td>
<td>339</td>
<td>510</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>869</td>
<td></td>
<td>128,270</td>
</tr>
<tr>
<td>FAW Commercial</td>
<td>1780</td>
<td>2,989</td>
<td>1,643</td>
<td>-</td>
<td>6,412</td>
<td>19,2399</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Derways</td>
<td>681</td>
<td>710</td>
<td>-</td>
<td>-</td>
<td>1,391</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ZX Auto (Tianye)</td>
<td>260</td>
<td>1,610</td>
<td>96</td>
<td>1,303</td>
<td>694</td>
<td>4,029</td>
<td>40,480</td>
<td></td>
</tr>
<tr>
<td>Dadi</td>
<td>123</td>
<td>246</td>
<td>1,097</td>
<td>-</td>
<td>-</td>
<td>1,466</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Tianma</td>
<td>210</td>
<td>67</td>
<td>56</td>
<td>-</td>
<td>333</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Xinkai</td>
<td>425</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>425</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Shuanghuan</td>
<td>20*</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lifan</td>
<td>300</td>
<td>4,755</td>
<td>2,673</td>
<td>7,728</td>
<td>30,362</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changfeng</td>
<td>25</td>
<td>12</td>
<td>-</td>
<td>-</td>
<td>37</td>
<td>2,578</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total of above</td>
<td>260</td>
<td>6,856</td>
<td>22,990</td>
<td>5,8807</td>
<td>41,375</td>
<td>18,759</td>
<td>149,047</td>
<td></td>
</tr>
</tbody>
</table>

Notes:
1) One portion of the record for 2007 consists of estimates created by doubling the figure for the first half of the same year, and these are indicated with a * mark.
2) Other than the above manufacturers, Beijing Automobile, Foton, Fuqi Huaxiang, King Long, Nanjing Yuejin, Southeast Motor, and other manufacturers also export, but are not counted in the Russian statistics.
3) A portion of Derways projects consists of CKDs from Siberian-Dadi, SGI, Tianma, Beijing Automobile, and Huanghai Automobile.
4) Manufacturers in the shaded areas are not manufacturers of completed cars but modified car manufacturers which receive outside supplies of engines and chassis and produce unique vehicles.
5) Due to in-transit inventory and dealer inventory, there is a disparity between the number of vehicles exported to Russia from China (the number of vehicles received) each year and the number of vehicles actually sold in Russia.


Table 5. Group divisions among independent manufacturers in the Russian market

<table>
<thead>
<tr>
<th>Manufacturer scale</th>
<th>More than 100,000 units</th>
<th>Less than 100,000 units</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Early top-ranked group</strong></td>
<td>(Chery, Great Wall Motor, BYD, Hafei Automobile)</td>
<td>(Body manufacturers such as Dadi Auto, Tianma Auto, Xinkai Auto, Derways, and Shuanghuan Automotive; commercial vehicle manufacturers such as ZX Auto and FAW Commercial Auto)</td>
</tr>
<tr>
<td><strong>Late top-ranked group</strong></td>
<td>(Geely, Brilliance)</td>
<td>(Shuanghuan Auto, Lifan Automobile, Changfeng Motors, etc.)</td>
</tr>
</tbody>
</table>

Source: Created by the author.

distinguishing entrance timing. Table 4 displays these groupings divided by horizontal and vertical lines.
(I) The early lower-ranked group—the expansion of ZX Auto

This group includes manufacturers who entered the market in 2006 or before with a production of fewer than 100,000 units per year. It includes ZX Auto and FAW Commercial Auto as well as modified automobile manufacturers Dadi Auto, Tianma Auto, and SG Automotive, which provided CKD parts to Xinkai Auto and Derways. In terms of its environment, FAW Commercial Auto, which focused on commercial vehicles, differed from passenger vehicle manufacturers in that its production was generally on a smaller scale than that of other manufacturers. Other companies in this group concentrated on producing pickups and supplying the low end of the SUV market, in which vehicles sold for less than 100,000 RMB. Moreover, many of these products were reconfigured copies of pre-existing products with a high degree of resemblance to the originals. ZX Auto is a representative example.

