

# OPERATING IN SHANGHAI & INCREASING SUPPLY CHAIN COST EFFICIENCY

Case: Company X Ltd.

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Antti Orasvuo

Lahti University of Applied Sciences  
Degree Programme in International Business

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#### ABSTRACT

Main objective of this thesis was to present insight to Chinese economy and create a tool which could be used for determining the problems companies may face when entering new markets. Thesis contains general information about China as well as knowledge about the case company's new operations.

Thesis is divided into to case study and theory. The theory goes through generally the environment in which business is conducted. The case side is concentrated on Company X. Company X is an American company which sells pet accessories globally. The case study's focus is on research about the company's new supply chain implementation. For readers this part of the thesis gives an informed view on how to handle logistics operations in China.

The thesis was drafted in, Shanghai China. It is based on several books about Chinese economy, culture and logistics. The researcher gained knowledge during the investigation and was able to make more accurate conclusions toward the end. Interviews with international business professionals played an important part in this thesis. The case study was drafted with help from Shanghai representational offices employees.

Company X was also analyzed in Strengths Weaknesses Opportunities Threats (SWOT) analysis. Calculations and all information presented on case study are based on Company Xs shipment logs. These logs contain information on shipments from China during past five months.

The findings of operational environment in China where similar to the conclusions made in most literature used during the research. China still has to be seen as a high risk country for conducting business. This risk comes from various factors. There is still political risk present. This risk decreased after joining the World Trade Organization, (WTO) but it is still making huge changes in legislation and can be seen even destructive for some fields of business. The Chinese infrastructure can not be placed on the same level as western infrastructure. Depending on entry mode, there are also many other risks involved in communications and culture.

Conclusion on case study about Company Xs new supply chain project was that it is highly recommendable. Because Company X has not finalized its plans concerning China, some recommendations could be considered as references on future decisions.

Key Words: International trade, China, Risk management, Company X, supply chain.

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### TIIVISTELMÄ

Päätavoite tässä lopputyössä oli määrittää millainen bisnesympäristö Kiinassa vallitsee ja luoda työkalu, jota voidaan käyttää riskien ja ongelmien hallintaan. Lopputyö sisältää yleistä tietoa Kiinasta ja tarkennettua tietoa caseyrityksen toiminnasta.

Lopputyö on jaettu kahteen pääosaan, jotka tukevat toisiaan. Teoriapuoli keskittyy yleisesti bisnekseen Kiinassa. Case-puoli keskittyy Company Xn toimintaan. Company X on amerikkalainen firma joka myy lemmikkitarvikkeita ympäri maailmaa. Tutkimus keskittyy kyseisen firman uusiin logistisiin muutoksiin. Lukijalle tämä osa antaa hyvän kuvakulman, kuinka Kiinassa logistiikka toimii.

Lopputyö kirjoitettiin Shanghaissa. Tutkimus perustuu kirjallisuuteen ekonomiasta, kulttuurista ja logistiikasta. Tutkija sai paljon tietoa aiheesta, kun tutkimus eteni loppua kohti ja pystyi lopulta päättämään tarkempiin lopputuloksiin. Haastattelut alan ammattilaisten kanssa olivat tärkeä osa tätä lopputyötä. Case-puolella Company Xn työntekijät toimivat yhteistyössä tutkijan kanssa. Nämä henkilöt olivat omien alojensa vastaavia henkilöitä ja täten erittäin tietotaitoisia. Company X myös käytiin myös läpi SWOT-analyysissä. Tutkimuksen logistiikka laskelmat perustuu firman laivaus asiakirjoihin. Näistä saatiin tieto firman viiden viime kuukauden kontti liikenteestä.

Lopputulos Kiinan bisnesympäristöstä on jokseenkin samansuuntainen kirjallisuuden kanssa. Kiina on edelleen korkean riskin maa tehdä kauppaa. Poliittinen riski on edelleen läsnä. Tämä riski pieneni WTO jäsenyyden myötä, mutta suuria muutoksia tehdään edelleen lainsäädännössä. Nämä muutokset voivat olla jopa tuhoisia joillekin aloille. Infrastruktuuri ei ole vielä länsimaisella tasolla. Kommunikaatiossa ja kulttuurissa piilee myös omat riskinsä. Näiden vaikutus riippuu suuresti siitä, millä tavalla yritys on läsnä Kiinassa.

Lopputulos Company Xn uusista suunnitelmista on selkeä. Firman tulisi mahdollisimman nopeasti pyrkiä muutamaan toimintansa niin, että se pystyisi toimimaan uudella järjestelmällä logistisesti. Koska lopulliset päätökset firman toiminnasta Kiinassa ei olleet tutkimuksen aikana vielä selkeitä, niin lopputyö tarjoaa muutamia vaihtoehtoja näiden kohtien osalta.

Avainsanat: Kansainvälinen kauppa, Kiina, riskienhallinta, Company X, logistiikka

TERMS:

BREAK BULK-	Break producer's deliveries in smaller quantities for end customer.
CBM-	Cubic meter.
CONSOLIDATION-	Gather goods from producers and combine for end customers.
DC-	Distribution center.
EXPATRIATE- China	Person who is representing foreign operations in e.g. China
FCL-	Container which is packed full.
JIT-	Just In Time delivery, goods are delivered for sales on basis of need.
LCL-	Container which is not full.
LTL-	Less than truck load.
MOQ-	Minimum order quantity.
SKU-	Stock Keeping Units.
SUPPLY CHAIN-	Consists of the series of activities and organisations that materials move through on their journey from initial suppliers to final customers.
TL-	Truck load.

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## 1. INTRODUCTION

### 1.1 Objective

The purpose of this thesis is to be guidebook and an effective tool to anyone who desires to enter the Chinese markets. Due to the increasing volume of companies entering these markets, this guidebook gives a general view on the environment which they will be conducting business. These companies are facing huge obstacles such as legislation. Overcoming these problems is essential. There are also smaller issues companies have to face. These small differences can make a distinction between successes or disaster for ones business. The research is not focused on one specific field of business, therefore the study looks at various entry modes. Objective is that guidebook would give company some kind of idea which type of entrance should be looked into.

The case study in this thesis is focused on logistics. Its first objective is to benefit companies who already have entered the markets and are evaluating their supply chain methods. It also would be seen as useful tool to companies which don't have supply chain operating in China but the need for one is already determined to exist.

Objective of case side for case company is to determine the forecast of possible future changes in company's supply chain. This includes predicting possible expenses and savings. The company may use these findings for future planning and the execution of new ways of operation methods.

## 1.2 The Research Problem

The thesis will be used to find out what kind of basic information one has to acquire before entering the markets. Mapping out these problems and risks are the main focus. Also evaluation on the case company's operations and new implementations is important for this study. This is because it makes the thesis well rounded and more credible.

China can be seen as a difficult environment to conduct business. This is not only because of geographical distance from the west, but also cultural differences in the way of thinking. Finding out what these problems are and making recommendations on how to overcome them can be the most valuable information this thesis has to offer to its reader.

A logistical evaluation of China is found in this study. The goal was to find out which methods can make supply chain operations more effective for case company. Problem in this is many obstacles legislation and custom policies set for organizations. To find logistical zone where to operate in future for the case company is somewhat multilayered. Three definite conclusions on where new warehousing should be set is defined. The decision on this matter will come when Company X chooses their operation model and goals. Defining international goals will help solve this matter also.



### 1.3 Analytical tools

This thesis will look into the cultural, economical and political aspect of doing business in China. In these parts information gathered relies on literature and interviews. Interviews are constructed the way that most information could be received from experts of their own fields. Interviews with professionals of their own field work mostly as pin pointed information to complete this research. Literature on this topic played an important part in the analysis process. Before starting to thoroughly investigate the Chinese economy and business operations, it was important to have general view of China. The literature used spans from the Cultural Revolution to modern day China. This gave the researcher a clear view of the general environment and social atmosphere.

In the case study tools used where more concrete. Shipping logs, interactions with co-workers and interviews with consultants. The most valuable information in the case study was received from actual data of the case company's operations. This data was sorted then boiled down to learn most relevant information.

While living in Shanghai, the researcher's individual experience of the Chinese way of life and behavior had a major impact on this research's final form. One had possibility to view and experience surroundings in one of the busiest Asian marketing capitals. Almost five months of this kind of influence allowed for an immense amount of information to be obtained.

