



42TM
Rules
for Sourcing and
Manufacturing
in China

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2ND EDITION

A Practical Handbook for Doing Business in
China, Special Economic Zones, Factory
Tours and Manufacturing Quality

ROSEMARY COATES

FOREWORD BY TEX TEXIN, CEO, XENCRAFT




**SECOND
EDITION**

“42 Rules for Sourcing and Manufacturing in China (2nd Edition)” Book Excerpt

A Practical Handbook for Doing
Business in China, Special
Economic Zones, Factory Tours
and Manufacturing Quality

By Rosemary Coates

Foreword by Tex Texin, CEO, Xencraft

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Foreword by Tex Texin, CEO, Xencraft

When I first visited Pudong in 1993, an economic development zone outside of Shanghai, foreign companies were just beginning to take up residence. Many of them had unclear strategies and invested solely on faith in the size of the Chinese consumer market. Today, Pudong's GDP is greater than US\$50 billion. I have been fortunate to see first-hand how many Chinese companies, from Guangzhou to Beijing, have transformed themselves from makers of simple labor-intensive products to high-tech manufacturers of sophisticated products. China is rapidly changing, and I am amazed with every visit at how it has evolved yet again.

Earlier this year, Rosemary Coates introduced me to a plastics manufacturer in Shenzhen. Towards the end of our visit and factory tour, Rosemary began asking about the employee dorms. Rosemary had connected very well during our meeting both with the executives and our guides (as she always does). Consequently, we were granted the very rare privilege of being invited to see the dormitory and the guide's quarters. We saw the facilities and the living conditions and discussed how room assignments were made.

This particular incident epitomizes for me Rosemary Coates and her approach to China, people, and business: she is affable, inquisitive, knowledgeable, experienced, and hands-on. Rosemary uses her knowledge of the history of China and the culture of its people to understand their influence on modern business practices and relationships with clients and partners. She

validates this knowledge with site visits and by getting behind the façades to a more in-depth and comprehensive picture.

Traveling through Shenzhen, the change from a fishing village just twenty-five or so years ago to one of the largest cities in the Pearl River Delta region and the largest manufacturing base in the world is astounding. Even my previous visit only a few years earlier hadn't prepared me for the city's further urbanization. Living standards improved to the point that Shenzhen residents were sporting clothing more fashionable than some Manhattanites.

Shenzhen may be extreme, but this rapid change is not rare for China. Through its Special Economic Zones (SEZs), China has brought investment, growth, and evolution on an incredible scale to many of its cities. An important message that Rosemary brings within her book is that you cannot view China through conceptions that may have been valid only a few years ago.

The factory we toured was a case in point. If you still think Chinese companies compete on cheap labor alone you are very mistaken; this factory made parts for high-tech and biotech clients using automation and clean-room environments for precision and purity. The company had a multi-year vision for extending its technology that will continually increase its capabilities and its competitive advantages and ensure its industry leadership. This plan does not rely on cheap labor to succeed.

The implication for businesses today is that to ignore China is to ignore opportunity. To make decisions about China based on dated information or aged stereotypes is to act out of ignorance. To dismiss Chinese manufacturers as low-tech suppliers or sources that are of value where only cheap labor matters is to dismiss a sophisticated visionary that can bring you efficiency and collaboration.

With these 42 Rules, Rosemary brings you the key knowledge elements that you need for sourcing and manufacturing in China. She interviewed numerous experts to substantiate the Rules with the experiences and wisdom of others.

Rosemary Coates' years of experience in Asia have shaped and developed these Rules. Her book will give you the guidance you need to initiate and conduct business with Chinese partners. Follow Rosemary's rules, visit and come to understand China yourself, and embark on new opportunities and successes in sourcing and manufacturing.

Tex Texin, CEO, Xencraft
Silicon Valley

Twenty executives with real hands-on, supply chain manufacturing and sourcing experience in China were interviewed for this book.

Introduction

I have always been fascinated by China, and have always felt a deep connection to Chinese people and culture. When I was seven or eight years old, I remember spending the entire summer in the heat of Phoenix, Arizona, trying to dig my way to China. The feeling that I wanted to get to China never went away.

Over my professional career, I have worked on consulting projects throughout the world, including extended periods in Korea, Japan, Australia, Singapore and China. I am so fortunate to have had these kinds of opportunities to travel and help companies achieve their goals worldwide. I have led projects at Samsung in Korea, Exxon in Japan, Microsoft in Singapore, and many more in Australia and throughout the U.S. and Europe. When I finally landed my first project in China and traveled there for the first time, I was completely awestruck and wanted to absorb everything I saw and heard and experienced. I could barely sleep. I wanted to drink in the culture, sounds, smells, and energy I felt everywhere. I wanted to sightsee, tour the factories, and meet as many people as possible.

