



## **Notes on Manufacturing Transfer, Product Sourcing and Contract Manufacturing**

*Brief plain language notes suggesting typical factors that smaller and medium sized UK based companies take into consideration when embarking on contracting manufacturing and manufacturing transfer.*

### ***Introduction – Size No Longer Matters***

Not so many years ago only the largest companies could consider sub-contracting the manufacture of their goods on another continent, now in 2005 this route is open to any sized company.

With the growth of manufacturing in Asia, sub-contracting production allows companies with good ideas to concentrate on the design, branding, marketing and distribution of their products, while working in conjunction with a contract manufacturer who produces the actual goods on their behalf.

### ***Brief History – Made In Hong Kong***

Hong Kong became a major manufacturing source for non-Asian companies in the 1950's and grew steadily until China opened up in 1979 first in the south just north of Hong Kong, and then in Shanghai, which is now the most modern city in the world and a powerhouse of world manufacturing. The migration north now means that practically nothing is now made in high volumes in Hong Kong.



*Practically no manufacturing is now carried out in Hong Kong, average incomes in Hong Kong are on par with the UK, and in the secretarial sector considerably higher.*

### ***Geographical Sources –***

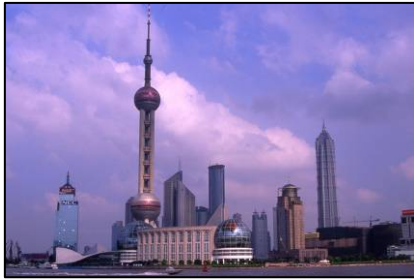
For smaller companies the main geographical areas of sourcing manufactured goods are:

China: Electronics, metal, wood, paper, stationery, books, injection moulded plastics, electronics, soft toys, furniture, etc, indeed practically anything.

Taiwan: Injection moulded plastics and metals, Taiwan is the centre of the world cycle industry, sports goods and many steel products, however transfer of Taiwanese industry to China is a feature of the present day Asian economy. Taiwan is a major source of goods into the west, and it should be noted that



many of the mainland Chinese companies and ventures are owned by Taiwanese companies.



*Shanghai has become the major city for arranging manufacturing transfer and product sourcing*

Thailand: Wood production in Thailand is sophisticated and highly industrialised, there are certain limits on the types of wood that can be sourced in Thailand (rubber wood dominates), more choice is available in China, especially around Shanghai where wood manufacturers will import stocks of wood.

Belgium: Carpets and rugs, Belgium is still the main producer of carpets in the world market; however they are starting to set up joint ventures with China as well, notably in areas near Beijing.

Eastern Europe: Carpets and Rugs, stationery, soft toys.

Other areas include South America for White Goods, India and Pakistan for leather and furniture, electronics and computer related products.

### ***Costs and Savings – How Do They Do it?***

As in any business venture, a company embarking upon a new venture has to look carefully at the cost implications for their business. Asian and particularly Chinese factories are pitching their services to the world based on the following:

- Lower margins in general made by Chinese companies than their European counterparts.
- Capital Equipment Costs lower.
- Labour Costs are cheaper.
- Skilled Labour Cheaper (but not that much cheaper).
- Flexible labour supply, this is still true to a certain extent, though not as true as it once was, China has a skills shortage in certain areas.
- MOQs – Minimum order Quantities - Have decreased markedly as more and more industry has developed in China.

Of these factors, experts agree that the most important factor which explains the competitiveness of Chinese industry is not the cheap labour, or the favourable exchange rate, but the fact that a Chinese company will work on gross margins which European industry would not consider.



### ***Savings – Should I think of Sourcing in Asia?***

When considering either sourcing an existing product or developing a new manufactured product from Asia, the rule of thumb which is generally accepted is that:

**If you cannot save 25 – 30%  
It is not worth going through the process.**

This figure has been used for some time and holds good for products right across the manufactured spectrum. Some companies do not realize that in the initial stages they will have to deal with extended supply times which consequently requires larger stock orders, which can tie up cash flow. This should be borne in mind when undertaking the switch of production of components or products to any foreign market.

### ***Typical Lead Times – How Long Does This Take?***

A realistic time scale for each product from specification agreement, through a couple of prototypes to the finished article with packaging is three months.

Most simple products or components can be completed in a shorter time than this, however as a rule of thumb this figure is one to bear in mind.

### ***Factory Selection – Who will I work with?***

The most important factor for the small company is selecting the correct partner. Which factory you select to manufacture your goods is crucial as you are dependant on their professional management, their ability to deliver and their on-going commitment to quality assurance and quality control.