#### 1.4 Limitations

China as a whole has various different local legislations and regulations. Therefore this thesis will not be looking into the business, economics, logistics or culture for all of China, but rather just Shanghai. All information is implemental in Shanghai when conducting business. Some information is implemental in other areas of China but defining this is quite impossible in the time frame that this study was conducted.

The case study of Company X also faced some limitations. The company has defined goals for its new project. Still some valuable information was unavailable to make final conclusions possible. Decisions on how the company would operate in domestic markets in the future had not been made yet. Therefore the importance of European markets and future investments was not clear. Most data received from the company was exact, but there were parts where the researcher had to make some predictions on shipment information. This information concerned the Cubic meter (CBM) amounts in less than truck load (LTL) shipments. Error margin from this missing information can't be seen as a major concern when considering the full scale of shipment costs.

## 2. WHAT IS CHINA?

### 2.2 Chinas markets

First the thesis will go through some basic information about Chinese markets. This will help the reader to gain an overall view on the subject. There are some aspects of China which are important to know before getting started with any form of operation. The cultural aspect should not be underestimated, for this is the first place in which a westerner will hit wall.

### 2.3 Why go to China?

There are many different reasons why company should start their operations in China. There is also many ways from which they can choose how to do it. When a decision is made for a business to start operations in China there should be strong base for which the decision stands on. China is the place to make huge profits and amazing contracts, but it is also a place to go horribly wrong.

### 2.3 Economy

Economy in China is still booming. This has been the trend for the past 20 or so years. The current economical trend is still highly growth-oriented. For many branches of business it is too late to enter markets. This is important to understand when considering operations in China. China is not the newest baby boomer, it is not the most cost efficient country in the world, and the fact is that a company should have come here 10 years ago. When looking at these facts it might be wiser to consider

operations in India also. India is considered to have much the same kind of indications of growth China had 10 years ago.

Before making a decision to enter the Chinese, markets a company should map out the real buying power of its consumers in China. Many companies that enter the China have the false belief that there are endless markets. China has more than a billion citizens and because the economy is booming middle class should increase at a steady pace. But truthfully the real buying power in China or the people who actually can afford to buy commodities with western price tag is not billion. In fact it is not even a tenth of this figure. It is estimated that this group is close to the population of Canada. When this is realized we can ask “Is any one rushing to Canada?” This is a rough comparison, but it will help an eager expatriate to start mapping out the market.

#### 2.4 Division within the Country

To fully understand the economic surroundings it is important to be aware that China is economically divided between coastal area and inland. This division can be seen very clearly when a looking at foreign trade. Many look at China as a 1.3 billion persons as factory of the world. The truth is that on the coastal area is the factory of world, not all of China. The inland is still mainly focused on domestic markets. There are many growing areas inland, but there is no comparison to the coastal area on foreign trade’s percentage (figure 1.).

	1998	1999	2000	2001	2002	2003	2004
<b>Proportion</b>	%	%	%	%	%	%	%
Coastal	88.7	89.2	90.7	90.9	91.5	91.4	92.6
Inland	11.3	10.8	9.3	9.1	8.5	8.6	7.4

Figure 1. Areal prosentage on foreign exports. Source: China Customs, 1998–2004

## 2.5 Profit

The possibilities for enormous profit, is the reason for the mass exodus to China. Companies all over the world are entering these markets just to get a small slice of the cake shared in China. Companies have much better possibility to sell or buy goods here. For sellers if the product is right China is an ideal place. In many fields of business the demand in China is so high that it can be considered a sellers market. Especially in the case of selling raw materials or production machinery. Even though there are many sellers, demand is still exceeding the supply. Buyers face somewhat the same situation (unless you're trying to buy raw materials), there are many different suppliers from which to choose from. This market situation gives buyers the advantage when negotiating prices. Buyers have to also be very aware of the fact that prices might not be the only issue to look at, there is also the issue of quality. Companies in both cases, buying and selling, must be well aware of their partners (Tugny 2007.).

### 3. WHICH ENTRY MODE?

#### 3.1 Defining the Mode

The company has to map out what it requires from China. How China can serve organization to the fullest. One should still remember that the Chinese government and business partners will think, “How this foreign investor can benefit China”. These points are important when assessing each option for entry mode.

##### 3.1.1 Exporting

This entry mode is somewhat simple to get started. There is no need to look at joint venture partners or go through Chinese legislation to start a trading company or rep office. This entry mode is used by many companies within China. Some are using mixed exporting and direct investment in China. This comes from the fact that many companies still have direct investments in Hong Kong as sales offices and service centers. Naturally this is an entry mode mainly for corporations which are selling goods to China. There are no expenses on manufacturing and the support operations. Mainly costs will come from marketing. China as a special case should be considered to have a high need for good connections to government. There are examples when a company has had better connections to Chinese officials than its competitor and has used this to slow down the customs and other operations before their goods could enter the Chinese markets. If a company is operating in “just in time” basis, it can be very devastating for business.

This kind of entry mode could be recommended to companies who just got started in China. There are no huge investments at the beginning. It is said that if you are not willing to invest, don't bother to try when talked about China. This mode gives a company a stick to test how thick the ice is. Exporting is not only for small low capital companies who are getting started in China. There are some industries who

work with only exporting as an entry mode because of the legislation. Some industries are facing tariffs and other special requirements before they can operate as sole venture or joint venture. Chinese government has secured some fields of industry. Obviously everything related to the weapons industry is highly protected, but also more common ones like steel production.

### 3.1.2 Licensing

Licensing is a tricky entry mode to use for China. In licensing, a company sells counter party, the licensee a right to use their product design, technique or brand. So it is most commonly intangible assets. Return on investment (ROI) can be very high on these kinds of exchanges, because there is very low amount of investments involved. But for a longer period of time company can loose profits as potential returns in manufacturing and marketing.

This type of entry mode could land on the high risk end. One reason for this is the fact that in China contracting is not so strong. So even if a company has agreed on the use of a certain model or technique during some agreed period of time, this does not give full security to the licensor. Intellectual property is very wanted in China and it is also very badly secured. So giving your secrets for other parties to use here is high risk. Before doing such agreements one has to be very sure on the amount of trust he has for the licensee. This trust if founded to stand on good personal trust is ten times more valuable than any contract you can draft in China.

### 3.1.3 Joint Venture

Joint venture is very popular way to enter the Chinese markets. In joint venture foreign companies look for partner from China. In most cases the reason for this is either legislation or need of expertise on Chinese markets. Legislation means that some industries are not allowed to enter the market unless they work in joint venture

with a Chinese counterpart. Usually this also means that one counterpart will be the one with the decision making power with 51 percent of the share. Steel industry is one of these fields which government has shielded from sole venture investors. Many companies have managed to succeed with the share of intellectual property entry mode. They have gained more than a strong hold of markets and it has been very beneficial for the whole organization. Volkswagen must be the most famous company to use this type of entry in China. For European it is quite stunning to come this far from Germany and notice that the most common hood ornament is this combination on letters v and w. Everything is not so simple of course. They also used many brilliant tactics to secure their intellectual property. Most of VW models sold in China are more or less a lower technique level than its European sisters. It is also seen as beneficial for Chinese markets to sell less advanced machinery for transportation. There is no strong high-tech after management for cars in this country, so it's important that cars can be fixed in more common manor.

The joint venture entry mode faces some what the same problems as licensing. To be able to trust and operate with you partner is important. In smaller scale there are examples in which company starts joint venture with a Chinese counterparty, after intellectual property has been exchanged and techniques are mastered. Partners have then given this information to other companies operating across the street and the old joint venture has been driven down. In this way the Chinese party can get 100 percent of the operating profits. When taking in consideration trust issues, cultural issues and all other possible clashes between primary goals, having a joint venture can be very at least challenging as an entry mode.

#### 3.1.4 Direct Investment

This is the heaviest of all entry modes. Direct investment is the most committed way of entering the markets in China. Before choosing this mode, a company needs to be very clear on legislation, culture and connections. Organization also has to be prepared to invest high amounts of capital to achieve successful entry. It is very



important for companies to define the needs that a direct investment would fulfill. It is also important to assess other modes of entry, possibly even more advantageous. When all these facts are viewed in detail, a decision can be made.