Even though I had already worked for extended periods in other Asian countries and thought that I was somewhat familiar with Asian cultures, that first visit to China was a startlingly different experience. There was much to do and learn. There was so much opportunity everywhere I looked. I felt an energy and connection unlike anywhere else in Asia I had worked or visited. Having spent twenty-five years in supply-chain operations and consulting, I could see that China

was clearly the future for sourcing and manufacturing. Over time, my interest and excitement grew into a specialty-focus area for my consulting company.

As so many of the people I interviewed for this book told me, the Chinese people think they can accomplish anything. This "can do" attitude is evident throughout China, particularly in the metropolitan eastern provinces and the growing industrial base. I love this about the Chinese. They are eternal optimists and will never tell you "no," even if you ask the impossible.

After a few years of helping my clients to source products and manufacture in China, I wanted to share what I had learned. In addition, there were many executives with China experience, (my clients or in my professional network) whom I thought would be willing to share their experiences. So I set about conducting more than twenty interviews with the best strategists and tacticians on China, to complement my own expertise. The results are in the following pages.

Interviewing this many executives with real hands-on China manufacturing and sourcing experience was a truly extraordinary opportunity. That they were willing to share their experiences is our good fortune. Read on and you will find enormous insight into conducting business in China.

But before we get started, we should answer the question, "Why do businesses in China?" Here are a few reasons. You can add some of your own.

- 35–40 percent of the world's production is already in China. The significant cost benefits are causing manufacturers everywhere to consider alternatives for global production.
- In a recessionary environment, manufacturers look for cost savings in their organizations. Outsourcing manufacturing or sub-assemblies, or finding Chinese vendors can save you up to 85

percent of your domestic costs. The average savings through sourcing in China are 40–60 percent.

- China is America's fastest-growing export market. The potential market to sell goods and services in China is enormous. The Chinese middle class is rapidly expanding and hungry for Western goods.
- Businesses involved in exporting, both large and small, generally weather downturns in the U.S. economy much better than those businesses that are strictly domestic.

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Expect the Unexpected—Betty's Story

Betty speaks four languages and has an MBA from Shenzhen University.

"Betty" (her adopted Western name) is a fascination and an inspiration. I was introduced to Betty while I was touring a plastics factory in Shenzhen, about forty miles northwest of Hong Kong in Guangdong Province. As mentioned earlier, Shenzhen is part of the Special Economic Zone (SEZ) established by Deng Xioping. Now, twenty-five years later, Shenzhen's population is roughly fifteen million. About six to ten million of these people are migrant workers who return home on the weekends and live in factory dormitories during the week. Shenzhen is the largest migrant city in China.

Betty was born and grew up in northern China where the native language was Mandarin. Her parents were rural farmers, but they insisted she go to school and study hard. Betty was a good student, hardworking and smart, and she was interested in many subjects. She studied Russian in elementary school, high school, and college, along with math and science. After college, Betty relocated to Shenzhen to take a "factory girl" job, where she assembled electronics for about US\$80 per month. There, she had to learn Cantonese, the language of southern China, by studying at night in the dormitory and practicing with her co-workers and supervisors during the day. Eventually, she became fluent in Cantonese and was able to get a better job at the plastics factory at a higher salary and with better dormitories.

When I met Betty, she was the supervisor at the plastics factory, overseeing the production of semiconductor trays, medical device parts, and other plastic components, plus several hundred workers. As we toured the design and production facilities it was

obvious she was in charge, being treated with respect by the employees. Her cell phone rang several times and she exchanged conversations and seemed to give instructions in Cantonese.

Over time, Betty was introduced to many American and Western European visitors. Betty decided she should learn English to improve her chances for promotion, so she started taking English in night school. A few years and a couple of promotions later, she returned to Shenzhen University for her MBA, so she could understand more about Western business.

I was astonished that she would study graduate business administration (and that Shenzhen University would offer this degree) in the context of Chinese Communism. After all, an MBA is the most pro-capitalist education you can get anywhere in the world. But what we all come to realize is that China practices a kind of economic capitalism together with governmental communism. Business is done with a profit motive always in mind. In thinking about Betty, it seems that studying capitalism fits perfectly with her desire to have a successful business career. Profit has become the motive in China, and the tremendous growth throughout Chinese manufacturing over twenty-five years is the result.

Betty is a good example of the surprises in store for you in sourcing and manufacturing in China. Any preconceived notions about what is and isn't happening in China and about dealing with the Chinese are probably, at best, inaccurate and typically completely wrong.

