

SUCCEEDING IN CHINA - CASE STUDY : A EUROPEAN MULTI-NATIONAL - IT'S ALL ABOUT THE PEOPLE

[Les Lothringer, West/Asia Strategy Consultants]

It is said of China that everything is possible and nothing is easy.

And yet, while some foreign multi-nationals do manage to construct an effective manufacturing and supply chain operation (in-house or out-sourced) for trading to the rest of the world, others find it impossibly difficult to achieve the most basic of their objectives. They remain dazed and confused about why their every effort to succeed seems thwarted or seemingly committed to fail.

Surprisingly, the solution to these problems can be obvious, yet remain elusive.

Here we will examine one foreign multi-national, a Western European manufacturer with operations in Western and Eastern Europe and limited assembly and sales operations in these locations as well as the United States, Asia and Australasia. Here in China, they have several manufacturing plants in northern China, a manufacturing plant in southern China and sales and distribution throughout China.

Our European multi-national manufacturer continues to experience major difficulties with their China infrastructure developments. These include their manufacturing plants, manufacturing technology, IT systems, materials supply, plant safety, product quality and product distribution in to the China domestic market as well as export, production control and staff capability. Yet, the products they make are simple, uncomplicated industrial consumables and equipment to the welding industry. A most critical factor, their relationships with their Chinese partners and staff, has not been characterised by patience, sensitivity or receptiveness to Chinese points of view.

Viewed from a competitive standpoint, their manufacturing processes are straightforward and competitors face low barriers to entry. Important raw materials are subject to international commodity price movements and thus beyond the ability of management to directly control, although commodity price hedging is available.



A welding consumables plant. Most northeast China industry is still in a fairly primitive form (Les Lothringer).

A simple and effective strategy gone wrong

Thus, this company's strategic opportunity comes from three coordinated parts : economies of supply and distribution, backed by a group of stable Chinese manufacturing plants working at full capacity with production demand coordinated by the European head office. This strategy is an enabler for significant cost reduction and is the only strategy available for manufacturers of products that have a low "value added" perception. That is because their products have, or will, become commodities themselves.

So, to retain a presence and a position of integrity with their international customers means one simple thing – keeping promises. That is, orders delivered on-time, delivery of acceptable quality product and near zero returns.

Domestic Chinese factory competitors copy these industrial consumable products at reduced cost but often at lower quality. What these Chinese companies lack, though, is the supply chain experience described previously. The domestic Chinese market, always price sensitive, is increasingly made up of foreign multi-nationals and suppliers to foreigners. The Chinese domestic market is raising its quality standards to meet the standards of foreigners.

This suggests that our European multi-national manufacturer could expect strong demand for its products, both inside China's emerging domestic industrial markets as well as globally. Yet, the opportunities in both markets were slipping away as foreign and domestic sales managers resisted placing large orders on their own Chinese plants and resisted making promises to foreign industrial customers out of concern for keeping promises - not delivering on time and not delivering with acceptable quality.

The remoteness of Chinese law

Our analysis revealed that the Chinese manufacturing plants acquired by this European multi-national were performing badly and had been for some time. Sales managers knew this and saw the problems as largely technical. Chinese joint venture partners and WFOE managers knew the problem was more basic. The European partner blamed their Chinese partners and managers for missed goals. They expected to rely on their Chinese legal contracts to exert control over their plants and their Chinese management. In some locations, the Chinese minority partners asserted themselves and simply took back control of their plants.

They knew that they could do that. It has happened before in Joint Ventures between Chinese and Westerners. Indeed, the Chinese have an old saying the sky is high and the Emperor is far away - which basically translates that the rule of law is subject to local needs.

JV partners need to take an interest in all their staff and foreign investors can make a big difference to health and safety standards for Chinese workers (Les Lothringer)



They forgot about the people

Chinese businesses are family-centred and trust-based. As one Chinese minority partner expressed to me of his foreign partner CEO, quick decisions and rule by directive was his trademark style. Discussion, negotiation, patience and listening did not come naturally. Little wonder then that the Chinese saw their European partner as arrogant and changeable and not someone in whom they could trust.

Adding to their difficulties was the choice of technical specialists to work in their Joint Ventures with the Chinese partners and their staff. One foreign specialist was unprepared to adjust to Chinese ways and means, was habitually distrustful of the Chinese and was without empathy skills. The Chinese partners saw the appointment of this foreign specialist as a devaluation of the relationship. The second foreign specialist was the opposite - too accommodating and incapable of exhibiting the professional technical leadership they sought to lift production performance and quality.

Business structure versus management personality

This foreign multi-national was in a crisis management phase, entering China and buying factories. This made every decision they took more urgent and less considered. They had lost direction. Making decisions on how to move forward became increasingly difficult. The pressure of day-to-day problems caused their Chief Executive to function like a Chief Operating Officer with a short term outlook. It became very apparent that they did not have the discipline or the patience necessary for developing their China operations.

The purchase of several operations in China brought with it the commitment to human investment, a high level of relationship building and management of staff, elements in the West that are important but require less time in the West. In comparison, Chinese managers commit a large amount of their personal time to staff relations, whereas Western managers may interpret that staff relations are governed by contracts of employment and can hence distance their personal involvement with their own staff.

As a result of these accumulated problems, the performance of their several China operations fell short of internal targets. It is unlikely to improve any time soon.

Outsourcing - a solution that can work

Let us consider the management persona or operating mode of this European multi-national as an avenue to a solution that works. We can describe their management persona as directive with a remote control style, bottom-line focused with less or no value attaching to relationship management. Their purpose in initiating a China presence was purely to achieve cost reduction, a noble objective in itself. What they did not welcome was the baggage that comes with a China presence. Here this meant relationship management and this was not anticipated, not appreciated and not wanted.

It follows that buying into Joint Ventures and setting up Wholly Foreign Owned Enterprises was not consistent with this foreign multi-national's preferred operating method.

This leaves one avenue for success and recovery of their China manufacturing and supply ambitions. Instead of taking an ownership position in China, export product demand could be satisfied through outsourcing. That means contracting with Chinese manufacturers to satisfy export and domestic demand. Risk management comes about via the support of a smaller local management group, in turn supported by a team of China experienced Quality Controllers.

This has several benefits for companies that wish to limit their investment and involvement in China. Outsourcing allows the possibility of having alternative factory supply sources, should one product source become troublesome or lapse into non-performance. Outsourcing contracts are more suited to a remote control style of management wherein the relationship can be (more easily) governed by the contract.

The principal challenges then become those of guaranteeing quality standards and on-time supply. Quality Control teams of foreign staff and domestic Chinese staff can satisfy these needs. The Quality Control team can rotate from factory to factory. Non-performance by the contracted supplier is much more easily handled by negotiation and training. Changing suppliers no longer means a loss of investment value in a Joint Venture or WFOE. This is no longer a concern with outsourced suppliers. This is in contrast to the limited flexibility a foreign partner actually has over his Chinese domestic minority partner, regardless of what the Joint Venture contract says. Outsourcing allows the foreigner to avoid being locked in.

Succeeding in China takes patience and determination. For foreign companies wishing to succeed in China, the choice comes down to choosing the method of entry that fits best with their style of management. But whatever approach is chosen, success will always require considerable work and patience.

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