This mode would be beneficial for a company which is looking into possibly entering the domestic Chinese markets as a major player. If a company needs many supporting activities for its operations such as distribution and warehousing, it is getting to the point of establishing its own trading company in China. This can add risk for your company. But when talking about China, it could be seen as a measure to lower risk. In China commitment is seen as a very positive thing for a company. When your organization is not only seen as a western company but also as a Chinese, it will give you more trust equaling less risk. Everything depends on how this entry is conducted. A company which has been operating at some level in China for a longer time always has a better chance of succeeding than a company which is trying to invest directly within a short time of presence.

## 4. COOPERATION ISSUES

### 4.1 Choosing Partner

Choosing a reliable partner in China is a much bigger challenge and an entirely different process than in Europe. Background information should be scouted thoroughly. This will give you some insurance on the reliability of your future partner. One should always remember that contracts and agreements are not 100 percent binding in China (Eriksen 14.09.2007).

### 4.2 Contracting

Chinese companies usually add terms to their contracts. These terms may give them the ability to exit a contract. A term could be: if nature of business change juristically, company has right to quit or renegotiate terms. This kind of term can be used in any kind of situation (Eriksen 14.09.2007) This fact should be taken in consideration when a company is doing its risk management assessments.

A solution for this volatile environment can be seen as a very caveman-like method of conducting business-you do business so long as it is beneficial for the Chinese counterparty. In China contracts don't make your business risk free. Best way to keep your business running smoothly is to be fair and respect your partner. This way the continuance of business relations has a much stronger platform. Normally in European business environment if one has the upper hand in negotiations they tend to push the other party against the wall. In China you should avoid this kind of behavior, profit you gain can be lost in other expenses (Company acts very dependently, which will rise your after management costs) (Tugny 05.09.2007)

Process of making a contract is also very elaborate in China. Many Chinese corporate negotiators have good knowledge of negotiation tactics. Like Boye Lafayette De Mente says in his book Chinese etiquette & ethics in business “The Chinese negotiation techniques has been likened to both guerilla warfare and psychological warfare-strike, retreat; strike, retreat; confuse the enemy, get them off guard, weaken their will, make them feel guilty for opposing you, make “final offer” that is considerably below what they know is acceptable.”(2004, 28)

As example story of Norwegian business negotiation in Shanghai. Negotiations trip was planed to last ten days. Chinese side took Norwegians to the nicest hotels and clubs, feeding them only the finest foods. After a week Norwegians started to get nervous because Chinese side had not made any effort to make any kind of negotiations on creating contract. Pressure built really high until finally the Chinese agreed to negotiate two hours before Norwegians had to leave country (Eriksen 14.09.2007)

Other famous strategy among Chinese is to try to delay contracting over the Christmas and New Year holidays. Chinese are aware of the fact that Europeans are eager to close deals before their holidays. If negotiations go to this kind of delay tactic, there is very little to be gained. European counter party should pack their back go home for holiday and continue negotiations at a later time. This tactics can also be reversed, Chinese are very eager to close before spring festival (Chinese New Year).

#### 4.3 Partnership

There are rules concerning doing business in China. Some areas of business require compulsory partnering. This usually means that when a company is manufacturing products in China they have to have a Chinese joint venture. This concerns some areas of business such as steel processing and other heavy industries. For these kinds of companies it is compulsory to have a partner which has 51 percent majority on

operation. This makes it almost impossible for some companies to come and do business in China. This regulation is levied for a couple of different reasons. One reason is that through these kinds of joint ventures Chinese companies can get their hands on other party's technology. Because they have majority on stock they are free to use this information as they please. Other reason is that China wants to profit on these mergers.

It is also possible to make special deals with the government. Honda was the first car manufacturer who managed to have a fully owned car factory in China. The contract with government included a term in which Honda was not to sell these cars on the Chinese markets. Every car should be exported and sold outside of China. This way China protects the markets of its own car industry (Fishman 2005, 212.).

All industries do not fall under this regulation of compulsory partnership. There are industries which can operate individually.

#### 4.4 Quality

This topic is challenging to many exporters in China. Quality control is very crucial in China. It is very important that one comes and checks the manufacturing of a product. After-inspection of products in China before exporting goods to destination country cuts risks down drastically. For example exporter of golf trolleys from China visits factories and demanded changes on defects on products he exports. Wheels tend to fall after while so he had this changed on design, electric switch tends to jam, so he had the factory change it (Attwood 10.10.2007)

When there is conversation about Chinese quality being inferior when compared to other nations it is not Chinas fault in all cases. Most commonly quality depends on the buyer. If the purchaser is not willing to pay for good quality they will not get it. It is also true that Chinese producers need more after-management concerning the

quality and keeping it on the same level. Sometimes quality can change. Because of this following your products quality at all times is very important. Chinese partners tend to have the reputation of being unpredictable.

## 5. LOGISTICS

### 5.1 Evaluating

After choosing a good forwarder with reliable rates and services, a company can start to look into making their supply chain as efficient as possible. It is also important to be aware of future efficiency even before the forwarder is chosen. It should be evaluated at all times that is there some parts of the procedure which can be improved. There are many changes in legislation and regulations at the China end so it is important to be aware what these changes are. There are also many special zones for companies exporting over seas from China. These should also be investigated before making a decision on which location to use for possible warehousing etc.

### 5.2 Cost Efficiency of Logistics

When cost efficiency is an issue, supply chain is right there next to it. The perfection of logistics is the most cost efficient and a very important process for all companies which are operating globally as well as domestically. When operations are small logistics is easier to handle. This is because a company can see cause and effect more clearly. When operations grow a need for special tools raise to see these causes. Tools vary from very complex six sigma, lean management to other simpler ones. If a company has no resources or know how to conduct these kinds of projects it could look at a supply chain or more down to earth procedures of assessment. Big board and post it notes set in order as a supply chain goes on can be a very useful way to notice choke points or wasteful resource use. So there are many areas where logistics can be improved. Also many different factors can have effect on logistics. Infrastructure of destination country has effect on logistics. Legislation can have major effects of logistics. Human resources also play an important part.

### 5.3 Logistics in Warehousing

Warehousing is an important part of logistics. When we think about logistics many times we fail to remember that storing of goods before they travel is a large part of what we know as logistics. Warehousing is very complicated, especially when it is designed to work in the fullest possible volume. Usually warehouses are receiving 75-85 percent efficiency rate when they can meet the needs of peak season. If a company is facing these kinds of high and low seasons it is unnecessary to have all of this space privately owned. In these kinds of industries it is advised that a company rents warehousing during these peak seasons. With this kind of warehousing model company can receive as high as 90 percent efficiency rate on warehousing (Waters 2003, 291.) Warehousing has many different factors and can be perfected almost endlessly. One planning to establish their own warehousing has to be very clear on all aspects of warehousing. All the way from location, facilities to people working there and conditions they need for their work environment.

12 step program from introduction to logistics. This is good way to get started when defining the warehousing needs.

1. analyse the logistics strategy – setting the context and finding what the warehouse has to achieve
2. examine current operations – to see the failings and how these can be overcome.
3. design an outline structure – finding the best main location, number of sub-depots, and so on
4. make detailed plans – finding the size of facilities, stock holdings, material handling equipment, systems to develop, people to employ, transport needs, and so on
5. get final approval – submitting the plans to senior managers to agree the funding
6. finalise building design – purchasing land, choosing contractors and building

7. finalise equipment design – choosing equipment, suppliers and purchasing
8. finalise systems design – designing the ordering, inventory control, billing, goods location, monitoring, and all other systems needed
9. fit out – installing all equipment, systems, staff and testing
10. open and receive stock – to test all systems, finish training and begin operations
11. sort out teething problems – to get things running smoothly
12. monitor and control – ensuring that everything works as planned, measuring performance, revising incentive schemes, and so on.

#### 5.4 Logistics in China

Logistics is facing some special features when operating in China. When making assessments of possible costs and risks it is very different from Europe or the USA. Infrastructure in China is not as good as in these western areas. On railroads choosing double deck transportation as used in the USA is impossible because China is very mountainous country. Water transports can't be used as efficiently as in Europe, rare rivers in China could be considered as navigational with barges. That's why highways have become the backbone of Chinese transportation. This can cause delays on shipments or other kinds of problems like damaged goods etc. When this is added to the fact of poor condition of transportation vehicles, out come is not positive. China has realized this as problem which is slowing down the growth of the economy. On 2004 China invested 728.3 billion Yuan on infrastructure (at current exchange rate it would be approximately 80 billion euros). From this investment 80 percent was directed to transportation (see figure 2.). This was a 24 percent increase from the previous year. Mostly this money was invested on highways, deep-water berths and civilian airports (Waters 2007, 393.)