When you come to China, expect the unexpected.

Find Multiple Suppliers

Finding reliable and capable suppliers may be very difficult.

One of the more difficult aspects of doing business in China is finding reliable and capable suppliers and manufacturers. Not that there is any shortage of suppliers wanting to do business with you. But how do you know which ones to choose? If you have a product that you want produced in high quantities (multiples of one thousand), then there will be many companies anxious to do business. If you have smaller quantities, finding a reliable supplier may be difficult.

Alibaba—I encourage most small companies to start with Alibaba, <http://alibaba.com>, a website that matches buyers with sellers and manufacturers. On Alibaba, you can search for manufacturers in a category or post a request for information. Interested businesses will contact you via email through Alibaba much like they would via eBay. Alibaba is a good place to start as you can learn about a supplier online and sometimes even see a video clip of the factory. Just like buying something on eBay, you assume the risk. Alibaba suppliers post many different types of products—metal parts, toys, T-shirts, etc.—and are generally not manufacturers, but rather manufacturing representatives or sales companies with ties to multiple factories. This means there is an additional layer involved, less control, and possibly more cost.

Here are some guidelines for posting a sourcing request on Alibaba:

- Write your requirements very clearly and simply but with sufficient detail so that the manufacturer knows exactly what you want.
- Provide precise specifications, including material weight, material quality, thickness, standards for colors and sizes, etc. Americans are notorious for

not being detailed enough in the specs and being disappointed because the product did not meet their unspecified requirements.

- Be prepared to answer a lot of questions from Chinese suppliers. They will be trying to quote and produce the exact product you need. It's best to correspond via email using clear and simple language. Help suppliers understand *exactly* what you want.
- Expect large minimum quantities to be quoted—typically multiples of one thousand. While you may not have planned to order in such large quantities, it may be economical to do so. Chinese manufacturers are very good at producing large quantities with repetitive processes.
- Ask for digital pictures of their products.

Once you select two or three potential vendors, ask for samples. Evaluate the samples of the product before committing to purchasing anything. Samples are typically no charge to you, but you will have to pay for shipping (typically via UPS or DHL). Samples can generally be imported into the U.S. duty-free.

Other Online Sources—There are plenty of other on-line sources such as <http://globalsources.com> that can provide leads to potential sources for industrial products. Remember that these are unqualified sources. I strongly suggest that you visit these factories in person before you commit to sourcing anything.

Trade Shows and Fairs—You can also find potential sources at the many trade shows across China, but especially in Guangzhou and Hong Kong for electronics, and Shanghai for industrial products, textiles, and electronics. The Canton Fair (China Import and Export Fair) is especially good for discovering potential suppliers. Talk to as many people as possible when you visit there and you will typically find multiple sources. Many buyers go to the Canton Fair and then visit the factories of the suppliers that interest them.

Sourcing Consultants and International Procurement Offices—For larger buys, I recommend a Chinese sourcing company or an international procurement office such as ThreeSixty Sourcing or Bamko that can research, recommend, and supervise the production inside of China. Companies such as PCH China Solutions may also offer engineering services. Some of these sourcing companies provide analytical tools that help to qualify suppliers on many aspects of their business. A sourcing company can also assist you in negotiating a deal and supervising production. These people work hard at developing *guanxi* with the factory management and look out for your best interests.

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Do's and Don'ts Are Helpful to Know

At a Chinese banquet, never eat everything on your plate.

Many sources discuss the various do's and don'ts in China. There are plenty of resources available to you online and in print. It's always a good idea to review before every trip to China, just to refresh your thinking.

Here are some of my favorite reminders:

- Shaking hands is a common practice. Greet Chinese people by saying "ni-hao," which means hello.
- Don't take offense when a Chinese asks you how much money you make, how old you are (what year are you in the Chinese Zodiac), how much you weigh, or if you are married. These questions are seen as nothing more than getting acquainted. You should give some personal information such as where you went to college and about your family.
- At a Chinese banquet, never eat everything on your plate; always leave at least a morsel of food behind. Eating everything on your plate implies that your host didn't serve you enough food, a harsh insult. Never leave your chopsticks propped up in your rice bowl as they look like the sticks of incense that Chinese burn at family graves.
- Chinese do not tip. The price you agree to pay for service is the one you pay. Some tourist hotels will add service charges to your restaurant bill.
- Chinese don't stand in line. They prefer to push and shove. Forget being polite if you are trying to get in somewhere.
- Avoid political discussions. Chinese are very uncomfortable hearing criticism of their political leadership or their government.
- Study the tenets of Confucianism, which influence everything Chinese.

