

E-House

Country Garden's People-centered Growth Strategy



Sponsored by



OCTOBER 2019



Country Garden's People-centered Growth Strategy

In 2017, China's investment in real estate development reached 11 trillion yuan (US \$1.7 trillion), a 7% increase year-on-year.¹ A significant chunk of this capital went into Tier 2 and 3 cities, which had seen stunning increases in population growth in recent decades. Soon, Tier 4 cities were also growing. Against this backdrop, Country Garden, one of China's largest real estate developers, achieved robust growth by meeting new housing demand in these locations. It did so by combining a rapid build-and-sell model with an employee risk- and profit-sharing scheme that made the company one of the fastest builders in China. Today, however, the sustainability of Country Garden's way of doing business is in question as China's national economy slows and credit conditions tighten.

BACKGROUND: CHINA'S TIERED CITIES AND HOUSING POLICIES

China's real estate market comprises four types of urban areas known as Tier 1, 2, 3 and 4 cities. The first-tier cities are the country's largest and perhaps best known locations, such as Beijing, Shanghai, Guangzhou,

and Shenzhen. Subsequent tiers are distinguished by differences in level of economic development, population size, population growth, and political ranking.²

Nevertheless, housing prices have risen across the board. From 2016 to 2018, they jumped 23.5% in Tier 1 cities and 14% in Tier 2 cities, raising concerns that a property

1 Xinhua. China's Real Estate Investment up 7% in 2017, Accessed March 14, 2019, http://english.gov.cn/archive/statistics/2018/01/18/content_281476018133681.htm.

2 Lili Wu, "Applied Economics Letters," Taylor and Francis Online, December 1, 2017, Accessed March 14, 2019, <https://www.tandfonline.com/doi/pdf/10.1080/13504851.2017.1412069?needAccess=true>.

bubble was in the making.³ A common way to assess the stability of the housing market is to look at the home price-to-rent ratio. Multiples above 30 imply a potential housing bubble is building. In Shenzhen, the ratio rose to 66.7. In cities such as Xiamen, the multiple was as high as 100.⁴

Alarmed, Chinese authorities implemented housing market controls to thwart real estate speculation, which had contributed to the sharp price increases. For example, the Beijing city government raised the minimum down payment for a second home from 50% to 60% of the housing cost. Restrictions have also been put in place prohibiting individuals from purchasing properties under the name of their enterprises.⁵ The well-known slogan, “houses are built for living in, not for speculation,” exemplifies the new attitude toward real estate investments.⁶

Predictably, stricter policies and rising prices reduced demand in Tier 1 and Tier 2 cities, but not Tier 3 and Tier 4 cities. From 2013 to 2017, investments increased by 6% while the average selling price of commercial residential buildings went up by 5% (Exhibit 1).⁷ After

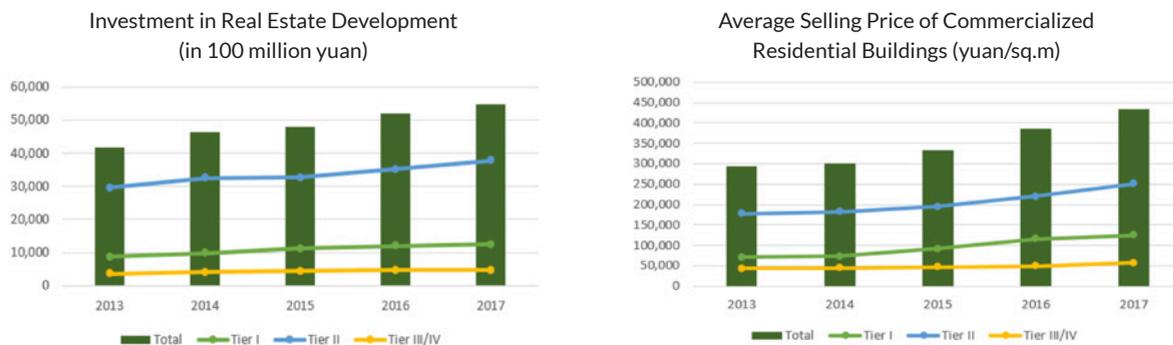
2017, growth stayed at around 6% year-on-year, which has served Country Garden well.⁸

