

# RISK MANAGEMENT APPLICATIONS IN CHINA-FINLAND TRADE

Case: Woodim Euroboard Oy

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## ABSTRACT

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This thesis was set to find out the risks present when importing products from China to Finland and to map out the state of China, an already huge economic power, risk management –wise.

The thesis had 3 main objectives. The first one was to analyze the state of China generally, and to map out the risks that affect foreign companies the most that operate on Chinese soil. The second one was to map out risks most commonly present in importing products from China, a business in progress by the case company Woodim Euroboard. The third one was to analyze the freshly started, ongoing threshold outsourcing project of Woodim Euroboard in China, and to develop solutions and recommendations for risks present in such business transaction, and also to analyze prospects of producing the thresholds in a closer destination, namely Estonia.

The study was carried out by first analyzing the Chinese market by studying literature and conducting internet-based analyses of China's current state risk management –wise. Questionnaires were also sent in Chinese companies regarding risk management. SWOT analysis was also used to analyze both the case company and the Chinese supplier. Data from the received shipments from China was also used.

The findings saw China as a relatively high-risk country to operate with. Logistical risk and cultural risk are relatively high, with political risk remaining seemingly low, attracting western investment. The case company's threshold manufacturing was deemed a high-risk venture, with low levels of communication present. With the case company, the benefits outran the risks with Chinese production, and production in Estonia was deemed to be more controllable, but yet too expensive because of lack of natural resources. Chinese-speaking consultancy and optimization of the logistical procedures was suggested in the China-end to ensure a working relationship in the future.

Key Words: China trade, Woodim Euroboard, Risk management, Cultural differences, Thresholds

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## TIIVISTELMÄ

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Tämän opinnäytetyön tavoitteena on kartoittaa Kiinan tuontikaupassa esiintyviä riskejä ja kartoittaa Kiinan, nykypäivänä jo valtavan talousmahdin, riskienhallinnallista tilannetta.

Opinnäytetyöllä on kolme päätavoitetta. Ensimmäinen liittyy Kiinan tilanteen yleiseen analysointiin sekä Kiinan maaperällä operoiviin ulkomaisiin yrityksiin erityisesti vaikuttaviin riskeihin. Toinen on kartoittaa kiinantuontiin liittyviä riskejä erityisesti silmällä pitäen case-yritys Woodim Euroboardin kiinantuontihanketta. Kolmantena tavoitteena on analysoida Woodim Euroboardin hiljattain Kiinassa aloittamaa kynnystuotannon ulkoistamishanketta, ja kehittää ratkaisuja sekä suosituksia kyseisenlaisessa kaupassa esiintyviin riskeihin. Tavoitteeseen lukeutuu myös lähempänä sijaitsevan tuotantomaa, Viron, riskienhallinnallinen kartoittaminen.

Tutkimus suoritettiin ensin analysoimalla Kiinan markkinatilannetta kirjallisuuden- sekä Internet- lähteiden avulla. Myös riskienhallintaan liittyviä kyselylomakkeita lähetettiin kiinalaisiin yrityksiin, ja SWOT- analyysiä käytettiin sekä case-yrityksen että kiinalaisen toimittajayrityksen arvioimiseen. Vastaanotettujen toimitusten tietoja käytettiin myös hyödyksi.

Tuloksissamme Kiina esiintyi suhteellisen korkean riskin maana kaupankäynnin suhteen. Logistiset ja kulttuurilliset riskit ovat suhteellisen suuria, poliittisten riskien pysytellessä siedettävissä rajoissa, joka osaltaan houkuttelee ulkomaisia sijoituksia. Case-yrityksen kynnysten valmistus osoittautui suuren riskin hankkeeksi, pääongelman ollessa todella vähäinen kommunikaatio. Kuitenkin, case-yrityksen kohdalla Kiinassa tapahtuvan tuotannon edut nousivat suurempaan asemaan kuin riskit, kun taas Virossa tapahtuva tuotanto osoittautui hallittavammaksi, mutta luonnonvarojen hintatason takia liian kalliiksi. Kiinankielisten konsultaatiopalveluiden käyttämistä sekä logististen palveluiden optimointia ehdotetaan ratkaisuksi kyseiseen riskienhallintaskenaarioon.

Avainsanat: Kiinankauppa, Woodim Euroboard, Riskienhallinta, Kulttuurilliset erot, Kynnykset

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# **1. INTRODUCTION**

## **1.1 The objective**

The objective of this thesis is to map out risk management methods that are necessary when importing products from China. It will specifically include analysis of the business relationship between Woodim Euroboard Oy and a Chinese supplier, which involves importing thresholds from Nanning, China via Shanghai. This thesis will also work as a base for a future risk management plan for Woodim Euroboard in terms of purchases made from Asian countries. The thesis will revolve around risks and risk management techniques that are applicable for this specific business relationship, but will also touch other matters that are of importance when importing from China. The main topics to be concerned are the cultural differences and more specifically the differences in the business cultures that are bound to affect the communication between the companies, and the large amount of distance between the companies, that will have its effect on production management.

## **1.2 The research problem**

The primary research problem is to find out what sort of risks are usually present in business relationships where there's a Chinese counterpart, and to propose solutions and techniques for effective management and handling of these risks. The thesis is also set to find out a solution for the case company, Woodim Euroboard, on their threshold importing endeavor. The company hasn't done any real risk management planning in the past, and has faced problems with it in the past. China is a risky country to begin with, combined with the fact that the manufacturer's logistical location isn't optimal, along with the fact that the company only employs one English-speaking person are facts that are going to affect the fresh business relationship eventually. China also has a business culture

that doesn't allow the companies to be transparent, but rather keep information to themselves. This is bound to pose a problem when troubleshooting the business relationship and mapping out risk management methods.

This thesis will also analyze the possibilities of producing such custom-made article as thresholds, in a closer production country than China. The hypothesis is that threshold production requires hardwood often growing in rainforest-type atmosphere, and it is estimated that production in a European country will require raw material to be imported. The question is, whether the benefits of production control and communication when producing in a closer destination overrun the benefits of cheaper production and better raw material availability, and what risks are included in both production possibilities.

### **1.3 Analytical tools**

The thesis is going to analyze risk management in general as well as the application of risk management methods in Chinese trade. The theory part is done by analyzing risk management literature as well as relying on websites for information concerning the theory part. Books will be used as a primary source for information, but when concerning county-specific data and things that require deeper analysis, interviews and questionnaires will be used. The analytical section, as mentioned, will be largely done based on literature and internet sources. When finding out specific risk management methods applicable to the Chinese market, and when mapping out China's risk situation, questionnaires will also be sent to Chinese organizations about their thoughts about risk management methods that are to be taken in to consideration when doing business with a Chinese counterpart. This part is done by simply emailing Chinese companies questionnaire forms with risk management-related questions translated to Mandarin Chinese. The analysis section of these forms is conducted after first translating them back to English.

The section concentrating on the risk management analysis of Woodim Euroboard's endeavors will be almost totally based on interviews and questionnaires done with the personnel of the company, and data extracted from the Chinese supplier. Interviews will be used more than questionnaires, as the managing director is the person in charge of finding news suppliers, and is thus the only one who possesses information about this particular endeavor. Interaction with the Chinese supplier will be handled largely by email questionnaires and phone conversations. Email will be used more, as it has become evident, from conversations with Woodim Euroboard, that when using email, not so much is lost in translation.

As the business ordeal with the Chinese is an already ongoing venture, real time data from the shipments will be used to analyze the risks concerning the business relationship. The same can't be done for the part that goes through possibilities of changing the supplying country and company. In this case, analysis based on internet and book sources will be used to determine the risks of venturing into the market. Both the analyses will follow the same pattern. First off, risks must be assessed and listed. After this, they must be analyzed in terms of whether they are acceptable or not. Third off, conclusion will be made on the grounds of the analyses made.

