



# The Transformation of Shanghai Enterprises before and after the First World War

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**Abstract.** There are already papers discussing the role factories of the Rong brothers played in the contemporary economic field. Few analyze the historical perspective of the Rong brothers' factories. This paper mainly focuses on the characteristics of the entrepreneurial implementation of the yarn mills founded by the Rong brothers in Shanghai to infer the changes in the focus of entrepreneurship in Shanghai. By focusing on the characteristics of the implementation of the yarn factory founded by the Rong brothers in Shanghai, this paper tries to figure out stand the entrepreneurial thinking of the Rong brothers and the focus of their work, understands the reasons and motives of the Rong brothers for choosing to found a yarn factory in Shanghai, and observes whether the entrepreneurial thinking of the Rong brothers changed before and after the First World War. If it changes, analyze the reasons for the change and try to infer from it the change in the whole entrepreneurial thinking in Shanghai and its causes. Studying the changes in the direction of entrepreneurship brought about by World War I and the reasons for them can contribute to a more comprehensive understanding of the multifaceted impact of war on society. Analyzing the shift in entrepreneurship in Shanghai can help provide a deeper understanding of the impact of the economy on people's lives and the foundations on which large cities are built.

**Keywords:** Shanghai Entrepreneurship, World War I, the Rong Brothers.

## 1 Introduction

Before World War I, Shanghai enterprises mainly consisted of state-owned enterprises and foreign enterprises. The canal transport in Shanghai, which is known as the water transport of grain to the capital, is state-owned. Plus, due to the opium war, the government initiated the westernization movement. In the 1860s, the government established industries producing weapons similar to western ones. The government founded the western gun bureau and built the Jiangnan Manufacturing Bureau within four years. These industries were all state-owned [1]. The Jiangnan Manufacturing Bureau was

founded by Li Hongzhang, an official of the Qing court, in 1965. The Jiangnan Manufacturing Bureau manufactured munitions, ships, gunpowder, machine tools, smelting iron, and steel. Li Hongzhang also opened a translation center to spread western industrial technology, which became the cradle of modern Chinese industry. Institutions like the Jiangnan Manufacturing Bureau and the translation center were state-owned.

Meanwhile, foreign enterprises were also building their institutions in Shanghai. With Shanghai as the center, foreign capital forces carried out large-scale commercial and trade activities in China. A large number of foreign firms appeared in Shanghai, and the port and shipping industries developed rapidly. Foreign investors formed ship repair and export processing industries, such as silk reeling, cotton ginning, tanning, and packing. Additionally, Foreign banks entered Shanghai, and traditional financial institutions such as money houses were active. In 1847, the Oriental Bank, the first foreign bank in Shanghai, was established. In the fourth year of Tongzhi (1865), there were 11 foreign banks in Shanghai, 10 of which were British commercial banks. The bank business was mainly engaged in international exchange, and some also used the difference between gold and silver in the East and the West to do business. In the 1890s, banks from the United States, Japan, France, Russia, Germany, the Netherlands, Belgium, and other countries entered Shanghai, and the influence of banks on the finance of Shanghai and even China was further expanded. The British seized the right of customs administration of the Qing Court, monopolized China's international exchange gap, issued banknotes without authorization, and expanded the scope of business [1]. In short, businesses in Shanghai were mostly controlled by foreign people at that time.

However, a few Chinese enterprises appeared before World War I. They made industrial investments actively, expanding from the three major industries of ships and machine repair, printing, and wood processing to silk reeling, cotton, and textile (including ginning), paper making, flour, glass, tanning, matchmaking, ice making, and smelting. However, due to the small scale of industry and the double oppression of domestic and foreign forces, Chinese businessmen had difficulties in development [2].

Most of the existing scholarship on the Rong brothers explores the analysis of the economic field in which the Rong brothers founded each factory, such as the interpretation of the business ideas of the Rong brothers, the way they managed each factory, and the analysis of their business techniques. Some of them also discuss the significance and contribution of the Rong brothers' factories to society at that time. There are few analyses of the historical perspective of the Rong brothers' factories. Thus, this paper examines the characteristics of the entrepreneurial implementation of the yarn mills that was founded by the Rong brothers in Shanghai and further analyzes the changes in entrepreneurship in Shanghai. The study deepens the understanding of why and how the center of entrepreneurship changed in Shanghai before and after World War I. In so doing, the paper further reflects the characteristics of social changes at the time.