KEY MANAGEMENT STRATEGY

In 2017, Country Garden reported 550 billion yuan (US \$80 billion) in sales revenue, making it the top seller in China that year.⁹ Behind these results is a management strategy that has given it a distinct advantage: Country Garden actively seeks to retain top talent through a range of incentives, both financial and otherwise, with a path for career advancement. Top performers could benefit directly from risk- and profit-sharing. Thus, Country Garden’s stunning growth was the result of more than just the success of its low-cost, fast-to-market business model.

Compare Country Garden to the experience of its key competitor, Vanke. Reporting the second-highest revenue in 2018, Vanke sits just behind Country Garden in the pecking order but its efforts at employee retention are far less successful, especially at the C-suite level.¹⁰ To drum up more company loyalty, Vanke introduced a two-layer employee partnership scheme in 2014 in which

Exhibit 1: Property Development and Sales Price Trends



Source: National Bureau of Statistics of China, National Data, Accessed March 14, 2019, <http://data.stats.gov.cn/english/easyquery.htm?cn=E0105>.

Notes: Tier I Cities: Beijing, Shanghai, Guangzhou, and Shenzhen

Tier II Cities: Tianjin, Shijiazhuang, Taiyuan, Shenyang, Dalian, Changchun, Harbin, Nanjing, Hangzhou, Ningbo, Hefei, Fuzhou, Xiamen, Nanchang, Qingdao, Zhengzhou, Wuhan, Changsha, Nanning, Chongqing, Chengdu, Kunming, Xi’an

Tier III/IV Cities: Hohhot, Haikou, Guiyang, Lanzhou, Xining, Yinchuan, Urumqi, Ji’Nan

3 Jie Zhang, “Shanghai Announces New Policies to Curb Real Estate Speculation,” Shanghai Announces New Policies to Curb Real Estate Speculation - Chinadaily.com.cn, Accessed March 14, 2019, <http://www.chinadaily.com.cn/a/201807/03/WS5b3b186ca3103349141e06a8.html>.

4 Yangpeng Zheng, “Are China’s Property Bubbles at Bursting Point?” South China Morning Post, July 20, 2018, Accessed March 14, 2019, <https://www.scmp.com/business/china-business/article/2103116/plunging-chinese-rental-yields-point-property-bubbles-major>.

5 Jie Zhang, “Shanghai Announces New Policies to Curb Real Estate Speculation,” Shanghai Announces New Policies to Curb Real Estate Speculation - Chinadaily.com.cn, Accessed March 14, 2019, <http://www.chinadaily.com.cn/a/201807/03/WS5b3b186ca3103349141e06a8.html>.

6 Dominic Chiu, “Housing Bubble, Politics and Trouble: Problems and Policies for China’s Real Estate Market,” China Business Review, November 04, 2016, Accessed March 14, 2019, <https://www.chinabusinessreview.com/housing-bubble-politics-and-trouble-problems-and-policies-for-chinas-real-estate-market/>.

7 National Bureau of Statistics of China. National Data. Accessed March 14, 2019. <http://data.stats.gov.cn/english/easyquery.htm?cn=E0105>.

8 Sheng Songcheng, “6 Keys to Understanding China’s Rising Real Estate Prices.”

9 21st Century Business Herald, “Lu’an Country Garden Site Collapsed and Caused 6 Deaths and 3 Injuries. High Turnover Mode Should Reflect on This,” Lu’an Country Garden Site Collapsed to 6 Deaths and 3 Injuries High Turnover Mode to Reflect on This. Accessed March 14, 2019, <http://westdollar.com/sbdm/finance/news/1355,20180727914824169.html>.

10 E-House, 碧桂园集团:超规模房企多快好省的高周转经营模式, 中国房地产十大顶尖案例(2018-2019), Shanghai: E-house, 2018.

managers were required to invest in projects while the rank and file had an option to do so. Their equity stakes were capped at 10%. The hope is that by generating an ownership mindset among employees, they would support cost-efficient project development.