#### **1.4 Restrictions**

This thesis will not look into any other risk management issues of Woodim Euroboard than the production going on in China. Albeit the company does have production in Malaysia currently, also relating to thresholds, this will not be brought up in this thesis, apart from a few price-related issues. This thesis will also not deal with the risks of the logistical chain that occur after the goods have arrived in Europe, because after that, the risks at hand are no more specific to

China. The thesis will also not explain all of the risks that are present when doing such purchasing from China, but will concentrate on the issues that have, according to the gathered data, risen to the biggest role. This thesis will also not include the financial risk that is present when doing business with local currency, because the payments in this case are handled with dollars, so the fluctuations of the Chinese currency have little to none effects to business.

## **2. RISK MANAGEMENT IN CHINA TRADE**

### **2.1 Risk management in general**

In the past, risk management in business was considered to be just about getting the proper insurances to protect assets of the company. Nowadays, however, it is a more complex and scientific matter. Many companies now must realize the need for a well planned and organized management considering risks. It can be said that, around every corner there exist potential risks that could severely hinder or even bring down the organization.

What risk management exactly means in this case consists basically of two major points. Firstly, it means identifying all possible risks that the company may face. This is usually done for example by viewing checklists containing risky factors, and careful analyses of data acquired from within the company or from outside. Usually, a special team is assigned to this risk identifying and data collection task. The second aspect of risk management is the actions taken by the company to reduce and prevent the risks identified earlier. The most crucial such actions by the company might concern the company policies towards many different things, such as management-employee relations, legal policies, and strategy revisions in foreign trade. Only after proper and thorough analyzing of data, such risk management decisions can be made. However, once taken in time and in a proper fashion, such decisions might prevent disasters and improve performance in many fields.

In addition, attention must be paid to several issues while identifying risks. The company will face many smaller risks, with a low threat level, and also numerous risks of other categories, also including those of high threat level. It is crucial to keep the focus of risk management on those risks that pose the biggest threats. This brings up another important issue, the cost of risk management. With proper prioritization, costs will remain clearly lower than the possible losses from risks that have been prevented or otherwise managed. The biggest risk areas often require big changes within the company, which of course is also very expensive. With efficient risk management, a company can indeed improve its performance, and gain a solid protection against identified threats. For healthy company performance, having a suitable and up-to-date risk management system is very important.

## **2.2 Risk management in China**

Recently, especially during the past decade, China has increasingly attracted foreign investment, and many foreign and multinational companies have decided to start moving their operations to the quickly developing Middle Kingdom. What in China attract most companies are its vast and ever-increasing markets, as the new Chinese middle class grows in size and also wealth. In addition, the prospects of increased income in rural areas tend to further increase the immense purchasing power of the Chinese people in the future. Almost endless amounts of cheap labor also invite foreign enterprises to move their production onto Chinese soil. (Chen 2006).

In the eyes of foreign enterprises and other investors, China is also generally seen as a relatively safe target for investments, having a stable, although rather government-enforced political atmosphere. The government also offers many incentives, such as reduced taxes and quotas, in order to attract foreign companies and investors, especially those interested in China's Special Economic Zones (SEZ). Such actions by the government have created amazing economy boosts in many of such SEZs. For example the city of Shenzhen, which until 1980 was a mere fishing town surrounded by rice fields, is now a thriving business city with a population of over 4 million. The port of Shenzhen is one of the busiest in the whole of Asia. Shanghai's Pudong area is another good example of such amazing growth in a short period of time, now a home to the China operations of many foreign enterprises. (Chen 2006).

Although China has become very tempting with all its investment opportunities, and truthfully for many companies the only option for survival due to competitors moving their operations there, thus competing with the "China price", there also exist many risky factors in China. The main concern in the risk field for many companies is logistics. In China, there is loads of trouble to sort out, especially if big intra-China product hauling is required. This is due to many different aspects, including too poor, old and inefficient infrastructure, insufficiently trained workers, interference from local governments, and the lack in complete logistics solutions due to overwhelming focus on just transportation and storage services. Cultural aspects are also a major risk area, mainly due to language, and different values and methods affecting communication, decision making and information gathering. There are also many legal problems that foreign enterprises have to be well prepared for, such as intellectual property rights (IPR) issues, corruption and how to deal with it, and so on. (Chen 2006).

Thus, it can be said that even though China clearly seems a very interesting opportunity for many companies to expand or move their operations into, there are many things that the companies also need to be concerned with. In this chapter, we take a look at different kinds of possible risks existing in China-trade.

## **2.3 Legal and political risks**

### **2.3.1 Intellectual property rights**

For a foreign enterprise doing business in China, the lack in intellectual property rights (IPR) protection often poses severe risks. Especially in many branches of industry, the risk of infringed products appearing on the market is often high. The roots of this problem lie partly in history, affecting the very business mentality of many Chinese. Imitation and plagiarism have long been tools of trade for domestic Chinese enterprises, who often prefer adopting business ideas and products from already existing firms and using them as their own, often stomping prices by producing low-cost and low-quality infringed versions of such products. This has not been entirely negative development, though. Such cutthroat competition has helped in part to boost the economy development in China. (The infraction of intellectual property rights: Only China's fault? 2005).

However, for the healthy development of economy, innovation must be greatly encouraged, and thus new ideas and inventions protected by law. The establishment of IPR legislation in China, along with the development of economy, has started in a relatively late stage. The first step was taken in 1963, with the supplanting of PRC's Provisional Trade Mark Registration with the Trademark Control Act, followed by the US-China Agreement on Trade Relations in 1979. These steps provided the foundation for the development of IPR protection legislation in China. Since then, many new laws and regulations, regarding IRP

protection have been implemented, and China has also taken part in several international treaties concerning IPR protection. (The infraction of intellectual property rights: Only China's fault? 2005).

In this field, the most important landmark has been China's acceptance into WTO. This was the last push for the government to seriously tackle IPR issues in China, and these issues have since then gained more and more volume in national development plans. Seriousness towards IPR issues is indeed needed, as IPR violations are still a huge problem.

Today, the vital laws and regulations regarding IPR protection are at place, but their enforcement remains the major problem. Often the producers of infringed products can stay in business without much risk of being caught, and if getting caught, the penalties are not severe enough to keep such producers out of business for good. Penalties have been made more severe though, but this development could be faster, and it is also hampered by regional differences in dealing with infringers. A foreign enterprise planning to establish any kind of presence in China, must be very well aware of the risks regarding IPR protection. In many cases, companies have suffered heavy losses in this field, mainly due to poor precautions. This risk also varies from industry to industry, highly depending on the product in question. (The infraction of intellectual property rights: Only China's fault? 2005).

For example, producers of computer software and entertainment face some really disheartening figures in China. The software piracy rate, although now in a slight decline, is still extremely high: The 2005 figure was reported 86% of total software used, resulting in 3.9\$ billion worth of losses to companies (BSA 2005).

In general, the problems regarding IPR protection in China still remain a great challenge, both for companies and the government itself.

“The protection of intellectual property rights is a responsibility that both the government and the enterprises should undertake. While the government adopts macro modes, enterprises themselves need to do those idiographic and detailed jobs and constitute preventive measures according to the characteristics of the enterprises and their products.”  
(Chinaeconomic.net. 2005).

Foreign companies must bear in mind that without appropriate protection, they might lose their core competitive edge, due to domestic companies imitating their products and selling them at lower prices. To protect against this, the foreign company must be well aware of the legislative system of China, and how it works. The government does crack down on producers of infringed products and often effectively put them out of business, but does not do so if it is not well informed of such operations taking place. Thus, the key is information and knowledge of these environments. Also, the very basic business plans for the foreign company must take IPR issues into account. For example, entering the Chinese market only with one product category, which is very difficult for other companies to imitate. In addition, appropriate patents must be well in place, before starting operations. (The infraction of intellectual property rights: Only China’s fault? 2005).

### 2.3.2 Politics and risk

There is always political risk in every nation, but China is one of those nations where that risk is quite low. This has been one reason why such huge amounts of foreign investment has poured into China during the last few decades, but there are some “what if” –scenarios that come to mind, which also the companies must consider before starting any deep business relations in China, or even with a Chinese company as a supplier.

