

**Taking a Chinese agricultural company public in  
the United States: The case of Yongye**

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## ABSTRACT

The problem of interest in this research is providing insights into the difficulty perceived by Americans that foreign agricultural companies have little chance raising capital on Wall Street. The thesis narrates the path used by one Chinese firm to raise capital on the US stock market. The story is even more remarkable because Yongye is a Chinese company, unknown and inexperienced in the world of initial public offerings (IPO), yet made a bold entry into the US financial markets.

The thesis tells that story from the author's vantage point as a vice president in Yongye, and from the front row seat of all the negotiations leading to the successful IPO. The story focuses on the author's personal experience working in Yongye as it sought to finance the company's growth to support its vision to increase the prosperity of Chinese smallholder farmers. The company executes this vision within the context of China's industrial expansion as well as its institutional structures. It also presents the product and technology which were the products that Yongye offered to the market.

Yongye's success in raising private and public funds in the US market from 2008 to 2010, came after overcoming many internal structural obstacles, and "lumpy" developments which existed in China's agriculture sector. On a macro level, it is also juxtaposed against a planned economy driven forward by successive Five-Year Plans implemented by the communist government starting in 1953 and acceptance of the UN's Millennial Development Goals implemented from 2000 to 2015. On a micro level, Chinese smallholder farmers found Yongye's specialty fertilizer a compelling value as it helped them increase crop production and sell at higher prices which were in direct opposition to

trends which saw arable land shrinking and becoming less productive due to over utilization.

Ultimately, this story weaves together the description of how a SME agribusiness in China, through local entrepreneurship and foreign business expertise, was able to overcome major structural obstacles in China, and attract enough interest from foreign investors to finance its business and achieve company, national and UN goals. It provides insights into how small to medium size companies in any developing country, with the right product, a clear vision, and the tenacity of its leaders can procure the requisite financial resources to fund its growth. After all, capitalism is about opportunity to expand capital. Politics is only relevant if it becomes a barrier to the process of capitalism meeting its reason for existence.

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Finally, I also want to acknowledge my close friends and mentors who helped make this story possible.

## **DEDICATION**

Selecting the person to dedicate this thesis to is an easy task as it has to be my wife, Florence, who is the consummate educator, and has taught me so much over the last 27 years. She supported our family throughout the course the story I tell in this thesis, the ensuing MAB program and the years it has taken to write this thesis. Together, we could not have survived our time in China, and all of the unwritten experiences we had, without the guidance of our savior and faith in His plan.

## CHAPTER I: INTRODUCTION

China is a very old civilization, with some dating it as far back as 1600 BCE. As a result of that, or maybe despite it, the Chinese take an unusually long view of things. There is this story about a foreign reporter asking the Chinese Communist Party leader to comment on the Party's stellar achievements on its 70<sup>th</sup> anniversary in 2019. The leader held open both arms about three feet apart, and then followed it with holding the thumb and forefinger of his right hand about an inch apart. The significance of this gesture may be lost on many foreigners, but the Chinese understand it as a 70 year anniversary is a very small accomplishment within the context of the nation's history. They obviously still have a ways to go. This thesis presents my small contribution to the Chinese journey in the modern era. The progress China has made in recent decades is nothing short of phenomenal. This is even more so when viewed from a viewpoint which has said this type economic progress within a communist socialist political system has not been able to produce such results. Benjamin and Kautsky (1968) hypothesize that the strength of communist parties deteriorate with increasing economic development. And while some might argue that this success is partly due to some free market adaptations by the Chinese leadership, and others may argue China's growth and development may falter in the future, it has thus far not been the case. We show in this thesis that the strategic approach to development adopted by the Chinese Communist Party may have contributed to this success. One thing is certain, the inherent innovative nature of human beings, individuals and collectives seeking to improve the wellbeing of their neighbors and fellow citizens underscore the unprecedented economic growth that has occurred in China over the past 70 years. This thesis describes the case of one such Chinese individual, the partnership he forged with a young American

(me) who shared his vision for socio-economic progress among some of the world's poor through enterprise development, and their ultimate success.

### **1.1 Research Problem and Question**

The research problem of interest in this thesis is the provision of insights into the struggles foreigners, and particularly Americans, have in creating real business success in China. Of course, there are many hurdles to success in a foreign country, where language and cultural expectations are very different, where the role of government and the responsibilities of the citizen are almost orthogonal to each other. Yet, at the base of these differences is one thing: human beings. And the interesting thing about human beings is that regardless of their cultural and political differences, they seek the same thing: peace, progress, and happiness. The success I discuss in this research is not necessarily financial success, but a deep-seated success from knowing that you have contributed to improving the lives of millions of small farmers through your commitment to the dream of a Chinese entrepreneur whose culture is very different from mine, but whose vision was very similar.

The research question is this: What is the process that a Chinese company with a proven agricultural technology can use to list on a US stock market? Generally, agricultural companies do not have the compelling story necessary to attract attention of Wall Street investors because it just is not “sexy enough”. This is especially the case for “fertilizer” companies which do not have flashy marketing and branding campaigns of a consumer good IPO would have and is much easier to understand – think “NPK” vs. “Beyond Meat” IPO . Wall Street’s skepticism is exacerbated by the fact that the company seeking to list on the US stock exchange is an unknown Chinese company. So, it was not a company listed in Beijing, or Hong Kong, or some other Asian stock market, which is seeking to extend its

reach for capital into the US. This is a Chinese company, small, unknown, inexperienced in the world of initial public offerings, that is making a bold entry into the US stock market.

## **1.2 Objectives**

The overall objective here is to tell a story: the story of the process used by Yongye to enter the US stock market. The story will encompass the challenges and triumph and the underlying strategy used to achieve the objective. It is hoped that this story will provide insights for others seeking to take their own small ventures to the capital markets. The specific objectives are as follows:

1. Describe the situation of Chinese smallholder farmers within the context of Chinese industrial expansion;
2. Provide an overview of Yongye's vision and strategic imperatives it used as its anchor to drive its vision;
3. Describe the vehicle (technology) that Yongye used to achieve its vision;  
and
4. Describe the process that Yongye used in its fundraising efforts, and the eventual success of achieving the objective of listing on a major American stock exchange.

Achieving the foregoing objectives should provide some insights into the driving force at Yongye, and the near religious commitment to the vision. It is also hoped that it will illustrate the importance of passion and tenacity in the entrepreneurial process.

## **1.3 Layout of the Thesis**

The rest of the thesis is laid out as follows. The next chapter presents the overview of the Chinese smallholder farmer within the context of China's industrial expansion, an "event"

that has been unfolding over the past six or seven decades, and has accelerated in the past five. It will describe the modification of communist processes to incorporate entrepreneurial character into the development model. Chapter 3 presents Yongye's vision and how it was perceived in the West by investors. It also presents a description of the technology that Yongye had developed, and which it believed could unleash wealth in China's agricultural production to significantly reduce poverty and increase incomes and wealth. Chapter 4 presents the characters in Yongye's fundraising efforts. It describes the efforts they undertook together to passionately pursue the objective of getting listed on a US stock exchange. The summary and conclusion are presented in the final chapter.

## CHAPTER II: THE CHINESE SMALLHOLDER IN CHINA'S INDUSTRIAL EXPANSION

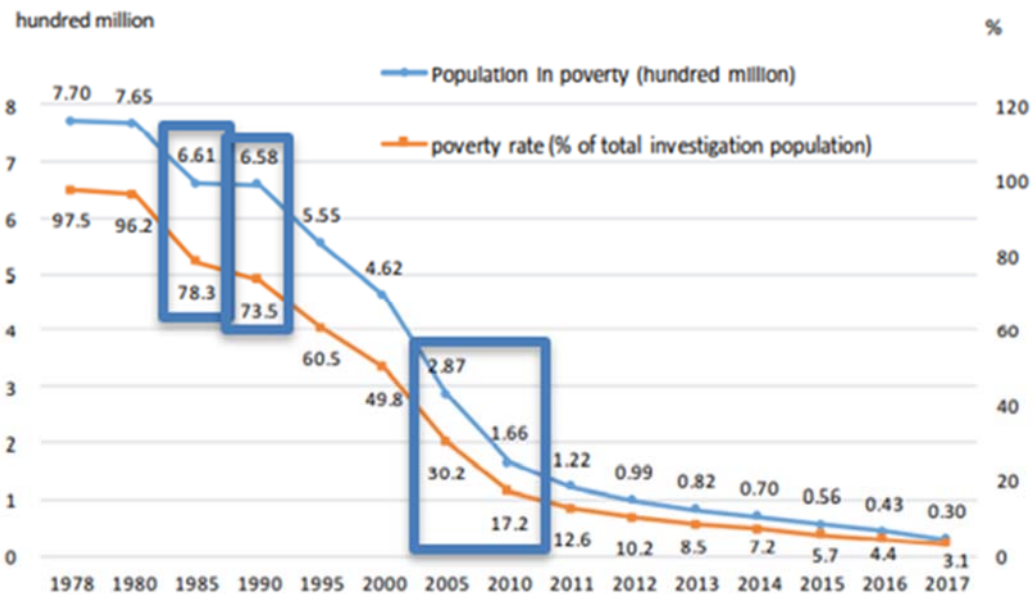
That China's growth and development over the last 40 years has been phenomenal is undeniable (Bijian 2005; Whyte 1995). These successes have also been well documented, leaving very few unique ways remaining to tell it. It is for this reason that I have chosen a personal narrative to present the story of a particular event to illustrate the big picture of what had been going on at the macro-level for many decades.

