# Prime Source Forum: strategies for China

By Andrew Jobling, WGSN, 13 April 2012

**With China suffering due to higher production costs, strategies to adapt to the changing landscape were key at the Hong Kong-based global sourcing event.**

Ronald Fromm, chairman, Brown Shoe Co, at Prime Source Forum 2012

TAKEAWAYS

- China's costs are going up, but for many, moving locations is not an option; finding strategies that work in the country is key
- Driving efficiencies is more crucial than ever, with collaboration and effective supply chain management important tools
- Technology investments can reduce labour costs and boost productivity, while there is also room for savings by way of lateral thinking, such as payment currency

## Challenges in China

**Wages:** China's strong ability levels, speed and infrastructure are likely to ensure it remains the world's dominant garment supplier in the coming years, despite an expected reduction in its overall market share, but the rising cost of producing there is creating a number of challenges as the changing landscape prompts some strategic rethinking.

The major issue, of course, is labour. Wages have been rising steadily and the Chinese government's 12th five-year plan calls for a doubling of income for the domestic population. That can only mean further increases and the pressure is telling on manufacturers.

"People aren't willing to pay more, but how can we still sell at the same price?" said Henry Tan, CEO of Hong Kong-based garment major Luen Thai Holdings, adding that he would prefer the market to decide wage levels rather than the government. "If we can't find workers we put the wages up: that's more healthy than the government increasing the minimum wage and driving the industry out."

Ronald Fromm, chairman, Brown Shoe Co, at Prime Source Forum 2012

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**Changing suppliers:** High labour costs also lead to other difficulties, such as the need to move to cheaper suppliers in the country. Ronald Fromm, chairman of Brown Shoe Co, said that 50% of his

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company's products are now made in cities and villages in China that the company wasn't even in 24-30 months ago. That means a steep learning curve for those factories – plus a lot of hard work from Brown Shoe – in order to maintain consistent quality levels. But with higher costs pushing sourcing to less developed areas it's something that needs to form part of many companies' strategic planning.

And it highlights another important issue, namely that although competition for China is increasing and orders are moving elsewhere, China still offers a combination of quality, efficiency and infrastructure that can't be matched - and for many products, there aren't any strong alternatives.

I THINK THE IDEA THAT WE CAN JUST PACK UP OUR TENT, MOVE OUR SHOP AND FIND SOMETHING CHEAPER THAT WILL SOLVE ALL OUR PROBLEMS IS OUTDATED."

*Stephen Forte, MD of global sales, Coats*

**Trading difficulties:** Another challenge is finance, with Peter Liu, MD of AsiaNet Consultants, saying it is now harder to borrow from banks because it is harder to make a profit, while another challenge Western companies wishing to source from China need to be prepared for is that some Chinese manufacturers, in certain situations, are becoming less interested themselves.

"I think the issue will be when it's more profitable to supply domestically than to export," said David Hampson, country manager for The Jones Group. "I think that line is getting closer. A factory has turned down my order because it can supply domestically for a better price."

## Finding efficiencies


Peter Hevicon, GM, Debenhams Hong Kong, at Prime Source Forum 2012


David Hampson, country manager, The Jones Group, at Prime Source Forum 2012

**Supply chain management:** Cost challenges in China mean that it is more important than ever to become more efficient. One way to do this is to put a priority on a better organisation of the supply chain, adding clarity, eliminating inefficiencies and speeding up the whole process.

"We signed up for SAP," said Fromm. "It was three years of pain and suffering, but you do it because it's worth it, because you couldn't compete without that sort of supply chain management."

But adding in IT capabilities is a challenge in itself, said Tan, although one worth persevering with.

"We're finding it very challenging to work with our customers with IT," he said, adding that in the industry everybody had their own system but this year he is working on a platform with adidas where information can be shared between the fabric mills, adidas and the suppliers.

**Collaboration:** Just as retailers and brands naturally push hard to get the best prices, manufacturers

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push back to get the best margins; but working together to find efficiencies in the process can be beneficial to both. It doesn’t happen enough, speakers said, but that kind of collaboration is crucial to improving efficiency, cutting costs, adding speed and improving production flows.

Numerous strategic ideas for achieving this were voiced during the forum, including: provide initial product orders to allow yarn to be booked without commitments on final colour or design partner, so that orders are put through suppliers at quieter (cheaper) times, guarantee minimums to vendors and retailers buying fabric in bulk themselves then distributing to their individual suppliers.

“If there’s one thing we should do, it's collaborate more between suppliers and customers,” said Tan. “If we’re able to build real partnerships, a lot of the waste can be eliminated."

I THINK THE BIGGEST OVERHANGS ARE BETWEEN US AND OUR FABRIC MILLS AND US AND OUR CUSTOMERS. IF WE CAN REALLY WORK SEAMLESSLY, I THINK THIS IS WHERE WE CAN GET REAL BENEFITS.”

*Henry Tan, CEO, Luen Thai Holdings*

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**Currency:** Peter Hevicon, general manager at Debenhams Hong Kong, said that there is a cost saving to be made by paying for goods in China’s renminbi because every supplier has to account for the appreciation of the currency in their pricing.

“I persevered with RBS and as of November 2011 Debenhams was the first retailer to pay Chinese suppliers in RMB,” he said. “It worked out to be a 7% saving, but when you take into account our own risk it was more like a 4% saving.”

**Reducing labour:** With the cost of labour such an important issue in China, strategies to reduce that strain are important. Investment in new technology and productivity is seen as a must, with the old methods of just throwing extra workers at problem areas now seriously unforgiving.

“There’s an opportunity to invest in efficiency, technology and actually reduce labour costs,” said Hampson. “Rising labour costs and labour shortages were the major factors in the UK to drive productivity. Now China has the opportunity to improve productivity, profitability and reduce lead time so that nobody can challenge it.

“It’s a change of mindset that’s necessary – it’s not the cost of labour that’s important, but what you get for that labour. Broaden people’s jobs, pay them more, but use fewer of them.”

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