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Evergrande's Sea Venice: Developing China's Leisure Real Estate Sector



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China's tourism, or leisure, real estate sector is becoming a popular alternative investment choice of Chinese consumers, as rising urban housing prices, greater demand for retirement housing and other factors bode well for this market. But property developers have been rather wary of this sector, given the higher capital requirements and longer investment horizons the projects typically demand. However, the experience of Evergrande Group's Sea Venice, located just 90 minutes away from downtown Shanghai in coastal Qidong, suggests such prudence may be a mistake. The project sold out at record speed, largely owing to its clear value proposition that was deftly communicated through its targeted marketing channels. As the Chinese real estate market continues to grow more competitive, Sea Venice is a reminder that product quality and sales strategy are as important as ever.

Evergrande: China's Premier Real Estate Conglomerate

Established in 1996, Evergrande is one of China's largest real estate conglomerates with headquarters in Guangzhou, Guangdong province, near Hong Kong. As of December 2017, the company had 766 projects across 228 cities, with a reported USD \$48 billion in annual revenue.¹ As of the first quarter of 2018, Evergrande ranked as China's third-largest developer by sales.²

Xu Jiayin, Evergrande's founder and one of China's richest people, built the company by acquiring land at a substantial discount during the Asian financial crisis, and then developing low-cost, no-frills real estate properties in one of China's most economically dynamic provinces.³

After a decade of high-speed growth, Evergrande grew from being a regional player to one of China's first private developers operating on a national scale. As competition intensified, Evergrande diversified away from low-cost housing into hotels, cultural tourism, and other real estate segments, including leisure real estate.

1. The Evergrande Group Annual Report (2017), page 8 and 16. Reuters. 2018. "Evergrande lays out Aggressive targets in Quest to enter Global Elite," March 26. "<https://www.reuters.com/article/us-evergrande-results/china-evergrande-lays-out-aggressive-targets-in-quest-to-enter-global-elite-idUSKBN-1H21BZ> . Accessed March 30, 2018.
2. "Establishing the enterprise with great efforts and developing at a high speed Three-year plan #1." Evergrande Group - About Evergrande. Accessed March 03, 2018. <http://www.evergrande.com/en/about.aspx?tags=5>.
3. Magni, Yuval Atsmon and Max. "Meet the Chinese consumer of 2020." Accessed March 03, 2018. <https://www.mckinsey.com/global-themes/asia-pacific/meet-the-chinese-consumer-of-2020>.

Leisure as an Investment Opportunity

Even though the average Chinese household income is expected to double from USD \$4,000 in 2010 to USD \$8,000 in 2020, according to consulting firm McKinsey, disposable income has not been able to keep pace with the meteoric rise in urban property prices.⁴ Prices for Shanghai's existing homes, for example, have roughly doubled in just the last two years. Meanwhile, the capital requirements for property investments have also

outpaced the gains in income. As such, the new Chinese middle class is faced with this conundrum: Most families would like to invest in a second home for leisure, but only the very wealthy can afford multiple properties in China's largest cities. Furthermore, government policy interventions aimed at tamping down speculation in the residential real estate sector, such as new rules on purchasing restrictions and quota allocations, have imposed greater regulatory hurdles for all.⁵

Figure 1 - Evergrande's resort project in Jiangsu



Source: <http://www.travel62.com/Italy/946.html>

- Ding, Ding, Xiaoyu Huang, Tao Jin, and W Raphael Lam. "Assessing China's Residential Real Estate Market." Working Paper. Interational Monetary Fund, November 16, 2017.
- "China's domestic tourism growing faster than outbound traffic in H1 2017." ChinaTravelNews. August 20, 2017. Accessed March 03, 2018. <https://www.chinatravelnews.com/article/116748>.