The CCP (Chinese Communist Party) has a tight grip on every aspect of control in China, though this varies regionally, China being such a huge country. There are, however, things that might increasingly stir the people to question this uncontested leadership. One such issue might be increased unemployment due to state-owned enterprises being privatized or entirely put out of business. Despite the development of economy, many people are left aside in extremely poor living conditions with no means to come out of it, or no-one to complain about it. Also, regional leaders have often been seen to mismanage, and to have a tendency to corruption, leaving the interests of many people in the background. In many regions, people have a lot to complain about, the 1 million people who had to relocate from the Yangtze river valleys in Hubei province due to construction of the Three Gorges Dam, just to name one. (Three Gorges dam project sparks new relocation 2004).

The people have been kept rather quiet so far, but the government needs to reform its own structures and legislation to keep up with the increasing demands of developing economy and desires of people to gain more freedoms. Whether the stability in China will continue, is mostly up to the government. At the moment, the risk for an uprising or a coup is very small, however. If such an event would

take place, it would also be destructive for all international business taking place in China, in addition to other hardships.

Also, the Taiwan issue remains a question mark, and could possibly stir the political stability of the region in the future. Considering the huge amounts of capital flowing to mainland China from Taiwan, the island nation also has a multi-sided issue in their hands. It remains to be seen, how this issue affects the future prospects of the region, and foreign businesses with it. (Dan 2006).

China's foreign policy is a peaceful, cooperation-seeking way to deal with other nations. Many both bilateral and multilateral treaties have been forged with numerous nations and organizations, promoting improved trade relations and understanding. Behind the official lines, there are of course many agendas and attitudes. For example, USA and especially Japan are seen as old rivals and some grudges still remain behind there. One great challenge is the mending of Sino-Japanese relation, which has a great impact on the political situation of the whole Eastern Asia. Another major issue is the situation of North Korea, and its relationship to South Korea. China has long been a supporter of North Korea, providing it with huge amounts of food, fuels, etc. Considering political risks, this could be one flashpoint for a conflict in the future, but some progress has been made in the issue also. Ever since the nuclear test performed by North Korea, many six-party talks have been held, the goal being to achieve non-proliferation of the Korean peninsula. (Dan 2006).

For a foreign company, there is little to fear in China's foreign policy. Sudden changes in global politics could always take place, but that is an acceptable risk almost anywhere in the world. In general, the current leadership of China sees the importance of a neutral and friendly foreign policy, to promote trade and investment, and thus economic development. (Dan 2006).

All in all, the political risks in China for a foreign company are relatively low. According to current knowledge there are no absolutely critical political issues that could destabilize the current situation.

“A firm’s director of Chinese operations should be responsible for implementing a system that can work around disruptions caused by public health crises, environmental calamities, or large-scale social unrest.” (Bremmer I., Zakaria F. 2006).

Although there are many challenges for the Chinese government in the future, it has so far kept things under control quite well. This has also been noted by international institutions, which see the political situation in China a stable one.

### 2.3.3 Bribery and Corruption

Due to lack of political reforms, corruption among government officials in China has been a major problem for a long time. Especially since the beginning of economical reforms, officials have had more and more opportunities to receive bribes. These problems have roots in the traditional system of *Guanxi*, which is a complicated system of ties between individuals, families and all the actions taken to keep these ties in good condition. Now, with the relatively new market-based economy, officials with fixed incomes find it hard to adapt to this new type of system, which still is, paradoxically, centrally planned and governed. This has lead to a kind of environment, where many companies, in order to receive benefits or just day-to-day necessities, have to keep “good relations” with officials, often meaning corruption. This happens usually by offering gifts or straight cash, and is often needed to gain the favor of local officials. There are other ways of corruption too, such as embezzling allocated funds and so on, but our focus here is on the corruption going on between companies and officials. (Li Hong Xin, Dan Bing-Ru & Cao Shi Hui 2006).

The government has indeed seen the problem, but it has not seen the structural causes of it, namely the political structures of the government itself. Only really visible acts against corruption have been the occasional crackdowns on it, resulting in officials being jailed and even executed. However, the problem of corruption is so widely spread, that this is not enough. Actually for officials, the threat of being caught, and especially of being persecuted is so small that many still continue to do it. In addition, in many cases the most top-ranking corrupted officials are not even investigated, because they outrank the investigators and have a lot of influence, leading to more confusion. (Li Hong Xin et al. 2006).

For a foreign company, the corruption issues often pose a dilemma. Since the domestic companies still widely “grease the wheels of government” with the officials they are dealing with, this many times gives them an unfair advantage against foreign companies. These corrupt officials will of course grant favors for these bribing companies rather than those that do not do it.

Often the foreign company faces a question, whether to bribe or not. In addition to being a major ethical issue, there are also many laws that must be taken into account. Even though this might be the “way things work” in the operating country, there are laws of the home country that also bind this foreign company. For some companies, the disadvantage may be that they are bound by an anti-corruption law in their home country, while competing foreign firms may not be. Many times the exposure of such corrupt activities will be very harmful, but many companies see these kinds of activities as necessary means in dealing with the government. (Li Hong Xin et al. 2006).

There are also some not so direct ways to keeping up the relationships with officials, such as holding traditional banquets and inviting officials as quests. Many companies need to do this, in order to gain and keep the favor of these officials. If good relations are not properly kept up, the support from the local government might suddenly disappear, causing difficulties to the company. (Dan 2006).

In many situations, foreign companies face the issue of corruption when operating in China. They must do careful investigation of local government structures, and how they operate in practice. Maybe using a third-party organization to do some research in this field might prove useful in providing information, as how to plan company operations regarding government interaction. The company must carefully consider the aspects of corrupt actions, and take the legit route whenever possible.

#### 2.3.4 Trade barriers

Ever since the first economical reforms, China has realized the importance of free market, and has been pushing towards it ever since. This development, like in many other fields, took an important step with the China's WTO membership in 2001. However, since the strictly CCP-run government still plays an overwhelming role in the development of the national economy, many trade restrictions are still in place. Often devised to protect local and emerging industries, such restrictions still greatly block market opportunities from foreign companies. These trade barriers mainly consist of relatively high tariffs and taxes, restrictions of trading rights, and non-tariff measures. Ever since joining the WTO, China has been forced to cut tariffs, and has also quite effectively done so. However, in many industries, foreign companies looking for a market opportunity face many non-tariff barriers. For example, to protect the Chinese agriculture market, restrictions regarding needs for quarantine and sanitary controls have been raised. (Chen 2006).

In order to protect their own industries from cheaper China imports, the EU and USA like to impose trade barriers for Chinese products, and this often may lead to "trade wars", since the Chinese government might take counteractions and be more keen to impose new trade barriers to protect its own trade fronts. Thus, for a company doing business in China, new trade barriers may cause trouble. Naturally, depending on industry sector, the risk is highest for those importing products to China, but foreign enterprises may experience sudden changes in trade rights and other restrictions, forcing them to radically change operations or move out of the market. For a company with good relations and connections to the government, and an operating method that also benefits the development of China itself, these risks are slightly lower. However, all companies must be aware that sudden policy changes might greatly affect the performance of foreign enterprises operating in China. (Chen 2006).

## **2.4 Cultural risks**

### **2.4.1 Language**

Language, being possibly the most important aspect of culture, is always a major challenge in international business. China is no exception, and it can be said that the lingual aspects can indeed cause problems for a company willing to do any kind of business there. In business operations, language generally serves the following main purposes: Information gathering, access to local society, company communications, and better understanding of contexts. (Czinkota, Ronkainen & Moffett 2004).

For business operations to be effective, many kinds of information about the country in question, the markets, etc. is needed, prior to starting company operations, and also while the company is up and running to keep competitive. In addition, knowledge of the local language is needed in ongoing company communications, negotiations, and many other aspects. (Czinkota et al. 2004).