## **2 The Establishment of Rong's Business Empire**

At the end of the 19th century, the world's industrial enterprises set off the trend of integration strategy development. The implementation of enterprise group integration

strategy can be divided into horizontal integration strategy and vertical integration strategy. The Rong enterprise group in China was an implementation of a dual horizontal integration strategy. The founder and senior management of the Rong Group were deeply influenced by the management mode of western industrial enterprises, realized the integration strategy of their enterprises, and established their industrial empire: Rong Group started from the Wuxi Flour Mill, expanded to Shanghai, and based in Shanghai to expand to the whole country. The group's top management was known as the "King of cotton yarn" and "King of flour". Shenxin Cotton textile production system and Maoxin Fuxin flour production system constituted the dual horizontal and strategic integration model of Rong Group [3].

## 2.1 Strategic Steps: Powder Before Yarn

In their early years, the Rong brothers operated traditional financial institutions in Wuxi and Shanghai. In practice, they became familiar with the operation rules of the financial market, which became the first step for them to start their own business.

In 1900, the Rong brothers found that all industries were miserable except the flour industry, so they decided to set up a flour mill. The First World War led to the withdrawal of a large number of foreign imported flour from the Chinese market and there was a huge demand for flour and grain during the war. This historical context facilitated the horizontal integration of the flour production system of the Rong Group, which reached its climax. After 1921, the sharp increase in the quantity of imported flour and the sudden decrease in the demand for flour exports caused the flour production division of the Rong Group to show signs of declining sales and losses. After 1921, the focus of the Rong Group's development shifted from flour production to cotton textile production.

In 1907, the Rong brothers jointly established the Zhenxin Cotton Mill. The First World War caused a vacancy in China's cotton textile market, and the relatively complex textile machinery could not easily be transported from foreign countries, so China's traditional manual cotton spinning industry was revived. In the early post-war period, the foreign cotton spinning industry did not recover quickly, so Rong's cotton yarn industry developed rapidly in this period. In 1921, the third Shenxin Factory was established, marking the beginning of the horizontal integration of the Shenxin cotton textile production system of the Rong's Group.

The cotton textile industry was in depression in the early 1930s, and coupled with the competition from Japanese cotton textile enterprises, the Rong Shenxin system struggled to expand. However, it still achieved the second largest scale and capacity in the national cotton textile industry. In 1934, the Young Group faced difficulties that threatened the survival of the entire group.

## 2.2 Strategy Implementation: Self-Construction, M&A, and Renting

The horizontal expansion of the Rong's enterprises was mainly through the addition of enterprise units. There were three ways to add business units: self-building, merger, and lease. Self-construction required a large amount of capital, and the relationship with

the group was very stable. The leasing method required much less capital, but it was not stable as well. However, the withdrawal of production capacity would cause shock to the enterprise group. Merger and acquisition also required a large amount of capital but saved a lot of tedious matters, and it was stable. In the development of the Rong enterprise, the advantages and disadvantages of the three ways of self-construction, leasing, and merger were considered comprehensively, and the proportion of their use was reasonably allocated.

### **2.3 Strategic Capital Sources: Borrowing for Expansion**

The Rong brothers operated banks in their early years and were familiar with the business of the silver and money industry. They also set foot in the modern industry earlier and had a deep understanding of the dependence between industry and finance. Among modern Chinese enterprises, the Rong's were the most typical representatives of using financial resources to promote their own development. The Rong brothers' Shenxin is "the only textile company in China's textile history". Because of this unlimited liability system, credit advantage, in the process of development they obtained more loans. The Yung family maintained close relationships with major banks for years to facilitate loans. The Rong family had huge investments in a number of banks, and these relationships played a significant role in financing the Rong family's rapid expansion and helping it go through crises [4].

## **3 Changes in Shanghai Enterprises**

Before World War I, some of China's more enlightened landowners, such as Hongzhang Li and Guofan Zeng, set up the Shanghai Shipping Merchants Bureau and the Shanghai Jiangnan General Administration of Manufactures in Shanghai. Before World War I, the development of the Chinese economy depended mainly on foreign capital, but there were also institutions opened by local Chinese to develop the economy. Among them, the foreign affairs faction was the most prominent. The foreign affairs faction opened two main types of institutions, one for civilian industries to enrich the country and the other for new military industries to strengthen the military. The new military industries were completely government-run, while the civilian industries were divided into three main types: government-run, government-supervised, and government-business co-run [5]. At that time, more enterprises were government-supervised, which were mainly financed by businessmen and managed by bureaucrats. The four most influential government-supervised enterprises were the Shanghai Ship Merchants Bureau, the Kaiping Mining Bureau, the Tianjin Telegraph Bureau, and the Shanghai Weaving Bureau [5]. Among them, the Ship Merchants Bureau was the first foreign enterprise to shift from government-run to government-supervised commercial enterprises [5]. The Shanghai Ship Merchants Bureau mainly developed its economy by transporting goods and trading with foreign countries.

In general, before World War I, the center of entrepreneurship in Shanghai was mainly controlled by the government, with merchants playing a major role in finance.