While urban families may not find it easy to own multiple properties, they are nonetheless a key driver of China's expanding consumer sector, which includes tourism. According to the China National Tourism Administration, a staggering 4.4 billion domestic trips were taken in 2016, which is more than three times the nation's population.⁶ Ctrip, China's largest online travel agency, noted that the domestic travel sector grows annually at 10%, twice the growth rate of outbound travel. The desire to travel is also the function of a desire to escape crowded urban centers. For example, the density of Shanghai's Huangpu District is now more than 40,000 people per square kilometer, or approximately twice the density of New York City.⁷

These two trends — the desire of increasingly wealthy urban families to find cheaper properties and interest in domestic travel — are making real estate developers sit up and take notice. Evergrande has been a first mover, investing in several high-profile real estate tourism projects, most notably in Jiangsu province and the tropical island of Hainan, located off Guangdong province. In Jiangsu, Evergrande's 1,500-acre tourism project, just 100 kilometers away from Shanghai, includes Venetian-style hotels, aquariums, residential

properties, private beaches, and other facilities.⁸ In Hainan, Evergrande is investing more than USD \$24 billion to build an artificial archipelago.⁹

Challenges in developing tourism properties

A well-executed tourism real estate project can be the crown jewel in a property developer's portfolio as it draws upon and displays a wide range of expertise and products. These projects typically include residential properties, office towers, hotels, shopping malls, related infrastructure, and other amenities to be enjoyed by visitors. Compared to a high rise in downtown Beijing, a successful tourism project is a much stronger testament to a conglomerate's capabilities and brand strength.

The development of tourism real estate projects also tend to increase the overall value and population of an area. Typically, the cost savings from acquiring cheap land are allocated towards heavy capital expenditure to build up an area's provisions — ultimately contributing toward its popularity. But that means a tourism project could take a decade or more to complete compared to a few years for urban residential projects. In the case of

Figure 2 - Evergrande's Hainan archipelago project



Source: <http://evergrande.com/>

6. "Shanghai struggles with growth." http://usa.chinadaily.com.cn/epaper/2013-07/11/content_16762602.htm Accessed March 03, 2018; Density Using Land Area. Accessed January 3, 2018. <https://www.census.gov/population/www/censusdata/density.html>

7. Evergrande Internal Data.

8. Ocean Flower Island, Hainan, China. Accessed March 03, 2018. <http://www.oceanflowerisland.com/en/index.aspx>.

9. Evergrande Internal Data.

Evergrande's Sea Venice project, the developer spent seven years just to put the basic infrastructure in place.¹⁰

While project quality and good locations are key to any tourism property's success, ultimately it is a company's marketing and sales strategy that encourages consumers to purchase leisure property. Compared to urban projects, tourism properties have to convince buyers of its distinct value proposition that justifies an investment unlikely to be used as a daily residence.

Sea Venice: A 'Blue Ocean' for Shanghai

In 2005, Evergrande acquired more than 11 million square meters of land in Qidong at less than USD \$150 per square meter.¹¹

Located only 90 minutes away from Shanghai, and east of Nantong City, Qidong had been long positioned as a spillover area for Shanghai's growing overpopulation.

Evergrande invested heavily in Qidong's infrastructure and coastline to reinvent the city as Shanghai's weekend coastal getaway. Most notably, it built submerged groynes to prevent beach erosion and planted algae to clean up the Qidong coastline. In due time, Qidong's water became so blue that Evergrande marketed Qidong as Shanghai's "Blue Ocean," the premier coastal getaway for urban residents. Housing in Qidong ranges from apartments as small as 40 square meters to villas of more than 650 square meters.¹² To attract investors, Sea Venice included Venetian-inspired canals, gardens, hotels, a sports arena, and other amenities to craft a resort atmosphere for its residents.

Figure 3 - Qidong as a coastal getaway from Shanghai



Source: Google Maps

Figure 4 - The Sea Venice resort with coastal views



Source: <http://evergrande.com/>

10. Evergrande Internal Data.

11. Evergrande Internal Data.

12. Evergrande Internal Data.

A Successful Product and Marketing Strategy

In early October of 2016, Evergrande began sales of the third phase of its Sea Venice project. In just the first day, Evergrande sold 4,000 units for \$2.4 billion RMB (USD \$380 million).¹³ It had released half of the units for sale, and of those, 90% were sold in the first three hours with smaller apartments snapped up in the first hour, according to *The South China Morning Post*.¹⁴ Evergrande had invested close to USD \$38 million in a marketing campaign for the project's third phase — and its strategic market positioning, rigorous customer outreach, and comprehensive campaigning paid off handsomely.

