

The China Connection
Selling in China through Manufacturers Representatives

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Abstract. The consideration of China as a business opportunity, particularly for the electronics sector is frequently misunderstood. Even today, for many individuals outside of China, the thought of Communist rule, closed trade, oppression, 100% government ownership and autonomy make up the opinion of what China is all about.

In reality, China represents a country experiencing dazzling economic and social change, one that is taking a more confident place in world affairs. China's top priority remains building an advanced market economy, exemplified by China's entry into the World Trade Organization.

In general, younger and better-educated individuals hold the new top government positions. The new leader of China's Communist Party, Hu Jintao, 59 years old, was born to a merchant's family and trained as a hydroelectric engineer.

The opportunities for expansion into this land of 1.3 billion people, who are embracing a free market economy and rapidly becoming more frequent consumers of goods and services, today represents the world's largest growth opportunity.

Speaker Biography. I have had the pleasure of being associated with the electronics sector for over 40 years in numerous capacities including engineering, marketing and sales. For almost 20 years, I have had the opportunity to travel frequently to China, and have seen first hand the emergence of a huge opportunity for companies participating in the marketing and sales of electronics components in China.

The key objective of this presentation is not only to provide an accurate assessment of what China can represent in terms of opportunities for manufacturers and manufacturers representatives, but also clarification of some of the common misconceptions about China, that are the result of our own local education's during the Mao era, and perhaps the propaganda our own governments may have provided.

China at a Glance. By the numbers it is apparent why China represents such a massive opportunity – the landmass of over 9.5 million square kilometers and 1.3 billion people. There are currently over 65 million cell phone users, and over 30 million computer users. The cell phone and computer usage is growing at a staggering rate. As are just about any consumer or industrial category.

If you think the Chinese government owns everything, you are wrong. In fact, according to the "China Daily" newspaper in a story on August 12th of this year, over 80% of Chinese urbanites own their own residence.

The Chinese people do have cash to buy consumer goods. The consumer boom started in the 80's. Today there are TV sets in over 90% of urban homes.

At the heart of any progress and quality-of-life improvement is the need to fuel the lights that allow students to study at night using their computers to facilitate learning, sitting in a heated house to make the harsh winters bearable.

A major economic undertaking in China that is the final construction on the Three Gorges Dam, which upon completion is estimated to provide China with about 10% of its electricity. It will be the largest hydroelectric dam in the world. Work began on this \$20 billion US dollar project in 1994, and is expected to be fully completed in 2009. However, like with all major undertakings of this magnitude, it is not without controversy. Some say the land was illegally grabbed, others complain that it will destroy over 200 important archaeology site, and that it has displaced over 1.5 million people. However, throughout this region, the government to house those who have been displaced has constructed new modern communities. These new communities also facilitate further private ownership of homes.

China – General. If you look at this snap-shot of the Chinese economy, you see an enviable position. The Chinese movement to a freer economic situation has been very gradual and controlled. It has been said many times that they watched their neighbor – the former USSR – change over night – and witnessed some of the economic disasters that followed.

The China GDP grew 7.3% in 2001, and for the first quarter of 2002, 7.6%.

Morgan Stanley is predicted an 18% full year export surge for 2002.

Foreign currency reserves ballooned 34% year on year.

In addition, business incentives are available. As a developing country, China offers more incentives than other countries to attract investment. Standard incentives include a complete income tax exemption for three years with a 50% exemption for a further two years and a business tax rebate, according to sales volume.

China – Electronics Industry. To gain a quick appreciation for the magnitude of China's current status in the electronics sector, just consider cell phone usage, home Internet users and the market for PC's.

China now ranks number 1 in the world for cell phone usage – and even more important to note is that the current usage represents only a fraction of what the usage will be in 2005.

The same holds true for home Internet usage – China ranks number 2 currently – but will become number one in the near future.

Same holds true for PC usage – number 3 now – destined to be number 1 soon.

Moving to the design sector, over 120 companies have emerged in the past three years, a trend that is growing rapidly.

Why China? We've already discussed the sheer numbers – the 1.3 billion population, and how that automatically relates to a huge ultimate consumer base for products and services. It also means a huge, skilled labor force for competitive manufacturing.

There are over 900 million people standing in line to get \$1,200 a year job – therefore the labor supply is practically inexhaustible in our lifetime. What's more Chinese workers are not just low cost labor, they are smart. As part of its drive to become a world electronics power, China has put huge resources into improving technical and scientific education. In 2000, 37% of Chinese University graduates were engineers, compared with 6% in the United States.

While it is prudent to stay away from political opinions, the Communist government of China today is a distant reflection of the Communistic government we remember from our own earlier education. The single party system of China is embracing free enterprise.