ZX Auto’s expansion into Russia

For ZX Auto, the first Chinese automobile manufacturer to successfully expand into Russia, this opportunity arose by chance. In 1999, Zhu Jingcheng, who had been living in Russia for approximately ten years, transferred to the China Institute of International Affairs International Business Inquiry Centre, continuing his involvement in Chinese–Russian exchange. Apart from the demands of the Russians described above, Zhu Jingcheng also sensed the sudden increase in demand for vehicles, which came with economic growth. Particularly in 2002, the demand for used cars began to shrink with the implementation of the Russian government’s used car regulation policy, and the demand for new cars suddenly began to rise. Zhu Jingcheng sensed the possibility of introducing attractively designed, inexpensive Chinese cars of uniform quality into Russia as a substitute for imported used cars. At the time, a used 1998 Toyota pickup sold for $16,000 in Russia, and a new Mitsubishi sold for a much higher price of $22,300–$28,500. In 2003, Zhu Jingcheng happened to see a pickup truck by ZX Auto on display in Beijing. He was convinced of the possibility of exporting a ZX Auto pickup truck priced around 100,000 RMB ($15,000) to Russia. In May 2003, together with a Russian dealer friend who had handled German cars and imported Japanese used cars for many years, Zhu Jingcheng visited Baoding city, Hebei province—known in China for its large amount of pickup truck production—and began negotiating. On 30 May, he signed a contract to export 506 ZX Auto ‘Admiral’ pickup trucks.

ZX Auto was established in 1949 as Baoding Auto Manufacturing, and was later reorganized as Tianye Auto, a large-scale, state-owned enterprise. In 1992, it suddenly became famous for selling the first pickup truck in the Chinese market for 48,800 RMB. However, the small profits were not enough to cover high operating costs, and the company became unprofitable. In 1999, Brilliance Auto provided capital, restarting the enterprise as a joint venture called Hebei ZX Auto Manufacturing Co., Ltd., with 60% of capital contributed by Brilliance Auto and 40% contributed by Tianye Auto Group. In 2002, when Brilliance Auto’s business began to decline, Brilliance Auto became a subsidiary of Zhejiang Huaxiang Group when Zhejiang assumed its shares. In 2003, ZX Auto acquired the right to manage itself independently from Zhejiang Huaxiang Group, and continued to operate with its focus mainly on pickup trucks (ZX Lightweight Automobile Manufacturing) and SUVs (ZX Passenger Automobile Manufacturing). It started exporting earlier than other companies did. In 2000, it began by exporting 500 vehicles to Iraq, and went on to pioneer new export markets in Egypt, UAE, and Vietnam. Not only did it record sales of 28,701 units in 2003, it shone as the year’s top exporter, with 7,126 units. Later, however, they struggled to reach annual sales of 30,000, and the number of units exported peaked at around 10,000, showing no further progress. When exports to Russia began, the first Chinese vehicle to arrive—ZX’s Admiral Pickup truck—was sold for $16,900 and basked in the limelight. Later, a change in strategy from finished car exports to CKD exports was planned, but not completed. In 2005, Avtotor Russia agreed to 75,000 CKD exports over five years, but this plan also never became reality. In 2006, problems occurred regarding product quality and an inadequate after-sales service network, and, on losing the price war that ensued when Great Wall Motor expanded into Russia (cementing ZX’s decline), ZX Auto was forced to withdraw. In 2007, ZX plotted a return

---

12 Except in cases otherwise noted, the description here is based on the internal Siberian document, ‘The Path of Chinese Vehicles into Russia’.  
13 In order to limit these used car imports that had been increasing since 2002, the Russian government revised the original usage time limit from seven years to five, and greatly increased import duties. The cost of new cars began to fall, and the gap with used cars shrank. For instance, a 1600 cc Ford or a 2000 cc Hyundai Sonata cost $16,000, while a new imported 1600 cc AT Mitsubishi cost just $18,000. As the attraction of used cars decreased, the $10,000–$20,000 market went into gear.
to Russia, completing an SKD trade assembly agreement with Amur Russia for 3,500 Grand Tiger pickup trucks. Unfortunately, as its application to be registered under the terms of the favorable ‘Industrial Assembly’ policy, popularly called as Government Ordinance 166, was rejected, implementation of the agreement was suspended.