The Evergrande Sea Venice Customer

Given major capital requirements and long investment horizons, tourism real estate projects require rigorous segmenting, including identification of its customer base. The industry typically targets the short-haul vacationer, the retiree, and investors.

One target market is the Shanghainese. As residents of one of China's wealthiest cities, they are no strangers to travel. The Shanghai Bureau of Statistics noted that 52% of Shanghai residents had plans to travel in 2016, with more than 60% of travelers opting for more casual, self-planned getaways. But they had very few options for short-haul beach escapes. Hainan Island is four hours away by plane, and Japan's Okinawa Islands require visas and higher budgets. As such, Shanghai travelers, especially those with limited budgets and leisure time, were the ideal customers for a nearby short-haul beach vacation.

Qidong's location is also ideal for Shanghai's retired seniors. Defined as people older than 60, Shanghai's

seniors comprise 31% of the city's population as of 2017, higher than any other urban area in the world.¹⁵ Projected to reach 5.3 million people by 2020, Shanghai is an ideal market to sell retirement housing. Currently, Shanghai's increasing density and unaffordability means most elders either share their urban housing with their adult child, or as becoming more common, settle in a more comfortable, inexpensive location nearby where the lifestyle is more enjoyable and basic amenities are provided.

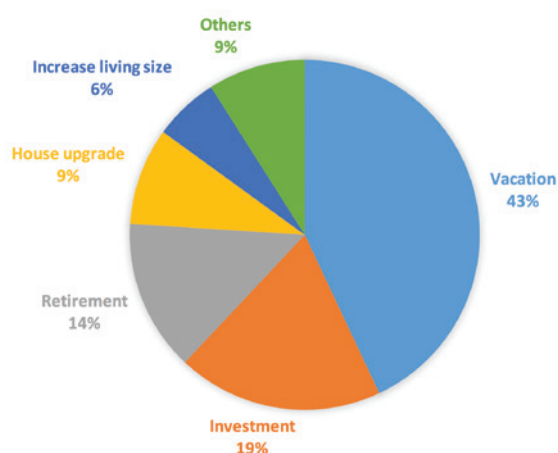
Sea Venice meets the latter requirements. While central Shanghai properties sold for more than \$50,000 RMB (USD \$7,500) per square meter in late 2016, Sea Venice properties were priced as low as \$6,000 RMB (USD \$950) per square meter. Residential units start as low as \$350,000 RMB (USD \$55,000), a staggering value few urban middle class families can ignore. Moreover, Qidong properties are excluded from quota measures, meaning that customers can buy multiple units under a single name.

Sea Venice also targeted local Qidong residents and buyers from other parts of China as well. Local residents looking to upgrade living standards were drawn to Evergrande's national brand and Sea Venice's amenities, though for many of them, it also meant paying a price premium compared to properties available elsewhere in Qidong. Sea Venice targeted national investors as well, including wealthy individuals from Hong Kong, Macau, and Taiwan. Overwhelmingly, these buyers were drawn to invest in Sea Venice properties as a vacation location. In a customer survey, Sea Venice discovered that the primary reasons buyers chose its homes were for vacation, real estate investment and to have a place for retirement (Figure 5).

13. Li, Sandy. "Shanghai investors rush to buy homes China Evergrande's project near Chongming Island." October 10, 2016. Accessed March 03, 2018. <http://www.scmp.com/property/hong-kong-china/article/2025718/shanghai-investors-rush-buy-homes-china-evergrandes>.

14. "Shanghai caps population at 25 million but experts doubt it will work." December 27, 2017. Accessed January 8, 2018. <http://www.scmp.com/news/china/policies-politics/article/2125739/shanghai-caps-population-25-million-2035-experts-doubt>.

15. Li, Sandy. "Shanghai investors rush to buy homes China Evergrande's project near Chongming Island." October 10, 2016. Accessed March 03, 2018. <http://www.scmp.com/property/hong-kong-china/article/2025718/shanghai-investors-rush-buy-homes-china-evergrandes>.