In the case of China, the lingual aspects are even more challenging, due to unique differences in the language, when comparing with many others. Most visible point is the written language, which at least to Western companies, seems completely different and often incomprehensible. In addition, the structure of Chinese language often poses trouble to translators, and this can result in mistranslated information, or wrong message carried out to Chinese partners or customers by the foreign company. In this context, the importance of selecting a good translating service is paramount. Not only does it enable the foreign company to gain better understanding of both the verbal and non-verbal meanings of messages and talks, but also enable it to get new suggestions and ideas through properly. For joint ventures, the challenge is not so big due to the Chinese counterpart often

handling the local communications within China, but still the communications within the joint venture remain a challenging ground. Therefore, in any case the foreign company often needs help from well-selected local translation and market research companies, who can act as a channel between the company and environments in China. (Suo Ming-Xiang 2006).

Another challenging issue, even further emphasizing the importance of knowing the local language, is the fact that language education is still rather infantile in China. This means that English, the common language in international business, is still only spoken by a small percentage of the population. However, improvement has happened in this field through educational reforms, and nowadays in China it is easier and easier to find professionals with good English skills. Nevertheless, language barriers often exist in business life, whether it is negotiations, or a simple inquiry sent by e-mail. Especially in small and medium-sized companies these problems persist, as they often lack language-skilled professionals. This can further lead to severe difficulties in communication. For example, a foreign company requesting a Chinese supplier to make some changes to a product, and the Chinese company not completely understanding these changes but carrying them out according to their own interpretation, can result in big losses. (Questionnaire conducted in Chengdu, China 2007).

For a company planning their communication structure well, the risks related to language are far less severe. Such well laid plans could include the usage of a good translation and interpretation service, or setting up a team of language-skilled professionals to handle communication with the Chinese partners and/or clients. Of course today many Chinese companies have people who can communicate exceptionally well with foreigners, but this is not always a certainty. (Questionnaire conducted in Chengdu, China 2007).

### 2.4.2 Values and attitudes

Different values and attitudes reflect on many aspects of business dealings and communication, and can bring with them some challenging aspects. One of these is the typical Chinese attitude towards criticism, opinions and orders coming from “outside”. For example, in order to improve quality and lessen the risk of faulty production, a foreign company might give a Chinese supplying company some advice how to improve their performance. In many cases, this kind of criticism would be disregarded in the belief that the homegrown methods and procedures that have been used before, are the way to go. This also shows in the lack of communication; what is not known is often not asked about, and this can lead to many kinds of misunderstandings. (Czinkota et al. 2004).

Additionally, contacts and relationships are extremely important to the Chinese. Thus, building connections is very important, and often a challenging aspect in conducting business. Local companies and officials often prefer to conduct business with a person or company that they are well acquainted with, over another party that might offer otherwise more interesting services or products. This could be interpreted as valuing such personal ties over material things, meaning that a careful adaptation to local culture, customs and people is often a good way for a foreign company to start their China-operations. (Czinkota et al. 2004).

### **2.4.3 Culture and business culture**

As mentioned before, conducting business in China is all about contacts and relationships, especially in the beginning. For example, the first negotiations are usually more like social get-togethers and dinners, namely all about getting to know the other business partner and what they are about. Many do not realize this, and jump too quickly and impatiently into actual business talks, making the Chinese counterpart uneasy. Patience is truly a virtue here. A good perspective when establishing operations in China, is not to expect everything to happen in an instant. Dealings take time, and only after the Chinese counterpart feels that they know the other party well enough, can negotiations lead to actual business. Such a social way to view business relations does not stop after the beginning, though. In China, it is often required that relations are kept up well, by meeting for dinner from time to time, or by other means. (Czinkota et al. 2004).

Some foreign companies and individuals often fail to see these aspects of Chinese traditional culture affecting business culture, and the importance of it. Truly, for a person not so familiar with China and its culture and history, the local business culture might seem confusing at first. Without familiarizing oneself with the culture and local way of life beforehand, dealing with local companies can prove difficult, and lead to misunderstandings and start business relationships with the wrong foot. (Questionnaire conducted in Chengdu, China 2007).

## **2.4. Logistical risks**

### **2.4.1 Infrastructure**

In the past several years, the Chinese government has increasingly invested in developing the logistics industry, mainly in the form of building new highways and railroads. These efforts have helped the state of China's logistics infrastructure only somewhat. There are still many problems in it, which make transporting goods, especially within China, very challenging. (Chen 2006).

One of the most basic problems is the geography of China. Since China boasts such a huge landmass, distances are the first thing to note. Efficient transportation is difficult to acquire, and transit times can be very long. Additionally, the land is also very mountainous, actually mountains and hills cover roughly about 50% of China's land area. Many of these areas are situated so, that key transport routes have not been able to be built in the most efficient way, and also cause longer transit times on many areas. (Dan 2006).

The former strictly state-run policies still show strongly from the state of Chinese logistics infrastructure. Generally, the people working in the industry are not very skilled or well trained. Usually transportation methods are geared towards transporting large bulks of goods, a remnant from the system of centrally providing different areas with supplies. This is especially true in rail transport, where it often is not even possible to hire transportation for cargo under 10 tons. Local governments often hamper transportation of goods by imposing restrictions against transportation companies from other areas, making inter-China transportation a very difficult ordeal. (Chen 2006).

Such strict actions and poor fund allocations from local governments are also one of the reasons why many of China's roads and railroads are in a poor shape. Even though new have been built, for the vast majority of tracks and roads there is not enough upkeep. The routes are often just barely functional, and can cause many problems. This is especially true in the more remote areas, such as western and north western China. Paradoxically, the many regulations that hamper the efficient operation of transport companies also include safety and quality regulations for transportation, which are often ignored. Trucking companies try to cut costs by overloading, many times trucks can carry even 50% of excess cargo, which of course is dangerous. The trucks, and also trains, are mainly in poor condition, since official safety checks are often disregarded. Regarding water- and air transport, these problems are not so severe, although booming trade and thus, transportation, further accelerate such development of risky areas. (Chen 2006).

Due to the poor state of transportation routes, and the lack of maintenance, safety and security controls, transporting goods in China indeed comes with risks. This also means that there are not so many options for foreign firms, and not so much variety in transport. For example, easily perishable goods can be especially challenging to haul across China. (Chen 2006).

#### **2.4.2 General problems of logistics**

Clearly the greatest logistical challenge for companies setting up their operations in China is the amazing speed at which all logistics activities are increasing. This is a natural continuum to the fast development of Chinese economy, and is further emphasized by several other issues. One is the mentality of Chinese people, regarding logistics. It is usually viewed just as means of transportation and storage, and other aspects are not considered. For example, the flow of information and

efficient logistics information systems are a rarity. Many times it is impossible to trace and track a shipment within China, due to poor technology in this field, and the sheer amount of goods moving all around the country. Logistics firms offering complete solutions and service are also rare, as most companies are only focused on getting the products from place A to place B as cheaply as possible. Speed is often a luxury, mostly due to infrastructural issues mentioned above. (Czinkota et al. 2004).

Although water- and rail transport are clearly the most used transport modes on a tons/kilometer scale, priorities remain a problem. In rail transport, passenger traffic practically always has a higher priority over cargo traffic, thus causing drastic reductions in delivery times. This also shows in a severe risk for goods to be damaged in rail transport, due to poor handling methods. Also, the importance of road transport needs to be further emphasized in the future, as it can positively hold a greater burden in the inter-China cargo traffic. Being more flexible and often faster method over rail- and water transportation, it will see a great increase in transport volumes. The government has to set more focus on this prospect. It has been construction many new roads and highways, mainly in the busy eastern corridor consisting mostly of the Beijing-Shanghai route, but more needs to be done. All around the country the need for better roads, among other types of transport routes, increase vastly all the time. This is not just about highways between major cities, but also better smaller roads are a key element in bringing up the rural areas by better connecting them. The priority issue here also touches the local governments, which need to be made to see the big picture, and not only use funds to their own needs and agendas. (Czinkota et al. 2004).

Air transport is a fairly new area in the Chinese logistics industry, and cargo hauling rates are still very low. As often is the case, also in China airways are used to transport high value, and fragile goods which make the high transport cost worth it. An increasing demand for infrastructure expansion also touches air transport, and it remains to be seen as to how high priority it will get in the eyes of the government. (Czinkota et al. 2004).