In general, exports to Russia by lower-ranked manufacturers (who mainly sold highly similar, low-priced pickup trucks and SUV products) tended towards over-reliance on Siberian. Most of the manufacturers (which were even smaller than ZX Auto) were so-called body manufacturers which lacked the capability to produce completed cars, and they sold and exported parts to Siberian at the lowest level of participation in Russian expansion—the CKD parts trade. Siberian would then assemble the parts as local brands it owned at the factory of a local Russian manufacturer (Derways Russia) and sell the vehicles. (For instance, Dadi Auto did this.) Due to lack of technical capability, all businesses, which belonged to this group, have now withdrawn from the Russian market.

We will describe only the unique characteristics of the overseas expansion strategies of this group. Exports of products requiring low technical skill (copies/imitations) relied completely upon trading companies, and sales distribution (as well as after-sales service) was left entirely to trading companies, so that sales based solely on a pure ‘parts trade-based export method’ uniquely characterized the overseas expansion strategy of this group. This method of overseas expansion, that is, the parts trade method, in which expansion relies upon low prices and the manufacturer disappears as soon as problems arise, is most easily linked to a ‘cheap but bad’ image and must be called a ‘cancer’ on the overseas exports of Chinese cars. A similar expansion method was seen in the expansion of Chinese two-wheeled vehicles into the Vietnamese market. As long as this problem remains unsolved, it will continue to have a negative influence on the foreign expansion of all Chinese cars.

(2) The early top group—the expansion of Great Wall Motor/Chery Automobile

This group includes manufacturers which entered the market in 2006 or before with production of more than 100,000 vehicles per year. It includes Chery Automobile, Great Wall Motor, BYD Auto, and Hafei Automobile.

**Great Wall Motor’s expansion into Russia**

Like ZX Auto, Great Wall Motor, located in Baoding city, Hebei province, was established in 1984 as a car conversion maker belonging to Great Wall Industries Co. In 1990, Great Wall Industries Co. had become unprofitable, and Wei Jianjun entered as a contractor to reorganise the company. In 1998, as Great Wall made the transition to a publicly traded company, Wei Jianjun’s management performance up to that point was highly praised, and the company’s stock was transferred to him. Later, Wei Jianjun used the IPO to successfully gain ownership of more than 40% of Great Wall Motor’s stock, and the company was privatised. Under Wei Jianjun, Great Wall transitioned from its original core business of producing oil tank cars to modifying buses and lightweight trucks; and in 1996, the decision was made to enter the world of the pickup truck business. In 1998, the number of pickup trucks manufactured and sold exceeded 7,000 units, and it promptly took the top spot in the business. Later, it pursued a combination of new products development and reforms, and has now become the number one manufacturer of pickup trucks and SUVs, with the number of units produced annually topping 100,000 units. In 1998, it began by exporting 240 units to Iraq, and continued expanding its foreign market to North Africa in 2000, Central and South America in 2003, and Russia in 2004. In 2007, the number of vehicles it exported topped 50,000 units, making it one of the top-ranked exporting companies.

Great Wall Motor’s expansion into Russia was in response to its learning of competitor ZX Auto’s expansion there; it quickly followed up by planning to enter the market through investment in the pickup truck product ‘Deer’ and the SUV ‘Safe’ ($16,000). In 2006, to reduce costs, a plan was made to establish an assembly factory in the Russian Federation Republic of Tatarstan, and an attempt was made to begin local production, but as the application for the favourable ‘Industrial Assembly’ policy was rejected, the plan was halted. Currently, exports to Russia consist of completed cars.