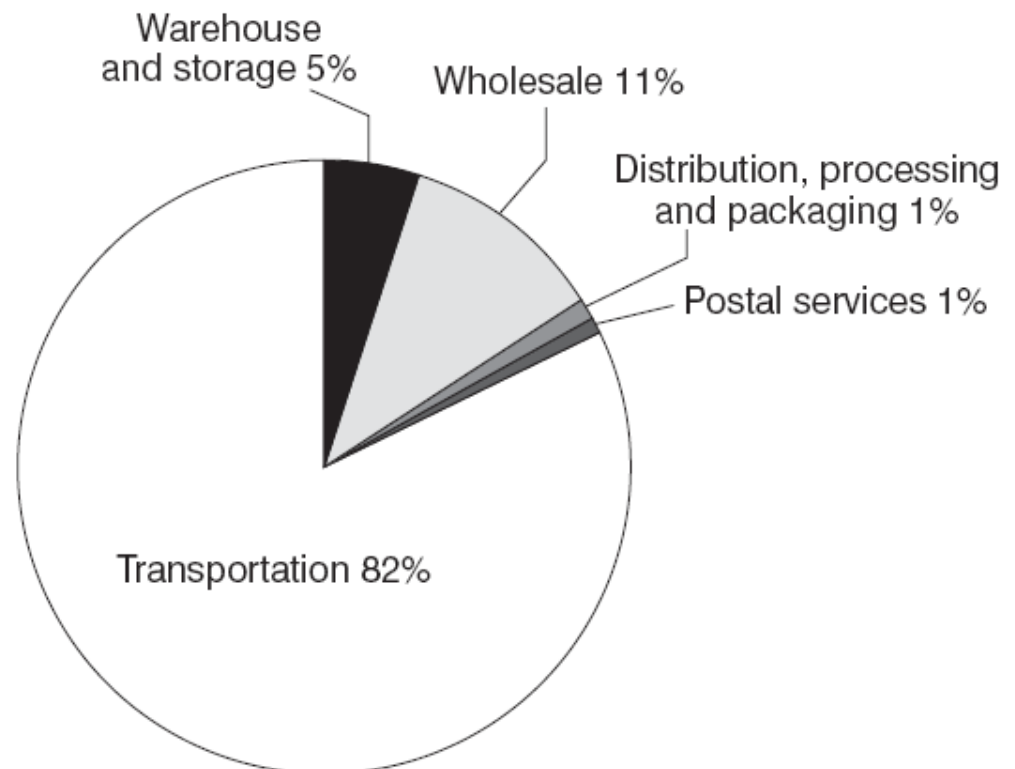


Figure 2. Source: Li & Fung Centre for Supply Chain Management and Logistics, Chinese University of Hong Kong, 2004

### 5.5 Export Procedure Example

This is one example of possible export procedure. This example can be applied when a company is operating on a basic level and is not exporting any special items, such as hazardous materials or goods which are specially regulated in Chinese legislation.

1. What kind of status I need to be able to do this?

To be able to take container loads of goods to Europe there is three ways. One can operate as company in Finland who does imports. This means that one brings goods to Finland under their company's flag.

Second way is to get export license in China. After one has this document one can sell goods to third party companies in Europe.

Third is to use some local third party's export license. Forwarders and some factories usually have these rights.

Ideal situation is when a company has bought an export and import license. This gives a company the freedom to move and be more flexible with its imports (Attwood 10.10.2007)

2. As a customer you have a container of goods which need to be exported to your destination country. Where do one start?

First one should compare forwarders. Using a forwarder is simple and safe way to make international movement of goods. It is also a good idea to negotiate with the producer in China. In many cases they offer door to port services. This usually is considerably cheaper than Finnish forwarder for example. This kind of service is possible because these producers have an export license. If the producer doesn't offer this, they are usually willing to help you find good Chinese forwarder. Chinese forwarders are generally cheaper than Europeans (Attwood 10.10.2007)

3. Forwarder selected. What documents I need for customs?

Bill Of Lading (BOL) is most important. This document contains what one is exporting these documents has to be signed by company buying and producer of sold goods. This is important for customs. One cannot put anything in the container other than mentioned on the BOL.

There are also other documents which must be given. Such as fuel surge charge. This is for situations when fuel price is volatile. In practice you pay the gasoline of these massive container ships (Attwood 10.10.2007)

#### 4. After goods leave China?

After all papers and customs are cleared. There is not much other to do than wait. Depending on ones method of transportation, how long it takes to receive your goods. Most common transportation method is via container in ship. When exporting to Finland it takes between 6-7 weeks. When posting it takes about two weeks for goods to arrive. There are also some services (under the table) which offer you cheaper ways to post with in five days to Europe. Usually knowledge of these kinds of measures are found from your Chinese counter party you're doing business with. Postage and shipping durations are important to take in consideration when doing business. This also slows your possibilities to make profit from China (if using slowest methods of shipment).

#### 5.6 Special Zones in China

There are many different kinds of special zones for warehousing in China. Some of these special zones are located near harbors. There are various different rules and regulations under each type. So a company should look into what zone offers best advantages for their needs. Sometimes location on some area is perfect but regulations are not what company is looking for. In this case it is good to make list of pros and cons on which is more advantageous.

	Export Processing Zone	Free Trade Zone	Bonded Logistics Zone
Scope	Bonded manufacturing	Bonded manufacturing, International trading, Warehousing, Distribution, Bonded commodity exhibition, Simple processing	International trading, Warehousing, Distribution, Bonded commodity exhibition
Inbound Equipment	No import duty/VAT or import license for self-use inbound equipment	Same as EPZ	Same as EPZ
Inbound Cargo	No import duty/VAT or import license for inbound material	No import duty/VAT or import license for inbound cargo	Same as FTZ
Domestic Sale	Import duty/VAT, import license & approval by EPZ Administrative are required	Import duty/VAT & import license are required	Same as FTZ
Export Tax Rebate	Tax rebate upon cargo entry into the zone	Tax rebate after cargo exported to overseas	Same as EPZ
Limitation	No Logistics Company is allowed in the zone	Tax rebate is not available upon cargo entry into the zone	No Manufacturing Enterprise is allowed in the zone

Figure 3. Chart above shows differences between logistics zones (UTS 2007.).

As shown in the chart we can see that there are various advantages. When a company starts to look into these differences there are some limitations which obviously take some zones out of consideration because they are only allowed for certain company types. Like Bonded Logistic Zone doesn't allow any manufacturing enterprise in their premises. Tax rebate is one important issue also. When a company operates in this kind of area they will receive their tax return after the goods enter the zone. If a rebate is given after the goods leave country it can delay receiving these funds for many months. For example if goods are brought to an area and stored there for month and then all export procedures added as time before goods leave country can delay on the tax rebate be as much as three months. This of course means that these funds can't be re invested during that time.

## 6. CULTURE AND LEGISLATION

### 6.1 Cultural Aspects

Skills one gains in European business can not be directly implemental in China. The basic mentality of business is totally different. There are hundreds of things that should take in to consideration, from very simple things like asking possible production figures and being able to see that the Chinese counter party is sure about this statement. This fact doesn't mean that the Chinese lie or try to look better than they are. This comes from two facts. First is that the Chinese are very eager to try even if they know in the back of their heads that filling a certain order is virtually impossible for their capacity to produce. If a European is to ask some over the top amount Chinese tend to tone it down by only partly agreeing. This fact comes from thinking of losing face "liang". The Chinese party doesn't want to seem unable and they also want to save their European counterparty's face for asking something totally impossible.

Second aspect of interpretative communicating with Chinese comes from age long tradition and culture. Irene Park, an American cross-cultural communications expert with several years of experience in China, says that Chinese is not built to communicate on specific information. Chinese is more on expressing feelings, emotions and polite escapes. It is said that eight percent of Chinese is polite escapes. For example if you are to ask Chinese is this white or black you may receive an answer: well it is not very gray. The affects of this communication follow and are divided to two distinct segments that Europeans are bound to face when doing business in China.

