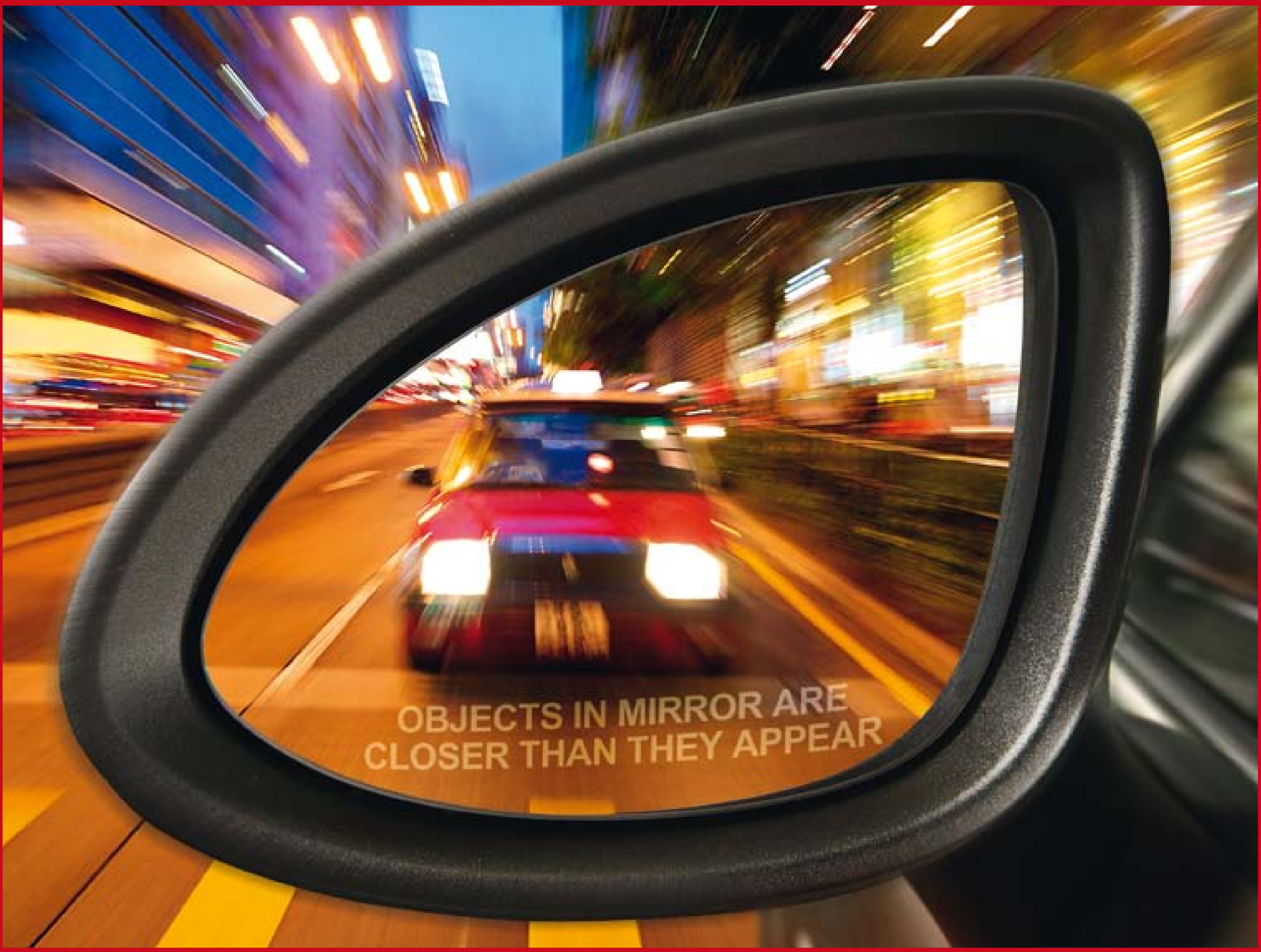
FOUR COMMON MISCONCEPTIONS – AND WHAT'S BEHIND THEM



CHINA IS AN ECONOMIC MAGNET FOR COMPANIES FROM AROUND THE WORLD – as a production site, procurement platform and, in the future, as the most important sales market. But what do we actually know about the Middle Kingdom? And more importantly: Is our picture of Asian culture and consumption correct? *Porsche Consulting Magazine* put a few (mis-)conceptions about China to the test.

CHINA

TO ERR IS WESTERN

1. "Growth in China materializes from thin air."