I choose the genesis of my story to align with Deng Xiaoping's, the "Great Architect" implementation of major economic reforms in the country. One of the major reforms was "opening the country" by inviting large numbers of foreigners to come and teach. I was one of those who responded to that call to go and help a developing country in need. After my initial visit, I made several "tours" in and out of China. What is remarkable is that when my family and I finally left in 2010, it was almost unrecognizable in many respects to the China I first encountered. And, in fact, major cities like Beijing, Shanghai, Guangzhou, Chongqing and Chengdu mostly resembled other metropolitan cities around the world. How China transformed itself within a single generation provides the backdrop for our conversation. We begin with discussing China's Five-Year Planning process, the UN's Millennium Development Challenge (MDG) and its subsequent Sustainable Development Goals (SDG) initiatives. We also explore the impact of Western businesses that make direct foreign investments and established wholly or partial foreign-owned companies in China on the unfolding results.

## 2.1 China's Five-Year Plans

Figure 2.1 summarizes China's growth and development during my personal sojourn. The figure illustrates the reduction in poverty between the end of the 1970s and 2017, and shows, for example, that in 1985, there were an estimated 650 million people living in poverty in China when I first traveled there. However, by 2010, it had decreased to 160 million. Some even say the figures for "extreme" poverty was under 100 million which is an amazing feat to accomplish in 25 years. As a percentage of Chinese population, the proportion of the population living in poverty declined from about 62% in 1985 to under 12% in 2010.

**Figure 2.1 China's Population in Poverty (100 million) and as a Percent of Population**



Source: State Council Information Office (2016); National Bureau of Statistics (various years)

The main vehicle China used to dramatically reduce poverty, on an historic and never to be repeated scale- in my opinion, was and continues to be the Five-Year Planning (FYP) Process. This structural vehicle was implemented in 1953 with the "First" plan and is now



in its Thirteenth iteration. This planning process is used to focus the efforts and resources of a planned economy towards specific achievable goals needed to move the country toward certain ends. The primary focus is social and economic development and encompasses all area of the economy, with major categories being Industry, agriculture, health, governance, Science and Technology, Environment, Land Use, Trade and Defense. Table 2.1 summarizes the themes for the Five-Year Plans from their inception.

The FYP is a policy blueprint and sets medium term goals and is the measure for success at the end of the five-year period. As 1421 Consulting states, “The purpose of the China’s five-year plans is to help the government and civilians to be on the same page regarding the importance and purpose of public initiatives. By announcing the country’s main strategic goals to the people, the party strives to give a sense of direction and unity to the country. For foreign expatriates and businesses, understanding the plan may give important insights into future policies that may significantly impact the business environment of China in years to come.” Each planning period has a basic theme which is noted below – of note, agriculture is less and less of a headline issue.

While not immediately evident in China’s FYP themes, it has long been concerned about food scarcity since the communist party assumed power and especially during the Great Famine between 1959 and 1961. This was something built into the FYPs as agricultural goals. The FAO refers to this as “the ideal in which all people, at all times, have physical, social and economic access to sufficient, safe and nutritious food to meet their dietary needs and food preferences for an active and healthy life.” China had difficulties on many fronts but especially in the production of “safe and nutritious” food

and they have had numerous food safety scandals over the years including the Milk Tainting scandal in 2008 which I will talk about later in this thesis.

**Table 2.1: Five-Year Plans and their Themes**

<b>Years</b>	<b>5-Year Plan</b>	<b>Theme</b>
1953 – 1957	First	The administration adopted the Soviet economic model, based on state ownership in the modern sector, large collective units in agriculture, and centralized economic planning
1958– 1962	Second	Furthering the cause of socialism by transferring more property to collective ownership; Encouraging the economic growth of China through industry, agriculture, handicrafts, transportation and commerce.
1966– 1970	Third	To spare no efforts to develop agriculture, solve widespread problems concerning people's food, clothing and other basic needs;
1971– 1975	Fourth	The average annual growth rate of gross output value of industry and agriculture to reach 12.5%
1976– 1980	Fifth	In 1977, the gross output value of industry and agriculture reached 505.5 billion yuan, 4.4% above-target and representing an increase of 10.4% compared with the previous year.
1981– 1985	Sixth	To achieve an average annual growth rate of 5% for industrial and agricultural products.
1986– 1990	Seventh	To further open up to the outside world, combining domestic economic growth with expanding external economic and technologic exchanges.
1991– 1995	Eighth	Outputs of coal, cement, TV, foodstuff, cotton and cotton dresses were the highest in the world, with steel and chemical fiber outputs second, and electricity supply third.
1996– 2000	Ninth	UN Millennium Development Goals Set; to cap population growth at 300 million by 2000; to quadruple per capita GNP as compared to 1980; to eliminate poverty; and to speed up the establishment of a modern enterprise system.
2001– 2005	Tenth	Increase the number of urban employees and the number of surplus rural laborers transferred to the cities to 40 million each, thereby controlling registered urban unemployment rates at about 5%
2006– 2010	Eleventh	Number of rural laborers transferred to non-agriculture sectors reaching 45 million in five years; Coefficient of effective use of water for irrigation up from 0.45% in 2005 to 0.5% in 2010;
2011– 2015	Twelfth	UN Sustainable Development Goals; Inviting of foreign investment in modern agriculture, high-tech, and environment protection industries
2016– 2020	Thirteenth	Greening: Develop environmental technology industry, as well as ecological living and ecological culture.

## **2.2 The United Nation's Millennium Development (2000 to 2015) and Sustainable Development (Current) Goals**

The UN describes its MDG's as "a milestone in international cooperation, inspiring development efforts that have improved the lives of hundreds of millions of people around the world" and these goals were the global driving force to eradicate poverty and hunger from 2000 to 2015 when they were morphed into the SDG's which are still under implementation. The MDGs were revolutionary in providing a common language to reach global agreement. The 8 goals were realistic and easy to communicate, with a clear measurement/monitoring mechanism.

It is important to discuss international, collaborative, development efforts as part of China's overall growth because these helped shine a spotlight on problem areas in China's economy for many years. The fact that China accepted and implemented these is also significant after many centuries of rejecting foreign engagement. I'll briefly discuss below the impact these goals had on China's growth and development. One important facet the UN initiative had was that it caused China to create a holistic approach where the government departments were actually accountable to the UN and national goals and in China, you have to "save face" or "mianzi" and this drives achievement. This created massive structural changes in the areas of agricultural technology, transport conditions, water facilities, access to electricity, and social assistance systems.

The MDG's were implemented in 2000 with the belief that, "The world possesses the resources and knowledge to ensure that even the poorest countries, and others held back by disease, geographic isolation or civil strife, can be empowered to achieve the MDGs." And in the ensuing years, China embraced the goals and even touted their achievement of them. In one report, they made it clear that, "Perhaps most important, it shows that the

Goals are achievable when nationally owned development strategies, policies and programmers are supported by international development partners.” The one goal I will concentrate on in this paper, since this is primarily the goal, I was involved with is Goal #1 – Eradicate Extreme Poverty and Hunger.

During the 15 years of the initiative, China stated they were fully committed to the MDGs and achieved 13 MDG targets. For Goals 1, Between 1990 and 2011, China lifted 439 million people out of poverty, and China has made great contributions to the global poverty reduction efforts. With its grain production growing for 11 years since 2004, China has supported nearly 20 percent of the world’s population with less than 10 percent of world’s farmland.

In 2012, the UN began reassessing the MDG goals in order to create a more people-centered, development agenda, which actively engaged citizens, scientists, academics, and the private sector from around the world. They developed a new set of Sustainable Development Goals (SDGs) which were implemented in 2015 and Goal #1 from the MDG initiative was morphed into 2 goals: 1) SDG 1 – Ending Poverty through agriculture, and 2) SDG 2 - Zero Hunger through agriculture. These are in place now.