Figure 5: Sea Venice customer survey on purchase reasons

Source: Evergrande internal data

The Sea Venice Product: Building out the Value Proposition

Tourism real estate demands that developers offer a more comprehensive product than urban projects, specifically around hard amenities to drive impulse purchase decisions. Landscaping, property maintenance, amenities and quality infrastructure justify long-distance purchases, assuring buyers that their investments will be cared for in their absence, and that their experience when visiting will be of consistent quality. Buyers, as such, are investing in both the tangible and intangible assets of Sea Venice. In contrast, the value of urban property is overwhelmingly driven by macroeconomic trends. For example, the value of a Shenzhen apartment is in no small measure determined by its location, as opposed to the apartment's own amenities or design.

With more than half of its customers citing vacation or retirement needs as reasons to buy into Sea Venice, Evergrande must offer more rationales than just the resort's location as a good enough motivation to invest. Moreover, as consumer desires change, Evergrande also needs to guarantee it will deliver an enjoyable resort

experience.¹⁶ While the company has not released cost figures behind its Sea Venice amenities, the offerings suggest that Evergrande shifted significant capital towards building out the area as a getaway experience.

Sea Venice includes a Hot Spring Park, spa facilities, sport clubhouses, and a children's theme park. The spa facilities and children's theme park each exceeded 14,000 square meters in size, equivalent to two Walmart stores in the U.S.¹⁷ Its sport clubhouse, offering Olympic-sized pools and more than 60 types of sport venues, is more than 24,000 square meters.

Figure 6 - Sea Venice's Hot Spring Park

Source: Evergrande Sea Venice official site

Sea Venice's emphasis on amenities is a deliberate choice to address possible consumer psychological hurdles. Semi-artificial beaches and full amenities convey a sense of easy living, at a low cost, to fuel 'impulse' purchases. The theme park-like setting then serves as sort of an "entrance fee" to a private and exclusive enclave of residences, one with year-round access — not unused buildings that are occupied only during weekends and holidays.

Targeted and Thorough Touchpoints Drive up Hype

Compared to traditional residential units, tourism real estate marketing faces a more challenging consumer

16. "Our Retail Divisions." Accessed February 5, 2018. https://corporate.walmart.com/_news_/news-archive/2005/01/07/our-retail-divisions.

17. Ciemiak, Robert. "Chinas Trillion Dollar Housing Market: A Few Figures To Think About." *Forbes*. July 14, 2016. Accessed March 03, 2018. <https://www.forbes.com/sites/robertciemniak/2016/07/12/a-trillion-dollar-market-chinas-housing-market-a-few-figures-to-think-about/#695f3a1a5362>.

outreach process. Urban properties are conveniently located near their target population. Tourist properties, in contrast, require more time and a commitment to travel just to see the location. Without these visits, consumers consider mainly the purchase price, and not the value of the intangible assets provided through their investment. As such, the marketing strategy for tourist properties depends heavily on raising consumer awareness. This is no easy feat in China's crowded real estate sector. In 2016 alone, China built more than 10 million new homes. That means thousands of property developers competed for a spot on prime advertising channels, each trying to win over a prospective buyer.¹⁸

Sea Venice's awareness campaign focused heavily on getting prospective buyers to visit Qidong through two distinct marketing channels. To target retirees in Shanghai, Sea Venice focused on Shanghai television, radio and newspaper advertising, whose loyal subscribers were mainly the elderly. To target younger, travel-savvy professionals looking for weekend getaway

properties, Sea Venice invested heavily in WeChat, online video advertisements, and public transportation media.

Once the marketing piqued the interest of prospective buyers, they could visit one of several Evergrande Sea Venice exhibition halls in their area. The hall in Shanghai deployed dozens of interactive, 3D projections to recreate Sea Venice's shoreline, emphasizing its unique access to the city's only nearby ocean.¹⁹ The exhibition hall also featured displays of most unit types, emphasizing the size and value that Sea Venice offers against Shanghai's housing market. There are 11 other such exhibition halls throughout Eastern China built by Evergrande to target residents.