Wrong! China has become the world's second largest economy in leaps and bounds—its real GDP has grown by roughly 10 percent annually since 2000 and experts are predicting annual growth rates of approximately 8 percent for the years to come—but it is nevertheless a mistake for Western firms in China to take growth for granted. On the contrary, many Western companies are finding it increasingly difficult to achieve profitable growth in China. For starters, many Chinese markets are changing from seller markets to buyer markets. With increasing experience and growing prosperity, Chinese customers are becoming increasingly demanding in terms of product quality, prices, delivery times and service. Competitiveness is also on the rise. Another stumbling block for profitable growth is rising factor costs. In addition to rents, personnel costs are a significant factor. Gross wages in China are still low compared to in the West—the average monthly wage in Shanghai, for example, is around 500 euros. However, wages in many sectors are rising by 10 to 15 percent per year. Moreover, many companies in China are less productive than in the West: More staff is needed to manufacture the same quantity of high-quality products. Where Western companies require 300 staff to produce a certain quantity of product, some Chinese companies may need 400 to 500 employees. This increases the need to focus on managing personnel costs. A third barrier to growth is the lack of qualified personnel (see misconception no. 2). "To continue growing in this environment, it's not enough to invest in property, buildings and machines alone," says Dr. Heiko Rauscher, China expert and designated head of Porsche Consulting Ltd. (see also "Porsche Consulting to Open Subsidiary in Shanghai" on page 65). "The productivity of employees as well as machines and systems must rise substantially. High and stable quality is an absolute prerequisite to being successful in an increasingly competitive environment."

2. "There are 1.3 billion people in China – it can't be difficult to find employees."

Wrong—at least with regard to skilled workers. China's rapid growth means a lot of new jobs. But finding qualified personnel to fill those jobs is a difficult task. China may be the most populous country on earth, but most Western companies are pouring into a few main centers: for example the Shanghai metropolitan area with the neighboring provinces of Jiangsu and Zhejiang, the Beijing/Tianjin metropolitan area or the Guangzhou/Shenzhen region. Western firms in these regions compete with each other for qualified workers. Education levels also fall short of the expectations of Western companies in many cases. Skilled tradesmen are all but nonexistent. Professional training in the white collar sector is likewise not comparable to German standards. According to the Chinese Ministry of Education, roughly 24 million students attend the approximately 2,400 universities and other institutions of higher learning, but the programs are seldom practice-oriented. It is equally difficult to find qualified personnel for management positions. Moreover, keeping employees →

is another problem—annual turnover rates of 20 to 40 percent are far from unusual. These challenges can be approached in two different ways. Companies can adapt work operations to local qualification levels to the degree that work processes allow. This might involve instituting a higher degree of division of labor: Positions with comparatively lower scopes of activity and higher repetition rates make it easier to train new workers and enable steep learning curves. Option two: Western companies need to invest more heavily in employee qualification. This includes systematic training programs for new and existing staff in the Chinese branches. Some companies even fly staff to the company headquarters to be trained by experienced instructors for a period of weeks or even months. Beneficial sideeffect: This simultaneously improves employee retention. "The most successful companies are the ones that combine these two approaches," says Rauscher.

3. "If it works in the West, it will work in China."