The declining rural, agricultural workforce, has been a major factor in achieving governmental goals with the urban population rising from approximately 500M to 700M between the years 2000 to 2010 which the rural population decreasing from 800M to 700M in that same time period with population being 50% rural and 50% urban. This was a major shift in the agricultural workforce with an estimated 20 percent of the population or 280M people being migrant workers coming from rural, farm labor communities and finding jobs in urban areas.

Another balancing act for China was their need for food security and national growth and development which required importing and exporting a great deal of food products. Between 2003 and 2010, China's import of food went from \$14B to \$53B and its export of food products went from \$20B to \$40B which illustrates their major "lumpy" issue in that national food security is hampered because, as reported by the USDA, China's entry into the international trade markets caused them to cease their own agricultural self-sufficiency which caused them to lower trade barriers and "rock the boat" in their own markets impacting their own farmers ability to produce and sell products. Then, upon entering the WTO in 2001, trade barriers were further eroded, SOE monopolies ended on many products and the economy grew further and farmers continued to experience the lumpiness of growth and development.

Finally, one of the other important hurdles barring many farmers and SMEs from success in agricultural ventures was the limited finance available to them. This was true throughout the agriculture value chain which primarily meant SOEs would gain advantage in capitalizing their traditional business activities from state funded loans, and private enterprises and farmers would struggle to growth strong and innovative businesses because banks would not lend to them. In an OECD report, the authors note that, "It is estimated that, between 45-55%<sup>5</sup> of formal SMEs do not have access to loans from formal financial institutions in developing countries, and this figure increases to 72%<sup>6</sup> when informal SMEs and micro-enterprises are included. As will be discussed later, Chinese farmers do not hold title to their land thus cannot use it for collateral and thus cannot even qualify for traditional loans. As the OECD further noted, "This is particularly pronounced in China due to the land tenure system and the fact that contract rights are not well defined, and tenure is

limited. The 2009 OECD Rural Policy Review of China emphasized the importance of continued reforms that improve the availability of finance in rural areas (OECD, 2009). While progress has been made, rural financial development should remain a policy focus. And when foreign or local companies looked to set up microloan or banking programs, the government would set very high barriers such as barring deposits and requiring high capital holdings.

### **2.3 Western Business Model and China's Development Challenge**

One might think that western agribusiness models, innovation and manpower would be a sure source of help to China when looking to meet its UN and even national goals, but these Western and American assets were not a major resource for Chinese businesses and farmers. One reason for this is that western companies in general, use a method of multinational business expansion which is based upon corporate growth strategies, new target market research and financial projections which typically end up with some hope that, "all we need to do is sell 1 to every person in China". Companies establish a "beach head" in a major city, establish business development and sales activities, bring experts from the USA, hire a few good locals, and pump money into ramping up the machine.

The number of Fortune 500 businesses that failed in China is large; the number of smaller companies who tried to make it in China is even more numerous (I was part of one). The reasons for most are similar. As noted by Carlson (2013) in an article for CNBC business news:

Some suffered from a lack of flexibility, or a failure to localize. Others fell because of bad timing, or a superior local competitor. While the causes are as varied as the industries themselves, a pattern can be discerned among the biggest failures in China: an inability to grasp just how different — and cutthroat — the Chinese market can be. "It's a lack of understanding of the legal and cultural environment

that leads to most failures,” says Shawn Mahoney, managing director of the EP China consulting group. “The only difference between a success and failure in my experience is that people who are successful are more willing to talk and learn about how things work on the ground.”

The key to success in China is “work on the ground.” Many foreign companies did not (and some still do not) understand that to be successful and ultimately “sustainable”, they need to integrate into the Chinese culture, and follow Chinese practices and regulation. The fail because of a lack of appreciation of the differences in culture and as a result, in everything. This is not surprising for Americans abroad (Whyte 1995; Abramson and Ai 1999; Ester and Maas 2016).

China has been a very tough market even for “successful” American companies. Companies who succeed in China have done so at great cost and over a long period of commitment to their success in China. Coca-Cola thought it were invincible in China, being one of the most recognized brands in China, even before it arrived. It neglected the politics and local customs when buying Huiyuan juice and it was an abysmal failure (Xian-Chu 2009; Chin 2010). Google has struggled with political issues (Tan and Tan 2012). Best Buy (Sharma 2020) and Home Depot (Shedd 2019) both found the competitive landscape too complicated and tough, and pulled out of the market(Sharma 2020). Google has been called a “political tool.” My first start-up company pulled out of China for similar reasons that have befallen these US corporate giants. Understanding the culture and doing business the right way is important in the new China.

Another reason is because most American businesses are not prepared to do battle in China the Chinese way. Previously, a foreign venture would waltz into town, set up shop and run the show. China was developing and needed the exposure and the foreign direct investments (FDI) – so they ignored the cultural ignorance and brash behavior for the



ultimate goal. While there were many failures, there were enough successes to keep the pipeline flowing of funding and expertise. Similarly, many businesses failed because they used a strictly western, numbers-based business approach. The Chinese, in general, focus on the “heart, mind and soul” approach to foster and grow relationships. Recognizing this helped me succeed in a Chinese agribusiness company which garnered much notoriety, including investment by Goldman Sachs, a “Tiger Cub” and Morgan Stanley Private Equity, and the recognition of Harvard Business Review and Blue Ocean Strategy Institute.

#### **2.4 Chinese Smallholder Agriculture**

The declining rural, agricultural workforce, has been a major factor in achieving governmental goals with the urban population rising from approximately 500M to 700M between the years 2000 to 2010 which the rural population decreasing from 800M to 700M in that same time period with population being 50% rural and 50% urban. This was a major shift in the agricultural workforce with an estimated 20 percent of the population or 280M people being migrant workers coming from rural, farm labor communities and finding jobs in urban areas.

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many products and the economy grew further and farmers continued to experience the lumpiness of growth and development.

Finally, one of the other important hurdles barring many farmers and SMEs from success in agricultural ventures was the limited finance available to them. This was true throughout the agriculture value chain which primarily meant SOEs would gain advantage in capitalizing their traditional business activities from state funded loans, and private enterprises and farmers would struggle to growth strong and innovative businesses because banks would not lend to them. In an OECD report, the authors note that, “It is estimated that, between 45-55%<sup>5</sup> of formal SMEs do not have access to loans from formal financial institutions in developing countries, and this figure increases to 72%<sup>6</sup> when informal SMEs and micro-enterprises are included. As will be discussed later, Chinese farmers do not hold title to their land thus cannot use it for collateral and thus cannot even qualify for traditional loans. As the OECD further noted, “This is particularly pronounced in China due to the land tenure system and the fact that contract rights are not well defined, and tenure is limited. The 2009 OECD Rural Policy Review of China emphasized the importance of continued reforms that improve the availability of finance in rural areas (OECD, 2009). While progress has been made, rural financial development should remain a policy focus. And when foreign or local companies looked to set up microloan or banking programs, the government would set very high barriers such as barring deposits and requiring high capital holdings.

About two-thirds of the developing world’s 3 billion rural people live in about 475 million small farm households, working on land plots smaller than 2 hectares .<sup>1</sup> Many are poor and food insecure and have limited access to markets and services. Their choices are

constrained, but they farm their land and produce food for a substantial proportion of the world's population. Besides farming they have multiple economic activities, often in the informal economy, to contribute towards their small incomes. These small farms depend predominantly on family labor.

Imagine an infographic which concisely and beautifully shows China's food supply chain as it efficiently and effectively sources and feeds 1.3 billion people every single day. Import shipments come in, export shipments going out, port supplies move inland, remote rural crop production moves out towards cities, processing occurs, distribution happens, store shelves get stocked, consumers buy groceries, go to restaurants, etc. Then it all starts over again the next day. China is able to feed its close to 1.4 billion people with less than 10 percent of the world's total arable land and only 6.6 percent of freshwater resources. By comparison, the US has 1.3 times as much arable land. From 1978 to 2017, China's average annual agricultural growth rate was 4.4 percent, the best in the world. In current dollar terms, China's agricultural value added increased from 7.6 percent in 1981 to 28.9 percent in 2017. China has already surpassed the US to become the world's largest agricultural value-adding country [China Daily].

In China, nearly 98 percent of farmers cultivate farms smaller than 2 hectares – the country alone accounts for almost half the world's small farms. These farms are located in very remote areas outside of very small towns and take hours to travel to. China's land resources are distributed among 231M people so that farm size is approximately 1 acre each. In the USA this would be a "hobby" farm, but in China, this is poverty alleviation, food security and a career all together. Now imagine being at his small land holder with limited technology (except spray bottles and our product) and no margin for failure and no

wiliness to risk anything new. Now also imagine that your daily existence and success as a farmer relies on those around you, the governmental policies allowing your success and you can't own any of your land in the long run. This means you only profit off of what you make from your crops and you cannot build up any equity over time. Studies show that they are not linked well to the retail sales supply chain so need to struggle to get their crops purchases in local farmers' Markets (cai shi chang) or small stores in small cities which adds to their daily struggles.