#### 6.1.1 Public Officials

Some times when operating with Chinese government you can hit a wall of communication. In some cases it seems very slow and just too complicated. Behind

this is the same culture of communicating. Many times European don't know the right questions or procedures, this is of course a responsibility of one doing business. Another factor is the culture of avoiding responsibility. Forms travel slowly to the top of the organization structure. When the form reaches the top it travels down same way it came up. When this process is viewed by European it seems like a very ineffective way to operate. This moment we have to remember that there are serious consequences if a mistake is made. Frustration and getting angry is the last thing one should do, this will only slow the chain of command. When this is understood operating in China gets lot easier.

#### 6.1.2 Private Business

This is an environment where every business person in China is bound to meet polite escapes. For example if something is said to be inconvenient it probably means impossible. Answer to question might be yes, as in-yes I understand the question. It takes lot of time to beginning to understand the real meaning behind the words. It is advised that during the early stages of a relationship language used in presentations should be kept frank and direct so as to avoid any misunderstandings. One goal of using vague language is so as to not bind yourself to anything. The same can be used in Chinese contracting.

## 6.2 Chinese Legislation

This part will be a problem for many companies who operate in China. Not only does it change very rapidly but to know the legislation which is applied currently. The USA department of commerce performs sourcing and information services for American companies in China. When a researcher asked the department how you find out which legislation to follow, the answer was somewhat surprising. We have information about legislation but in most cases we have to refer the company to the Chinese government. So if governmental organization of this magnitude doesn't have the answers how are the small companies expected to find them. This is the challenge when operating in China. Lean SCS is American exports specialist in China, with wide knowledge of local legislation and procedures. Even they face situations of realization that some parts of business can be made more cost effective. When asked about one case concerning VAT refunds they had realized that an easier way to do it has been available for two years. Full gain on efficiency can take years of experience and operations. Taxation is one tricky part in China. When a company is finding about tax procedure about their industry it is many times referred to go directly to local tax office. When this assessment is received company has some idea on tax issues, by some I mean that company could go to other local office and receive a different answer. When asked from both which one is correct one might be facing a situation where both insist that their answer to the problem is the correct one. This gives some idea of the environment and legislations in China.

### 6.3 Changes in Legislation Concerning Operation as Logistics Company

When operating in China as a logistics organization it is important to be aware of the changing platform of legislation. To help understand this, it is good to have brief look in to the past. After joining the WTO the legislation and its changes has slowed down. On post WTO accessions huge changes have been made between 2002-2007. Here are some major ones...

2002- Minority ownership on joint ventures, road, warehousing, courier.

2003- Most of these fields received right to be majority owners.

2004- Majority ownership on rail transport.

2005- Wholly owned subsidiaries for road transportation and warehousing.

2006- Shipping fully owned and no limitations of foreign companies. Courier business fully owned.

2007- Rail transport fully owned subsidiaries.

The logistics industry is opening up more and more for foreign companies. China has no other choice than make regulations more attractive for foreign investors. Chinese economy is dependent on these investments. If one should make its own prediction of the future it could be said that China will keep opening at fast rate for at least next ten years. When China reaches this point we would not be talking about opening its borders any more. Are we saying for example that Germany is opening its borders for foreign business?



## 8. CASE COMPANY COMPANY X LTD

### 8.1 Company Overview

Company X is United States largest, privately held, mail-order pet supply distributor catering to pet care professionals. Company X provides the most comprehensive selection of over 12,000 pet care products to groomers, breeders, kennels, veterinarians, pet shops and people who show dogs.

Company X has operations globally. Currently company is selling their products mainly in USA. Company sells also products in Japan and Korea. Europe is becoming increasingly important for the organization. New interest can be seen as new presence in European dog shows as a tool of marketing.

Additionally, a Company X Representative office was set up in Shanghai, China in March 2006. This office facilitates the sourcing and logistics of overseas products.

#### Current facilities and locations

Administrative offices are located at the Cummings Office Center in Beverly, MA. This office includes a state-of-the art Customer Contact Center. The company's 84,000 square foot warehouse and automated distribution center is located twenty miles south in Boston, MA. A second warehouse is located in Reno, NV. All merchandise is received, stocked, packaged and shipped to customers throughout the world from the warehouse located closest to their facility.

### 8.3 Company X Project General

Company X's rep office in Shanghai China, is working in fields such as sourcing, control of exports, follow up with suppliers etc. Company X is looking into cost effectiveness of their logistics and internal operations in Shanghai. One area of this is to find means to decrease unnecessary transporting/improve efficiency. In this perspective it should be researched which is the most efficient way to deliver goods to United States. Movement of goods from China are divided between East coast warehouse and West coast warehouse. There is also research of setting up a warehouse in China, and where this warehouse should be located. How this is going to affect to supply chain, and is there logistically new possibilities after the new warehouse is in operation (just in time delivery in USA).

### 8.4 Structure of the Project

The project is divided into four different main areas. The researcher's task was to go over each of these parts and present results to Company X. In this thesis I will represent each area of research as an individual part. Firstly determining the project and goal. Secondly I go through the research, explaining how it was conducted and what kind of tools were used in it. Thirdly I will represent results and recommendations based on my research. There is also one main factor which is the most important part of this research. This factor is Company X's plan to have future warehousing in China. This factor has great impact to all four different areas of the project. Before going over these four different areas I will explain this information in general.

## 10. COMPANY X SUPPLY CHAIN

### 10.1 Analyzing Supply Chains

As explained in previous paragraph there would be quite an immense change in supply chain. Here is a represented current model and new model in comparison. First is global supply chain.

Shanghai rep office does not have any status as a trading company thus it can't sell to other countries. This means that goods have to travel all the way to the USA before they can be sold to other destinations. When goods can be directly sold from Shanghai to other destinations goods will travel less and this will cut expenses on shipping (figure 4).

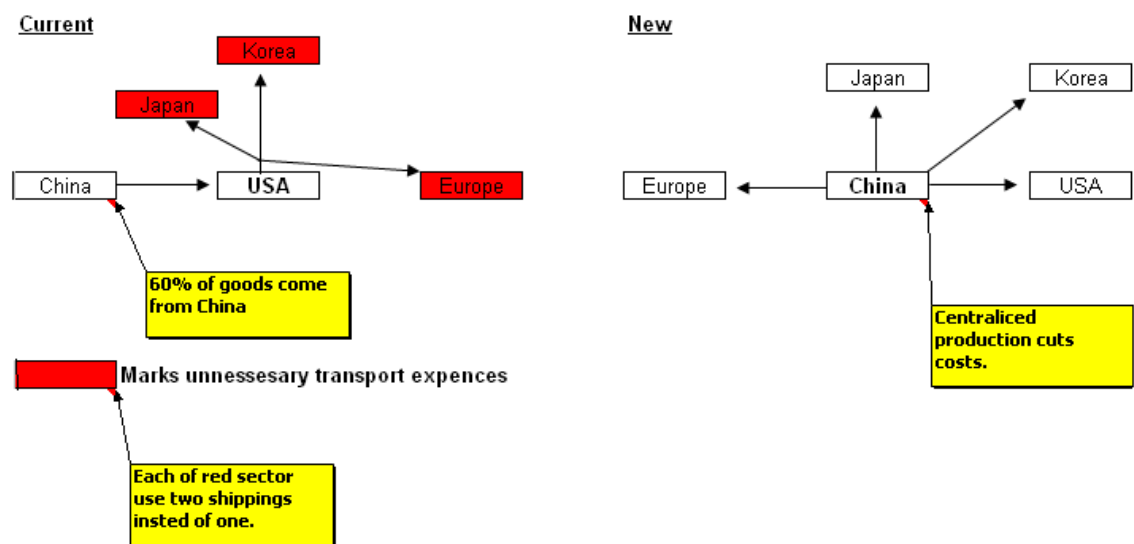


Figure 4. Global supply chain.

Secondly we go through supply chain from producer to end customer. The biggest changes in producer to end customer supply chain can be seen in the second part of the chain. This part is the new warehouse in China. When in operation it would mean that Company X would be able to store goods and feed them to the USA on a basis of the needs of the markets. Forwarder would still do the booking of vessels for Company X. The next biggest change in the supply chain would be the loss of the forwarder DC at the US end. Goods would be already packed in a way that they would be more or less ready to go to Company X DC or directly to the customer (figure 5).