---

14 Great Wall Motor’s ‘Great Wall Motor’s opportunities and challenges in a globalized market’ document distributed at the 2007 China Automotive Export Conference.
Chery Automobile’s expansion into Russia

When Siberian introduced Russian buyers to Chinese automobile manufacturers, Chery Automobile was one of the candidates. In April 2004, Siberian signed an agreement to cooperate in Chery Automobile’s cultivation of the Russian market. With this, Chery Automobile’s expansion into Russia officially began. Also in 2004, once 476 completed cars were exported, the company began investigating local production possibilities. In 2005, through the mediation of Siberian, Transservice, the parent company of Pekinsky Jeep16 (the first dealer of Chinese cars which became involved in importing from ZX Auto), agreed to conduct CKD manufacturing of Chery’s SUV, Tiggo, by establishing a factory in Siberia’s capital city Novosibirsk. Also, the companies established Chery Automobile as a joint venture, and began trial production while applying for the favourable ‘Industrial Assembly’ policy. However, as the Russian customs policies stipulated that imported parts which were ultimately to be assembled as finished vehicles would be assessed for taxes at the same rate as completed cars, the cost of the first 100 vehicles assembled via KD was even more expensive than that of imported finished vehicles. Chery Automobile realised that assembling vehicles in Siberia was thus unprofitable.

Avtotor—a business group in which a deputy prime minister of the former Soviet Union, Vladimir Scherbakov, has had 100% ownership since 1991—is involved in diverse businesses including agriculture, industry, and banking. It has used its advantages17 in terms of industrial promotion policies, as a company in the Special Economic Zone in Kaliningrad, to create knockdowns of Kia as well as of BMW, GM Chevrolet, and Hummer 2 vehicles. However, the company experienced a severe conflict with SOK Group Russia over the acquisition of assembly qualifications for Kia vehicles, and preparing for failure in acquiring these qualifications, it decided to fill the gap by using its spare manufacturing capacity to assemble Chinese cars. In 2005, through Siberian, Avtotor visited Beijing Automobile, Nanjing Automobile, and ZX Auto, exploring the possibility of cooperation and agreed to KD production of Nanjing Auto’s Yuejin truck and ZX Auto’s pickup trucks. Since Chery Automobile was in negotiations with Transservice, Siberian did not dare introduce Chery to Avtotor. However, Chery Automobile, understanding the importance of legally avoiding customs duties through the privileges enjoyed by Avtotor, wished to form a partnership with that company. In November 2005, Chery Automobile began secret negotiations with Avtotor regarding onsite KD production, and a contract was drawn up in January 2006. Then, on 24 April, locally assembled Chery brand cars were taken offline. Both companies looked at the sales records and agreed to use a total of $200 million of additional capital to establish a new factory. The partnership with Transservice was halted. With this, Chery Automobile used the Kaliningrad manufacturing site to sell 37,000 vehicles in 2007, rapidly increasing its presence in the Russian market. However, in March 2008, due to the decline of the dollar (Avtotor’s operating currency), the company announced that it was putting a halt to the KD manufacturing of Chery cars.18 When this occurred, sales of Chery Automobile vehicles fell rapidly (Table 4). In August 2008, Chery Automobile announced that it would begin local production again in partnership with TagAZ Russia, but it is unlikely to be shielded from customs duties as was the case in its partnership with Avtotor.

A special characteristic of this group is that, in general, when independent manufacturers belonging to it planned

---

15 Regarding the introduction of Chery Automobile, see Li (2007a, 2007b). Except stated otherwise, this is based on two interviews with Siberian Automobile Export (Beijing) Co., Ltd., President Zhu Jingcheng in August 2007 and April 2008, the internal Siberian document ‘The Path of Chinese Vehicles into Russia’, and content posted to the Siberian Website.

16 The name of the Pekinsky Jeep Company has been translated in China as ‘Beijing Jeep (Zhongshin)’ and in Japan as ‘Beijing Jeep (Centre)’; this company has no relationship with the automobile manufacturer Beijing Jeep Group. As described earlier, the dealer Company A, which was on friendly terms with Zhu Jingcheng from Siberian and was the first to become involved in ZX Auto imports, later defaulted on its contract. Company A established Pekinsky Jeep to continue the contract. The head of Pekinsky Jeep’s import division is the same as the head of Company A. Consequently, when Chery Automobile expanded into Russia, reports stating that it used the sales network of ‘Beijing Jeep’ were essentially erroneous; in fact, it used Pekinsky Jeep’s sales network.

17 Speaking only in regard to automobile manufacturing, the policy was designed to invite investment, so as to raise the local supply rate to 50% over five years, and allow the levelling of zero-duty imports of automobile parts.