A second plan to retain talent came at the corporate level. Vanke pooled the profit-sharing bonuses of its employees in an investment vehicle that let the company buy its own shares in the open market. The idea was to give employees the option of having their own ventures in partnership with the company rather than leaving and starting their own firms. However, even with this scheme, top Vanke employees left to launch their own ventures or moved to other companies.¹¹ Every year since 2010, a vice president has left the company.¹² That is largely due to what has been described as an ‘unfair’ reward system. Executives and board members were highly rewarded, while those who worked hard at the regional branches claimed they did not get their bonuses.¹³ Country Garden has avoided this conundrum.

THE COUNTRY GARDEN WAY

Country Garden had a 62% increase in sales revenue

in 2018.¹⁴ This rapid expansion was due to its unique organizational structure, profit-sharing model, and high turnover operation model. Specifically, Country Garden has adopted what is known as the ‘456’ project development model, which implies four months from land acquisition to launch, five months to collect payments from buyers, and six months to recover all costs associated with the investment.¹⁵ As of March 2018, Country Garden’s average time from land acquisition to launch was 5.2 months, well above the industry standard and still one of the fastest in China.¹⁶

As real estate profit margins continue to narrow, high turnover has become the only way to ensure a high return on investment.¹⁷ Country Garden encourages adherence to the ‘456’ model through positive and negative employee incentives. For example, if a project launches within 3 months of land acquisition, its manager will get a bonus of 20,000 yuan (US \$2,840). Conversely, for every day of delay past a scheduled launch date, the project manager loses 10,000 yuan (US \$1,420) in bonuses.¹⁸

In 2017, Country Garden had around 124,000 full-time employees (up 32.17% from 2016).¹⁹ Among them were 600 Ph.Ds from top Chinese and international

Exhibit 2: Country Garden Employee Costs

	2017 RMB'000	2016 RMB'000
Wages and salaries	15,220,964	10,115,129
Contributions to pension plans	106,191	69,928
Staff welfare	242,730	159,842
Medical benefits	212,387	139,861
Share-based compensation expenses	265,268	82,834
Other allowances and benefits	60,679	39,959
	16,108,219	10,607,553
Less: capitalised in properties under development	(6,624,506)	(4,143,353)
	9,483,713	6,464,200

Source: “Country Garden 2017 Annual Report,” March 22, 2018, Accessed December 10, 2018, <http://www.bgy.com.cn/UploadFiles/cnn/Files/2017/4/20170405180826.pdf>.

11 Langi Chiang, “Vanke Builds Loyalty with Partnership Scheme,” South China Morning Post, July 15, 2016, Accessed March 14, 2019, <https://www.scmp.com/property/hong-kong-china/article/1531479/vanke-builds-loyalty-partnership-scheme>.

12 “万科又走一员大将！钱少了？还是心里委屈了？”，凤凰网财经, March 03, 2018, Accessed March 14, 2019, https://finance.ifeng.com/a/20180303/16007869_0.shtml.

13 Ibid.

14 史颖黎. “碧桂园”强推”高周转：设计院通宵出图，3个月内开盘奖20万.” Sohu.com, April 12, 2018, Accessed March 14, 2019, https://www.sohu.com/a/228088526_100001551.

15 “碧桂园急令强推高周转 40天不开工撤项目总 Country Garden urgently pushes high turnover for 40 days without starting work,” April 13, 2018, Accessed December 11, 2018, <http://companies.caixin.com/2018-04-13/101234053.html>

16 史颖黎. “碧桂园”强推”高周转：设计院通宵出图，3个月内开盘奖20万” .

17 E-House, 碧桂园集团:超规模房企多快好省的高周转经营模式

18 史颖黎. “碧桂园”强推”高周转：设计院通宵出图，3个月内开盘奖20万” .

19 “Country Garden 2017 Annual Report,” March 22, 2018, Accessed December 10, 2018, <http://www.bgy.com.cn/UploadFiles/cnn/Files/2017/4/20170405180826.pdf>.

universities.²⁰ Many were drawn to the company's remuneration package, partnership scheme, and investment in the workplace culture and employees. In addition to the salary, bonuses and cash subsidies, Country Garden pays each employee's social insurance premium or pension as mandated by the regional governments (Exhibit 2).