In order to be truly successful, a small farmer must also be business savvy, and entrepreneurial in ability. Agriculture studies show that small farms are actually very capable of using inputs at similar or better rates than larger farms and studies also show that entrepreneurial farmers are able to have a major impact on rural poverty and that governments can seek to, "alleviate rural poverty by putting more emphasis on rural policies, such as the promotion of farmer entrepreneurship in rural areas." Some of the policies the government needed to change were: land and property rights, R&D Technology and Transfer, Human Capital, Income Support, Capital Investment, Protecting Natural Resources, Hukou Reform, Entrepreneur Support, Infrastructure Investment, and Improving Government Services. Huang et al. (2008) observe:

They can search for off-farm employment (and almost always find a job) or they can go into the production of high-valued fruit and/or vegetables. According to our data, there is absolutely no income penalty for doing so. The average grape-producing and apple producing households (selected from a provincial representative sample) had assets that were statistically indistinguishable from the average rural resident earning a wage in the off-farm market. Even when all other factors were held constant using multivariate analysis, it was found that the average horticulture-producing family in Shandong made almost the same level of earnings as a family that had chosen to work off the farm.

My first visit with smallholder farmers in China was an amazing event; and since then I have walked many miles on small farms throughout China, all the way from Beijing to Hainandao, and encompasses small plots and large, hot humid weather and cold frigid weather, saved only by a greenhouse respite. From a personal standpoint, the stories of the farmers are amazing, but I also want to set the context here with some of the structural challenges because obviously, many of those lifted out of poverty were farm workers and their families. This was definitely one of the goals of Yongye, the company I worked for and traveled all over China with.

Chinese farmers are hardworking and super productive when given the right inputs. However, they do not have much beyond basic hand tools and other rudimentary resources. (I did see satellite dishes on many of their houses). Studies show that smallholders are indeed more efficient and produce amounts closer to the maximum output, as compared to larger holders. Smallholders use their assets more intensively, probably to substitute for other inputs, such as land. Fertilizer is a land- augmenting input: its intensive use is supposed to substitute for land – a capital input smallholders have not in abundance – through increased yields per hectare.

China was built and sustained upon the rural farming community and any hope of staving off mass poverty and hunger and achieving food security is dependent upon the rural workforce and small hold farmers who do most of the farming in China. With this obvious challenge in front of it, China needed to reform many structural underpinnings of its society, but these were slow in developing and thus continue to cause the uneven development I mentioned earlier in my thesis. Below are some of the major structures

China needed to reform and yet did so very unevenly which impact farmers in the agricultural supply chain.

#### *2.4.1 Land Tenure System*

It is an understatement to say that land use is a critical right for successful farming business. While land ownership and use is something we take for granted in the west, in China this isn't the case because land is owned by the village collective and is in the village leadership's control as to what happens with it including being converted into construction use for large scale apartment/condo development or other commercial use. This land ownership in China is called the Household Responsibility System and each village typically has 5 to 10 plots to allocate to families living there. While farmer's land ownership is tenuous, they do secure 30-year rights from the village to work the plot. This plot is typically 1.2 acres or 6-7 mu in the Chinese measurement.

If this is decided by the village leadership, the farmer and his/her family lose the land they may have been farming for decades with no recourse. Recently, they have been given the right to transfer the land at a market price, however, this also can be taken away if the land is redeveloped. Many protests in China's rural areas occur because of this issue where village leaders' profit from conversion of land and tenant farmers are forced into becoming migrant workers or finding another plot of land to use. Notwithstanding the above, farmers understand the context in which they are developing their businesses, and in all cases hope for the best given the sometimes-staggering odds against them.

#### *2.4.2 Hukou System*

One government policy which was implemented early on in the communist structural reform is the population registration system of "Hukou". Back in 1958 when this was set up, it was a way to ensure resources were sufficient and controlled at a local level

and could be “rolled up” to a country, province and state level. This system, once implemented, began to create a two tiered system whereby urban and rural residents were prioritized with soviet styled work and resource commitments and heavy industry became the national emphasis along with agricultural production to feed and sustain the country. In order to keep this system intact, the government used the Hukou system to restrict the flow of internal migration by limiting resources such as housing, food and necessities to each person’s Hukou and to move away from your Hukou would mean no government resource allocation. Later in the system’s development, this also included education and medical services being restricted to your Hukou. Once born in a Hukou, that became your “anchor” for government tracking and this can only be changed in certain circumstances.

Over the years, this effectually locked rural residents and their dependents into farming without any way to change your circumstance. For rural residents this did have the benefit of land use for farming and for urban residents this became access to health insurance, retirement allowances, maternity benefits, unemployment insurance, etc. And for rural residents, this again, was the ability to work the land, live on it and provide agricultural production for the rest of the country. Obviously, over time, this evolved into a situation where urban opportunities, wages and benefits increased over time while rural opportunities grew much more slowly. Ultimately, this system became a huge deterrent on any internal migration from rural to urban areas – as intended and while something that started out protecting access to resources, now locked residents into those resource centers with no hope of change. This led to the migrant worker crisis, which is described below. Yet, despite the attractiveness of urban life and employment opportunities, most migrant

workers continue holding on to their land rights in their rural communities because that is where they would actually like to be.

#### *2.4.3 Migrant worker Crises*

Since the 1980s, a great deal of research has been done on the “migrant” class for workers in China which describes those workers who give up local benefits (as described above) in the rural areas and move to the urban areas for better working opportunities. This “liudong renkou” or “floating population” They typically move from rural, Hukou locked areas to small and large cities where jobs are typically more abundant and usually higher paying, but where they have no social benefits. The number of migrant workers increased from around 30 million in 1989 to 62 million in 1993 and further to 250M by 2015.

There are several reasons for this migration of rural residents, but the first is the catalyst for the event which was mass unemployment in rural areas which occurred in the 1990s and then the further structural problems related to the Hukou system as noted above which “kept people tied to where they lived by making government services contingent on their occupation and place of residence. While agricultural laborers received land, nonagricultural hukou holders received rations as well as public services. [china’s internal migrants] Basically, If you were lucky enough to be granted a plot of land by the village leaders, you could make a living, and if not, you worked for the farmer or a lower paying job in the village, or you became a migrant worker.

#### *2.4.4 Resource Constraints and Chinese Smallholder Farmers*

While the above brief description only touches on the myriad of challenges the small holder farmer had and still does have in China, the picture painted is stark for the most part. Now layer in the Fiver Year Planning goals, global expectations, and UN MDG goals, all on the backs of the small farmer, and you can imagine how distressing it could be



for farmers. This is exacerbated by the fact that Rural communities and small holder farmers were basically powerless to push for any reforms until the migrant worker crisis exploded into international news. Thus, for the farmer, with uneven development, no political power, and inability to change much about his/her circumstances, attention turned to making the most of his/her farming business and making it as profitable as possible. This sets the stage for the Yongye story.

## **CHAPTER III: YONGYE'S STORY**

The Yongye story is a Chinese national story about freeing small farmers from the shackles of an uneven structural reform by providing them with a more effective and much cheaper local solution. In this chapter, we present the vision that motivated the formation of Yongye and its value proposition to its smallholder farmers. We also present the charismatic leader behind the company's vision, establishing it as the source of the tenacity that emerged in the search for funding to transform the dream into reality, make the vision real for the millions of Chinese smallholder farmers.

### **3.1 Yongye's Vision**

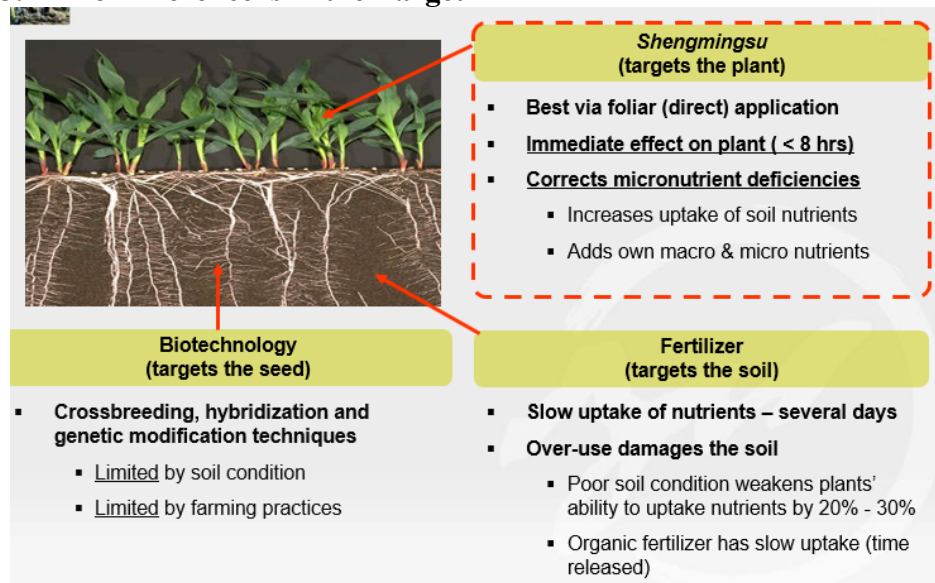
When I first set foot in the new Yongye offices, I saw the "Just for a Peasant's Smile" poster, a poster showing farmers smiling. The company's story is that using its novel nutrients in production increased yields, increased profits and made farmers smile. That product is Shengmingsu. Herein, therefore, was the vision driving Yongye: Happy farmers, happy employees. That employees felt they were part of a tangible change in the lives of people they could all relate to, may be were even part of, was a strong motivation for them to work hard on improving farmers' wellbeing.