18 Avtotor seemed obviously insincere in its explanation. As ‘the decline of the dollar/the rise of the rubble’ would reduce the price of CKD imports calculated in dollars, this would in fact have been an unparalleled opportunity for Avtotor. Underlying the halting of production were appeals to the Russian government by other domestic firms in the same industry to do away with Avtotor’s uniquely favourable tax status. To maintain this uniquely favourable tax status, Avtotor had to stop assembling Chinese cars. Also, in May of that year, Avtotor halted production of the Chinese Yuejin truck, which had made up only 1% of the cars it produced, apparently attempting to improve its situation by hurriedly distancing itself from the production of Chinese cars.
expansion into Russia, they did not rely too much on Siberian but were able to maintain a certain degree of independence. Of course, the certainty of this independence must be considered separate from success at expanding into Russia. Although it did not succeed, the plan for factory construction put into place at the time of expansion shows that the overseas expansion plan of this group was ‘Greenfield-esque’. By using every possible method, the early manufacturers somehow managed to survive in the Russian market. However, the situation was not necessarily pleasant. The reasons will be described later, but it is felt that there were problems with the risk management of independent manufacturers regarding the method of expansion as well as method options.

(3) The late top group—the expansion of Geely Automobile

This group includes manufacturers which entered the market after 2006 with production of more than 100,000 vehicles per year. It includes Geely Automobile and Brilliance Auto.

*Geely Automobile’s expansion into Russia*[^19]

In 2007, Geely Automobile independently signed a contract for KD production with Amur, which had been conducting KD production of Siberian’s ‘Siberian-Dadi’ brand SUVs. In 2007, it planned to produce 17,000 Otaka cars. However, transportation to the Ural region, where Amur is located, is extremely inconvenient, making it difficult to fulfil the KD manufacturing contract.

The Russian company Rolf is the largest group importing and selling foreign cars, dealing in thirteen foreign-branded vehicles. In 2007, it was involved in importing and selling Mitsubishi, Hyundai, Mazda, Ford, Mercedes, Audi, and Peugeot cars, and with yearly sales of $3 billion, it qualified as a megadealer. In 2007, through the Russian Business Society and the Chinese consulate in Russia, the company expressed a desire to import $1 billion worth of Chinese passenger vehicles. At first, FAW and SAIC Motor were mentioned as candidates, and Geely Automobile was added as a candidate on the recommendation of a friend of Zhu Jingcheng. Then, Siberian investigated Geely Automobile on its own, gained confidence in exporting Geely Automobile’s cars, and made it the number one candidate. Once individuals on the Russian side had been invited several times to Geely Automobile and persuaded, a contract was established to export 200,000 units over five years—$1.5 billion worth of completed cars. Geely’s creating this partnership with a powerful local importer helped it to successfully counteract difficulties encountered in expansion, such as channel maintenance and provision of after-sales service. Also, it can be said that since cars assembled in China were higher in quality than cars assembled onsite in Russia, a favourable environment had been prepared for expansion. Currently, the export of completed cars by Geely Automobile to Russia is viewed as a very promising project. This group’s overseas expansion strategy is still stuck at the stage of ‘exporting completed cars’, but in that it exports original products with full-scale after-sales service (when compared with the previously mentioned ‘parts trade-based expansion method’), the expansion pattern of this group is relatively favourable in terms of competitive position.

(4) The late lower-ranked group—the expansion of Lifan Automobile

Lastly, we will take a brief look at the late lower-ranked group. This group includes manufacturers which entered the market after 2006 with production of fewer than 100,000 vehicles per year. It includes Lifan Automobile and Shuanghuan Auto. Because the reputation of ‘cheap and bad’ had already been established for the Chinese cars produced by the late lower-ranked group because of early manufacturers, it is easy to imagine that the independent manufacturers in the late lower-ranked group operate in a more trying environment. Young manufacturers like Lifan Automobile, Changfeng Motors, and Shuanghuan Auto could not find their way into the market on inexpensive prices alone. They needed another strategy in order to break into the market.