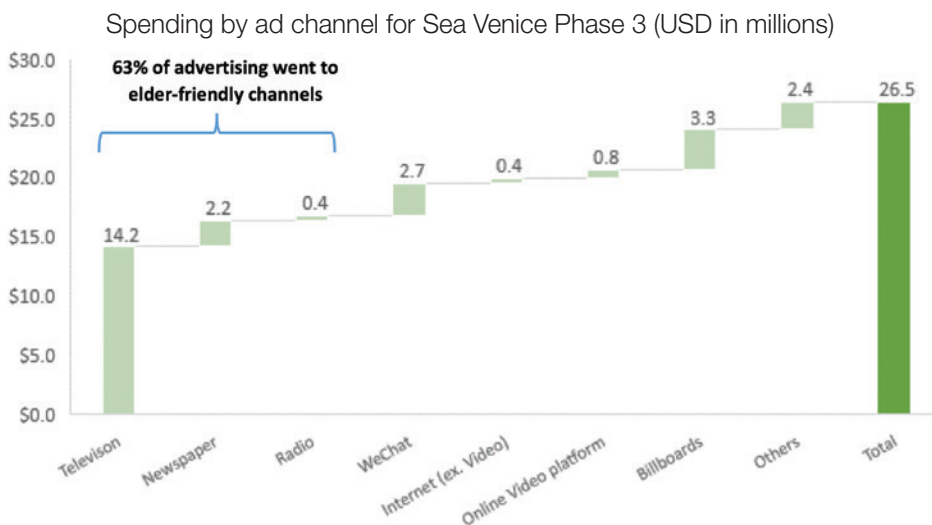
The next step was a site visit to Sea Venice. To make access convenient, Sea Venice offered free bus tours as well as access to dozens of free events on-site, such as circus performances, soccer matches featuring Fan Zhiyi, China's former national team captain, or hotel grand openings with Chinese celebrity Fan Bing Bing. During its Beach Beer Festivals, Sea Venice attracted

an average of 10,000 daily visitors.²⁰

Collectively, these events aimed to illustrate that Sea Venice was attainable to everyone.

Perhaps Sea Venice's most powerful marketing tool was word-of-mouth recommendations. More than 58% of visitors to Sea Venice said in a survey that they came on the recommendation of a family member or a friend.²¹ Also, more than half of buyers indicated that they were referred to Sea Venice by current unit owners. The influence of personal recommendations on the project's overall success thus serves as a

Figure 7 - Sea Venice's advertising expenditures



*Others include hotels and marketing agencies.

Source: Evergrande internal data

18. "Evergrande builds 3D Seaside Mock Display Center." May 15, 2012. Accessed January 8, 2018. http://news.ifeng.com/gundong/detail_2012_05/15/14534522_0.shtml.

19. Evergrande Internal Data.

20. Evergrande Internal Data.

21. Evergrande Internal Data.

reminder to on-the-ground staff about the importance of their day-to-day interactions with existing and prospective owners.

Behavioral Sales Tactics to Maximize Conversion at Site

As important as marketing is to attract buyers, a strong sales strategy is critical to finalizing a property purchase. Sea Venice's sales tactics are especially notable as it was able to quickly convert prospects to purchasers on its Phase 3 opening day. Indeed, Phase 3 of Sea Venice was oversubscribed; Evergrande made good use of this high demand to spur immediate sales.

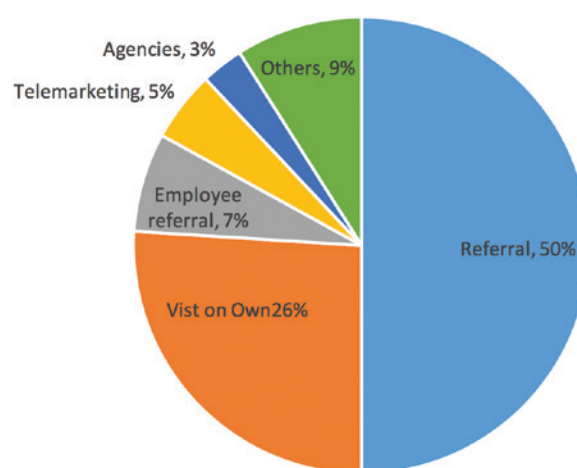
Specifically, prospective buyers were placed into a lottery system to underscore that the number of units available was extremely limited. Outside the sales complex, a live screen broadcasted the newest "lottery" winners as well as the number of units available for purchase. Every hour, around 600 winners were invited into the sales complex to complete the transaction.²² This sales tactic created a sense of urgency: Snap up the unit soon or risk losing your spot in the lottery queue, missing out on a purchase.