### **3.2 Shengmingsu: A Novel Product**

Directly from the marketing material we produced at Yongye, the following describes Shengmingsu. It is a nutrient that farmers apply to the foliage of their crops. Its base is a fulvic acid compound. Fulvic acid is an acidic, organic polymer which can be extracted from lignite coal or other organic matters developed from the natural decomposition process of plant/animal residues. Fulvic acid strengthens the metabolism of a living organism and increases its ability to withstand adverse conditions. It also improves uptake of nutrients and minerals by cells by acting as a transport agent.

China has abundant reserves of lignite coal, the raw material for fulvic acid. Yongye actually purchases humic acid, another derivative of lignite coal, and extracts fulvic acid from humic acid. The company combines the base extract with its proprietary formula of micronutrients including nitrogen, phosphorus, potassium, boron, and zinc, which stimulate the growth of plants and animals. The finished product is “Shengmingsu,” which translates as nutrients for life. The company offers two distinct lines of the product: one for plants, and the other for livestock. Not only did farmers using the product see increased yields, they also saw healthier plants, and in some cases, extension in the growing season due to healthier roots and leaves. The farmer could see over 10 times return on their investment into the product, a return unheard for many agricultural inputs, especially plant nutrients. The differences between Shengmingsu, on the one hand, and biotechnology and fertilizer on the other, are presented in Figure 3.1

**Figure 3.1 The Difference is in the Target**



Yongye’s customers are committed to the product because its benefits are visible to them.

This has led to a cult-like devotion to the product, with some saying they are “hooked on

it”, like a drug. But it has also made the man who brought to them assume a messianic status among these small farmers because of the product’s impact on their wealth situation.

### **3.3 Mr. Wu Zishen, CEO**

The brain and heart behind Yongye and its Shengmingsu product is an impatient, local Chinese, serial entrepreneur who needed to raise a great deal of independent, non-government capital to transform a vision of increasing smallholder farmers’ incomes into reality. Given the funding environment in China, to achieve this dream of non-government funding required looking outside of China. The strategy then was to raise capital on an American stock exchange.

In late 2007, on the eve of the global financial meltdown, I joined the team at Yongye as Vice President of Corporate Strategy. Wu Zishen, the CEO, was a hugely successful Chinese entrepreneur from the deserts of Inner Mongolia. His success had come from building a business in the electronics industry. His team included a local Chinese scientist, who, on the eve of his state-mandated retirement, shared his discovery of the “essence of life” formula with Wu Zishen. The product that was to become Shengmingsu seemed almost too good to be true for Mr. Wu. How can a natural plant nutrient help crops grow in the harshest of climates, with more strength and better taste than synthetic fertilizers? But like all entrepreneurs, Mr. Wu let his question drive him to answers, instead of despair.

I became Mr. Wu’s strategy “guru” as we devised a way to take this product forward after trials with local farmers had shown it to be probably more promising than the old scientists had envisaged. To avoid becoming entangled in Chinese government bureaucracy, the focus was set on Wall Street as the source of funds to take Shengmingsu to market. The amount we needed to raise was \$180 million if the dream was to be

achieved. But the year was 2008, and the US (and the rest of the world) was just getting ready for a financial meltdown that would, at the time, create the biggest recession since the 1929 recession. Mr. Wu was a man of the highest integrity and he despised sleazy salesmen, or NY investment bankers, who spouted “huyou” talk, or hot air with no substance. Mr. Wu meant what he said, and always followed through on his word. This would be critical, considering the journey ahead.

By the time I joined the company, Yongye was already a national power and had achieved many of its goals, including the improvement of farmers’ lives all over China. The company’s CFO, Vini Liang, was also new to the team, having joined just a few weeks prior. Thus, Mr. Wu needed to “indoctrinate” both of us in the ways of the Chinese farmer and Yongye’s unique way to reach them. Using the prescription of a book written by one of Yongye’s VPs, “Learn Marketing from Chairman Mao,” we all learned how to engage and communicate with Chinese smallholder farmers successfully. Embedded in the lessons were two things. First, you had to employ the best concepts in marketing strategy. Second, you had to do it Chinese style, and who best to learn from that one of China’s most revered communicators: Chairman Mao.

## CHAPTER IV: ENGAGING WALL STREET

Mr. Wu and I were embarking on our journey from the fertile farmlands of Inner Mongolia to the hallowed halls of the investment community on Wall Street, requesting millions of dollars - at the same exact time venerable names like Bear Stearns and Lehman Brothers faced their downfalls. The American economy experienced one of the worst years in 2008. Storm clouds were gathering on the horizon as we prepared to go public. The financial system was on the verge of economic collapse, with a perfect storm of a real estate bubble, credit crunch, and revelations of Ponzi schemes from the likes of Bernie Madoff. On top of all this, the American public's attention was diverted by an election year, with John McCain and Sarah Palin fighting wars of words against a new guy on the scene, Barack Obama and his affable sidekick Joe Biden. Meanwhile, the Chinese economy continued to locomotive ahead, as they gleefully anticipated hosting the Summer Olympic Games.

We landed in Los Angeles on February 2nd, 2008, having no idea what we were in for – including the cataclysmic financial downturn that was already looming over our heads. It was the beginning of Chinese New Year, and for anyone familiar with Chinese New Year, you know that it is a sacred time. The entire country essentially shuts down for two weeks, as twenty percent of humanity clocks out of the office, and commits to fifteen days of traveling through heinous traffic to see relatives, eating tons of food, drinking and toasting, staying up late playing mahjong, and setting off illegal fireworks until dawn. If you are running a company and you have a factory located in China, do not expect anything to be produced during Chinese New Year. While it is unthinkable for a Chinese person to work during this sacred time, that was the exact time that Mr. Wu, our CFO, and I boarded a plane to have our first fundraising meeting with investment bankers in the USA.

For many years, when my Chinese friends compared Chinese New Year to Christmas, I just could not see it. But over time, I realized that beyond the lights and decorations that go up at Christmas in Beijing and stay through Chinese New Year (two birds with one stone), the family time, food and the celebration are very much the same. However, Wall Street never sleeps so we started the trip just before and continued it through Chinese Christmas, which we in the West would typically not do. Now, just three years later there is a growing appreciation for this Chinese holiday.

#### **4.1 First Meeting**

February 3, 2008 - We arrived in Newport Beach, California to prepare for our meetings with Roth Capital. Newport is the crown jewel of Orange County, located south of Los Angeles, with year-round perfect weather. It was barely 20 degrees when we left Beijing, but by the time we got to Newport, it was in the mid-80s, with clear skies and endless sunshine.

As we went over last-minute details, Mr. Wu said to me in Chinese, “Larry, we have to be successful because so much is riding on this venture. Our families, our employees, our farmers.” I smiled. We had a great business model, a great team in place, and Yongye was on the way to establishing a stellar reputation in China as a company with ingenuity and integrity. We had nothing to hide, and the bankers had everything to gain by investing money with us. Why worry? After being with the company only several months (94 nights into my 1001 nights journey), I knew I had a lot to learn - only I really didn’t know how hard it would be to do so on the road.

As the meeting began, I helped lead the conversation as we went through our corporate presentation, financial projections, and mechanics of the business model, tethering them all together into a story format. Vini and I worked with the Roth staff in

English, and Mr. Wu would add his input in Chinese, with translations as needed. Our rag-tag team, assembled only recently, struggled to put a chassis, wheels and a high-speed transmission, which would harness Mr. Wu's high-speed vision of over five years. This was a challenging proposition, and a tiring one.