You must have a contact who is fluent in written and spoken English.

### ***Logistics – How DO We Get The Goods Back?***

Transporting the goods back to your home market or forwarding them onto export markets is one area where you need to have all the correct documentation and reliable contact who again, must be fluent in written and spoken English.

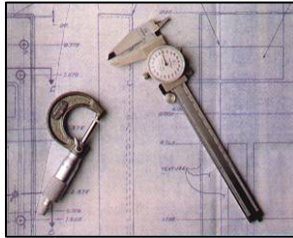
The vast majority of Chinese factories can recommend a freight forwarder or transport company, but it pays to get your own contacts in this area.

### ***Investment***

All of this costs time and money, you must be prepared to have an up-front outlay to develop your ideas from the drawing board to the point where you have the product manufactured and sitting in your warehouse back in the UK.



Tooling for manufactured products is much less expensive in China and Asia in general than it is here in Europe, as here all tooling is paid for up front on approval, no difference from here. Certain companies will however offer to finance tooling usually in exchange for the rights to sell the products, while paying you a royalty.



*Tooling is both faster and less expensive in China than it is here in Europe.*

### ***Control of Quality***

ISO 9000 family (9001, 9002 etc) is primarily concerned with quality management and auditing, while the ISO 14000 family is concerned with environmental factors.

When you are dealing with the factory of your choice, you must set a realistic standard for quality control and quality assurance. This means that the factory will guarantee to inspect one in a certain amount of products they are producing to check for quality

Different "standards" of QC exist for different markets, for example if you are selling to the Ministry of Defence your requirement for inspection may be 1 in 100, while for a supermarket retail chain, quality control may be 1 in a 1000.

It cannot be stressed too strongly that all of your requirements need to be clearly expressed:

- Clearly expressed in plain, simple English
- Do not leave anything to chance.

(e.g. not 100 boxes in assorted colours, but 20 brown, 20 blue, 20 green, 20 red 20 orange)

A **Pre-Shipment Inspection** is highly desirable, sometimes this can be arranged by an independent third party working on your behalf, but not associated with the manufacturing factory.

### ***Packaging and CE Marks***

To sell certain products (notably electrical devices, most educational goods and the majority of toys amongst others) into the European Union all goods must



have CE Marks, meaning that they have been tested and that they conform in all respects to European test standards.

An indirect benefit of sourcing from China is that testing is also cheaper than it is in the European Union and the as all of the reputable laboratories have offices in China this is a fairly straightforward exercise.

- Specify at the outset your regulatory requirements and who is responsible in practice for these.
- Also make sure that it is clear from the outset who pays for the testing and very importantly **re-testing**.

Although most Chinese companies will issue a test certificate for goods they manufacture if your clients are large retailers (e.g. Boots, ASDA, Tesco, B&Q etc.) these companies in general will **not** accept a certificate in the name of the Chinese factory.

### ***Benefits For Your Clients – FOB Pricing***

As you may expect, if you start saving money on manufacture you can be more competitive, but you will also find that your customers may want some of the saving passed onto them.

A popular way of selling great volumes is to offer FOB Pricing, this means that the clients can arrange their own transport of the goods from Asia to their home markets. Minimum order quantities may come into play here.

An FOB pricing offer is particularly suitable for export markets where it makes both financial and logistical sense for companies to offer FOB pricing. However, it can work equally well for domestic customers - especially those who are experienced in FOB procurement. (For example SIBD Ltd has Australian Customers who arrange for manufacture in China and sell this to their Australian clients through FOB showrooms in Hong Kong and China.)

Other examples are where your clients are actually closer to China than you are, e.g. West coast USA, it makes no sense to have the goods travel half way around the world to the UK to subsequently be sent to the West Coast of the USA.

Although the figures may vary according to the sector, those seeking FOB pricing are generally looking for a saving of 25% on wholesale UK pricing.

### ***Social Audits***

Over the last few decade high street retailers in western markets (including Japan who has it must be said has been the leader in this type of inspection and audit) demand guarantees from their suppliers that the goods are not produced by child labour or in a way which harms the environment.

Child Labour is particularly associated with the Indian sub-continent rather than China, but there are some reported cases and you should bear this factor in mind.



Factory visits are welcomed by the best companies and while you may not wish to travel to the factory in person, Social Audits can be commissioned by independent consultancies or on a questionnaire basis.

Factors that retailers are particularly concerned about include:

- There is no child labour involved in the production of goods they sell.
- Employees are well treated and reimbursed properly.
- Environmental Policy.