INNOVATIVE EMPLOYEE INCENTIVE SCHEMES

The chairman of Country Garden, Yang Guoqiang, upholds the idea of "shared interests — shared risks" — letting employees participate in the risks and benefits of a given project. In doing so, the company found that it has helped to increase productivity and sales. Here are two of Country Garden's best-known employee incentive programs:

'Achievement Sharing' Plan

In 2012, Country Garden began profit-sharing with its employees under this plan, in which 20% of a project's net profit in the form of cash and stock is awarded to general project managers and the regional presidents if they meet targets. But if there is a net loss, 20% of the loss is assumed by the general project manager and the regional presidents until cash flow is corrected. If there is no improvement after one fiscal year, the project is removed from the achievement sharing plan, meaning that all profit-sharing opportunities are eliminated.²¹ The plan has largely been a success. Indeed, in its first year of operations, sales more than doubled.²²

'Concentric Sharing' Plan

In 2014, the 'Achievement Sharing' plan transitioned into what is now the 'Concentric Sharing' plan. This plan requires a project's top leadership to put their own money on the line by way of a 'project company' comprising all members of the project and senior management. This includes company directors, vice presidents, central-level managers, regional presidents, and project managers.

The group is expected to hold at least an 85% stake in the project. Management staff may hold the additional 15% of project shares. Projects jointly developed by the group and third parties are calculated based on the proportion held by the group.

The parameters of Concentric Sharing aim to ensure accountability and profitability as follows:

- **Mandatory Investment:** The management staff has to invest in the projects and ensure that these are completed.
- **Additional Limited Investment:** Management staff can hold 10% of the equity shares of the regional venture. Other employees can hold up to 5% of the shares.
- **Return Mechanism:** Profitable projects result in profit distribution in the form of cash or an investment in the next project. If a project loses money, participants cannot withdraw.

Using this mechanism has been beneficial to Country Garden. It significantly shortened the average opening time by approximately 2 to 4 months and the return-of-cash-flow cycle by 1 to 2 months (Exhibit 3).²³ It also positively impacted relationships among employees.

Exhibit 3: Impact of the Concentric Sharing Plan

	Before Implementation	After Implementation
Time to project opening	9 to 11 months	6.9 months
Net profit growth rate	10%	12%
Annualized rate of return on own funds	About 30%	81%
Positive cash flow cycle	10 to 12 months	9.1 months

Source: E-House, 碧桂园集团:超规模房企多快好省的高周转经营模式

'CONCENTRIC SHARING' VS. VANKE'S 'CO-PARTNERSHIP'

The two programs differ in important ways: definition of qualified participants, follow-up investment mechanisms, dividend payouts, and the number of projects eligible for equity sharing among employees. For example, Vanke directors, project supervisors, and senior managers cannot join the firm's 'co-partnership' system. However, Country Garden's Concentric Sharing plan is open to everyone, making the reward for profitability a possibility for all.

In terms of how much employees need to invest to participate, Country Garden strictly adheres to the follow-up plan previously described, but Vanke does not stick to a uniform standard. In addition, Country Garden employees can share in the benefits only if the project's net profit is positive, whereas Vanke rewards employees

20 李颐晖, "在碧桂园工作是一种怎样的体验?," 36氪, Accessed March 14, 2019, <https://36kr.com/p/5089830.html>.

21 E-House, 碧桂园集团:超规模房企多快好省的高周转经营模式

22 聚考拉, "你家公司与碧桂园之间,隔了一个亿的年终奖!" Baidu Wenku, Accessed March 14, 2019, <https://wenku.baidu.com/view/eb1bde51cd1755270722192e453610661fd95a69.html>.