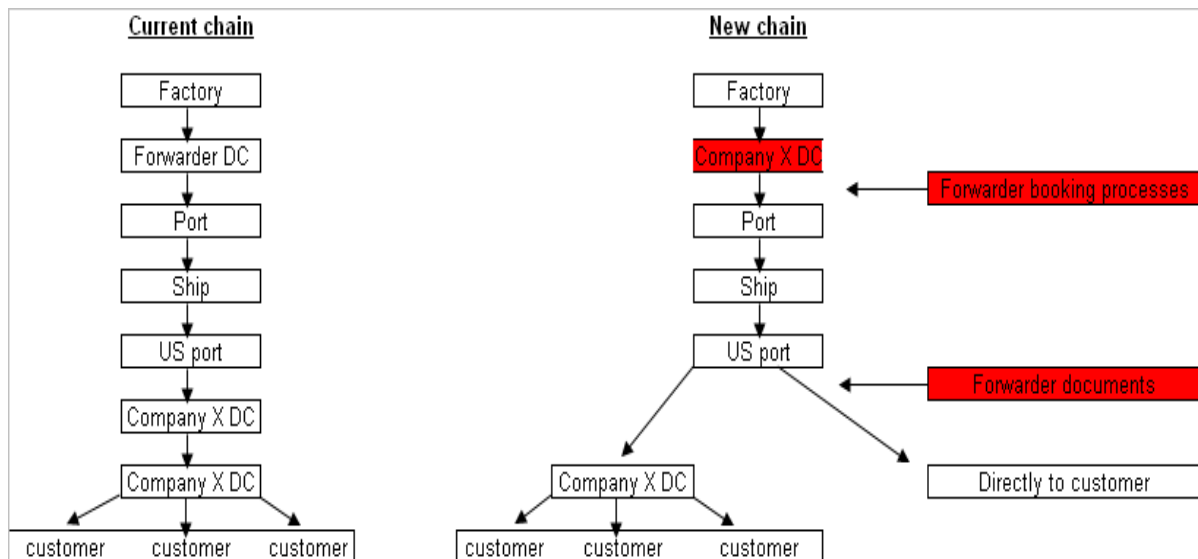


Figure 5. From producer to end customer chain.

## 10.2 Advantages on Having a Warehouse in China:

Company X Shanghai office is planning to change their company's status in China. At the moment the Shanghai office is not able to sell directly to other locations because of the representation office status. Company X sends produced goods to

USA, Oakland and Boston ports from where goods continue to local warehouses and finally to the end customer.

When Shanghai office gains status as a sales office, they would be able to sell directly from China to all over world. This would change supply chain drastically. Savings in time and cost would give big possibilities to penetrate European markets more efficiently. Also Japan and Korea would be closer when USA loop on transportation would be unnecessary.

When Company X has a warehouse in China a new export system could be implemented. At the moment China produced goods are delivered directly to USA. When the new warehouse is operational it is possible to feed USA warehouses the amount they need weekly. This would reduce the need of warehouse space in America. Warehousing would be more cost efficient to make at the China end, thus warehousing and staff in China would be less expensive. The trend in China is currently to have warehousing closer to suppliers (Timothy S. Chang). When company has possibilities to warehouse goods in China the possibilities on minimum order quantity (MOQ) rise. The company could concentrate more on what goods are needed rather than what kind of shipments they have to fill up to be cost efficient on shipping commodities.

The warehouse would also increase the amount of 40ft containers. There would be no need to send so many 20ft shipments any more. The price difference between 40ft and 20ft is quite small. When this is added to the fact of having double on added cargo space, savings would be evident.

LCL and FCL loading are used in containers in current system. Future own facilities would allow the decrease of LCL which is more expensive.

## 11. THE PROJECT

### 11.1 Step 1 New Supply Chain Affect on Suppliers

Step ones goal is to save expenses from freight forwarder. These expenses come from specific services which could be reduced when new supply chain would be in effect. Currently the company's forwarder, either stuffs producer's containers from many different factories or sends containers to a producer to be filled at the factory facilities. When the new warehouse is in place Company X would be doing the stuffing of containers independently. Reduction in cost would come from two separate factors lowering the cost of documentation fees and stuffing fees. In this part it is calculated what the saving would be.

Calculations in this part are based on shipping logs provided by Company X. Logs contain period between 04.07-23.12.2007. Main idea is that the LCL is taken away from new model. This drops down the documentation fees. Secondly 20ft and LCL which are 20ft are all converted to 40ft. This cuts down stuffing fees and documentation fees. At current system LCL containers can contain four different documentations, which make the payments on the documents four times more expensive than FCL.

<b>FCL</b>	<b>20</b>	<b>40</b>	<b>40HQ</b>
Documentation fee	\$17.00	\$17.00	\$17.00
stuffing fee	\$125.00	\$165.00	\$180.00

*Figure 6. Costs for the supplier*

Stuffing fee on LCL is based on CBM amount. This information was not available in this research. Stuffing fee is estimated on basis of 20ft stuffing fee (125\$). LCL stuffing fee per CBM is 8.5\$. Documentation fee for 20ft is 68\$.

On documentations company could save some resources. This \$1000 saving would come from the fact that there would be no need to pay for any different documentation. There would only be a need for one payment (figure 7).

<b>Current document fees</b>	<b>LCL</b>	<b>20</b>	<b>40</b>	<b>40HQ</b>
Documentation fee in				
total	\$1,590.00	\$342.00	\$2,554.00	\$1,784.00
New fees	\$417.00	same	same	same

*Figure 7. Decrease of cost in LCL documentations.*

There is no need for LCL and 20ft in new system they show 0\$. Increase on cost of 40ft comes from the LCL and 20ft which were changed to 40ft (figure 8).

<b>Stuffing fees for all</b>					
<b>types</b>	<b>LCL</b>	<b>20</b>	<b>40</b>	<b>40HQ</b>	<b>Total</b>
Current costs	\$2,901.00	\$2,394.00	\$24,310.00	\$18,736.00	\$48,341.00
New costs	\$0.00	\$0.00	\$25,945.50	\$18,736.00	\$44,681.50
Save					\$3,659.50

*Figure 8. Savings on stuffing fees.*

Finally the savings from documentations and stuffing fees is not huge. But this was also discovered during research that there is some resources saved in new system. These savings would amount to 1,210.50\$ on documentations, 3,659.50 on stuffing fees and as total end up to 4,870.00\$.

## 11.2 Step 2 New Warehousing in China

This part is focused on defining which type of warehousing is best for Company X. In this part the company is presented more than one option to choose from. The final decision on where warehousing should be is made by Company X after the company has clearly defined what their future goals concerning Chinese markets are.

Research is based on information about locations of Company Xs suppliers, regulations in various special zones, costs and possible changes in infrastructure around Shanghai. Suppliers are mainly based around Shanghai, which sets the location of potential warehousing as close as possible to these factories. Regulations can restrict business some what. When looking at special logistic zones such as export processing zone, free trade zone and bonded logistic zone all these zones have their own regulations which are to be followed at all times when warehousing is operated there. Regulations are very important if warehousing is located to mainland



China within Chinese custom borders, in this case Chinese legislation is more involved. There is also always possibility for hiring a third party to do warehousing for the company. This is also one choice a company can consider. Mainly we focus on BLZ and Free trade zones.

#### 11.2.1 Bonded Logistic Zone Wai Gao Qiao

Bonded logistic zone is a special zone with its own rules and regulations. For Company X this zone seems to be most appealing at the moment. From many restrictions and regulations there are no problems for Company X because it is not manufacturing company and is taking goods out of China. Location is in old harbor which is currently doing USA shipping. Location is also ideal because most of Company Xs producers are close to Shanghai where this zone is located. The most important regulation in BZL for Company X is VAT refund. When goods enter BLZ, VAT application can be levied more or less immediately. In other zones or in non special zones companies have to wait for a VAT refund until goods leave the country. This is problem for Company X as they don't want to wait for a refund. This concern is based on the fact that this refund can't be re invested during the waiting period.

