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Are China Manufacturers Simply Low Cost Producers – or Serious Global Competitive Threats?

McKinsey Survey latest to Show Disconnects Between Western Beliefs, Chinese Company Actions; the "Dragons" have Ambitious Plans

SCDigest Editorial Staff

While China has obviously seen exceptional growth as a source of finished goods and component supply for Western and Japanese corporations, are Chinese companies strong threats to those same companies in terms of global competition down the road?

The answer seems clearly to be Yes, but many Western companies appear not to take the potential competitive challenge too seriously.

A recent survey of over 1000 companies by McKinsey, for example, found that 41% of executives believe overall Chinese manufacturers are "weaker" than competitors from most other countries.

McKinsey notes that "Besides lower prices, companies in China have little to offer global markets, say respondents, who particularly dismiss Chinese product quality, marketing skills, and brand strength. From the Chinese perspective, the results suggest that low costs will go only so far and that moving up the value chain is more important than ever."

The perception that Chinese companies are laggards, McKinsey says, might explain why many executives report mounting a muted business response to Chinese competitors at best, viewing manufacturers as a low-cost source of supply and little else.

But is that view a smart one?

Chinese Dragons are Coming after Western Business

In their recent book "*Dragons at Your Door: How Chinese Cost Innovation is Disrupting Global Competition*," authors **Peter Williamson** and **Ming Zeng** eloquently described how a new generation of Chinese competitors is using total "cost innovation" in product design and the supply chain – not just low labor costs – to gain competitive advantage and growing market share in a number of markets and industries. (See **The Supply Chain and China's Dragons**.)

McKinsey says that "While the global competition appears to have its guard down, executives at companies based in China are preparing for a battle royal."

They cite the example of China International Marine Containers Group (CIMC), which has moved from a company without a purpose in the early 1990s to one that now enjoys ***70% global market share*** in the ocean container business through aggressive strategies and cost innovation principles, wiping out seemingly entrenched European and South African competitors in the process.

McKinsey also sees Western executives failing to fully appreciate the future competitive threat.

"This lackluster reaction to the global ambitions of China's companies raises the question of whether business executives elsewhere are setting themselves up for some unhappy competitive surprises," the report notes.

While 80% of the McKinsey respondents did expect

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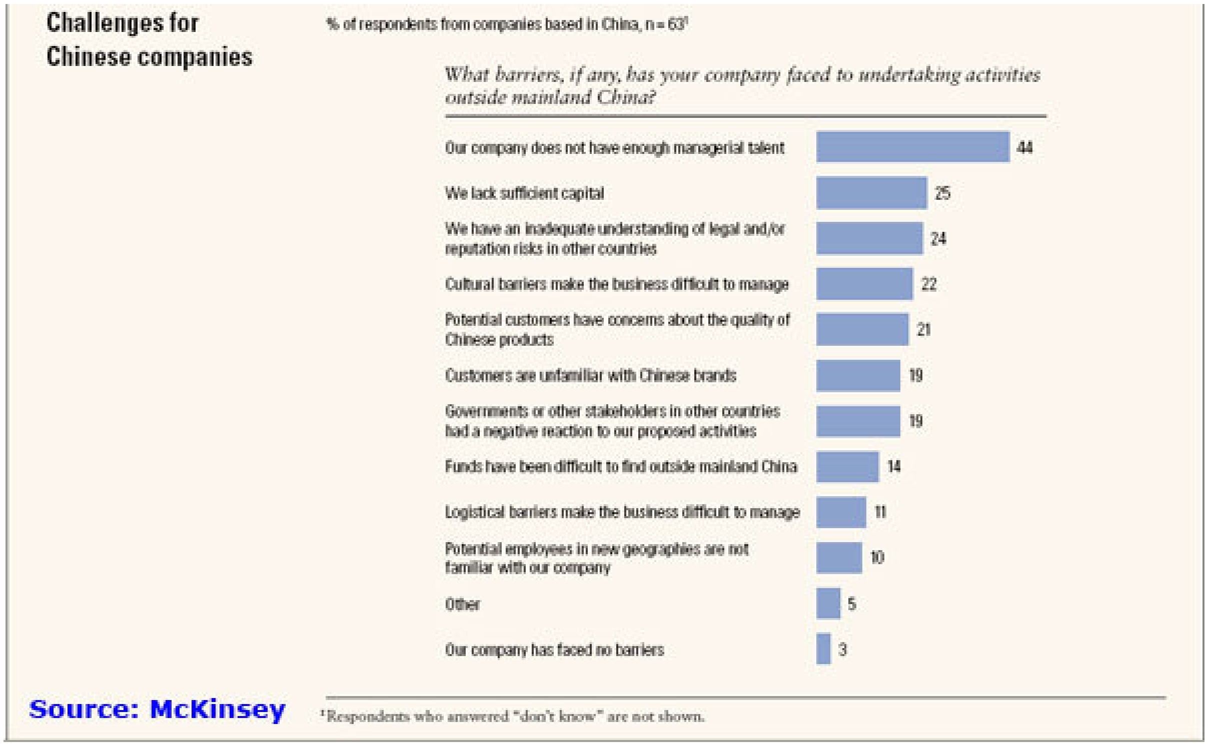

competition from China to increase over the next few years, only 6% of North American executives expect Chinese competitors to have any serious impact on their company's global revenues.

Echoing the perspective of Williamson and Zeng, McKinsey says that "While the global competition appears to have its guard down, executives at companies based in China are preparing for a battle royal."

Among respondents from Chinese companies to the survey, an overwhelming 77 percent say they expect their companies' revenues from outside mainland China to increase over the next three years, including 29 percent who foresee a significant increase in foreign revenues.

These expectations are in line with the respondents' recent experiences. For example, 74 percent say that the foreign revenues of their companies increased over the past three years, with 31 percent reporting a significant increase. 59% of Chinese respondents say they are actively marketing products outside the home market, with North America being the most important target region.

Chinese companies do see barriers to their international expansion, however. As shown in the chart nearby, managerial talent and limited capital are cited as the two biggest hurdles.

What to Do?

Both McKinsey and Williamson and Zeng believe companies need to take the potential threat from Chinese manufacturers on the global stage more seriously in their strategic planning.

Williamson and Zeng also argue that companies need strategies from the top to create a "***global China mandate***," in effect using China as the basis for their own global cost innovation strategies.

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