The fact that China is now a member of the World Trade Organization has positive attributes regarding commerce, which occurred in late 2001. But keep in mind that WTO is a trade agreement, not an investment agreement. And implementation of China's commitments will not be automatic.

Another sign of globalization on the part of China is the government's desire for its population to learn English. A daily occurrence, using mass media, is the English word of the day. "English as a second language" or ESL for short – is growing in popularity and of course internal controversy – but another indicator that China is getting ready and willing to be a more viable player in the world market.

China Manufacturing Future Designs. New designs are making their way to China from throughout the world, coming from all directions – not just surrounding Asian countries, but from the Americas and throughout Europe.

Again, the fuel for this invasion of new designs is an exploding work force, ready to move from the remote farmlands to the major urban centers.

Doing Business in China. Obviously, doing your homework is essential in even beginning to think about expansion into China. Center and most important is to think of the Chinese government as your partner. It is essential to establish a dialogue with relevant government agencies.

It's a good idea to talk to other companies that have invested in China. Get their advice. Partnering with a Chinese company can help a western company navigate difference in culture and business practices.

Due diligence includes checking the financial wherewithal of potential partners. Confirm that their connections and the networks they have are really extensive or as developed as they say they are. For customers, research their ability to pay on time.

You cannot necessarily rely on your Chinese partner to tell you what approvals are required.

One cannot consider China any more homogenous than you would Europe. Remember that this is a country spanning over 9.5 million square kilometers, with well over a billion people.

Regarding consideration of the competition from both Chinese and foreign competitors, there still remains some elements of protectionism although the protection domestic companies have enjoyed will be removed.

China – Potential Problems. To provide a clear picture of what to expect, keep in mind some hazards to doing business in China.

There is great difficulty for this country in terms of tax collection.

While there is an abundance of labor in China, the subject of labor unions is taboo for the government. Worried that union members might challenge the government as the Solidarity movement did in Poland two decades ago, China's Communist rulers are quick to suppress any labor group not under their direct control.

On a banking note, China has its own mount of non-performing loans. As reported in the New York Times on October 26, 2002, "For years, banking decisions depended not so much on creditworthiness as on personal ties to government officials and even bribery. China's banks ended up lending hundreds of billions of dollars worth of yuan and renminbi to unsound enterprises, usually state-owned, that soon defaulted."

Piracy is a problem troubling many developing countries. In the past 13 years, the Chinese Government has spared no efforts to fight piracy and the smuggling of audio and video products.

While you should treat the government as your partner – a point that is supported by the fact that the VAT on selling foreign products is 17.5%, also, remember China's legal system is one where you are "guilty until proven innocent". Just some words to the wise.

Seven Industrial Zones of China. Let's now move into some of the specifics of industrial development in China. How do you start your focus in China where there are over a billion people, and over 9 million square kilometers of land?

There are seven major, synergistic clusters in China – Beijing, Shanghai, Tianjin, Xiamen, Shenzhen, Suzhou and Zhuhai.

China Industrial Zones. Focusing your efforts on the major industrial zones has a number of benefits.

There are eight key benefits or attributes to these industrial zones

1. each zone consists of a high tech park
2. the factories in these parks are the most modern in China
3. a complete infra-structure exists in these high tech parks
4. the labor market is extensive, as millions of workers are available from surrounding farmlands

5. the customs clearance is quick
6. transportation through China from these zones has been a focus of attention
7. exporting is easier
8. approval processing is increasingly transparent

In summary, there are eight key elements to the major Chinese industrial zones – the lucky Chinese number for PROSPERITY is EIGHT, and adding your involvement equals nine – the Chinese number for LONGEVITY.

China Prospects. To give you an appreciation some of the key customer targets in China, I have broken them into three geographies – first Chinese companies that represent major opportunities for electronic components in China. Telecom and medical equipment manufacturers are prevalent.

Among the Chinese companies that are key targets for electronics sector are: Haiwei, Datany, ZTE, Great Dragon Telecom, Beijing Telecom Factory, Eastern Communications, Long Well Electronics, China Star, Shanghai Bell Company and Shanghai Bond.

Taiwan Prospects. The list of Taiwanese companies who have set up manufacturing in China is rapidly growing. Over 100 million Chinese workers are working for Taiwanese based companies. This means it is imperative not to ignore the significance of Taiwan as a design center.

Among some of the Taiwanese companies that are manufacturing in China include: Foxconn, Intek, First International Computer, HTC, Well Communications, Eastern Broadband, Taiwan Fixed Network Telecom, Acer, Microtek, Tanung and Mitac.

North American Prospects. US and Canadian companies have made a significant presence in China as well. Major US and Canadian distributors, such as Arrow, Avnet and Future, have invested significantly in China. Contract manufacturers also play a big role in the economic development.