[^19]: Regarding Geely Automobile, unless otherwise noted, the description here is based on the same content as that listed in Footnote 12 and Li (2007a, 2008).
Lifan Automobile’s expansion into Russia

Lifan Automobile, as an important manufacturer of two-wheeled vehicles, was allowed to enter into passenger vehicles manufacturing (which it had long wished to do) in 2005. Due to its late entrance into the market, it adopted a growth plan which emphasised both domestic sales and overseas exports from the beginning. In 2007, it was already exporting to 20 countries. To facilitate its entrance into the Russian market, in February 2007, Lifan Automobile entered into a three-party agreement with the Russian companies Derways and AutoMir in which KD parts from Lifan Automobile were assembled at Derways and sold by AutoMir. In 2008, it began to construct the welding and painting facilities it had requested under Government Ordinance 166, and it aims to achieve full local production by 2010.

Although Lifan Automobile made a late entry, it is the most discussed Chinese car manufacturer in Russia today. The reason is that in November 2007, the Lifan 520, which is being produced as a knock-down, passed the safety inspection conducted by Russian authorities. In 2007, the influential Russian car magazine AvtoRevu conducted a crash test using automobiles manufactured by Chery Automobile, and reported that ‘the results were the worst seen in the last three years’. However, the approval rating of the Lifan 520 is perceived as an opportunity to recover the trust of Russian consumers towards Chinese-made vehicles as regards safety. In this way, the late lower-ranked group were able to gain the high-quality image the original early independent manufacturers were unable to establish among Russian consumers and appeal to the latter other than on the basis of price. The price was set at $9,000–$14,000, making it possible to distinguish between this and products from Russian local manufacturers, which, it would seem, meant that one chance still remained for Lifan to penetrate the Russian market. However, as described later, Government Ordinance 745 increased KD manufacturing costs by 10%, and Lifan Automobile was forced to react.

4. How should Russian expansion by independent Chinese manufacturers be evaluated?

(1) Analysis in terms of expansion timing

Firstly, we will examine expansion timing. In 2003, the emergence of the previously mentioned Siberian made it easier for all independent manufacturers, regardless of scale, to expand into Russia. Also, around 2003, the family cars (less than $10,000) that made up 80% of the Russian market became a significant factor spurring on expansion (see Figure 3).

The fact that Chery Automobile’s Amulet was at one time sold for $9,000 and became popular was also due to the ever-present demand for family cars. It can be said that, for a time, the company was blessed by a large number of owners who emphasised price over quality. However, with economic growth, the scale of the family car market shrank as the years went on, and in 2007 it shrank to less than 30% of the market (see Figure 3). The management ability of independent manufacturers was tested by such sudden changes in the market environment. The interior configuration of small manufacturers’ pickup trucks and SUV products was designed for the Chinese, and it was often pointed out that these cars were not intended for tall Russians. However, small industry manufacturers lacked the ability to make large-scale design changes. Also, sales and market cultivation were left completely to Russian dealers and Siberian, and responses to problems of rubber and resin parts becoming fragile in the low-temperature environment were slow. As a result, the reputation of Chinese cars as ‘cheap and bad’ became more and more entrenched. Consequently, young, small manufacturers like ZX Auto were forced to withdraw because they lacked the product development/improvement skills and also the wide-ranging sales capabilities needed to respond to these sudden market changes. To some extent, the top manufacturers possess the product improvement and market cultivating skills to respond to the above-mentioned sudden changes in the market, but are limited by lack of operational know-how regarding expansion, which will be examined next.

(2) Analysis in terms of market entrance methods

When we look at past Russian expansion by independent manufacturers, we see a tendency for manufacturers to initiate CKD or SKD manufacturing after a brief period of exporting completed cars. In the Russian tariff system, the
International business strategy of Chinese auto in Russia

The tariff for imported completed cars is 25–40%, and the import tariff for automobile parts is ordinarily 5–15%. At a glance, it would appear that KD manufacturing is a more reasonable option than finished car exports, but like the previously mentioned Chery Automobile Siberian project, KD parts intended for assembly into completed cars are ultimately subject to the same duty rate as completed cars, so they are in fact more inefficient than finished car exports. Even so, KD parts exports have been favoured because of the existence of grey parts imports by Russian partners. In other words, another corporation separately obtains customs clearance for the KD parts, avoiding finished car tariffs. However, as Russia lacks clear operations regulations and laws regarding imports of KD parts, Russian KD production by independent manufacturers (except Chery Automobile’s Kaliningrad assembly operations) essentially falls into a grey zone in terms of the law, so the operational risk of such expansion methods is considerable.

