

Two experts offer some advice on the perils and pitfalls of sourcing from China. First, **Bernard Poon**.

Buyer beware

CHINESE CUSTOMS and traditions are very different from those of countries in the West. These differences are generally well observed, respected and expected. However, what is often overlooked is the cultural difference caused by the economic disparity between China and the developed Western nations. Westerners tend to be oblivious to the fact that it is only in recent years that Chinese people, and only those in major cities, that have had the privilege of worrying less about where the next meal will come from.

Conversely, since China has only opened its doors to the West relatively recently, the majority of Chinese possess a narrow view of foreigners, pivoting around the assumption that they are all wealthy.

This has an impact on the way business is done. What may happen is that a factory owner may say that something can be done ("no problem") even where they do not have the capability to do this. The reason is that they are keen to establish a business relationship in the expectation that this is their road to riches.

Bearing this in mind, it is always wise to exercise caution with the manufacturer who says 'yes'. It is in such situations that foreigners may be given a price that's too good to be true, to lure them in. If accept-

ed, the chances are that the outcome will not be successful.

One example I can give happened when a client asked us to co-source tubular metal fabrications from another factory. We asked for prices which we believed were very competitive – almost as a first step in the bargaining process – but, to our delight, the factory accepted. It was not the best approach, however. To cut a long story short, it took a period of one year to complete two small trial orders with countless visits, attempted price rises and endless empty promises. After the trial orders were completed, the relationship ended.

The company would have taken delivery of an expensive consignment of scrap metal

Fortunately, we didn't lose any money or investment, but we lost precious time developing a relationship with our client and other good suppliers.

The lesson that we learnt was that if a price is too good to be true, then corners are likely to be cut. Western companies

must realise that if they want Western standard products and services, they will have to pay more – even in China.

It takes a lot of time to be able to learn how to find the right factory with the right boss, the right attitude and the right staff. If one of those three is missing from the equation, forget it.

Know your product

It is also extremely important for the Western client to know the demands of their products in terms of their technical complexity and how compatible they are with the quality standards in the factory from which the product is to be sourced. If the product being sourced is simpler to make, then, as a general rule, the factory does not need to be cutting-edge and crammed full of high technology. Equally, if your product is of a high technical specification, then it makes sense to look out a factory that is well equipped and operates to similarly high standards.

That may seem obvious, but quite often we have seen Western businesses overlook this basic truth: either they underestimate the complexity of their product or they overestimate how good the factory from which they are sourcing it is.

Small factories in the UK tend to be of high quality in terms of product quality, delivery time and service. There are individual craftsmen who take pride in their work and have developed their skills over years, and as a result, they are also able to charge a premium for this.

However, this is (generally) not the case in the manufacturing sector in China. Small factories tend to offer inferior quality products and service, and deliver consistently late. One of the problems is that a small factory might invest in the same piece of

What can go wrong when buying components? Lots. **Robin Nunley** advises.

Drawing conclusions

LET'S CALL the company 'Heavyparts' (not its real name). It is active in the European 'aftermarket' for heavy automotive components for trucks and trailers, and was looking to source brake drums in China. Working on their behalf, I approached a number of potential suppliers with an enquiry for a large quantity of brake drums. We provided a list of his reference part numbers cross-referred to the original equipment part numbers together with the quantities required. (Companies have to be careful when using original equipment part numbers to avoid being accused of 'passing off' their copy product as genuine. Original equipment numbers are quoted 'only for the purposes of identification'.)

The replies from the Chinese manufac-

turers were interesting: some were direct from Chinese foundries and others from Chinese trading companies specialising in the supply of automotive castings. Offers from Chinese trading companies should definitely be considered; most can offer a wider range of products than might otherwise be available from a single manufacturer. This can save time and effort, as only a single supplier needs to be dealt with.

There may be price benefits as well. There is plenty of anecdotal evidence that Chinese companies offer lower prices to domestic customers than they do to export customers. Competition in the domestic market is cut-throat, which explains why much of Chinese production is directed towards the export market where prices are higher. It is therefore possible to have the paradoxical

situation where it is actually more expensive to buy directly from the manufacturer than from a trading company, even allowing for mark-ups.

Nevertheless, a company would be well advised to exercise caution with trading companies. It is easy to set up an elaborate website to attract customers, behind which there may be no substance. In such circumstances, it is easy to become victim of a scam, about which there are growing concerns.

Standard payment terms from a trading company (and often from manufacturing companies) are likely to be 30 per cent by telegraphic transfer payable at the time of placing the order, with the balance being paid by a second telegraphic transfer before shipment. Never accept these payment terms. If things go wrong or your supplier is fraudulent, you may lose all your money. Payment in advance leaves you with no leverage over the supplier. The minimum terms that are acceptable are those provided by a letter of credit with the standard terms and safeguards.

equipment as a larger counterpart, but then not use the equipment as it should be used, or fail to maintain it properly. Don't be fooled, therefore, by someone showing you a gleaming machine in an otherwise scruffy factory!