- Never give a clock as a gift. A clock is a symbol of time running out; in other words, impending death.
- Always wrap the gifts you bring, preferably in red and gold. The colors white and black are associated with death, so choose different colors. I usually put the paper and ribbon in my suitcase and wrap the gifts after I arrive, so they look neat and fresh.
- Never give scissors or knives as they symbolize the cutting of ties.
- If you are approached by young women wanting to "practice English," beware. They are probably associated with the Communist Party and gathering information about you, or will take you to a restaurant for tea where they get a commission.
- Learning a few words and phrases of Chinese helps. Learn how to count to ten and how to say "thank-you," "hello," "good-bye," and "where is the toilet?"
- Don't just take a person's business card and stuff it in your pocket. (Westerners are so guilty of shoving business cards across the conference table like Frisbees.) Receive each business card formally with two hands and study it with interest. This is a sign of respect. Give your card with two hands, facing forward, towards the recipient.
- Chinese business people have different ideas about time. Things happen when they happen, and westerners must learn not to get upset when there is no agreed schedule of events. Change your westerner paradigm about time.
- Recognize that despite all of your research, data, market analysis, preparation, and strategies for closing the deal, what is going to matter is people with *guanxi*.
- Avoid embarrassing anyone. Never disagree, argue, contradict, poke fun at, joke about, be sarcastic about, ridicule, correct, or discipline anyone in public because these things will cause a Chinese to lose face. Always praise people in public.
- Understand the power of reciprocity and how it relates to *guanxi*.
- If you are a consultant, be sure you are on a regular payment schedule. It is very difficult to get Chinese to pay on time, if ever.
- Don't be a seagull (swoop in, crap all over, and fly out). Plan to spend time and make many trips to build relationships.
- Learn how to tell when Chinese are saying no. Chinese don't like to give direct negative answers. They might say "maybe" or "I'll think about it," but never "no."

A u t h o r

About the Author



Rosemary Coates is the President of Blue Silk Consulting, <http://bluesilkconsulting.com>, a global supply chain consultancy. Prior to Blue Silk Consulting, she was a senior director at SAP, the supply chain consulting practice leader at KPMG Peat Marwick and at Answerthink, and a regional manager at Hewlett-Packard.

Coates is a Licensed United States Customs Broker. She is also a Lifetime Credentialed Instructor for the State of California Colleges and Universities. She taught management, international business and importing and exporting for ten years.

Coates has consulted with over eighty global and domestic clients, VCs, and private equity firms on supply chain systems and processes. She has considerable international experience and has worked for extended periods in Asia and Europe. She has extensive knowledge and experience in manufacturing and outsourcing in China.

One of today's most sought after China supply chain experts, Coates is a frequent speaker at industry conferences and a feature writer for global business publications. Coates is a member of Reuter's Insight, a Community of Experts, and Gerson Lehrman Group Experts where she consults on supply chain matters. She is an Expert Witness in legal cases involving supply chain matters.

Coates holds an MBA in Finance and Operations Management from the University of San Diego and a BS in Logistics from Arizona State University.

Coates has written two other books; ***Negotiation Blueprinting for Buyers*** and ***42 Rules for Superior Field Service***.

**Getting “42 Rules for Sourcing and Manufacturing in China
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(<http://www.happyabout.com/42rules/sourcing2china.php>)

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Please contact us for quantity discounts sales@happyabout.info or to be informed about upcoming titles bookupdate@happyabout.info or phone (408-257-3000)

"These '42 Rules' will help you navigate the shoals of doing business in China. Rosemary Coates' practical and accessible advice ranges from the value of guanxi (networking) to the importance of using a virtual private network for communicating with your colleagues. She realistically outlines the cross cultural challenges of differing views on topics as diverse as wages, intellectual property protection, and subcontracting. It should prove a valuable introduction to anyone contemplating outsourcing to China."

Donald A. DePalma, PhD, Author of 'Business Without Borders' and Chief Research Officer at Common Sense Advisory, Inc.

"Rule 43: For any person or company doing business in China, thinking about doing business in China, or even planning a non-business tour, Rosemary Coates' '42 Rules for Sourcing and Manufacturing in China' should be required reading. It is concise, accurate, and perceptive, and provides a superb primer on this fascinating, confusing, and eternally dynamic country that will lead the world in the 21st century."

Barry Horowitz, Global Logistics and Trade Consultant and former General Manager, Port of Portland

"As someone who has traveled internationally for decades, this book offers the ultimate antidote for faux pas. Ms. Coates' diligent research provides valuable guidance to anyone interested in doing business in China."

Joel Sutherland, Managing Director, University of San Diego Supply Chain Management Institute



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