23 E-House, 碧桂园集团:超规模房企多快好省的高周转经营模式

as long as the project's net cash flow is positive.²⁴

Within a year of implementing Concentric Sharing, two regional presidents at Country Garden were given more than 100 million yuan (US \$14.2 million) in stock. One year later, in 2016, the number of winners rose to six, and sales doubled again. As a system, Concentric Sharing encourages hard work. Moreover, as earnings are no longer directly correlated with one's hierarchical positions in the company, it has also profoundly shaped company culture.²⁵

THE TALENT CONCEPT

A trend in the real estate industry is that sales and development projects are increasingly concentrated among the top firms. In 2017, the top 30 firms accounted for 38.1% of the sales, a 9% increase from 2016.²⁶ As such, it is extremely important for top companies to recruit and keep talented employees. To do this, Country

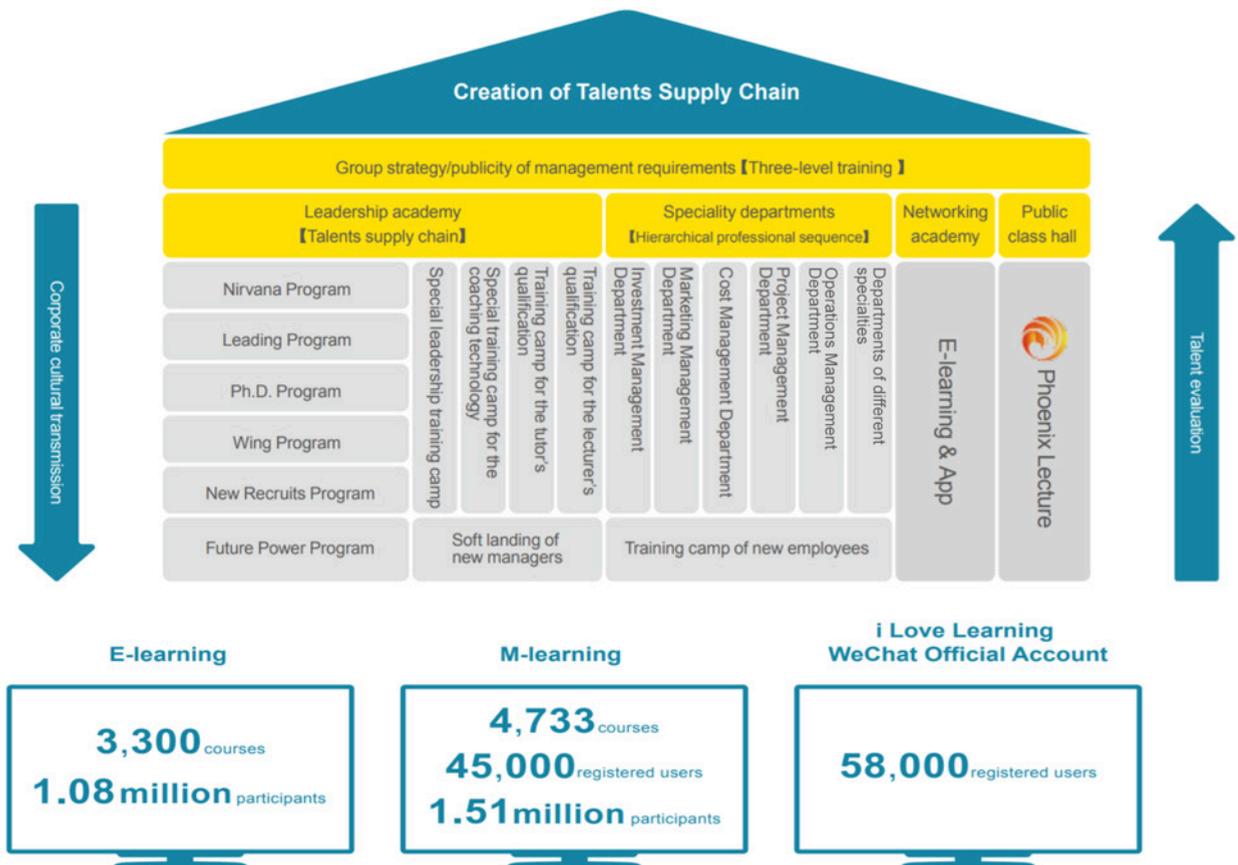
Garden adopted a talent retention strategy concept that promoted employee development both at home and abroad.