Just because the quantities may be low, neither should you assume that it is better to go for a smaller factory. I learnt this lesson when presented with a low-volume order from a UK manufacturer of 'high-end' machined assemblies. We thought that this order could best be met by seeking out a small factory in China. We would acquire a sample, and if the sample was not up to scratch, we thought we could then easily instruct that factory to make the changes. Because it was small, we assumed they would be flexible and responsive to our requests.

This proved to be wrong. Even with the best intentions of a very hardworking and genuine boss, sample after sample had to be rejected and eventually we had to pull out and accept our losses. There were various problems, not least technical and to do with the specification of the product. The factory had the equipment necessary to solve the problems, but were not able to manufacture consistently.

As a general rule, therefore, it is best to buy from large manufacturers who will have got to where they are by providing high-quality goods and services to schedule for a long period of time. What happens, then, if the order is too small for such a factory? There are two solutions:

- keep searching because at some point there must be a good factory willing to take the job
- work through a company with high-volume orders so that your 'small' order

Back to 'Heavyparts'. We obtained a number of replies. A couple were able to quote prices against part numbers but the rest wanted us to supply drawings, from which they could manufacture. This can present a company with a dilemma; handing over drawings to a Chinese supplier means (potentially) giving away intellectual property.

If the products sought in China are bespoke rather than off-the-shelf, UK companies will have to provide the drawings or pay for them to be drawn. And, even if they are off-the-shelf, that still may require drawings to be made. Either way intellectual property is at risk of being claimed or stolen.

In this case, 'Heavyparts' was unable to supply the drawings for the products and was unwilling to pay for them to be drawn in China. There were, however, concerns about the specifications of the products. Some European original equipment manufacturers are a little cavalier with their part numbers and make minor specification changes without changing part numbers.

can be run on the strength of larger orders

What about licences?

Another issue concerns the question of the import/export licence. When foreign companies look to source products from China by using the internet, they are restricting their choice. This tends to be because they will hit on Chinese companies with import/export licences who, in turn, are the companies most likely to have their websites in both English and Chinese.

But there are many other factories, including high-end factories, who neither have import/export licences or who have an English-language website. These factories may be missed (unless, of course, the researcher in the UK can read Chinese).

The big disadvantage of sourcing from the companies with import/export licences is that they tend (in my experience) to be more focussed on trading aspects, rather than on the quality of the product being manufactured.

A better option is for the Western buyer to look first for a factory that will do a good job of manufacturing or supplying their product, and then use another company through which the products can be exported. That is easily arranged, especially if working with those who have China knowledge.

Yet more difficulties can arise when asking Chinese factories to quote to supply. In the West, it is assumed that you win some, you lose some. If you quote for one job and don't win it, then you will try again, after perhaps revising your price. Chinese factories often assume that if they have not won the order, then there is no point in quoting again. My advice is, if you think that one potentially good factory is worth cultivat-

Companies that manufacture non-genuine parts have then to be on their guard that the products supplied will fit the current range of vehicles.

To protect against this eventuality, 'Heavyparts' insisted on seeing the drawings against which the products would be manufactured. Now the roles were reversed, the Chinese suppliers were reluctant to supply their own drawings, which they regarded as their intellectual property. (None of the companies involved were concerned with the fact that the intellectual property really belongs to the original equipment manufacturer!).

In the first instance the potential suppliers refused to supply drawings, but it gradually became clear to them that the only way out of the impasse was to provide them. Eventually, their eagerness for business overcame their desire to protect their intellectual property and they sent the drawings of the products. It was a good thing that they did. The drawings showed that specifications offered were not suitable for the European market. If an order had

ing continue to invite them to quote and emphasise that you are genuinely interested in doing business.

Finally, trade fairs. Quite often, foreign companies sourcing off their own bat must also negotiate the pitfalls of going to trade fairs. Many of the companies advertising their services at such fairs are trading companies with no special product knowledge - they merely have contacts in the right factories. This can cause a lot of problems because the Western client's first port of call is someone that knows little if anything about the product.

Always remember that you need to identify a supplier with extensive specialist knowledge and who is able to provide quality control of shipments before leaving the factory and possibly at critical points during manufacture.

I haven't mentioned the importance of having good interpreters because that was covered in the December *Review (Tips from the Front)* but I would just emphasise that, in addition to linguistic skills, most successful business transactions between foreign and Chinese companies rely on the negotiator having a good understanding of both cultures.

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been placed the company would have taken delivery of an expensive consignment of scrap metal.

Fortunately, there was goodwill on both sides and by working together, 'Heavyparts' and the Chinese suppliers were able to make modifications to the products to meet the correct specifications and the right products were delivered to the customer.

The lessons are clear: companies need to take every precaution to ensure that the product delivered meets requirements. Take nothing for granted and ask the difficult questions. Always take up references and visit the company. No matter how reluctant they might be to provide information, a Chinese supplier knows that it must supply products that meet the customer's specifications - otherwise, all deals are off.

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