



Understanding China

THE IMPACT OF THE ECONOMIC DOWNTURN IN CHINA AND WHAT IT MEANS FOR WESTERN MANUFACTURERS

If you think the China story is over, think again...

The “financial tsunami” that has engulfed the world over the last 18 months has had a profound effect on most economies. Unemployment is rising and is expected to continue to do so. Some countries have returned to overall growth and more will achieve this in the coming quarters, yet the situation

remains fragile and competition will remain fierce in most markets resulting in continued pressure on purchased costs.

In China, by contrast, despite exports being down 22%, growth in 2009 is forecast to hit over 7%. The primary reason for the growth is

the government’s fiscal stimulus package which is already in full swing (\$588bn US). So how is this impacting manufacturing for the West and are there still opportunities for Western buyers?

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"The medium term opportunity for the Western manufacturer is to develop and embrace the manufacturing capability in China through local partnering."



Infrastructure and rural development are in line for heavy investment as well as investment into the upgrade of the overall industrial capabilities, with significant emphasis going on higher technology industries. The creation of ongoing mass employment is still the key concern and affects both Beijing and local government thinking.

Although it is a Beijing initiative, much of the actual financial stimulus will be provided at a local level. Many of the local governments have weak finances so can only raise money through taxes, specifically VAT. The primary source of VAT generation is from manufacturing, the increase in which also drives employment. The ultimate consequence of this is that government support for manufacturing growth, even at low profit, is beneficial to the system and so is being aggressively rolled-out. Well over a third (38%) of the capital

influx from the government is targeted at infrastructure to make business easier, more efficient and more geographically distributed. Low technology, high emission, cheap labour driven businesses are being shut down and off-shored, with high-tech, clean manufacturing receiving significant investment. The intention is to compete with the West in higher value-added products.

The regional control and the need to increase employment also means that Chinese manufacturing will remain fragmented with significant over-capacity and thin margins. For example, there are many hundreds of piston ring manufacturers in China compared to the 6 in Europe and the USA.

Contrary to popular belief that rising employment will negatively impact China's ability to remain competitive, the manufacturing

landscape is likely to become more competitive. More of China will be able to genuinely compete with the West and have the scale to do this effectively. All of this will remain based on low labour costs and virtually free capital.

The opportunity for the Western manufacturer is to embrace this rather than become a victim of the continuing Chinese phenomenon. There are two clear opportunities to developing partnerships with manufacturing businesses in China. In the short term, there remains the well-understood and tremendous opportunity to enjoy reduced manufacturing costs. In any case, market forces will mean that this work will migrate to China and other low cost sources over time. Given that high-technology is now being targeted by cash-rich China, the protection that the current technology gap affords Western companies will become eroded over time.

The second opportunity for the Western manufacturer in the medium term, is to develop and embrace the manufacturing capability in China through local partnering. This gives access to the local market and the significant growth opportunities that this presents.

Through a presence in Europe and in Asia, Vendigital is well positioned to help European manufacturing companies successfully deploy this important strategy by supporting clients with outsourcing and partnering with Asian manufacturers. Given the markets are currently recovering, this is the right time for businesses to fundamentally change their cost base and to be ready to compete when growth fully returns. Being able to exploit the Asian growth as it happens is a significant and realisable opportunity. The investment can be modest with significant and fast returns. Vendigital believes that now is the time to take advantage of the Asian phenomenon. ✓

Comment



"It is vital not only to recognise the opportunities, but to distinguish between those that will become unprofitable distractions and those that will potentially transform the fortunes of your business."

BY RICHARD LAMMING

The current economic climate has presented many challenges to companies and individuals, particularly given the speed of events leading us into recession. This presents companies with short and medium-term challenges but also medium and long-term opportunities. The challenge of the pressing need to reduce costs when faced with operational difficulties such as reduced volumes is not new but this time it clearly has increased urgency.

The real challenge I see for company board rooms is establishing the agility to take a leading role in embracing the opportunities that will present themselves. This takes a new culture; not only challenging the status quo but also having the talent and tools to ensure the correct strategic direction is taken and the first mover advantage is secured. I have often written on the importance of understanding disruptive innovation when a new idea or opportunity comes along and fundamentally changes the game.