Established in 2013, the talent program is continually being improved to fit the growing needs of the company. About 70% of the people serving in critical positions at Country Garden came from the internal talent pool. In addition, Country Garden utilizes diverse platforms of learning to deliver training programs that suit its employees (Exhibit 4).

RECRUITING TOP TALENT

Country Garden emphasized the importance of talent recruitment in 2010 through its 'Future Force' development program. Designed to recruit exemplary graduates, the program would invest 5 or 6 years in training them, and then place them in critical management positions. In 2017, the company launched

Exhibit 4: Supply Chain of Talent



Source: "Country Garden 2017 Sustainability Report," May 14, 2018, Accessed December 12, 2018, <https://en.bgy.com.cn/upload/file/2018-05-14/e5a6683e-e727-42a1-8349-df2e95eef4f2.pdf>

24 孺子牛, "碧桂园猛推" 同心共享" 激励计划." 个人图书馆, Accessed March 14, 2019, http://www.360doc.com/content/18/0224/15/51240793_2101013.shtml.

25 聚考拉, "你家公司与碧桂园之间,隔了一个亿的年终奖!"

26 E-House, 碧桂园集团:超规模房企多快好省的高周转经营模式

a new version of the program, called the 'Super Future Force.' More than 110,000 undergraduates submitted their resumes in on-campus job fairs in 2018. Once recruited, new employees can join training programs, including training camps, tutoring sessions, job rotations, first line operations, field practices, and using online modules.²⁷ In 2017, more than 50 'Future Force' trainees were promoted to key employee roles and 350 joined the management team.

Country Garden also cast its eye abroad for talent. For example, it initiated a Ph.D. program. Thousands of doctorates from top colleges and universities in China and overseas applied to be a part of the Country Garden team (Exhibit 5). As a result, Country Garden has talented employees from schools such as Harvard, MIT, Oxford, and others.²⁸ This talent pool enables the company to gain a global perspective and the expertise to expand its investments overseas.

THE CORPORATE CULTURE: FOSTERING A SENSE OF BELONGING

Country Garden has a healthy corporate culture. In addition to its excellent talent pool and competitive incentive program, it developed a company culture that is inclusive and caring. The chairman sees employees as the company's building blocks for success. The corporate mission is "to create a better society with our existence."²⁹ And it demonstrates its commitment to

social responsibility through donations and charities. The company and its employees have donated 792 million yuan (US \$115 million) in 2017. Overall, it has supported a total of 9,664 impoverished students and has contributed towards alleviating poverty.³⁰ (Exhibit 6)

Studies have shown that promoting corporate social responsibility facilitates employee recruitment and retention. Nearly two-thirds of people will only work at companies whose values are aligned with theirs.³¹ As such, companies often use social programs to incentivize employees. For example, Deloitte improved its retention rate after letting employees tutor students while still getting paid. Corporate social responsibility efforts boost worker motivation and self-confidence.³² As employees become more invested in their work, the company has the potential to be more profitable. Talented and motivated employees are big contributors to a firm's success.

RISKS: FAST TURNOVER MODEL, CONCENTRIC SHARING

With a business model that works and a motivated workforce, Country Garden seems to have everything under control. But outside pressures from government policies and regulations are putting the brakes on real estate market growth, reflected in the flat to declining home prices in major cities such as Shanghai. While some Tier 3 and 4 cities remain robust, there are fewer of them compared to three years ago.³³ Such market upheavals

Exhibit 5: Ph.D. Program List of Colleges and Universities

CHINA	OVERSEAS
University of Hong Kong	Massachusetts Institute of Technology (MIT)
Tsinghua University	Nanyang Technological University
Tongji University	Harvard University
	University of Cambridge
	University of Oxford
	Imperial College London
	University of Tokyo
	National University of Singapore

Source: Country Garden 2017 Sustainability Report

27 "碧桂园未来领袖计划 Country Garden Future Leader Program 2018," Accessed December 12, 2018, http://www.doctorateassociation.org/careers/18/career_sections

28 "Country Garden 2017 Sustainability Report," May 14, 2018, Accessed December 12, 2018, <https://en.bgy.com.cn/upload/file/2018-05-14/e5a6683e-e727-42a1-8349-df2e95eef4f2.pdf>

29 Ibid, 4.

30 "Country Garden 2017 Sustainability Report".