In March 2005, in a bid to develop Russia’s own automobile industry, the Russian government issued a favourable policy to attract foreign manufacturers called ‘On Amending the Russian Federation Duty Rate on Automobile Parts Imported for Industrial Manufacturing Assembly’ (popularly known as Government Ordinance 166). In other words, when automobile manufacturers imported parts intended for assembly, pre-existing manufacturers with annual manufacturing volume of 25,000 units or more were given seven years, and new manufacturers were given eight years to achieve localisation of welding, painting, and assembly. If the applicants fulfilled certain conditions, including gradually raising the local supply rate to 30%, their tax rate would be reduced or eliminated. Every important Chinese independent manufacturer applied under Government Ordinance 166, but everyone was rejected. This perhaps had something to do with the fact that they were involved in grey imports and lacked operational know-how regarding expansion methods.

(3) Analysis from the perspective of operational know-how regarding expansion methods

From the beginning, independent manufacturers failed to understand that, by attracting foreign manufacturers, the Russian government intended to promote the parts industry in its own country. For this reason, there were many cases in which conflicts of interest existed regarding the Russian government’s intentions and the local
production/manufacturing methods or investment publicity of Chinese independent manufacturers. This is the main factor behind the sudden decline of Chinese cars in the Russian market from 2008 onward.

Table 6 is a listing of new OEM projects planned as of 2006 in Russia and the CIS. Of course, these are plans, and mass communication strategising was involved, so they cannot be said to necessarily reflect reality with accuracy, but it is certain that this information was present in reports in general. Consequently, regardless of the accuracy of the information, the image of Chinese independent manufacturers that ignore contributions to society through investment and pursue maximum manufacturing scale for minimum investment is becoming entrenched. Also, since Russian manufacturers that manufacture Chinese cars locally are in general not major Russian manufacturers, they have little interest in protecting the industry of their own country. In addition, because young, small Russian manufacturers obtain separate customs clearance for chassis and bodies through grey imports as described above, they are derided by major Russian manufacturers for doing ‘screwdriver assembly’ using one screwdriver. In 2007, sales of Chinese cars in Russia leaped forward, exceeding 50,000 units. Even so, compared to the 3,131,000 cars sold in the entire market, they hold only a 1.6% market share, and are not significant. However, mistakes have been made regarding the positioning strategy of Chinese cars, as when Chery Automobile put the Amulet into direct competition with the major local Russian manufacturers AvtoV AZ and Kalina. Also, since it adopted a manufacturing system which barely fulfilled the needed investments in facilities, its share of the total market stood at a mere 1–2%. A protectionist view regarding the ‘Chinese car threat’ (that is, that the entrance of Chinese cars contributed nothing to Russian society or the development of the Russian automotive industry, and caused only damage) has become more and more mainstream.

5. Conclusion

Inexpensive Chinese cars in direct competition with local Russian manufacturers, which are in a continuing decline, are a problem the Russian government cannot overlook. Apart from its providing competition with local makers, ‘screwdriver assembly’ had the effect of suppressing hiring in the domestic Russian automobile industry, so that it became an employment pressure factor. For economic reasons, it could be said that eliminating Chinese cars was an unavoidable choice for the Russian government.
control over grey imports and rejected Chinese applications under the ‘industrial assembly’ scheme in order to
minimise the negative influence of independent manufacturers expanding into Russia. Also, to completely eliminate
‘screwdriver assembly’, the Russian government issued Ordinance 745 on 10 October 2008, amending the import
duties assessed on bodies for automobiles, mainly passenger vehicles. Beginning on 14 November, a transition was
made from the original flat rate of 15% to one of 15% or 5,000 Euros per car body, whichever is higher. The increase in
manufacturing costs caused by such policy regulations has become an unavoidable problem affecting the continuation
of the advancement of Chinese vehicles into Russia. In particular, local mass manufacturing by other foreign
manufacturers, which benefited by complying with the ‘industrial assembly’ policy, began from 2009, and the
favourable status of Chinese cars in terms of cost has been lost, pressing Chinese manufacturers towards inevitable
withdrawal. Due to policy regulations of the Russian government deliberately designed to eliminate Chinese cars, even
Chery Automobile’s partnership with Avtotor, referred to as the sole success, was halted in March 2008. Although
Geely Automobile, which planned to expand into Russia and export the completed cars in partnership with Rolf, and
Lifan Automobile, which aimed to achieve local manufacturing, were seen as promising, it has become more and more
difficult to eliminate the cost increases caused by revised customs duties. In 2009, sales of Chinese cars in Russia
essentially consisted of dealers disposing of stock, and the number of units sold fell drastically.

