

China Sourcing Skills

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Topics

- Price
- Quality
- Delivery
- Sourcing Structure
- Other Suggestions

Price

—What you should know about the prices you receive from China.

A. Rule of Thumb: 20-40% cost reduction

B. Most Chinese factory owners are honest, and do keep their promises. We rarely see any fraud. Overall, it is very safe to buy from China.

C. There are some small, unprofessional factories with nice websites. If you end up picking them, their price might be low, but you'll often have quality problems or severe management headache. This

type of suppliers also tend to subcontract out a lot of the works, thus creating unnecessary complexity, and you may lose control of lead time and quality.

D. Chinese factories receive many inquiries everyday, but the success ratio is fairly low.

Consequently, they are not willing to invest significant amount of time to carefully quote you.

When you place a PO with them, they'll often adjust price.

Price

Carefully Validate Price Given By Chinese Firms.

- Did they ask good questions? Do they really understand your needs?
- Find out which portion of the work is subcontracted out (analyze their equipment list and top 5 product lines)
- Obtain multiple quotes. We usually talk with

10-20 factories and get 3-8 quotes. By comparing these quotes, we can spot problems and opportunities

- Always ask for price breakdown. You can do your own quick calculation. Assume material price is the same as USA. Labor (Technician) cost is a 1/8 the US cost. Engineering Cost is the US cost. Overhead is half the US cost. As for equipment depreciation, many Chinese companies don't even factor it in.
- Always negotiate, but think Win-Win

Besides quality issues, we have seen companies switching supplier for 2

reasons

Symptom: Price Hike - after first few runs, some factories might raise price.

Analysis: In hopes to acquire new customers, some factories will do the first project at cost (especially when they are not busy). These aggressive prices are not sustainable.

Symptom: Poor Service:

Analysis from a price point of view: In face of stiff competitions, most Chinese factories are running on very thin margin. They don't provision for service costs or R&R/ RMA costs.

So, when problems rise, even though they want to keep you as their customer, it is not economical for them anymore. We have seen importers always beat down prices to the lowest possible and switch frequently. This can save money occasionally, but their supply chain is not stable and hard to maintain.

In our view, **a stable and agile supply chain** is imperative!

Quality

- Chinese factories tend to have good engineers and equipments, but are not good at process management. (Though we have discovered many good ones)
- You cannot depend on ISO certification. You should understand the factory's QA paper trail, check points, and agree on AQL (quality level).
- Deal with engineering/ quality manager directly rather than the sales person for faster response and straight answers.
- Try to come to China to audit the factory before placing order.
- Intense, prompt communication.
- Use Consolidated, Clear Quality Inspection Criteria
- Start slow. Sampling -> Small Batch Production ->

Normal Production

- Anticipate early quality defects. Send simpler projects initially to warm up the relationship.
- Suggest pre-shipment inspection. Find problem before the goods leave China.

Delivery

- 6-8 week allowance for delivery of products.
- JIT inventory systems may not work. You will need to maintain more inventory to support your customers.
- Have a China team to closely monitor factory progress and aggressively push for ontime delivery
- Before major order, don't forget to do a production capacity analysis. Don't rely on the supplier's promise.

Rely on numbers.

- Put in buffer time for shipping delays, defect corrections, payment delays...
- Patience and understanding

Establish the right structure

Structure	Cost Reduction Achieved	Risks or efforts required to manage risk	Effective Communication	Service Level	Suggested Timing
Form joint venture or own factory in China	High	High	Very good	High	After 8 years in China
Buy from Chinese factory directly		High	Poor	Low	After 2 years in China
Use a sourcing company		Low	Very good	High	First 2 years in China
Buy from a trading firm in China		High	Good	Medium	Only for high mix, non-strategic items (order from catalog)
Buy from a turn-key trading firm in USA	Low	Low	Very good	High	Only for items that require very short lead time



Other Suggestions

- Come to China twice a year to get the "face time" that builds and maintains relationships with supplier.
- Start Early. Rule of Thumb: 1-4 months of continuous dialog before production.
- If your potential partner is too large, and if you would not

represent a significant part of their business, you might not be able to get the attention you need. You don't want to become a "low priority" client for them. => A small, medium size supplier might be right for you. (This is especially true for the packaging machinery industries High mix/ Low volume)

- Dual Sourcing. For negotiation power and product availability. It makes sense to develop a low cost Chinese supplier while keeping your current source in the US.
- Keep in mind, if you had chosen the wrong supplier and have to switch later, what you lose is not only some money, but time -- months of precious time.
- Different specialties of sourcing company. Some specialize in electronics, some specialize in mechanical parts, some specialize in factory opening.