Later that day, Roth's president came back into the conference room to see for himself how things were going. From a Western perspective, I knew why he asked Mr. Wu the next question. I also knew we were doomed with the answer, "Mr. Wu, who would you say are your main competitors?" Vini translated the question for Mr. Wu, and there was a moment of back and forth translation. At last, Vini turned to Byron and delivered Wuzong's brazen response - "Nobody." While it is basically true, I realized that we could lose credibility over this, and so did Roth Capital. Our host for the day could see it was time to regroup, and said, "Guys, it's been a long day. Why don't you take a rest back at the hotel, and we can resume in the morning?" In other words, "This isn't going well, take some time to get your story straight, and come back if and when you're more prepared." Back at the hotel, on this and many more nights to come, we would stave off "death" (in the 1001 nights genre) by walking to dinner, buying fruit and "fangbianmian" (instant noodles), then sitting down and going over every bit of our story again and again. We documented numbers; We poured over excel spreadsheets going over and over the financial model to get it right; We called China to get updates on the business to add to the PowerPoint presentation – no matter the hour; We called Zhu Ling our Board Secretary to help us get legal information correct; We translated certificates from the government, and on and on.



On some nights, I would get that 11 PM call from Mr. Wu to help with something like a hotel Internet connection. This was just a way to get me back in, to go over something else he forgot to say, or to work out our “guanxi” so we were on the same page and felt like a team.

I winced as I realized that Mr. Wu would be highly displeased with our first performance. Wuzong knew Yongye’s China plan down to a T, and was constantly discussing it with Vini and me. He taught us in the same way that he would teach us how to serve tea the proper way. Repetition, over and over again.

Given the language barrier (Mandarin was not the first language of either Vini or me), Vini and I were ‘getting up to speed’ more slowly than Wuzong would have liked. This roadblock was not in the plan, it was in our presentation of the information. It was my fault, I felt way in over my head, and knew there would be hell to pay back at the hotel.

#### **4.2 Hammering, Tightening and Tweaking**

We continued preparing for the road trip, and things slowly began to improve. Iteration after iteration, we went over the presentation, played out on PowerPoint slides, and I gradually learned the nuances of the Yongye story and business plan. Vini became more comfortable with the metrics, as the banking team saw the real value of what we were doing. These days of hammering, tweaking and tightening our story had their impact, and Mr. Wu saw the foreigners were finally getting it. The vision and business model were becoming clearer to everyone, and thus its potential value was increasing.

To complicate things, we found out that we were actually the last of three similar companies who had recently approached these same investors, for the same express purpose – to raise funds to jump-start ventures in the Chinese fertilizer sector! They had heard this tune before, so it was all the more critical for us to differentiate ourselves. Years

later, investors would mistakenly group Yongye into this same basket of Chinese agribusiness companies, comparing us to them over and over again. Yongye would eventually outstrip our ‘competitors’ in both revenue and notoriety in China, but in the beginning, it was a yoke around our necks, making it crucial for us to go the extra mile and prove our worthiness.

We waited, and prepared, and prepared some more. Finally, we got the approval from Roth to hit the road on my Day 98 with the company (after almost 100 days after my first day in the fishbowl office at Yongye HQ). Once the days were set, the appointments began to fill up. I still had no idea what I was getting into. Mr. Wu did not either.

We hit the ground running, planning to start on the West Coast, then made our way thru the Midwest to the East Coast. The days would be grueling, and the nights also. Our daily schedule would begin at 7:30AM with a breakfast presentation, then continue relentlessly hour after hour as we visited different funds in different buildings all over each successive town. After finishing our final presentation at 5PM, we would be off to the airport, and the next city. Each meeting at each office with each investor was different, and we were constantly grilled about different facets of the company. It was tough, but it made us get tougher.

One casualty on the road trip would be sleep. The other, especially for Mr. Wu, would be a lack of proper Chinese food. From city to city, Wuzong would practically starve during the day. At night, we would scour the city, seeking the local Chinatown for some ‘real food’. Then it was back to the hotel for a late-night strategy session to learn more about the company, tighten our story, and prepare for the next day’s battles.

In Chinese fashion, we entered each meeting with a big entourage and announced ourselves to the receptionist. Incidentally, after the financial crash of 2008, we noticed that many companies started dispensing with their front desk help, thus we would have to announce ourselves to the buzzer at the door, or phone at the front desk. We would meet with one or two representatives of the fund, typically the analyst and the fund manager. Our team would sit on the window side, with the fund managers getting the good view of outside. Almost always, we were in a nice boardroom.

The companies were all in varying sizes, from \$100M to over \$1B under management. To me, at the time, this was very intimidating. In order for me to prove my worth, I would have to navigate the gauntlet. It was David vs. Goliath. Gordon Gekko vs Bud Fox. Kirk Gibson vs. Dennis Eckersley. One pitch was all we got to make the right impression. To prepare for each meeting, I would read each investment company's strategy statement - which generally intimidated me more than anything, with their boilerplate language.

February 9-10, 2008 - Chicago, IL. The first weekend out, we found ourselves on a stay over in Chicago, on the way to Minnesota. On Saturday night, after freezing in below zero-degree weather at Navy Pier, I jumped on a conference call with our legal team to discuss our SEC documentation. After talking to our crack legal staff at Loeb and Loeb, and getting raked over the coals about the company's first iteration of the business section for our "Super 8-K" (because it isn't specific enough, or is too "marketing focused", etc...) - I realized that this work was going to be tougher than I thought, and I had another steep learning curve to navigate.

My “favorite” lawyer kept saying, “cut out all of the marketing language” (i.e. “Huyou”) and stick to only what was real and verifiable – this was difficult, since I was still learning about the company on a daily basis – thus, more calls back to China, more long nights with Mr. Wu and getting everything documented correctly. Getting your lawyer to trust you is key and I would spend many hours doing so by taking his advice. Later, he would become an invaluable resource as we battled in many proverbial trenches together in successive rounds of fundraising. But on this day, he was “in my face” which was a reminder that going public was not for the faint of heart.

How did we finally get everything right? We had a great team in China who were on call 24/7. This especially applied to Zhu Ling, our Board Secretary, and an amazing person when it comes to executing on a plan. She can quickly grasp what needs to be done and in the complex milieu of the Chinese business environment (made more complex by having to follow SEC and FCPA regulations), then she can marshal the troops, interact with lawyers, accountants, bankers and internal staff to get the job done. Many times on the road, I would verify with her, at all hours of the day and night, information about the company first before putting it in our SEC documentation. She is a stickler for facts and truth and worked tirelessly to get us what was needed when it was needed.

Zhu Ling and other people on our team were adept at wading through facts, figures and mounds of documents in English and Chinese and pulling together financial and business related information much better than I had ever thought possible, and I believe this strong work ethic comes from the Chinese educational system. This was always critically helpful when dealing with the SEC’s relentless requests and requirements.

February 11, 2008 - Minnetonka, MN. Back to meet Rich Gammill at Black River Asset Management, the asset management arm of Cargill, which is the world's largest privately held agriculture company. We had met up with Rich in Shanghai back in January to pitch our story (also practice it for the first time) and gauge his fund's interest level. We had not sealed the deal and we were back for what would be the second in a long string of meetings and phone calls, which would be needed to seal their participation. As true agriculture investors, they were intrigued by Mr. Wu's vision and the growth of the company, however they were not easily convinced.

In true form for every meeting, Mr. Wu insisted on bringing gifts to each special meeting, and this was one of the funds he wanted to convince. I told him many, many times that we did not need to bring gifts, and this could actually work against us if the gifts were disallowed by some compliance officer. In this regard, he never listened to me and only listened to his cultural upbringing.

Rich was one of the sharpest and most prepared fund managers we met on that trip, and for that matter, on any trip. He knew the agriculture sector and peppered us on all sides about the business model, the research behind the efficacy rates we were promoting, the structure of the company, the cash flow needs (given our high growth rate), and all things Mr. Wu.

Most investors skipped over the "getting to know the management team" part of investing, but Rich delved into knowing and understanding the background of the CEO well, and got to know Mr. Wu and I very well over the two years we met with him. This convinced him to invest, and he clarified and kept us true to our word on every detail we announced to investors. While most were looking to take a risk on anything remotely good,

in order to capture the early profit and exit quickly, Rich and most of our early investors would turn out to be long term holders of the stock.

February 12, 2008 - New York City. at last! It was late in the road show. Nine days in, and still no storied meetings on Wall Street. Finally, the time had come.

You would think an American would have some past experience with NY, but I had been there only one day in my life. I had not avoided it, but had not pursued it – I was from Los Angeles, and NY was our mortal enemy in baseball and in culture. We could not imagine being friends with people who are so “in your face”, and anyways, I was a Dodger fan and despised New York teams. In New York, we kept the same crazy schedule, and if we did not have a meeting at night, we would search for Chinese food to feed a starving Mr. Wu. We would start the next day with the same schedule and so on, until all the funds who would take meetings had taken them.

