

## Latest China Sourcing Trends

Sourcing from China has evolved from a straight-forward, cost-driven approach to more elaborate and strategic varieties. Did the recent product recalls affect anything? While the recent product recalls did not seem to have impact Chinese exports based on the overall figures, however we have come across anecdotal evidence suggesting the otherwise.

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Undoubtedly the initial sourcing interest was triggered by China's notorious low costs, both direct (such as those for labor and land or rent) and indirect (rendered under a myriad of government export incentives, such as subsidized fuel costs, export VAT refunds, non-taxation and/or tax reduction).

Over the years the exercise has evolved from a static, per item price-driven modus operandi to more sophisticated ones. For example, many US buyers now employ a vertically or laterally integrated approach, or both.

In the former scenario, a buyer would source not only a certain part or component that they had started with initially, they would now also source the finished product as well as its packaging. Some may go as far as getting the product ready to be shelved, complete with their in-store price tags.

In the latter scenario, a buyer would not only source single products, but also similar or complimentary products to form product bundles as a way to discourage direct price comparison and thus enhance their competitiveness in a price-sensitive marketplace.

Another form of advanced approach is value-added sourcing. In this approach, a buyer would also gain support from Chinese suppliers (often those with strong capabilities) such value-added services as new product R&D, design and prototyping.

In strategic sourcing, a buyer would employ one or more of the following tactics that don't seem to be directly related to what they are currently doing:

- Sourcing other non-related products from the same area for logistic concerns
- Sourcing new products to meet a potential demand upon foreseeing a trend
- Seeking alternative suppliers as backup to and/or to keep the primary supplier competitive
- Engaging in sourcing activities just to get a gauge on the marketplace
- Sourcing to change existing business model. For example, a US military supplier is required to make their products domestically. But they decided to resort to

sourcing from China to expand their otherwise rather minor commercial operation. This would enable them to turn their military side of the operation into a temporary 'loss leader' and thus better compete and win greater market share in that sector. Eventually they would be able to reap the resulted economy of scale and become profitable again in that operation.

Did the recent massive product recalls in the US hurt Chinese exports?

At the macro level, other than a tarnished 'Made in China' label in the media, it seems 'business as usual' for Chinese exports, which had enjoyed a 34% growth as of the end of October '07.

Bear in mind, however, that much of this growth came from non-consumer products, such as steel.

But at a micro level, however, we have come across anecdotal evidence suggesting the otherwise. For example, from talking to members in our network, we found that some companies are now more eager to locate alternative sources outside China, for example, in India and Vietnam.

One other anecdote involves a US-based manufacturer who suddenly saw a spike in inquiries and orders following the recalls. Incidentally, a recent New York Times story (<http://www.nytimes.com/2007/12/23/us/23toys.html?th&emc=th>) about this year being a wooden toy maker's best year ever seemed to echo this as well.

Yet another situation involves a leading North America-based personal health product company which encountered much tightened registration requirements in their sample sourcing efforts. Just for comparison: Before the recalls hit the news we had helped them source and launch a major product line with 6 months. But since the fiasco, the import approval process alone has already taken them 4 months and it is still far from getting done...