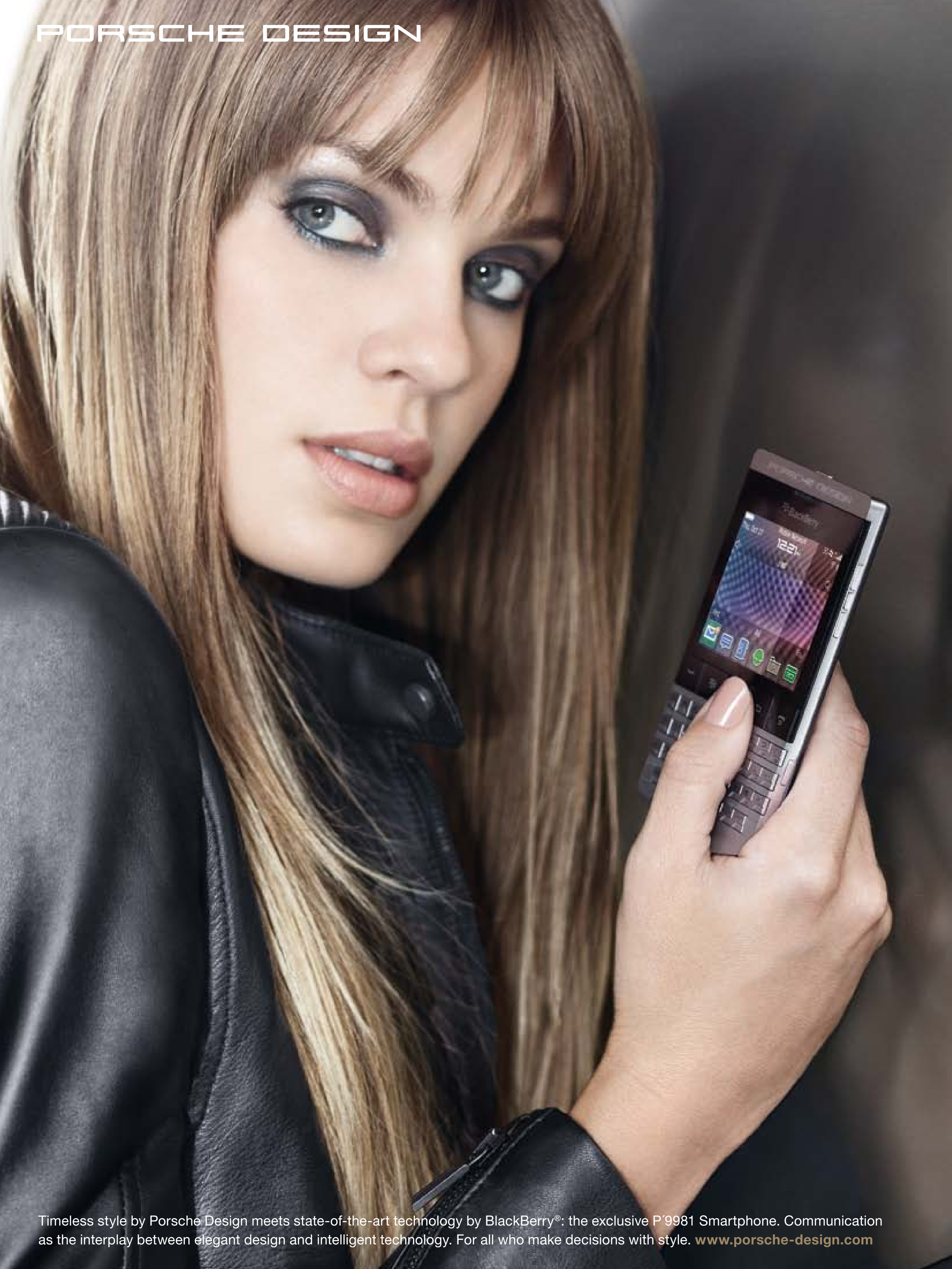
This is only partially true. Many products, manufacturing processes and management methods from the West are also successful in China. Adapting to local conditions is crucial, however, and here there is much room for improvement. For example, many companies transfer their production concepts that are successful in the West—with a high degree of automation and little local value creation—essentially unchanged to their Chinese facilities. The majority of material is drawn from their traditional international suppliers, and in some cases even imported. The result: The production costs in the Chinese plants are similar to those in the West—or even higher. Another example: The assumption that Supply Chain Management can function according to the same pattern in China as in the West is a grave misconception. Vast distances between suppliers and customers, many different points of delivery and a transport infrastructure that in many cases is still inadequate support the opposite conclusion. For many operations in China, this means larger inventories and longer delivery times. And there's another hurdle: Compared to the West, in China it can be difficult to find competent suppliers that have the required capacity. Moreover, local suppliers may have to be "developed" to ensure that they can deliver the desired quality, reliability and technology. "Our task is to work together with our clients to define the appropriate production strategies," says Rauscher. "The important levers are the production facilities, the production program, value creation, degree of automation and the processes. We also support supplier development and the establishment of effective supply chains."

4. "The Chinese are the masters of copying – they don't invent anything themselves."

Dangerous misconception! Many Western companies still primarily regard the comparative advantage of local companies as being low costs. But the days in which the Chinese meekly absorbed the knowledge of the West are long past. There are outstanding engineers and scientists in China as well. It's not only the numerous inventions of past centuries—paper, the compass and gunpowder, to name a few—that originated in the Far East. Patent applications in China have risen by 20 percent annually since 1985. According to official statistics, there were more than 300,000 new applications in 2009. An analysis by the World Intellectual Property Organization ranked China second behind the U.S. in 2010. Of course it's not the quantity that counts but the importance of the individual ideas to yield future products and production processes. Nevertheless, it is surely only a matter of time before more and more Chinese companies become technology leaders. In terms of quickness and adaptability, many Chinese companies certainly have no need for further instruction. On the contrary. In the West, decision-making processes are often burdened by tedious discussions and documentation. Chinese companies, by contrast, simply give it a try: "In China, new plants and production lines are set up or new procedures introduced with great speed. Effective distribution networks are set up within short periods of time. They respond to changing customer demands and competitive situations with new products in a flash," observes Rauscher. The assistance of professional project management in developing and expanding production facilities in China can save a lot of time. Companies can also become faster and more effective in the areas of sales and service as well. The establishment of locally adapted processes and standards can yield substantially increased profits. ←

Porsche Consulting to Open Subsidiary in Shanghai

Porsche Consulting Ltd. will open up shop in Shanghai in January 2013. It will be the fourth foreign subsidiary of the fast-growing consulting firm—after Milan (Italy), São Paulo (Brazil) and Atlanta (USA). The China-based subsidiary will focus on the areas of supplier development, production strategies and systems, supply chain management, client buzz creation, and first-class sales and service processes. “We help companies in China deal with rapid growth from an organizational standpoint while simultaneously increasing productivity,” says Eberhard Weiblen, Chairman of the Executive Board of Porsche Consulting, its German parent company. Porsche Consulting Ltd. in China will be headed by Dr. Heiko Rauscher (42). The industrial engineer speaks fluent Mandarin and has lived in China for more than six years. Porsche Consulting advises Asian companies largely in the automotive industry, the aerospace industry, the consumer goods industry, and the engineering sector.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