### **2.4.3 Customs issues**

In addition to issues in intra-China transport, there are also some regarding China customs that cause threats and challenges to foreign companies. One important issue to note is that China, having a huge land area, is very fragmented. Different zones (for example the aforementioned SEZs) have been originally planned to be self-sufficient, meaning that transporting to and from them, to China's inland areas or overseas, is not such a smooth operation as it should be. (Chen 2006).

Fragmentation also shows in poor or even non-existent communication between customs of different areas and zones. This poor flow of information again often shows in delayed shipments and other problems. Also, the complicated and numerous bureaucratic procedures further emphasize these problems caused by insufficient flow of information. Especially when transporting to or from China's more remote areas, customs procedures may restrict transporting from one mode to another. This is often a problem in air transport, which often suffers from inflexibility in such required connections. (Czinkota et al. 2004).

## **2.5 Environmental risks**

With economic development, the amount of pollution generated by China has also increased with immense speed. As China continues to conquer new markets with its relatively newborn industrial might, it is a natural course that with increasing demand, also new production facilities and other infrastructure such as power plants, are built. In this production and construction frenzy, environmental matters have been left on the background. Even though Chinese government has been more and more aware of these environmental matters, it has clearly not done enough to combat the issues at hand. The famous “economic development first, then everything else” -mentality is the doctrine behind such actions, or lack of proper actions. (Chen 2006).

The environmental problems themselves, although being a huge challenge and threat to the whole of humanity, do not pose a direct threat to foreign enterprises. However, clearly every company, especially those investing or moving their operations into China, must be very well aware of environmental-friendly actions and procedures. What more directly concerns companies, whilst identifying risks, are those matters caused by different environmental regulations. Currently such Chinese regulations are insufficient, and their enforcement is also lacking behind. Also in here, corruption raises its ugly head. Many Chinese companies draw from it to go around regulations, in order to cut costs. In reality this means that some local officials will look the other way while these companies, for example, dump their waste into local bodies of water. This is one of the most threatening factors in China’s environmental doom, and clearly should not be an option for foreign enterprises planning for production on Chinese soil. Thus, additional awareness and funds must be allocated to create solutions fitting well together with those required by the environmental state of China. (Chen 2006).

Up-to-date information about environmental issues, their future prospects and possible developments is very important for a company to possess. In addition to protecting the environment, such information and decisions made upon it will give a company a solid buffer against possible changes in environmental laws, regulations and policies. If a company undertakes production or other, such as different kinds of procurement operations, it must indeed pay attention to these issues. If proper attention is not paid, and precautions made, sudden changes in environmental policies can bring severe difficulties. For example, a company producing metal products with old production methods and not heeding environmental aspects, would have to almost completely rearrange its production facilities and other operations, if a change in government regulations takes place. Furthermore, such changes in regulations can bring additional, deeper repercussions for an unprepared company. Due to regulations, complete or partly relocation of facilities might be needed, or even a shutdown of operations on Chinese soil. Also, direct sanctions or other legal charges may follow, if proper environmental precautions are not made. In many cases, when a new environmental policy is taken into use, companies have a good amount of time to make proper adjustments. However, this might not always be the case. If a company is unprepared for the existing legal atmosphere regarding environmental issues and their control, some older or even new laws may cause very negative surprises, such as some key point in environmental law that has not been analyzed and realized properly. (Chen 2006).

### 3. CHINESE COMPANIES' VIEWS ON RISK MANAGEMENT

#### 3.1 Background information

We wanted to find out as much as possible about how Chinese companies think about risks and managing them. The best option was to devise a questionnaire, which then was distributed to several Chinese companies engaged in international business (APPENDIX 1). In the questionnaire, our main focus was on finding out (A) which risks are seen as the most threatening ones, and (B) what should be done to manage them, namely which methods or actions should be used. Risk categories that Also, open questions let the companies provide us with additional information, if such occurred to them. First, the questionnaire was done only in English, due to the assumption that companies doing international business could handle it, and that it would not reduce our answer percentage. This, however, was not the case. Only after translating, with some outside help, the questionnaire and other communication into Chinese, did we receive answers. The participating companies were found mainly on the Internet and through personal contacts. Questionnaire was sent out in both electronic form via e-mail, and in ordinary paper form given out by hand. In the end, we did receive a good amount of answers, but more would have been desirable. Sending questionnaires "blindly" over the Internet proved quite inefficient, working through personal contacts and schools etc. was realized to be more efficient.

Regarding risks, and then their management, risks were categorized in five different categories: Legal, political, cultural, environmental and logistical risks. In each category, answerers could rate the threat rate of each cause of risk on a 0-3 scale, 0 being no probable risk, and on the other end 3, high probability. In the second part, concerning risk management, there were several possible solutions and actions from which the answerers could choose the best ones to represent their views of risk management. Thus, foundations were laid to find out which

kinds of risks Chinese companies see as most threatening, and what they think should be done to manage those risks. Additionally, at the end the answerers could provide additional comments and information, which might have not been covered earlier.

### 3.2 Analysis of results –identifying risks

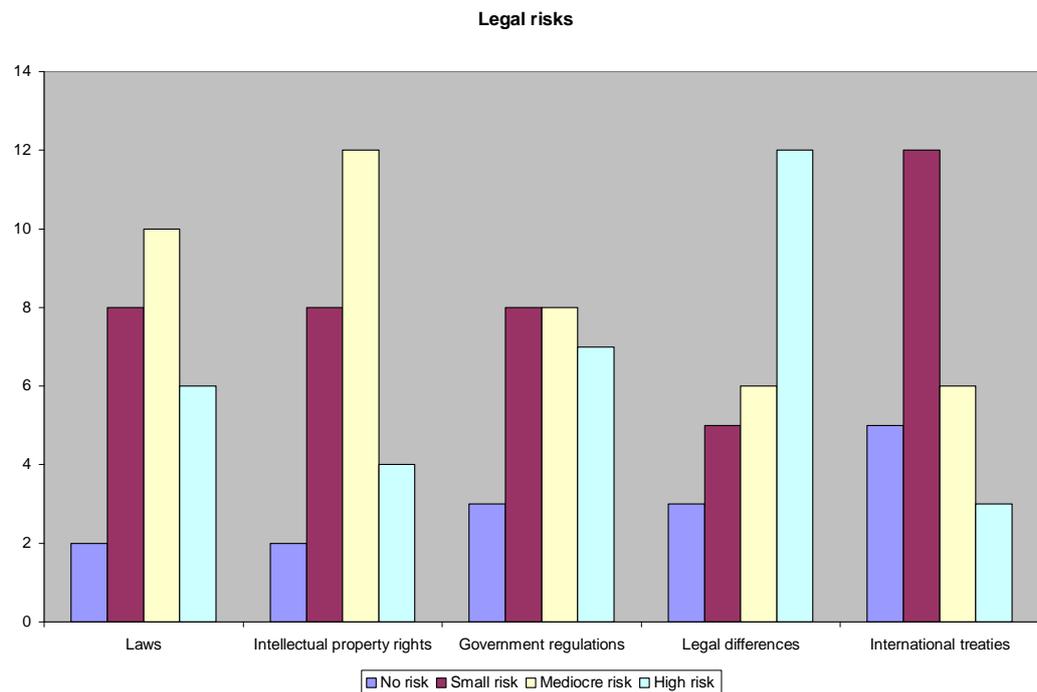


Figure 1. Questionnaire results regarding legal risks

From the legal risks, one category was rated clearly as the most risky, namely legal differences between host countries. This could have several probable causes. One quite clearly is the fact that indeed there is much diversity between the laws and regulations of different countries, namely what is legal somewhere else, might be interpreted in a completely different way elsewhere. For Chinese companies, the laws of China often do not pose as much as a threat or loss, as the laws in host countries of potential foreign business partners. Often some Chinese companies lose potential business due to some foreign or multilateral laws or norms not being met.

