

Sourcing In China

Beyond low cost possibility and realizing the hidden factors

Jonathan Zhang

Topics

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Your Supplier Base

Supplier	Engineering Support	Customer Support	Communication Effectiveness	Risk Level	Cost Save	Timing
US based or global supplier	Yes	Excellent	Excellent	Low	Low	Business as usual
JV or State Owned in China	Yes	Excellent	Excellent	Low	Low	2 years into China and not planning to have your own plant built
Chinese supplier with US sales rep.	Vary	Excellent	Excellent	Low	High	Seeking alternative ways to cut cost
Trading firms from China	Most likely none	Medium	Good	High	Med.	Catalog items, or high variety low volume
Direct buy from manufacturer in China	Vary from partial to none	Low	Poor	High	High	At least 2 or more years into China sourcing
Your own JV or solo-owned plant	Yes	Excellent	Excellent	Low	High	6 to 8 years into China with understanding of the market thoroughly

Your RFQ Package

■ Simple is the key. Here are the facts:

- English is a good language for your RFQ.
- A 2-D drawing w/ GD&T in PDF format is always preferred, if you only have 3-D, save it into a lower version or a different file format (thus .prt to .stp file in UG application etc.), and include a sample or some pictures if you could.
- Be specific of your material requirement – and always ask your supplier's GB (China National Standard) equivalent spec.
- Annual volume is not a big factor to the pricing, and don't be surprised when you see price goes up w/ the volume.
- Save you effort to write SOW and other documents, make your supplier read and sign them when you pick your source.
- Be specific of your packaging and logistic requirements

Understand Price Feedback

- It's safe to buy from China.
- Expect to see 20% to 40% piece price reduction, 50% or more in tooling.
- Expect to see just a final number without all the details you would like to see. The idea behind it is: “if you like our number, we can be serious and go for details, otherwise it is wasting time...” – a typical plant philosophy, because they are dealing with a large number of inquiries each day, it doesn't mean that they don't like you.
- In most cases, the suppliers will honor the price that quoted. You will see in-consistency in pricing, because they do make mistakes, and if they did, the price will be negotiated again when you are ready to have PO.

Understand Price Feedback

- Things need a bit of attention:
 - Raise your flag when a supplier asks for a “bottom line price”, that means they are having problems with the manufacturing process or their business model. They want to get the business first and figure it out later.
 - Did they ask knowledgeable questions about your product? Did they answer your question directly?
 - Find out more about their next tier, not by asking the name and address of the supplier, but asking for strength and capability. The last thing you want them to think about you is that you are going to quote the next tier directly.
 - There is always a room for negotiation, have a target in your mind and go for “win-win” scenario.

Understand Price Feedback

■ Verify your quote

- Try to obtain at least 3 – 5 quotes for your own bench-marking, it also helps you to identify the problems.
- Compare supplier's claimed capabilities with their out sourced next tier components, you might see some in-consistency and potential future headaches.
- For your own price check, use following percentage,
 - ✓ Material - 100% of US cost
 - ✓ Engineering - 25% of US cost
 - ✓ Labor cost - 12.5% of US labor cost
 - ✓ Overhead - 50% of US cost
 - ✓ No capital depreciation

Pick Your Supplier

- Pick the one who provided a full cost break down to your RFQ. Either a detail study was done for your product, or they already know their process and business model.
- Pick the one who is small or medium in size, who will consider you as their significant portion of the business so that you would get the customer support you need.
- Try to have more than one supplier on each product if possible, so that you will have the leverage to negotiate, extra capacity for growth, and have a back-up source – this is very important when you are in China market.
- Always ask for the cost break down. It shows you the supplier capability as well as the product knowledge.

Sourcing Concerns

- Don't go all the way to the bare bone on your pricing unless you have a back up plan in place.
 - Go see if the plant is busy. Most plants are running with a very little profit margin because of the tough competition. The first project pricing is usually aggressive (at cost in some cases) just to get the business, and it is not sustainable. Expect to see price hike after production.
- Supplier experience assessment plays a major role.
 - Ask your important questions and concerns multiple times in different ways to understand supplier's approach of dealing with material cost fluctuation, 20% and 50% capacity increase, maintenance schedule...

Quality Concerns

- ISO certification won't do any good for your quality control! Try to have your own audit before your PO is in place, and have someone on your side who's Bi-Lingual Chinese goes with you for the audit.
- Ensure plant's process capability. Most of the plants will have good engineering team and capable equipments, but lack of process control and management.
- Start slow with a low volume and simple product. Do your own necessary testing at prototype stage, and ensure the PV is in place and production part is more process depend, not operator depend.

Quality Concerns

- Have a simple and precisely spelled quality requirement, an inspection check list will be an easy way of monitoring quality, test it with a smaller batch of production parts.
- Find a way to communicate efficiently. A Bi-Lingual sales rep / engineer, plant quality manager will be the good source for prompt communication, but not as quick response and good result as someone with authority – say the plant manager. This is especially true in China.
- Establish a pre-shipment inspection procedure, send or hire someone to do this in China, to prevent bad parts get on the ship, this is necessary for the new developed supplier before a solid relationship has been build.
- If you hire a SQE in China locally, make sure the person won't stay in one plant longer than two days.

Delivery Concerns

- Consider 6 to 8 weeks for ocean ship delivery.
- Build 2 to 4 weeks inventory at both end of the ocean. Unless the supplier has a warehouse at your end, JIT will not be achievable.
- Be prepared to have sufficient inventory to deal with commercial conflicts (payment, etc), delayed shipment (weather, custom, etc), and defects...
- Keep in mind, airfreight is available for emergency, and it's only \$720,000 to charter a Boeing 747 from China to US, and I know someone did that from Japan to US a few years ago, so it's not the end of the world.

Afterthoughts

- China is a very safe and friendly country, if you can learn a few words of Chinese, you will make every stranger becomes your friend quickly than you think.
- Try to go China once or twice a year, have dinners with your suppliers and drink with them, you'll be surprised how much difference it makes to improve the relationship.
- Profitable suppliers will make a stable supply chain that becomes more manageable, so we can focus on exploring new opportunities.
- It seems like I just made your life a little difficult, but we are talking about a country with more than 5,000 years of history and philosophy. Try to be prepared, it's always better than charter a Boeing 747 later down the road.