There are many technology examples (for example the change from portable CD players to MP3 players) but the same is true in volatile markets when the competitive landscape changes overnight. It is vital not only to recognise the opportunities, but to distinguish between those that will become unprofitable distractions and those that will potentially transform the fortunes of your business. These are volatile times and as we start to emerge from recession, the opportunities exist for those willing and able to invest in challenging themselves to up their company performance. ✓

Case in point

Challenges in the Aerospace Sector

HOW CAN AEROSPACE COMPANIES BENEFIT FROM THE ASIAN MARKET?



In the aerospace sector there is relentless pressure to reduce costs and execute low-cost manufacturing strategies, particularly in Asia. The primes and tier 1 suppliers recognise the shifting landscape with a significant proportion of new build aircraft being required in Asia over the next 20 years. They are also, in many cases, planning to produce some of that requirement in Asia. Suppliers are therefore being tasked with increasing their Asian production or sourced goods. Likewise, the demand from customers for suppliers to sell in dollars, makes an Asian strategy a must for most suppliers.

The difficulty is that sourcing from or manufacturing in Asia is still challenging. Supply chains are extended, communication is difficult, currencies volatile and there is a fear of loss of proprietary knowledge. Some Asian countries have export licence restrictions on them and others are constrained purely because the supply base does not yet have the technical capability.

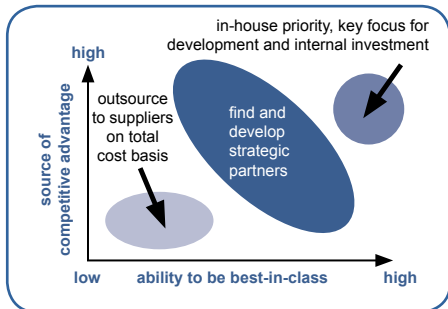
However, the huge Asian demand for aircraft and aerospace technology means the regional supply chain capability is growing dramatically. Singapore and Malaysia for example are well-developed hubs for aerospace suppliers and the supporting special processes. China, through its investment programme, will also become a key hub.

What should the best approach to Asia be? At one level it can be a short-term margin

improvement through product sourcing. Total cost reductions of 30-40%+ are still available and cannot be ignored. At a more strategic level it is about identifying core competencies, deciding the areas in which your business can excel compared to the competitors in 5-10 years time and matching an internal manufacturing capability to that. Using Asia as a partner to complement in-house capability, delivering the future manufacturing strategy, plus the broader market access, is a very attractive approach.

A model which many organisations have found useful in supporting this strategic review process is shown below:

Vendigital's strategic sourcing options matrix




The outcomes can be quite revealing. Clear decisions are needed on which partners to engage with and for what reasons. Are you looking for strategic partners or just low-cost

sources and where should they be located? A robust process is needed to find the best suppliers and to make the right decision for the location of each supply partner.

Vendigital can help you work through this process and provide experienced yet pragmatic judgement to make informed decisions and develop the necessary transformation plans.

As part of getting a supply partnership up and running, cost-effective, local management is needed that is both technically and commercially strong. To set this up in Asia is expensive for smaller businesses. Management salaries are broadly similar to Western salaries and the availability of talented and experienced resource very limited. Even the smallest, functional purchasing office comprising of a few people can cost £250,000 to £500,000 p.a. to set up and run. This can pay back for larger businesses with significant volumes, but for SMEs this can often be unaffordable.

A more cost-effective and viable alternative for SMEs and larger organisations, which is becoming increasingly common, is to outsource the Asian supplier management. In the case of Vendigital, as an outsource partner for Western SMEs, we not only secure the best pricing from the best suppliers, but we manage the day to day quality assurance of production through to expediting orders and logistics from our Asian base. Our other core competencies include local market knowledge to find the best suppliers, category expertise, a strong technical capability, as well as the other necessary logistical and linguistic expertise.