Additionally, government regulations laid down by the Chinese government are also viewed as relatively risky area. The development of legal system and governmental structures also pose many new challenges to Chinese companies.

IPR issues, not surprisingly, are not viewed as a high-risk category by Chinese companies. This might be due to the fact that many companies have already had to adjust their strategies according to the generally high risk in the Chinese IPR field, and thus do not see it as threatening as foreign companies do. Bi- or multilateral treaties are not felt as a threatening factor either, many companies felt it as a “low-risk” field. In the international legal environment, there are some laws and regulations that might cause trouble to Chinese companies.

There were also some additional important points that were discovered, regarding Chinese companies dealing with foreign companies. Some answerers wrote interesting comments, that considering legal issues, foreign companies should enter China well prepared. More importantly, the special attitudes and procedures towards authorities in China should be well studied. What this means, is that foreign companies should understand well how the legal system in China works, and how to deal with government officials. It was not mentioned, but from between the lines one could read that this also includes issues regarding corruption, and how to deal with it along the legal environment. Another important comment regarding dealing with government officials was that an increase in cooperation would be most recommendable. In addition, the cooperation and communication should be conducted on equal basis and terms.

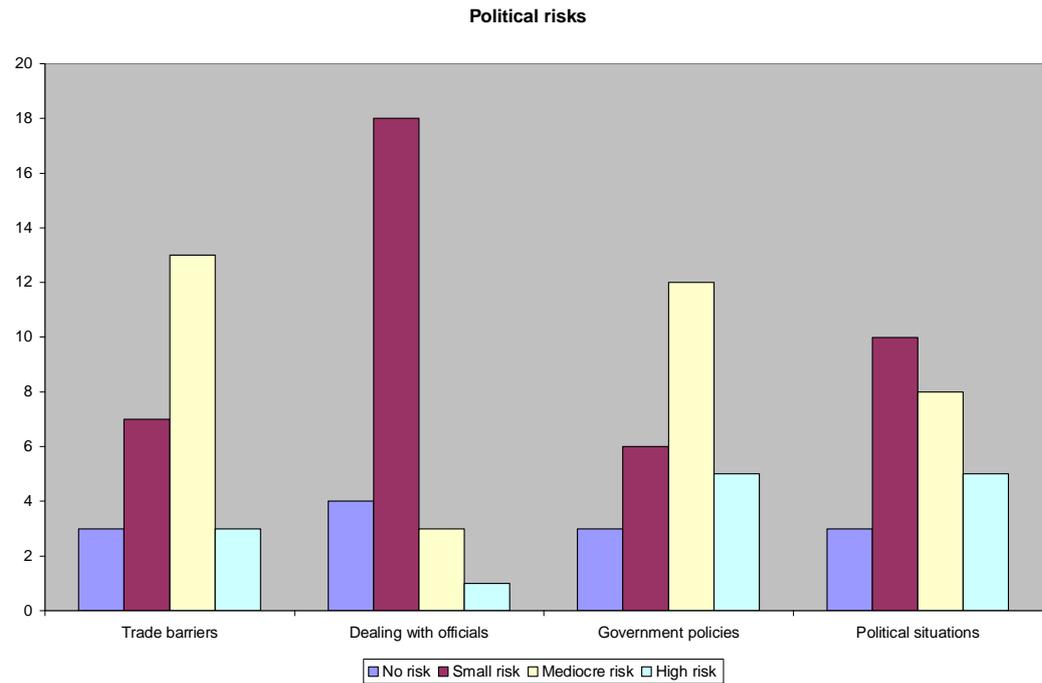


Figure 2. Questionnaire results regarding political risks

Regarding politics, Chinese companies themselves do not see dealing with the government and its officials as a very risky area. This is understandable, as most Chinese companies naturally have a clear understanding of the complex political circles and how to operate within the system. Also, personal contacts were viewed as very important, which the Chinese companies must all possess to operate effectively.

Government regulations were seen as a bit more risky field. Again, this could be explained by the constant developments and revisions in the legal systems of China. All these systems must develop along the economy, thus companies have many new things to adjust themselves into.

Trade barriers are generally a mediocre risk, as viewed by Chinese companies. Naturally, the risk here varies greatly between different industries, and is very case specific too. In the past, for example Chinese clothing products have been

constantly fighting against restrictions laid down by other countries.

General political risks are surprisingly high in the eyes of Chinese companies. For example, the situation of Taiwan and its possible repercussions are much more visible and concrete in China, than when seen from outside. In addition, other local politics and issues are felt more severely.

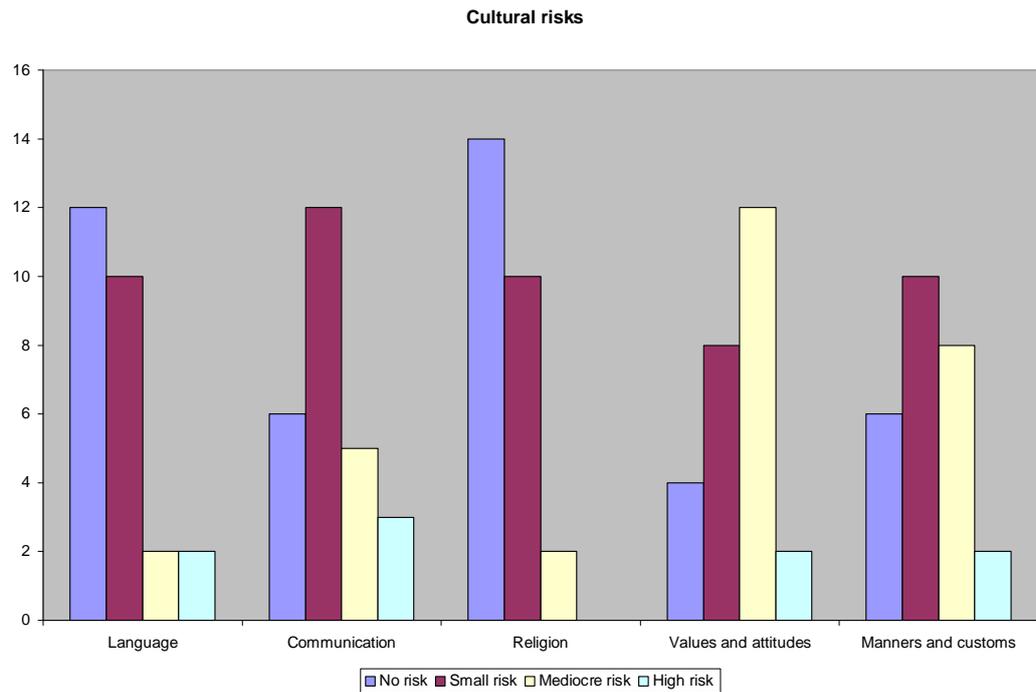


Figure 3. Questionnaire results regarding cultural risks

From cultural risks religion was, not surprisingly, found to be the least risky area. For example, none of the answerers ranked it as a “high risk”. In Chinese business life, religion does not act a big role. Of course considerations need to be made in company policies and so on, but it is far less a risky field as in many other countries. For Chinese companies, this issue is almost nonexistent, when compared to for example multinational corporations, which must see the needs of all its employees from different cultures.

From cultural aspects manners, customs, values and attitudes were found to be of higher risk category, when compared to language and communication, which were felt as rather improbable risks. The higher threat rate of the four aforementioned cultural aspects can be understood, when the approximately 3,000 year-old Chinese cultural background is considered. There are numerous bigger or smaller cultural features that are very important in business also, especially when the business is conducted between a Chinese and a foreign company. Chinese value personal ties and relations above all and this was shown to be true in our research also. Many answerers emphasized the importance of personal contacts, and that one should familiarize oneself with the cultural environment in China prior to starting serious business operations. This knowledge and mutual respect in business are the keys to managing cultural risks, as viewed by the Chinese companies.

