



Poorly Made in China: a reality check

Despite being hailed as ‘the world’s workshop’, China’s reputation of being a reliable and responsible manufacturer is far from world-class. In his new book ‘Poorly Made in China’, intermediary and author Paul Midler exposes the pitfalls of manufacturing in China, debunking several myths in the process.

The first -- that China exists for the United States alone to make things for Wal-Mart -- is a fallacy, says Midler. The reality is that Wal-Mart’s business in China, in terms of outsourcing, is less than one per cent of total Chinese exports.

Paul Midler

“It was a statistic that was widely published in 2008, that procurement for Wal-Mart out of China was steady at \$9 billion. And steady does not necessarily imply something good there. It may have remained steady over the course of three years, but meanwhile Chinese exports were climbing 20 per cent during this period,” he told INSEAD Knowledge. “That the largest of the largest is less than one per cent is telling. The United States doesn’t take more than a fifth of China exports.”

This ties in with the next preconceived notion of a one-size-fit-all approach to economies worldwide. “There are some people who believe that all economies are the same, that every place in the world is more or less the same. Supply, demand -- whatever their basis -- they believe that it’s all the same. But actually there are quite a lot of differences among us and some of those differences are cultural. Every place is different. Even a place like the United

States, you cannot say is uniform. You have Manhattan, you have Alabama, there are many different places.”

China, he adds, does not operate on the same economic principles as other countries. “What can you say about an economy where relationships get worse over time (and about) factories that are more successful are harder to work with than factories that are struggling? And what does that say about the Google case in China, and how China is becoming more and more successful; and the more successful it becomes, the more teeth it starts to show ... You have (this) exacerbation of the boom-bust cycle in China because people, when they are becoming more successful, are behaving in riskier and riskier ways and taking more and more liberties.”

He elaborates: “Some of the factories that are engaged in the quality games are not the poor ones, (it’s) the ones that are actually doing better. It’s the poor factories in China that don’t dare play games with quality that actually deliver a higher quality product.”

Ironically it is the ones who that have made their money, are bored with their success, have already

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gotten over the excitement of snagging their big customers, that are trying to show how clever they can be -- by taking shortcuts where possible.

Yet China continues to receive production orders from all over the world. Why?

“Some of that has to do with the things they’re good at, like finding the margin down the road and quoting lower in the beginning,” says Midler. “One of the singular ways in which they do business -- and, really, to their credit -- has been the way in which they’re able to take a chance on the long term with regards to a production relationship. Maybe in the beginning they have no profit, but down the road they’ll find their way.” And that level of confidence is something that I don’t know if manufacturers in other economies have seen.”

One of the methods used by Chinese manufacturers, he says, is the ‘arbitrage opportunity’. So while profit may not be generated from producing for first-market importers in the US, Canada and Western Europe, a manufacturer’s bottom line could, instead, derive solely from second-market customers in Latin America and the Middle East.

“A manufacturer accepts an order for 500,000 pieces from a first-market importer that produces a unique design. Rather than merely fill the order, the supplier keeps the machine running and its people working until it produces a total of 700,000 pieces. The original customer gets his order for half million pieces, and then the factory sells the surplus of 200,000 pieces at a considerable markup.”

Another tactic is ‘quality fade’ where manufacturers sometimes secure an order and then, over time, they lower the quality standard of the product in order to find their margin. “This is sometimes done to the detriment of the product itself and that’s when we’ve seen things go awry,” he says.

Midler thinks the quality issue can’t be addressed in a top-down fashion, but rather it’s those on the factory floor who can turn around the situation. “I think it needs to be handled from the bottom up, not from the top down. And I think a lot of the approach right now has been having high-level meetings. The United States’ watchdogs and the China watchdogs get together and they have dialogue and a lot of it is empty talk.”

The US though has been trying to make some headway on quality control via its Food and Drug Administration offices in China, which they opened in 2008 as part of its strategy to improve safeguards for US imports. “I think it’s the first time ever a major economy has ever had to take a domestic agency of that kind and set it up overseas ... It’s a sign of how bad everything is, that we’ve actually had to do

that.”

Midler says it’s “very disturbing” that, even after two people were executed in an earlier melamine scandal back in 2008, more new cases are still surfacing. “Cadmium in toys has now come up. And you’d think we’d learn the lessons already from the lead case (when Mattel had to recall millions of toys made in China), and here we are revisiting the same old issues.”

One of the reasons for this stalemate, he feels, is because there just aren’t enough whistle blowers in China, as the Chinese view whistleblowers with disdain because they are seen as acting out of self interest.

“With regard to the quality scandals that we’ve seen, in almost every case, we didn’t find out about the product failure until it reached the end market and there was a bad result. But in many of those cases, there were workers in production facilities that knew what was going on and that they didn’t say anything. You can’t fault them because there’s really nowhere to go. If you were working somewhere and you knew about the melamine scandal and you saw what was being done, who would you report it to?”

Convincing those at the upper echelons of any wrongdoing is even harder. “You can’t convince somebody that his methods are wrong, when his business is growing 100 per cent or more, (and) your business is growing only 10 to 20 per cent a year ... People who are doing well (are) emboldened by their business style and thinking.”

With no real safeguards in place, it seems then that the only recourse for now for those wanting to trade with the Chinese is caution. Midler offers this advice: “You want to temper expectations. I think a lot of people who were big boosters on China, convinced many who didn’t know better to rush in to China without weighing in certain risk factors. You definitely want to make sure that, for certain things, you’re budgeting enough on the compliance issue. If you’re in manufacturing, you want to make sure that you have a budget for doing things like quality control.

‘Poorly Made in China: An insider’s account of the tactics behind China’s production game’ is published by Wiley.

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