By far, NY was the most scenic place to meet investors. I have been to most major investment banks and funds in NY telling the story of Yongye. We have been in most of the major buildings, and have walked many miles looking for interested funds looking to invest in our company. Some funds were very cordial, and we had great and spirited conversations. However, I can remember one fund that barely gave us the time of day and spent most of that time talking about how great they were. Fortunately, this is not the norm for fund managers.

On February 15th, 2008, and we had been on the road for two weeks, working day and night under great stress, lack of sleep and with 6-8 iterations of the same presentation, and the same follow-up questions each day. Out in the morning, dinner at the airport or on

the plane. New city that night. Same thing the next day. All of this, with no idea if we would ever raise any money at all. It was tedious, frustrating, and nerve-racking.

We had spent a month on the road, meeting with all the right people, honing our message and communication style - we had prepared the right paperwork and everything was ready to go, and yet still no countdown to deal close. This was after hours of due diligence, 2AM phone calls and many emails back and forth. Now, Roth had to come with an alternative solution to keep the deal alive. Our saving grace was the fact that Goldman Sachs was interested in participating in our funding, and though not ready to invest at the time, they would help structure a term sheet, which would be “Goldman investable” later. Thus, with Goldman behind us, Roth worked to structure the term sheet without a formal lead investor, knowing that others would follow Goldman. While this was true, others dropped out, knowing that Goldman was not easy to please.

Night and day, we kept working on the deal. The good thing was that there was still interest was in China, because that is where the growth opportunities were. Money was chasing Chinese projects as America stumbled. The student was now teaching the teacher. Like every entrepreneur waiting for that first “real” infusion of cash, we felt frustrated. Humbled. Infuriated. Why was this taking so long? We had really gelled as a team, and received compliments by the end of the road show. At the conference, everyone spoke highly of us and wanted to get into the deal. We took on each investor as they came, and told our story. But still we waited.

#### **4.3 Mei Ban Fa**

With all this arduously hard work, by a whole team of industry experts and outside consultants and lawyers, we were still on hold as investors decided. China is familiar with famine, difficult times and tragedy and its people have a deep cultural value of patience and

strength which some have characterized as “bamboo swaying in the wind, but not breaking”. One saying used during a time of agonized patience is, “Mei Ban Fa” which literally means, “No Way” or “No Means”, but is understood to be, “I have no other alternative, but to accept this hardship in life”. At this point in our Wall Street journey, “Mei Ban Fa” was commonly said. [lonely planet]

We started that last call around midnight Beijing time, for what was the biggest conference call in my life up until that time. Under normal circumstances and under light of day, this would not be an impossible call, but after three months of 80- or 90-hour weeks, five cities a day, 3AM calls from insistent bankers, I was getting exhausted. However, *mei-ban-fa* (no other solution), so tonight the adrenaline had to flow, given the CEO’s mandate. I felt we were finally moving along, and the disparate parties seemed to be moving towards the culmination of the deal ... or so I thought.

Just as we were agreeing upon the closing terms, the banker from Hong Kong unexpectedly threw out one more deal-breaker into the term sheet. I knew if we did not close tonight, and this got back to the CEO, it would totally scuttle the deal. I braced myself for the worst and was ready to pull the plug on the negotiations, potentially sacrificing everyone’s stake in the deal, including my “sweat equity”. Only six months earlier, I had the crushing experience of having to return all the investment to our angel investors on the biodiesel deal, so this second catastrophe would be a hard pill to swallow. I said a little prayer then jumped back into the discussion.

About that time, Mitch Nussbaum, from Loeb & Loeb, did a bit of quick thinking (as he would on many an occasion after that) and found a solution that everyone could agree with. For Goldman, they got what they wanted - assurances that the structuring of the



deal now would allow them to participate in the next round - if so desired at that time. For everyone else, they got what they wanted - Goldman was staying interested. This got us over the hurdle, into the closing process and the “flow of funds” began the next day. I would live through many other such “life and death” decisions, but none felt quite so “near the cliff’s edge”.

April 17, 2008 - Day 169 - The Magic Day. The deal was finally over and the funds were soon to be transferred - \$10 million to back up Mr. Wu’s promises. This was the jet fuel the company needed to take off - which it did. He had leveraged everything possible, including his valuable reputation, to make sure we stayed on track during this tumultuous time. This was a major breakthrough.

At Yongye, everything is a campaign, system, and promotion. If you do not believe it at first, you will later. The farmers love Shengmingsu. Employees love the company. Yongye is different. We are all “Xingku” workers. The number of hours it takes to satisfy a Big Four auditor; the number of late-night calls. The business trips. Most of the management team either have or are in the process of getting MBA’s (except for my MAB). The laobaixing connected with Yongye love the product and the company and will “xinku” and “mingku” in order to make it successful. When new products roll out, watch out.

Most investors who have visited the stores, the farming villages and the grasslands in Inner Mongolia have immediately understood it. They have then become some of our best evangelists. Early investors such as Rich Gammill at Black River and Peter Siris at Guerilla Fund visited are perfect examples of this. They have seen the Yongye social

network in action. They know Mr. Wu and I very well. They can explain the story and why it works from a business point of view better than most. They are “Old China Hands” as they have scoured the country looking for good companies and have invested in many of them. This is why they are successful.

As a western insider, I see the company from two different perspectives. Of course, I understand the skeptical western point of view, which questions China, but I have also experienced the Chinese perspective first-hand. When my Chinese colleagues complain about the American way of doing things, I take the brunt of the complaint. It isn't directed at me, per se, as they almost see me as a Chinese, but I still feel the complaint. Less than ten years ago, Americans bashed China for quality issues and disregarded their ability to perform. Now they fret the loss of American manufacturing jobs, and wonder what will stem the tide. I listen to both parties, and explain that we are the two largest, industrial minded from both sides and try to make sense of it and explain its rationale, but in reality, people have to vent – this is a cross-cultural activity.

#### **4.4 Triumph at Last**

December 9, 2009. Times Square is New York City's tribute to the American Dream, the yin to Lady Liberty's yang, attracting the hopes and fascination of everyone who believes in life, liberty and the pursuit of happiness. Now attracting entrepreneurs and business leaders from some of the best companies in China. This cultural crossroad was the planned destination of a small Chinese agri-business company to celebrate a public listing on the NASDAQ stock exchange and the raising of \$100 million in funds on Wall Street over a two year period to fulfill a dream of building a socially-responsible business, which helped to alleviate poverty among many poor rural farmers in China. On this day,

December 18, 2009, amidst the lights and glimmer, our team would ring the bell to open the market for NASDAQ.

We were led by Mr. Wu Zishen, the Chairman and CEO of Yongye International, a son of the deserts of Inner Mongolia who seemed even more unlikely than me to be taking a company public on Wall Street. Yet here we were on this day, at the climax of an incredible journey.

That morning our group left the hotel at Grand Central Station and arrived in Times Square, entering the NASDAQ Headquarters on 42nd Street, where 7th Avenue meets Broadway. The heart of the Big Apple. Inside my head I couldn't help but hum to myself the old Frank Sinatra song, "Start spreading the news..." We were greeted by Jennifer Ok, Market Events Coordinator who ushered us through security and into the studio, where we met Bob McCooley, Senior Vice President from NASDAQ. Over the years since listing on NASDAQ, Bob has become a friend of the company, attending the Company's factory opening celebration in Inner Mongolia and hosting the first ever USA/Inner Mongolia NASDAQ Listing Seminar.

Finally, the momentous day had arrived early that morning in December of 2009. We were in Times Square, and ready to experience the glitz and glamour, like other major NASDAQ listed companies who were once startups but are now household names and lucrative investments such as Starbucks, Microsoft and Apple. Now, NASDAQ was giving our small Chinese company a royal welcome too. It was the reward we felt we deserved. Excitement was in the air as we now walked where so many notable CEOs and celebrities had walked before. Due to technical innovation, the bell ringing is actually more of a "mouse click" in the studio to open the market, but significant all the same.