The risks regarding language and communication seem even a little bit surprisingly low. Risks in language matters were seen as minor ones, if as any risks at all. It is clear, however, that many problems in language differences and communication exist, but the Chinese companies do not see it that way. According to them, small risks exist, but they see them as avoidable. What was well commented, was that the language problems of China are mending all the time, as the education system is developing along the economy. Also, it is natural that more and more language-skilled people are trained, following the demand for such people. In the current situation, it is more the foreign companies that are concerned about communication issues, as the Chinese counterparts see it in a rather different way.

Also an interesting notion was, that foreign companies should not focus too much on some of the problems that China has, namely the human rights issue. It was mentioned that all countries have their problems and characteristics, and that this issue is even exaggerated, and thus should not cause any considerations for

foreign companies. This view is very Chinese in essence, as in China people generally do not talk about or want to talk down such flaws.

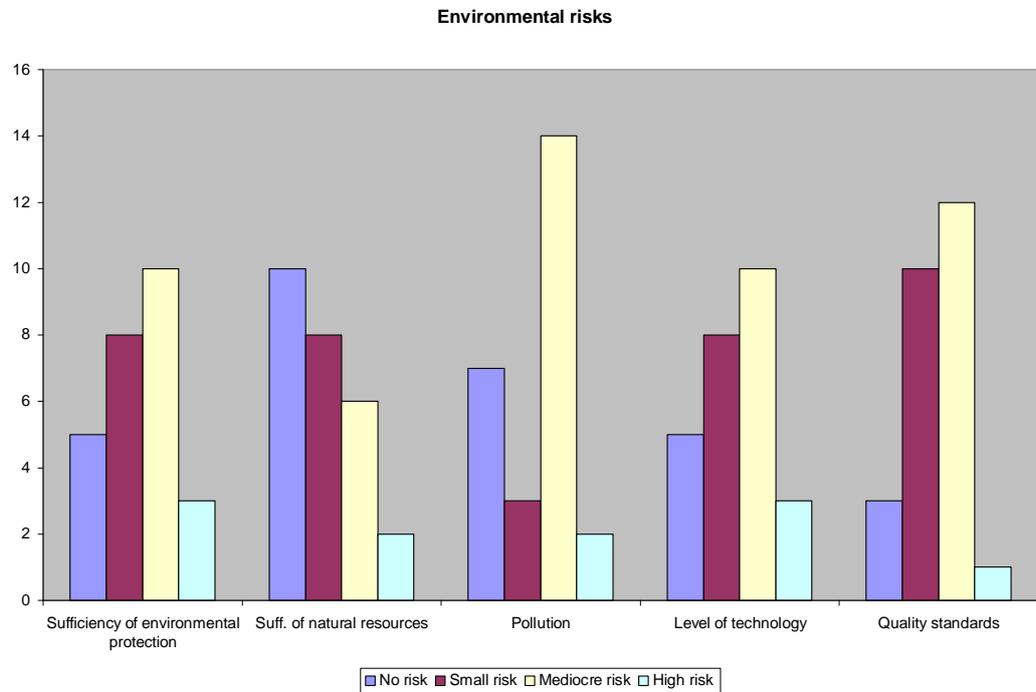


Figure 4. Questionnaire results regarding environmental risks

Understandably, pollution was seen as one of the biggest environmental risks. What was interesting, however, was that many also regarded it as not being a risk at all. Seemingly the threats of pollution still have not ascended to be a major issue in the minds of all Chinese, especially those engaged in such business that either in some way violates environmental laws, or is generally unaffected by such issues. Results were almost identical with the ones regarding environmental protection, and problems caused by it. Paradoxically, many seem to feel that much is already done against China's huge environmental problem, and that there is not so much that could be done better. In addition to personal level, companies also often fail to see the seriousness of environmental issues in China. Our results seem to indicate such a state also.

Regarding natural resources, and their continued supply, answerers were somewhat confident. Although many also saw it as a risk, many thought otherwise. China does have vast resources, but they also are bound to run out some time in the future. A more current problem seems to be the accessibility of many resources, as they generally are located in more remote areas, and behind difficult transport routes. A poor state of logistics infrastructure also further emphasizes this problem.

The level of technology available in China also divides opinions. Most thought that it is not a problem at all, or a very slight one. The other group mostly saw it as a risk of mediocre level. This must depend largely on industry and geographical location, as these are the greatest factors affecting the available technology. Almost the same rules apply to quality standards, with the addition of international standards however. These standards were seen as a slightly higher risk when compared with availability of technology. With economic development and multinational treaties affecting on the background, it is a natural course that better technology becomes available, and to wider and wider regions, while companies face more and more international restrictions in the form of standards.

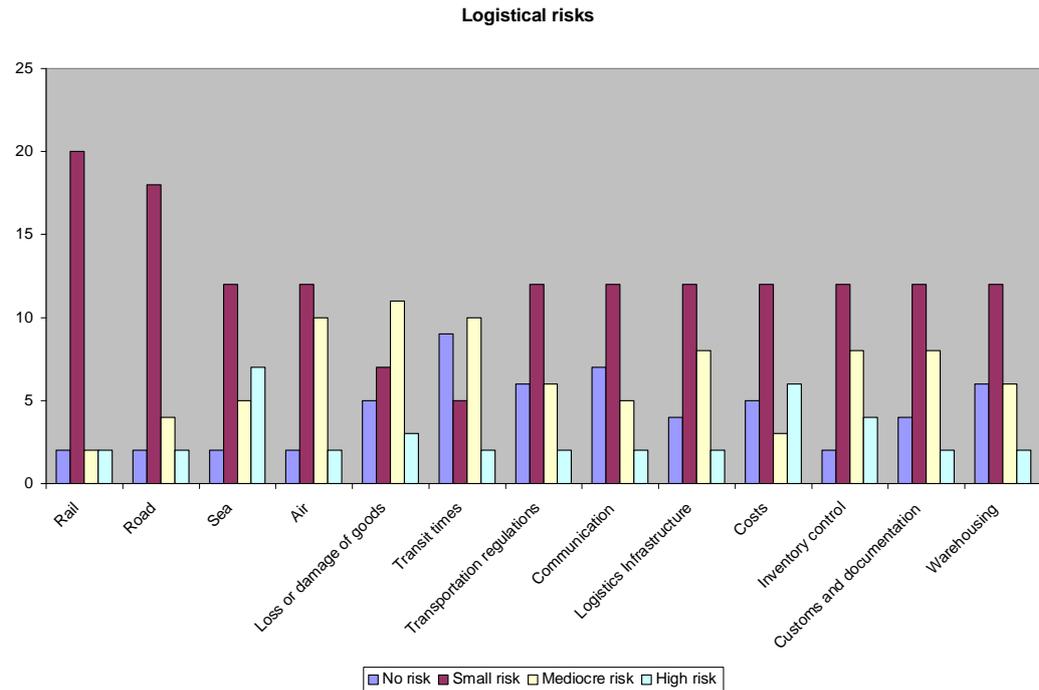


Figure 5. Questionnaire results regarding logistical risks

When considering logistics, the one of the most interesting questions was that which would be conceived as the riskiest and safest modes of transportation by Chinese companies. It was then interesting to find out that road and rail transportation were not seen as very risky. A vast majority ranked them as just a small risk, while sea and air transportation were seen as more risky modes, especially sea transportation. The most threatening risks in sea transportation could be identified as the restrains caused by long transport times, possibility of a great loss in case of a shipwreck, and China's over-capacitated harbors. In air transportation, it is harder to determine which could be the risky factors. However, it is true that the air transportation industry is a swiftly changing one, and for business this could cause troubles. For example, as air-routes may often change, and in China there still is not a wide coverage of such routes, this reduces the flexibility to haul goods using airways. As most saw road and rail transport as not so risky ways of hauling goods, what probably also affects this opinion is, that naturally these are the two major modes, and often either of them the only

possible mode in intra-China transport. Thus, many companies, especially those operating at least partly from or to inner areas of China, do not have anything to compare these modes with.