Sea Venice also offered financial incentives and streamlined contract processes to maximize quick conversion of sales prospects. On opening day, for example, Sea Venice offered expiring discounts of up to 20% to drive impulse purchases. Teams of sales agents had major banks' mortgage departments on call to verify loans. Dozens of contracted paralegals were also on hand, with prepared transaction materials to execute deals on-site.

However, the Sea Venice referral program was the runaway star. Months before its Phase 3 opening sale day, Evergrande offered a referral program to Sea Venice Phase 1 and Phase 2 owners. Owners who introduced a prospect that ended up buying a unit could earn up to 150,000 RMB (USD \$23,000) in shopping coupons and

home owner association fee waivers for up to nine years. Moreover, these new buyers were promised another 2% discount on top of the transaction price. No surprise that more than half of the sales came from referrals, far surpassing the performance of other acquisition channels. To Evergrande's surprise, more than 40% of current owners induced their prospects to buy — and 4% of them purchased more than 5 units.

Figure 8 - Phase 3 purchases by acquisition channels



Source: Evergrande Internal Data

Product, Marketing and Sales Excellence Not Optional

On the flip side of Sea Venice's success is the stark realization that it takes excellent marketing savvy and hard work to drum up profits in the Chinese real estate market. The sector is plagued by high land costs, increased regulatory pressure and intense competition from SOEs to large private companies, which are driving down profitability as clever marketing tactics quickly lure prospective buyers from the market. Greater information transparency and maturity of the primary markets, as such, imply that real estate developers can no longer haphazardly undertake projects and expect generous returns.

22. Evergrande Internal Data.

Sea Venice is an example of a targeted, clear value proposition built to meet a largely unaddressed demand. Thanks to its investment in infrastructure and the shoreline, Sea Venice captured the untapped short-haul vacationer, the retiree, and the investor constrained by rising prices and tightened regulations in Shanghai's real estate market. The lesson is clear: Developers need to run rigorous market studies if they intend to achieve above-market returns from targeted customer groups. This trend is particularly true for the tourism real estate sector, where overall capital expenditures and longer investment horizons mean taking on greater financial risks as consumer preferences remain highly significant to the value proposition of the investment.

Traditional above-the-line marketing, such as obscure billboards with stock photographs, no longer resonate with China's consumers. Years of generic real estate advertisements, as well as unmet property expectations, have made today's consumers far more skeptical. As a result, developers not only need to differentiate their marketing channels to attract the best customers for a given project, but it is increasingly important to do so through more personable, customized sales channels.

For example, word-of-mouth marketing addresses consumer skepticism through its use of family and friends they would find more trustworthy. Invitations to free events also assure consumers that they can pursue their interest in a property development without financial penalty. Finally, as the success of marketing tactics, such as those used at Sea Venice, become well-known, other developers will have no choice but to do likewise if they hope to remain competitive.

Risks and mitigations

Tourism real estate is an increasingly popular topic among real estate executives today. Some high-profile projects have returned substantial above-market returns, helped to diversify a developer's portfolio, as well as showcased a developer's capabilities. Nonetheless, this sector still faces greater capital and development risks than other project types.

As tempting as lower upfront land costs may be, building out a tourism real estate project requires substantially more capital than an urban project. Moreover, developers without experience in infrastructure development will likely face considerable margin compression, especially if these elements are outsourced. The long investment horizon, typically characterized by a decade or more, also means that future earnings will be severely discounted. All to say, this is a business for large developers. Smaller developers likely lack the brand equity, marketing capacity to attract customers, or balance sheet needed to offer sharp discounts to prospective buyers.

Conclusion

Sea Venice Phase 3's astounding sales performance is a strong reminder of the importance of business fundamentals: have a strong product, provide accurate marketing, and deploy an excellent sales team. While the industry rightfully emphasizes that land acquisition and financing costs are key competitive advantages, the increasingly competitive real estate market and rising popularity of the tourism segment highlights the importance of these factors. They may not save a strategically misaligned project, but they can make the difference between having a ghost beach town or a new Venice near Shanghai.