However, for the newcomer to this business, it is necessary to bear in mind that traditions, social customs and work conditions in China are radically different from those in Europe.

### ***Examples of Manufacturing Transfer arranged by SIBD Ltd***

SIBD Ltd has arranged many transfers of manufacturing to Asia including Injection Moulded Plastics, Books, Toys, Soft Toys, Carpets, Wooden Furniture for classrooms, pens and general office stationery, high end gift ranges, components for automatic packs, cots, Art and Craft ranges, and are currently exploring billiard tables, cycles, trikes and trampolines.



*SIBD Ltd arranged the manufacturing transfer of a range of high quality gift porcelain for children destined for the German market.*

This project on behalf of a major German company involved the transference of the production of the pottery from Europe to China. The exceptionally high quality of this product required detailed specification, trials and detailed quality control and quality assurance.

Porcelain is a difficult technical product to produce and involves detailed analysis of glazes, firing times, clays etc. All of this was a serious challenge for SIBD Ltd.



Metal Boxes



Pop-UP Books



Stationery

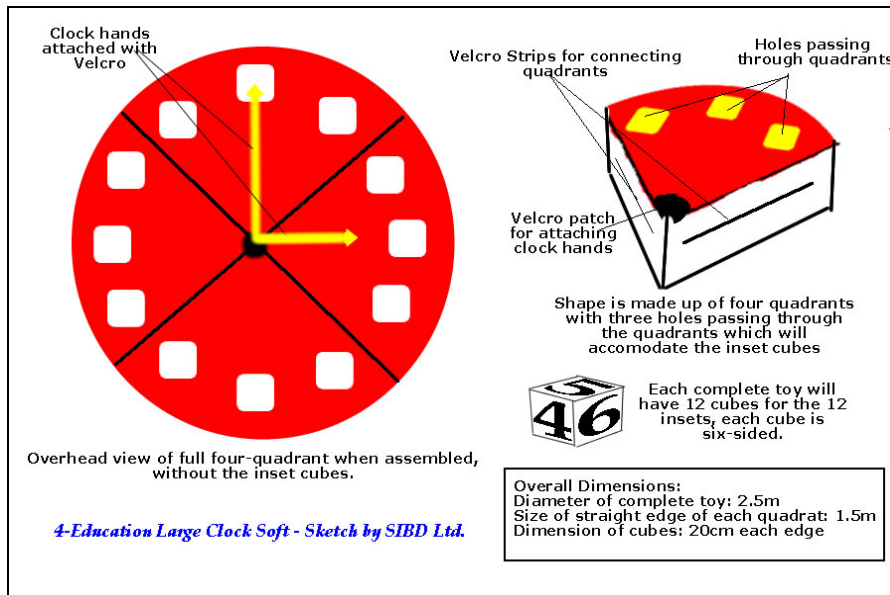
### Packaging

Never underestimate the importance of having the correct packaging for your goods if they are made in Asia. Design of product packaging is fundamentally different in UK, Europe, North America and even varies between regions on each continent.

You should have European design of the packaging.

### How to Start

For a small company interested in exploring the production of a new product all you need to start the process is a simple sketch detailing your idea. This is passed to typical manufacturers who will then take the idea to the next stage and outline costs.



### Confidentiality Agreements

When detailing these ideas, it is generally the policy that the sourcing agent and the factory costing the idea should sign a Confidentiality Agreement, do not feel inhibited about asking for this up front.



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SIBD Ltd began twelve years ago as agents for European and North American Companies selling into Asian markets, then the business developed by representing Asian companies into both Europe and North America.

Manufacturing transfer has grown greatly in the last three years from single items and components to complete ranges being arranged for manufacture in China and Taiwan.

Recent flagship projects have included **Invicta Ltd** (UK based company with the right to the Mastermind Game and a huge range of plastic educational games and toys) SIBD Ltd has arranged the complete Manufacturing Transfer to a Hong Kong owned partner with state-of-the-art production facilities in China.

**Haba Group** – Germany's number one mail order company, SIBD Ltd are Haba's number one agency and are used extensively for product sourcing (250 products at present) and an important manufacturing transfer project shifting uncompetitive production from Eastern Germany to a factory near Shanghai.

**Little Experience** – English company with a high end reputation selling into the likes of Harrods, Gallerie Lafayette, Liberty etc. SIBD Ltd has arranged the complete manufacturing transfer of their range of gifts to China, and secured them distributors in Japan, France, Italy and Australia.



  
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