The factors behind the loss of momentum of Chinese cars in the Russian market since 2008 lie not only on the
Russian side. Even more important factors lie on the Chinese side. The most significant one is the fact that, due to
non-payment of numerous mediator fees, the strong cooperative relationships between independent makers and
Siberian, which once functioned so well, are dissolving. A typical example is the suit brought against Geely
Automobile by Siberian.21 The differences in the two parties’ understanding of contract implementation are having a
definite negative effect on Geely’s sales in the Russian market. Problems regarding non-payment of mediator fees are,
ironically, occurring mostly among groups other than the least competitive, late lower-ranked group. Siberian, which
had been involved in the Russian expansion operations of 27 Chinese car manufacturers, temporarily stopped
performing mediating tasks related to expansion into Russia in 2009, and is devoting its attention to lawsuits.

In general, when Chinese cars expand into overseas markets, deficiencies in risk management know-how regarding
the local market have been observed even among top manufacturers, and the fact that they lack the proper and
necessary know-how required for conducting domestic and overseas partnerships has been especially conspicuous in
the case of expansion into Russia. The manufacturers have been unable to recognise in advance the operational risks
that might result from deficiencies in know-how regarding overseas expansion. Further, in terms of the timing of
expansion, lesser, smaller modified car (body) manufacturers that are easily branded with the reputation of ‘cheap and
bad’, appeared first, which negatively influenced the overall expansion of Chinese cars. Hence, corrective measures
are needed at both government and industry level.

Recent trends have seen many Chinese car manufacturers (including Chery Automobile) establish bases in the
Ukraine and move towards cultivating markets in the CIS after being shut out of Russia, but to the extent that they fail
to learn from the experiences gained in the Russian market, there is a risk that the Ukraine may be a repeat of
Russia. We must continue to watch developments.

21 Shi Baolin (2009), ‘Chinese car business defeated in Russia due to internal factors causing trouble abroad’ (21st Century
Economic Report, August 5, 2009). According to an internal Siberian document, in November 2007, through the mediation of
Siberian, Geely Automobile signed an automobile export trade contract with Rolf for a total of $1.5 billion. The contract specified
that regarding mediation fees, one of two options was to be selected through negotiation by both companies: either A, the
contractor (Geely Automobile) would use the total amount of the first three trade contracts signed with the overseas buyer (the
Russian company Rolf) as a base for calculations; or B, the contractor (Geely Automobile) would follow the payment contract
with the foreign buyer (Rolf) from the first trade contracts, and from the day the contractor (Geely Automobile) received
payment of the contract amount, it was to use the total amount of all trade contracts within one year as a base for
calculations. Ultimately, option A was adopted, but the two parties clashed over their very different understanding of the trade
contract. When the contract was first enforced, Geely Automobile supplied three batches to Russia, which totalled 1,000
vehicles. Each time, a car export acceptance contract was signed. Therefore, Geely Automobile insisted that these 1,000 units
should be the base of calculations for the mediation fee, but Siberian insisted that because these three vehicle export acceptance
contracts were incidental to the original $1.5 billion trade contract, they were not trade contracts. Therefore, they insisted that a
base for calculations of 1,000 units was not enough.
References


Siberian Automobile Export (Beijing) Co. Ltd. (2007), The path of the Chinese car into Russia (internal document)


[Received June 12, 2010; accepted October 31, 2010]