And foreign companies, such as US-based Applied Materials, continue to win new orders. As reported earlier this year in the South China Morning Post, Applied Materials - the world's top maker of chip-making gear, will garner orders worth more than \$30 million US in China this year.

Among some of the key North American companies with strong presence in China are: GE Medical, Motorola, Emerson, and Linear Technology.

As a side note – of the 277 Baja California based maquiladoras that have closed in the past three years, as many as three quarters of them have moved to China, according to the San Diego Union Tribune. This is being heard over and over again in Mexico, as factories face intense competition from low cost manufacturing centers in China.

Advantages of Manufacturers Reps in China. There are numerous advantages to the manufacturers representative sales approach in China. First of all is the leverage of the

multiple line selling approach. Costs are after sale, and paid in commissions. You get what you pay for. In a depressed market you are not strapped with overhead expenses.

Doing Business in China – through Reps. In China, most reps stock product and invoice customers. A major challenge to multi-national sales organizations doing business in China is the fact that few reps, distributors or agents provide transactional POS information to manufacturers – therefore, the whole issue of commission splits becomes a frustration.

A key point for considering setting up a rep network in China is that you must have LOCAL people conducting business with LOCAL people. You cannot import or move people into a region, anywhere in the world, and expect acceptance by the local customer base – and this same rule holds true in China.

Finding Good Reps in China. Finding good reps for the Chinese market is a methodical formula, starting with your research. Use directories, shows, the trade press, and referrals for companies you already do business with that have a history in China.

Finding Good Reps in China – using Directories. Excellent directories are the ERA Locator, the EEM Catalog, CCPIT.ORG, ISM tools, and China's Ministry of Foreign Trade and Economics.

The Electronic Representative Association publishes the ERA Locator, which is a global organization. Member representative companies are listed geographically, and by product marketing group.

The EEM Catalog is a multi-volume directory of products, where manufacturers also list their representative companies.

Finding Good Reps in China – using Trade Shows. The ERA is a visible support group at major trade shows throughout the world, including major global shows like Electronica, which was held in Munich in November and Electronics China, which was held in Shanghai in March. At such shows, ERA provides facilitation between rep companies and manufacturers.

Trade shows are also the best opportunity, in a short period of time, to talk to customers and manufacturers at shows. You can conduct quick research by simply talking to these individuals about their experiences and recommendations.

Using the booths or stands as an advertising vehicle is a smart and cost-effective way to solicit “lines wanted” or “reps wanted”. Simply posting a sign in a booth is an effective tool.

Finding Good Reps in China – using the Trade Press. If you are interested in advertising, key specific market publications are the most direct approach. The “Representor” which is the monthly magazine published by ERA, is a targeted vehicle.

Finding Good Reps in China – using Referrals. Just like anything else in life, networking usually turns out to be the best source of information. Recommendations from associates and other companies that you know who currently are using reps are a good starting point.

Finding Good Reps in China – the Interview. Prior to the face to face meeting, refer potential candidates to your web site so that they can obtain a general picture of what your business represents.

During the first meeting with prospective companies, again be prepared to review your:

- Products
- Markets
- Capabilities
- Niches
- Opportunities
- History of your company and sales coverage
- Management structure
- Sales and marketing support

And I cannot emphasize enough the importance to have a well thought out plan on what your expectations are for your sales representative company. This is often overlooked or too general, and early on in relationships, misunderstandings occur. This includes:

- Sales goals
- Specific customer targets
- market focus

And be prepared to go into detail on your rep training program.

Recommendations. There are a number of excellent web sites that will assist in your research efforts.

The first is WWW.CCPIT.ORG - this is the quasi-governmental china council for the Promotion of International trade. The CCIPT can help put investors in touch with authorities in China's many special investment areas and high tech parks.

WWW.TEDA.GOV.CN is the official web site of the Tianjin Economic technological development area.

WWW.TDCTRADE.COM is the official web site of the trade development council of Hong Kong.

WWW.MOFTEC.GOV.CN is the site of China's ministry of foreign trade and economic cooperation.

WWW.CIDVC.COM is the Taiwanese Venture Capital Group.

Summary. Why China? Reviewing the numbers, the population is the largest in the world at 1.3 billion people. As the free market concept continues to grow in China, the number of potential consumers for goods and services is exploding. An unlimited, highly skilled labor pool is available for manufacturing. An internal infrastructure is already in place for manufacturing, represented by the seven major industrial zones. The China GDP grew well over 7% in 2002. China offers more business incentive than any other developing country to attract investment.

A careful, well-constructed strategy, utilizing the knowledge base of other companies that have successfully moved into China from other parts of the globe can assist in the process of moving into this explosive economic business opportunity.

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