31 Kimberly A. Whitler, "Introducing The 'Corpsumer': Why Companies Need To Care About This 33% of Americans," Forbes. July 19, 2017, Accessed March 14, 2019. <https://www.forbes.com/sites/kimberlywhitler/2017/07/15/introducing-the-corpsumer-why-companies-need-to-care-about-this-33-of-americans/#38662c2248e4>.

32 Geoffrey B. Sprinkle, and Lauren A. Maines, "The Benefits and Costs of Corporate Social Responsibility," Business Horizons, June 15, 2010, Accessed March 14, 2019, <https://www.sciencedirect.com/science/article/pii/S0007681310000868>.

33 Sheng Songcheng, "6 Keys to Understanding China's Rising Real Estate Prices," CEIBS, August 21, 2018, Accessed March 14, 2019, <http://www.ceibs.edu/new-papers-columns/6-keys-understanding-china's-rising-real-estate-prices>.

Exhibit 6: Country Garden Sustainability Concept System



Source: Country Garden 2017 Sustainability Report.

put pressure on Country Garden especially in financing as investors become less confident in the prospects of real estate developers. Meanwhile, rapid expansion has caused Country Garden's total debt to balloon to 933 billion yuan (US \$132.6 billion).³⁴ Its asset-to-debt ratio soared to 89% in 2017. Facing such market and regulatory uncertainty, Country Garden is speeding up its home sales cycle to minimize exposure to shifting conditions. Chairman Yeung has said that sales turnover was "too slow."³⁵

It didn't help that in 2018, a work-site accident killed six people and injured a dozen. The company then halted current projects nationwide while it conducted safety inspections.³⁶ Incidents like this sully a company's name and carry major implications since many consumers are sensitive to a firm's reputation.³⁷ For a large company like Country Garden, branding becomes extremely important. This type of negative news could cause customers to lose faith in the quality of its products – and turn to its competitors.

Such accidents are likely caused by the tremendous amount of pressure Country Garden puts on its project managers.³⁸ As it sped up its operations and minimized costs to mitigate market headwinds, the company pushed employees to their limits. Country Garden's Concentric Sharing plan put tremendous pressure on the workforce. That's fine in hot real estate markets when sales are

abundant and everyone is motivated. But in a cooling market, sales falter and employees could quit from the pressure.

LOOKING AHEAD

Country Garden's '456' model has served it well in a fast-moving and changing real estate market. With its strong talent pool, the company looked to be the industry leader. It has set the benchmark for the high-turnover business models characterizing China's developers. This model fueled competition in real estate and also changed the structure of the market. But it also saw the downside risk of moving too quickly and putting enormous pressure on its employees. As it deals with strict regulatory policies in housing, as well as high indebtedness, Country Garden faces uncertainty ahead. It has to learn to manage these tough headwinds if it wishes to prevail.

34 天下粤商。“靠”高周转”称霸的碧桂园，还能转多久？” Sohu.com, July 18, 2018, Accessed March 14, 2019, https://www.sohu.com/a/241952810_716662.

35 "China Developer Lights Fire Under Managers for 'Slow' Sales," April 12, 2018, Accessed December 12, 2018, <https://www.bloombergquint.com/onweb/china-s-no-1-builder-urges-faster-sales-threatens-dismissals#gs.YB3VWu0>

36 "Country Garden Suspends Projects After Fatal Work-Site Accident," July 28, 2018, Accessed December 12, 2018, <https://www.caixinglobal.com/2018-07-28/country-garden-suspends-projects-after-fatal-work-site-accident-101309537.html>.

37 Kimberly A. Whitler, "Introducing The 'Corpsumer': Why Companies Need To Care About This 33% of Americans."

38 "Country Garden Suspends Projects After Fatal Work-Site Accident," July 28, 2018, Accessed December 12, 2018, <https://www.caixinglobal.com/2018-07-28/country-garden-suspends-projects-after-fatal-work-site-accident-101309537.html>.