Here is the definition of BLZ from Established United Logistics Group “There are many advantages provided in the BLZ. In the past, companies were required to ship all the goods to Hong Kong to complete the export process to receive value-added tax (VAT) rebate. However, this adds unnecessary logistics cost and lead time. Today VAT rebates can be applied directly at the BLZs. In addition, all goods within the BLZs are considered to be off-shore, thus they can be parted and regrouped, then shipped to different destinations. They can also be stored free of duty without time limitation. As a result companies can now have shipments containing mixed products to satisfy the customer requirements, specifically the delivery date and product mix (Established United Logistics Group, 2005.)”

Even though this is currently the most appealing choice for Company X, it does contain many fallbacks. The company's future plans to grow in Europe are in conflict with choosing this zone. All cargo sent to Europe goes through the new harbor,

Yangshan international deep water port. BLZ in Shanghai is located in the old port which does not handle European cargo. There are also estimates that the USA's exports will be taken to new port with in some time period. If this scenario comes true Company X would have warehousing on wrong side of the city, which would increase expenses when moving goods to new port. Roads from Wai Goa Qiao to Yangshan are not direct. The city center would have to be avoided and because of this the distance between the ports would be increased (figure 11).



Figure 9. The distances within Shanghai.

### 11.2.2 Free Port Yangshen

This port and warehousing area is the second of our main focuses when considering possible location for establishing warehousing. This port has many advantages when comparing it to the older port. Like mentioned above it handles lots of European traffic. If a company is going to grow to become major player in the European market it is very important that it takes this fact into consideration. Currently when volumes to Europe are not so high this fact would not be seen as major problem. Even a more striking advantage for this port is its future plans for taking over USA shipping. This could be seen as major change for current operations. Even if Shanghai would handle shipments to Korea and Japan from China the volumes to USA would still be almost 100 percent. If warehousing is in old port it would mean that almost every container should be transported to new port for shipping out of country.

Yangshen seems to be quite an ideal choice for Company X. But it has one major flaw. This zone doesn't offer VAT rebate application possibility when goods enter the zone. VAT would be received when goods leave the country. This period of time can be as long as three months in the longest cases when goods stay in storage.

### 11.2.3 Warehouse in Non Special Zone

There is also a third possibility on warehousing. Third possibility is to have warehousing in China territory, meaning that warehousing would face common Chinese laws when operating. This way the VAT would be received in accordance of Chinese government. This way Company X would have better possibilities to develop their Chinese markets. Domestic sales would somewhat require warehousing on a mainland area. Having warehousing in special zones would mean more traffic through customs which is time consuming and non cost effective. Establishing warehousing in a non special zone would also be cheaper for the company. When location of a warehouse could be freely chosen, it could be located close to future employees. Special zones are located some what out side of the residential areas. So it would be required that employees should be transported there from city central. Cost on warehousing space is also cheaper in non special zone than at these locations.

### 11.3 VAT Analysis

Because VAT seems to be a huge issue to Company X, it was necessary to analyze this part in detail. Head office has a good reason for being worried about VAT, and receiving it as fast as possible. When this tax return is sitting in governmental processing it means that there is more possibility to lose it. Governments change regulations all the time. VAT is facing these changes constantly. The Chinese government regulates their foreign trade volume with the help of tax rate adjustments. When a commodity is rendered surplus the government will increase tax on it. This is a very common protectionism procedure. This is the reason companies don't want to wait too long for VAT returns. If regulations are changed during this period, when application for rebate is in the tax department, it is possible that VAT is not received in full. For example if some commodity for exporting is receiving seven percent tax return, and then the government changes their procedure to five percent or even zero percent the company will have to deal with losses. In practice, when considering these special zones it would mean as follows. A BLZ company could submit an application for a VAT return straight away when goods flow in the zone. After this the new trading company would have to wait approximately three months before its return is received (new company mentioned because companies which has operated over year can receive returns in one or two months). Risk period for losing the VAT would be only three months and later on one month. Normal VAT areas like some special zones and mainland non special facilities would face different procedures. In Chinese VAT law it is stated that VAT returns can't be received until goods are exported out from China. So shipping would be the same as entering a zone in BLZ. In this case we would be looking at a VAT return on the basis of warehouse turnover. If the company turns six times goods would sit in the warehouse for two months before being shipped out of country. When these two months are added to the governments handling period it would total five months before receiving VAT during the first year and three to four months thereafter. This part can be seen as leverage to the BLZs benefit when choosing a final location of warehouse. Only after all these factors are weighted we can see the final form of efficient warehousing in China.

### 11.4 Step 3 New Supply Chain Affect on Shipping

In this part the goal of project is to reduce the costs of shipping. The main saving would come from shipping due to reduction of small containers and possibilities to send more containers to west coast instead of east coast which is more expensive. When the new supply chain with the new warehouse in China is operational it would give the company possibilities to send more goods to west coast warehouse which is smaller than east coast. But because of its own facilities in China Company X could implement just in time delivery more efficiently and thus saving warehousing space. This would also reduce the need of warehousing in east. In this part it is explained what was done to make these estimates on savings in shipping. Estimates are based on five month shipping logs from 04.07.2007 -23.12.2007. These five months are a good example to make an estimate which is close to a whole years shipping, as it includes high and low season.

To make an estimate on the future cost on shipping after collecting data on exact amounts from containers and what type of containers are shipped. It was simple to make a calculation on the Shanghai office manager's direction. When the new warehouse is operational there would be no need for sending LCL containers or 20ft containers at all.

Sending 20ft containers is a huge waste of resources. When each container is changed to 40ft the number of 20ft containers will half and the cost of 40ft in comparison is very small. There are a couple of types of products which would be still sent using a 20ft in future because it may be mandatory to have these goods packed in one container which don't have any other products (figure 12).

	<b>20ft Reno</b>	<b>20ft Boston</b>
<b>Average Cost</b>	\$1,637.50	\$3000.00
delivery	\$650.00	\$295.00
total	\$2,287.50	\$3295.00
	<b>40ft Reno</b>	<b>40ft Boston</b>
<b>Average Cost</b>	\$2058.75	\$3736.25
delivery	\$650.00	\$295.00
total	\$2708.75	\$4031.25
	<b>40ft HQ Reno</b>	<b>40ft HQ Boston</b>
<b>Average Cost</b>	\$2313.75	\$4025.00
delivery	\$650.00	\$295.00
total	\$2963.75	\$4320.00

*Figure 12. Price chart of containers.*

After the new warehouse the shipping would also change on the destination basis. In this case it was calculated that the east coast warehouse and west coast warehouse would take each others status in warehousing. This would mean that the shipping to west would increase and visa versa. The estimate was calculated on the basis that amounts to warehouses would stay consistent, and they would just go the other way around. With these new shipping destinations in effect there would be an immense decrease on shipping costs. Also a lot of time would be saved, because shipping to west coast is a lot faster than the east (figure 13).

<b>Between 25.06-23.12.2007</b>			
<b>Reno current shipments</b>			
<b>FCL</b>			<b>LCL</b>
			(calculated with 20ft cost)
20ft	40ft	40ft hq	
\$43,462.50	\$148,981.25	\$47,420.00	\$59,475.00

<b>Boston current shipments</b>			
<b>FCL</b>			<b>LCL</b>
			(calculated with 20ft cost)
20ft	40ft	40ft hq	
\$62,605.00	\$592,593.75	\$449,280.00	\$75,785.00

<b>If container volume of Reno would take Boston place as 60% of shipments</b>			
<b>FCL</b>			<b>LCL</b>
			(calculated with 20ft cost)
20ft	40ft	40ft hq	
\$43,462.50	\$398,186.25	\$308,230.00	\$52,612.50

<b>If container volume of Boston would decrease to 30%</b>			
<b>FCL</b>			<b>LCL</b>
			(calculated with 20ft cost)
20ft	40ft	40ft hq	
\$62,605.00	\$221,718.75	\$69,120.00	\$85,670.00

<b>Decrease in shipment cost after change</b>				
	20ft	40ft	40ft hq	LCL
Current	\$106,067.50	\$741,575.00	\$496,700.00	\$135,260.00
New	\$106,067.50	\$619,905.00	\$377,350.00	\$138,282.50
Change	\$0.00	-\$121,670.00	-\$119,350.00	\$3,022.50
Total savings	-\$237,997.50			

Figure 13. Shipment savings calculations.