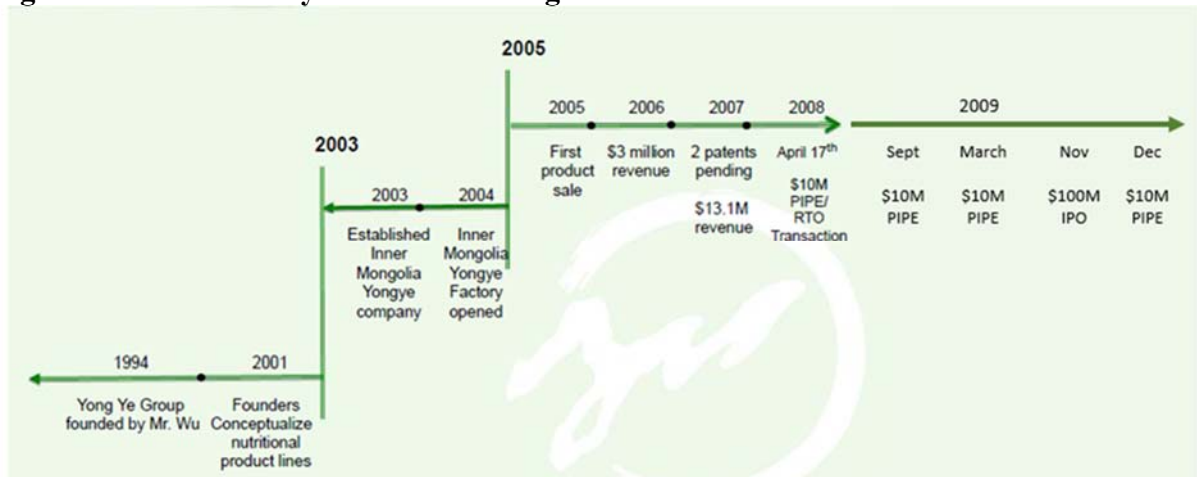
As Mr. Wu clicked the panel on the LCD screen, the market opened with a bang of confetti, shouts from the management team in English and a “Jia You” in Chinese, which means, “come on” or literally, “add more gasoline” to the fire, and the reality of the day truly sank in. After the market opened, we took time to take pictures, video the event and then make our historic walk outside to view the NASDAQ screen overlooking Times Square, showing the Yongye logo for all to see. It was all we had expected and even more. That night we held a gala celebration at the Grand Hyatt at Grand Central Station in Midtown Manhattan. The view of the city skyline was epic and while the room was a bit interesting to say the least, long and skinny with a “Cheer’s decor”, we celebrated with well over 100 of our close investors and business partners, including our major holders, Black River Asset Management, Ardsley Partners, Special Situations Fund and Guerilla Fund. Bob McCooley from NASDAQ also joined us.

We reveled in the success of our recently completed public offering of \$70M and the NASDAQ market open ceremony that morning. Mr. Wu brought everyone together for a brief speech and toast, celebrating, in Chinese fashion, our partnership together. I had helped fashion it in conjunction with Mr. Wu, the management team and all the staff. We all had been a part of building this “New Silk Road” through Times Square upon which we now trod.

This day had been in the works for many long months. Pulling it off required securing the public listing of our shares in the US equities market, getting on the road and securing funding from big name investors such as Goldman Sachs, a “Tiger cub”, Janus and Mitsubishi and finally all the planning for the dinner event. This was a 24/7 proposition for me and my finance team, including Zhu Ling our Board Secretary.

The journey is summarized in Figure 4.1

**Figure 4.1: The Journey from Inner Mongolia to Wall Street**



## CHAPTER V: SUMMARY AND CONCLUSION

### 5.1 Summary

The story of China's rise from third-world developing country to global powerhouse in most of the economically significant industrial sectors is remarkable in and of itself, however, having the opportunity, and even the honor as a foreign ("laowai") actor, to play a part in several of the scenes of this decades long drama is one of the themes I've endeavored to portray in this thesis. Additionally, I've endeavored to weave together the cathartic strands one local Chinese SME faced as it struggled to fund its mission of increasing the incomes of smallholder farmers through the sale of unique and effective agriculture specialty inputs. As with an expertly woven rug, the beautiful top side is the description of a successful ending, however, this ignores its messy and seemingly chaotic underside, and I've sought to describe both to some degree.

The objective here was to tell the story of Yongye's entry to the US equity market, what the driving forces were, the obstacles Yongye overcame, and why this was even necessary given the ability of China to finance its own agricultural achievements internally. As explained earlier, the agriculture sector was driven forward by the successive Five Year Plans implemented by the communist government starting in 1953. After facing some fits and starts, including a massive famine from 1959-1961, for many years, the agriculture sector became a strong foundation in China's growth and development. This was largely the case through the 1990's, however, as the UN sought more commitment for its Millennial Development Goals from the global community, China accepted the challenge to rid the world of extreme poverty and hunger which then pushed its agricultural efforts to a higher level to meet these goals.

If not challenging enough, other structural elements existed in China's communist planned economy including the land (production) being owned by the local village and the anchoring of residency ("Hukou") in the village of one's birth due to consumption planning. As described, these economic planning mechanics, due to lumpy execution over time, led to shortages in employment and lower incomes in the rural areas, and ultimately the Migrant Worker migration across China. While not described in detail, rural worker shortages put huge pressure on land utilization, including over fertilization, to keep up with national production goals which stressed arable land resources further disadvantaging smallholder farmers. Finally, and potentially even more limiting was the fact that rural SME's (private companies) in China were not well financed from local banks which forced them to seek financing from "loan sharks" which limited their growth and long term sustainability.

With so many structural and "lumpy" obstacles, a requisite number of advantages would be needed to empower a local Chinese company to even limited success, but how could this local company garner enough power to garner foreign investment and IPO in the USA? This would come from Yongye's unique blend of leadership vision and connections to Wall Street which is also part of my storyline. The linchpin of Yongye's success was definitely Mr. Wu's entrepreneurial vision which secured and self-funded the IP behind its Shengmingsu branded products for the first 5 years of its existence. Without this sacrifice, including a securitized loan against his home, Yongye would not have survived. What was Mr. Wu's vision locked onto? The same as when I joined the company and the same as that which we pitched to investors, "Just for a Peasant's (Farmer's) Smile". This theme

represented poverty and hunger alleviation not only for farmers, but the rest of the population, plus food security for the country as required by the UN's MDGs.

While success of the IPO required leadership and vision, the sale of Shengmingsu in China did as well. However, it also required a strong product which actually produced results which Yongye was actually seeing in the first few years of crop trials and use. The over utilization of the land and traditional fertilizer was a perfect set up for Shengmingsu as a foliarly applied specialty product. The company grew in Inner Mongolia through free crop trials and follow up sales over the first few years primarily for cash crops, but also for traditional crops such as rice, wheat and corn. This occurred village by village anchored by branded stores and in most cases saw 80% market penetration in a village once the farmers experienced increased crop production and value in the marketplace.

Even with the great vision for farmers and success of a well suited "specialty product" such as Shengmingsu, Yongye was struggling with its rapid growth plans when I joined the company in 2007. While the company originally launched in Inner Mongolia, it was now conducting crop trials in additional provinces knowing they would be success and would catapult the company's sales results – if Yongye could come up with the cash to produce more inventory for the next season. Mr. Wu knew his resources were limited and that local banks would not accommodate him thus started looking for other options - This was where I came in. Mr. Wu's plan was not to navigate China's financial obstacles, but to bypass them by going to foreign capital markets for financing.

Unfortunately, when Mr. Wu brought me on to help Yongye navigate the structures and process of foreign capital markets, it was the end of 2007 and we began our management road show with investors at the same time Bear Stearns and Lehman Brothers



were crashing in the markets. Interestingly enough, China was booming, and Beijing was gearing up for the 2008 Olympics so while in country, we barely noticed the downturn except on foreign news and when we hit Wall Street in February of 2008. Our initial goal was to encapsulate our compelling agricultural story into a pitch for US Private Equity funds in order to raise our first \$10M which would fund the next growing season's product through factory upgrades, purchase of raw materials, and increased sales staff. Then, hopefully, we would start an avalanche of interest from foreign investors in order to raise successive waves of cash and finally an IPO. As we worked with our investment bank in February 2008, this was not looking very good, however, through the next 3 months, and working mostly 16 hour days, our capital raising team tirelessly pitched the "peasants' smile" to investors on road shows and conference calls. While we waited and, at times, expressed our feelings of "Mei Ban Fa", we diligently worked as well and this paid off as we finally reached our goal in April of 2008 by securing our syndicate of investors, signing definitive agreements and Closing on the first of three \$10M rounds. An IPO was to come a one- and one-half years later.

## **5.2 Conclusion**

In this thesis, I've sought to weave together and describe how a SME agribusiness in China, through local entrepreneurship and foreign business expertise, was able to overcome major structural obstacles in China, and attract enough interest from foreign investors to finance its business and achieve company, national and UN goals. It was also able to IPO in the USA and become a NASDAQ listed company. Most importantly to many of us, this made Chinese smallholder farmers smile because they became more prosperous.

In describing and answering the research question of, “What is the process that a Chinese company with a proven agricultural technology can use to get on a US stock market?”, I’ve described how a Chinese SME agribusiness was able to overcome difficult odds in raising funds for agricultural growth, from outside of China, and in the end, garner premium equity analyst coverage, win awards from HBR China and BOSI Europe which were further feathers in the cap. I’ve also woven a story line showing how successful ventures can be accomplished by Chinese and American people who hold the same key values and desire to work together for long term success.

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