The bureaucratic corruption and incompetence of the Qing government at the end of the Qing Dynasty led to a group of enterprises that were more dynamic at the time when they were first founded but declined day by day. In addition, the Shanghai economy still largely depended on foreign capital before World War I. The share of local Chinese enterprises was small and suppressed by foreign capital. The focus of Shanghai's entrepreneurship before World War I was mainly on foreign trade and military industry.

After World War I, as the Western powers occupied themselves with the war and paid little attention to the Chinese economy and the domestic national product movement, Chinese national capitalists were able to grow, most notably the Rong brothers. The Rong brothers started a yarn factory in Shanghai, a privately run industry, unlike the government-run, government-supervised, and government-business joint industries of the pre-World War I era. The yarn factory was able to have its own management style and develop its own business strategies because there was no bureaucracy involved [6]. There were three types of enterprises: those originally affiliated with foreign companies that invested in their own industries after gaining experience, those that were originally bureaucratic enterprises, and those that started from scratch, as the Rong brothers did. Unlike the first two types of enterprises, the third category did not have its own innate advantages. Even though the background of the time was supportive of the development of local national capital enterprises, it was more difficult for enterprises that started from scratch. Therefore, it was important to have a phased plan for the development of the enterprise.

The success of the Rong brothers was partly due to the reasonable plans they made. The focus of entrepreneurship in Shanghai did not change significantly during this period, but there were still some minor shifts [7]. At that time, businesses starting from scratch such as the Rong brothers had no inherent advantages, so it was difficult to develop heavy industry and foreign trade, so the main focus was on light industry, such as textile mills and yarn mills. The Rong brothers started with a few production machines, and it took a few years before they had a systematic production line, so their productivity was not very high at the beginning [8]. Contrary to the pre-World War I companies, they had a difficult start and then became better and better [9].

The change in the focus of entrepreneurship in Shanghai, as exemplified by the yarn factory founded by the Rong brothers in Shanghai, was mainly a shift from enterprises with bureaucratic capital involvement to private enterprises, a shift that improved management efficiency, and therefore production efficiency to some extent in the later years. Before World War I, the military industry and foreign trade were more developed due to the dominance of bureaucratic and foreign-owned enterprises, but the light industry was also the focus of economic development. After World War I, the development of the light industry was further enhanced by the increase of private enterprises. However, Shanghai's economy still relied heavily on foreign investment, as it had before World War I [10].

## 4 Suggestions

During the First World War, the brief prosperity of national industry in Shanghai was unprecedented, mainly due to the government's relaxed policy. During the war, the import of foreign goods was greatly reduced, which opened up the development space for the national industry. At the same time, it also played a role in promoting the national industry. However, the development of this period was partial, mainly in light industries: cotton and flour, very little heavy industry, and almost no chemical industry. In this period, national enterprises in Shanghai were highly dependent on foreign enterprises. For example, machinery in the cotton spinning and flour industries depended on foreign enterprises, and technology was also heavily dependent on foreign technologies [11]. Speculative: The national industry in Shanghai is mainly invested by some businessmen, such as the textile industry, which is common: the business policy of the light industry.

After the first World War, foreign investment came back, and Rong's Enterprises was badly hit, but it quickly got back on its feet. The main reason is that they focus on attracting talent, introducing technology, and their advanced management skills. Many businesses, however, have been devastated.

We have learned from history that the government should give enterprises easy policies to promote their development; The enterprise establishes the modern management system, reduces the family enterprise management mode; pay attention to the introduction of talents, pay attention to the development and utilization of human resources; Attaching importance to scientific and technological progress, independent research and development, relying on innovation to get technological development leapfrog; optimize the industrial structure and give priority to the development of new and high technology industries; update the idea, take the market as the guidance, strengthen the international management consciousness.

## 5 Conclusion

This thesis mainly focuses on the transformation of Shanghai enterprises before and after the World War I, using the example of the founding of the Rong brothers' yarn factory in Shanghai. It is concluded that before the First World War Shanghai enterprises relied mainly on foreign capital and enterprises founded by the landowning class. These enterprises were mainly focused on foreign trade, shipping and light industry. During World War I, the national bourgeoisie was encouraged to set up businesses, the foreign powers were too busy with World War I to care about the Chinese economy, and a national product movement was launched in China, which led to the development of enterprises founded by the national bourgeoisie. By analyzing the yarn factories founded by the Rong brothers, it is possible to see the big picture in a small way and find that light industry developed faster during this period, compared to the period before World War I, when Shanghai's light industry had developed further, but Shanghai was still largely dependent on foreign investment.

The main shortcoming of this study is the use of the Rong brothers as a reference group to analyze the changes in the overall entrepreneurial situation in Shanghai. Due to the lack of time and manpower, the reference group can only be chosen from the more representative and famous Rong brothers, so the analysis of the situation will certainly deviate slightly from the real situation, which is unfortunate.

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