After all this data was set in a spreadsheet format it was quite simple to see differences on costs. The amount of saving is quite noticeable (figure 14). As recommendation to Company X I would see it very important to look into these possibilities which would come available after implementing this new supply chain structure. When looking at the shipping part of the change it is very clear that there are many resources wasted currently. When taking in consideration that this estimate was based only on five months, it should be taken even more seriously in consideration to make these changes as fast as possible.

<b>Best case scenario</b>	
	-
Shipments mainly to Reno	\$237,997.50
20ft would decrease 75%	-\$30,975.00
Decrease on LCL	-\$34,784.00
	-
<b>Total save</b>	<b>\$303,756.50</b>

*Figure 14. Total savings on shipments.*

#### 11.5 Step 4 Effects on Warehousing in the USA

Currently the company is using two main warehouses in the USA. One on the west coast (Reno) and the company's main warehouse is on the east coast (Boston.) At this moment the division within USA is that 2/3 of deliveries are made from east coast. In full scale this also means that east coast has 2/3 geographically of the country under its delivery responsibility. In this part the main focus is on recommendations concerning Boston facility. This part will work as referent for Company X. Within the time line of this project it was not possible to make exact calculations on expenses and evaluate all risks involved.

Goal of future operations would be that Boston would downsize from its current warehouse. When warehousing would be operational in China, sq feet used in Boston



could be moved closer to the producers. This would decrease expenses in warehousing in the USA. In comparison these same sq feet can be purchased cheaper in China. Reno warehousing does not need additional sq feet space even though the goal would be to shift the warehousing from 1/3 to 2/3. This would be achieved by increased deliveries directly to customers and the just in time delivery system. Reno could pull more efficiently goods from the China warehouse in future.

### 11.5.1 Statistics of Boston Warehouse

Here are some basic features of Company Xs other warehouse. This warehouse is located in east coast of USA. This warehouse is Company Xs main warehouse currently. It is also company's main warehouse.

- 7500 active skus
- 12000 total skus in warehouse
- 29,600 sq meters with 32' ceilings, racked
- Additional space of 36,600 sq feet
- Slowest selling merchandise is stocked farthest from the conveyer
- Products that are heavy are stocked close to the conveyer
- All products are stocked in a bin based on the speed (velocity) at which it sells
- Move goods in the warehouse when the status is changed. R1 to C1, etc
- Boston ships approximately 70% of the company's orders and Reno 30% so you can see why the MOQ for Reno is an issue!

(Company X, 2008)

### 11.6 Company X SWOT

Here we see Company X in strengths weaknesses opportunities and threats analysis. This analysis is good way to look in to company's core competence and operations. Company X has all this areas covered in this analysis. It has good strengths and opportunities but it also is facing some threats and weaknesses (figure 15).

<p><u>Strengths</u></p> <ul style="list-style-type: none"> <li>Strong financial background</li> <li>Long history on operating</li> <li>Presence in Asia</li> <li>Skilled employees</li> </ul>	<p><u>Weaknesses</u></p> <ul style="list-style-type: none"> <li>America centered home office</li> <li>Problems in basic office infrastructure</li> <li>Management structure in Shanghai office</li> </ul>
<p><u>Opportunities</u></p> <ul style="list-style-type: none"> <li>European markets</li> <li>Supply chain configurations</li> <li>Warehousing in China</li> <li>Asian markets</li> </ul>	<p><u>Threats</u></p> <ul style="list-style-type: none"> <li>Failures in new supply chain implementations</li> <li>Vendors finding out end customers</li> <li>Loss of position in US markets</li> </ul>

*Figure 15. SWOT analysis.*

The size of the company is huge, this gives it financial leverage that can be considered as a good strength in the market. Finances give the company more possibilities on research and development (RD) and human resource management (HRM). Marketing is also an important side of operations and for doing it the organization needs vast amounts of movable finances. A long history also gives

company strength. New partners can rely on a company which has a long and reliable track record in the past. Experience also gives stability to a company's business. The company has an established representation office in Shanghai. This gives the company strength in many ways. The company has possibilities to source new products from China and offer them at low prices in domestic markets abroad. Asia is also a market which is growing very fast. Being here now is better than later. This fact also gives companies a competitive advantage to its competitors who are not so well established in China. Staff of Company X are well aware on their tasks (Shanghai office, other staff unknown to researcher). In the Shanghai office Company X has hired mainly Chinese natives. This gives operations a strong foothold because many producers don't have such a strong command of English.

As a weakness, American based home office means that the view on operations and decisions are focused on US markets solely. Main office should concentrate more on possibilities outside of the US and also look into new methods and ways of doing business. If this is not noticed it might even change to a threat. There are some signs in the air that awareness is growing and this will definitely be healthy for the business.

Problems with the Shanghai office internet connection is marked as weakness because organization of this magnitude should not have these kinds of problems. Sometimes employees have problems using the internet or internet based software. Sending e-mails is impossible while the connection is down. All this time wasted costs company resources X amount.

Weaknesses can also be seen in the Shanghai rep offices organizational structure. There are three main areas of operations in Shanghai, office merchandising, order follow up and Quality control. Order follow up and quality control have main managers who work in their fields. Merchandising is divided to work under the same manager who is also responsible for whole rep offices operations. There are some higher merchandisers who help their manager. In some cases this seems to add a workload on other staff. It could be seen as effective to have one more manager to look after the needs of the merchandising department. Currently the operations work

efficiently, but when special circumstances occur, effects of time loss and stress in employees can be seen.

A company operating as a global organization usually has more opportunities than domestic corporations. Company X is somewhat a new player in the European markets. This will be marked as a huge opportunity for Company X. Europe currently has very powerful currencies such as the pound in England and euro in many member countries. This gives Asia/American company good leverage on markets. Goods are not so expensive for European customers. This opportunity is in the reach of Company X because it has resources, marketing and research. Supply chain also can be configured to the new system. This is an opportunity to save resources. China also has its domestic pet markets which have not been taken full advantage of yet. The company is considering a possible change to enter Chinese markets. This market would be huge if the company can harness it to its use.

Threats are always present when doing business globally. If this new model is taken into affect before it is fully ready, it can be very devastating for operations and effect the whole organization as China is the source of 60 percent of production of sold goods. It is unnecessary to mention the effects on whole sales if there would be longer gap on deliveries. There is a lot of hiding producer information from end customers to prevent them communicating with each other. This poses a great threat of losing customers. Bigger customers in the US end have resources to go directly to China and buy for themselves. So it is very important that this information does not slip into the wrong hands. Loss of customers in any market is always a threat in that markets economy. Because the USA is the biggest market for Company X it also would be the biggest threat to lose market position there.

## 12. RECOMMENDATIONS

China has to be seen as a complex multilayered business opportunity. There are many ways of doing things and sometimes finding the right way is very challenging. In some cases there is no right way and all options seem more or less non acceptable. This makes business in China so challenging and also interesting for companies who are willing to operate in China.

Company X has established very efficient representation office in Shanghai. This office has established strong employee base in Shanghai and they are operating in native language which makes the staff irreplaceable.

Now when the company is planning to do many drastic changes in their operations, close follow up is needed. Every phase of this new system has to succeed. It is highly recommended also that the company do not jump too fast into this system. It is very important to be sure that all things run smoothly before implementing a new supply chain.

Researcher's opinion is that Company X should look into the domestic markets of China. There are many possibilities to grow in China. Currently pets are not so popular in China, but it can be seen that this is growing trend in future.

European markets are the new objective for the company. This can be seen as huge market and possibility for growth. This is very recommendable course of action for the organization. European markets have lots of buying power and current strength of currencies makes the products some what cheap in Europe. Price is always a good sales pitch.

China is a market for small and big businesses. It covers most areas of manufacturing, selling and purchasing. There is everything in China. This is the problem, it is some what overwhelming. It has tendency to affect companies and expatriates in negative way. People come to China to do business, often whit out good background research.

When this occurs it will bring difficulties later as business is driven forward. In some cases it is completely normal because these companies did not have resources and knowledge to enter China. But in most cases companies get frustrated and draw back because nothing seems to be achieved. This is a shame because these companies where not lacking opportunity they where lacking know how. So doing your home work is more important in China than many other locations where business can be conducted.

Cultural aspects are important for anyone who comes to China. So I would like to conclude my thesis with simple sentence for any expatriate who arrives to China: have patience.

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