By understanding and focusing on your core manufacturing competencies and outsourcing the support services that others can do more effectively and competitively, your business will be stronger, more agile and better able to compete. Exploiting the Asian market to get the benefits without the risk or excessive investment must be the focus for Western manufacturing SMEs. 

Forthcoming Feature

Strategic Sourcing Programme within Global Aerospace and Defence Organisation




IAN JOESBURY
GROUP DIRECTOR
OF OPERATIONAL
EXCELLENCE,
MEGGITT PLC

Within today's economic climate, more and more organisations are looking at how they can reduce costs. Direct & indirect materials are an obvious target within the manufacturing sector, especially since materials can typically account for 50-60% of revenue. However, embarking on structured

strategic sourcing initiatives and using the purchasing power of the whole organisation rather than at local level, has its challenges.

Ian Joesbury, the Group Director of Operational Excellence at Meggitt, took on this opportunity starting in 2007. In the next

Vendigital Newsletter, we will interview Ian in order to understand his approach, the challenges he faced, the successes that followed and his recommendations for those who are looking to embark on a similar journey. 



Case Studies:



Budget planning at Taylor

"...not only has the Procurement Optimiser tool taken considerable time out of the budget loop but it is also uncannily accurate in predicting the available savings."

MARK ANDRIOLI: PURCHASING AND SUPPLY MANAGER, TAYLOR


Understanding savings opportunities and creating realistic budgets can be a time consuming and sometimes haphazard process. Vendigital has therefore developed a web based analysis tool "Procurement Optimiser" to support our clients in this process.

The Vendigital Procurement Optimiser Tool adds some scientific rigour to the process of savings prediction. Firstly the spend is divided into common supply market facing categories. Secondly through a series of questions on each category, using

algorithms based on historical data and Vendigital's experience, the tool presents powerful findings relating to potential savings, strategy and planning, all via a common language.

Mark Andrioli from Taylor, the world's largest manufacturer of metal bins engaged with Vendigital on just such an exercise which was conducted through a series of workshops with the Taylor team. The output of which has enabled Mark to quickly build a budget which he has confidence in achieving. With some

benchmarking from Vendigital combined with their ongoing strategic exercises, Taylor is already well ahead of their original expectations on savings in a tough market.

Both David Williams (Taylor's Operations Director) and Mark Andrioli found that this was a collaborative and enjoyable workshop which helped objectively analyse and compare their spend categories. The outputs, which are available to them on the Vendigital web site, can be revised throughout the year and the exercise repeated at the next budget planning phase. 




Talaris uses My Auction

"The eRFQ platform was an excellent tool that allowed us to complete an effective market tender very easily with both current and new suppliers. The result from the e-auction was a 40% saving"

MURRAY DILKS: HEAD OF GLOBAL PROCUREMENT, TALARIS

As part of a global cost reduction programme, Talaris made use of the Vendigital MyAuction platform to deliver rapid benefits in 6.5m Swedish Krona (€600k) of specialised packaging.

The objective of the project was for Talaris to complete a market tender for specialised packaging to deliver quick results and provide direct experience in the use of an eRFQ platform.

Vendigital provided training, headhunted additional qualified suppliers to Talaris' specification and supported the creation of the tender documents. The Talaris team managed the entire process through Vendigital's eRFQ platform, which resulted in a 40% saving. 

VENDIGITAL NEWS

VENDIGITAL has witnessed a number of exciting developments in recent times. In March 2009 Vendigital opened its Hong Kong office to support customers in Asia. Dominic Jephcott, the founder and CEO of Vendigital, has relocated to Hong Kong to lead the existing team based in mainland China and drive the business in region.

VENDIGITAL'S local presence will give it's customers a strong technical and commercial interface within these supply markets. We can support existing client resources in Asia or minimise the investment and risk for businesses looking to establish an Asian presence by acting on their behalf. Services are customised to suit and can range from supplier sourcing right through to outsourced management of the client's Asian team.

VENDIGITAL is pleased to announce the appointment of Roy Williams as Managing Director for the UK business. Roy, one of the company founders, was previously the Operations Director responsible for successfully growing the business capability across both the Procurement Services and Procurement Software divisions.

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