Regarding other logistics operations and aspects, the results were admittedly a little bit hazy. Many chose all of these parts to be just a small risk, without much explanation why. However, many saw the importance of efficient inventory control, as well as the general problems caused by the costs of logistics, which truly are relatively high in China. In transport times and the possibility of goods damaged or lost in transport, many saw these issues as medium-level risks. Generally, this is a fact in intra-China transport. There are many factors that often cause such troubles, often the reasons being poor infrastructure to support efficient transportation, and fragmentation which causes many legal restrictions and difficulties. In addition, poor safety and other standards are severe risks regarding possible damage, loss or delay in deliveries.

### **3.3 Analysis of results -managing the risks**

When looking at the most desirable ways of managing risks according to the Chinese companies, the first notion is that knowledge is valued most. In legal risks, information and knowledge about laws and regulations is clearly the top choice in the risk management strategy of many companies. On the legal field, the second choices often were to either hire outside help in legal issues, with which to coordinate these possible risks, and additionally increased international cooperation. Closer relations with authorities and officials were seen as a rather unimportant method. When planning the management of political risks, knowledge was also seen as the most important resource. Outside help, possibly the hiring of an expert or such was seen as an average method. Relations with officials seems to be a rather a minor issue, probably because it is not viewed as a political, big-picture issue.

The importance of cultural risks management was also seen by the Chinese companies. Many emphasized the fact that a foreign company should come to China well prepared in this area. As ways of managing such risks, many saw increased and more frequent communication as the basis of a solid cultural risks management. Such communication, with both foreign and domestic partners and authorities, would provide valuable information and a decent buffer to see risks before any damage is done. Cultural knowledge, with policies and methods of operation based on it, was seen as an important tool in managing cultural risks also. Indeed, a company should always know its operational environment in all fields and from many points of view. The need for focus on ethical issues was also seen in this context, as foreign companies should have their ways to deal with this hot issue, since in China there are many ethical questions that companies will most likely face, the often poor conditions for workers, just to name one.

Regarding environmental risks management, many saw the natural resources issues as quite unimportant, clearly confident about the current status of such issues in China now. What was further emphasized was the importance of investing and focusing on newer technology, and also innovation in general. Most importantly, environmental methods in production and also other company operations were seen as key methods in environmental risks management, and also the participation of international treaties, and the importance they carry within.

Regarding logistics, there was more variety in desired methods for managing such risks. In the big picture, perfecting ones supply chain management was rightfully seen as very important. Many companies saw that in this field in China, there is often very much work to be done. Outsourcing of logistics operations seemed also important, and it indeed is a good way to free up company resources to be used in some other field. Additionally, proper ways and methods of inventory control and a comparison of alternate transportation methods were distinguished as a solid

way of managing logistical risks. On the logistics field, communication remained an important tool also.

### **3.4 Conclusions of the questionnaire**

In general, the picture that Chinese companies have about risk management is a rather hazy one. Many still do not see it as an important tool in efficient company management, but nowadays more and more companies are beginning to realize its importance, as competition gets fiercer and thus more and more perfected management methods and strategies are required.

However, what often is a problem of Chinese companies is their overconfidence and the failure to see things objectively. This often means that risks are not considered in a full scale, and their often critical threats are not seen. Those that answered the questionnaire, however, often had also some good suggestions to foreign companies. Getting such insight about how to operate in China, and which information and other procedures should be possessed, was very intriguing. Additionally, the general knowledge about risks and preferred methods to manage them proved very interesting.

All in all, also the foreign companies who plan to do any kind of business in China must consider all the same points as the Chinese companies. Based on key information from different fields, versatile policies and methods of operation can be drawn up to dodge possible risks, and also the Chinese companies see that in China-trade there indeed are numerous risks.

## **4. CASE COMPANY: WOODIM EUROBOARD OY**

### **4.1 General facts**

Woodim Euroboard is a small sized company focusing in sales of wooden products, veneers and MDF boards. The company has been operating since 1995 and has 4 employees. The company is located in Lahti. Woodim Euroboard imports products from Central Europe, Africa, and Asia.

Woodim Euroboard Oy's main customers are those of the woodworking industry. These customers include mainly door manufacturers, but also smaller carpentry workshops that require wooden products suited for the production of for example doors and other construction elements. The company shares premises with Oy Woodim Finland Ltd, a company operating in the field of hardwoods, veneers and wood-based boards. The 2 companies have shared premises since both companies were founded in 1995. The 2 companies do not share anything else than the name and the premises, but they reserve the right to buy each other's products for a wholesale price to serve their customers.

The premises are located in Metallikatu 3 in Lahti. The premises are close to the Helsinki-Lahti motorway and thus provide ideal logistical connections to both the major harbour cities and central Finland. Majority of the customers are located in central Finland.

## **4.2 Organizational structure**

The company is operating with a 4 person staff, so the organizational structure is not that complicated. However, determining the organizational structure is of great importance when defining the weak and strong points in the communicative chain between the supplier and Woodim Euroboard.

The company is managed by the founder who is also the managing director. He also manages outgoing payments, purchasing and a part of sales. He generally travels around about 1 week per month, during which time his jurisdiction is left unattended. In addition there is a sales manager who handles incoming payments and sales. The 2 other employees are working in the warehouse.

## **4.3 Products**

The company has always had door manufacturers as their main customers, and imports all of its products from abroad. This is done because of several reasons. For one, Finnish lumber doesn't offer such elastic properties such as Fuma Veneer imported from Ghana. Also, fibreboards that have the qualities that the customers of the company desire, are not manufactured in Finland at all. With the thresholds the situation is somewhat different, as there is some domestic production, but in most cases the price is too high for the door manufacturers when comparing with Asian imports. (Woodim Euroboard: Asia 2005)

Africa, more specifically Ghana, is the source of Fuma veneer, used as an insulating component in doors made for weather conditions such as Finland has. The tree is not a rainforest tree and it grows to cutting height at the age of 20. Because of the rapid growth the lumber is really soft and offers great resistance to temperature changes. (Woodim Euroboard: Africa 2005)

The company also imports High Density Fibreboards (HDF) and Medium Density Fibreboards from Central Europe, more specifically Slovenia, Italy and Spain. These boards are used for various construction means, and HDF boards are almost solely used for door insulation, because of good humidity toleration. The boards provide different properties depending on the qualities the customer desires. For example the Spanish boards provide several different qualities. For example they have fibreboards that are fireproof, and certain boards also provide excellent protection against humidity.(Woodim Euroboard: Europe 2005)

Asia is used as a source for wooden components used in the production process of the doors, such as thresholds or door frames. Door frames are in most cases not made out of hardwood, so the most common article imported from Asia is thresholds. They are imported from Malaysia and China by sea containers.(Woodim Euroboard 2005)

#### **4.4 Suppliers**

Woodim Euroboard relies to a small group of suppliers, and isn't planning on adding any suppliers to any other department than the threshold manufacturing one. The largest batch is located in Central Europe, in the Slovenia-Italy axle, which holds the main suppliers for fibre boards and hardwood veneers. Ghana supplies the Fuma-veneers, and Asia has generally been the source of door components and thresholds.

Woodim Euroboard uses HDF/MDF boards that are manufactured in Slovenia. The business relationship has lasted for years HDF-boards are one of the company's most important products. The deliveries are made railways from Slovenia to Finland and the while there have been some problems with the supply

amounts not matching the needs of Woodim Euroboard, the company is still satisfied with the business relationship and is not seeking another supplier for HDF-boards.

There are also some companies in central Europe, namely Italy and Spain, namely, that have been supplying Woodim Euroboard with thicker MDF boards for years. The quantities in which thicker MDF boards are sold are significantly lower than HDF boards, which are often sold in bulks of 1000~ pieces. This means that the deliveries from these companies to Finland are not made that frequently as those that contain HDF boards from Slovenia, so there isn't a requirement for fast deliveries, and thus Woodim Euroboard is not planning to replace the producers, as the price is also affordable. When it comes to Fuma, Woodim Euroboard trusts the services of one producer of rotary cut Fuma veneers in Ghana, Africa. The company is renowned for the quality of the veneers, and has been supplying Woodim Euroboard from the beginning, over 10 years. The producer has raised the pricing along the years, but not to a level where it would hinder the sales of Woodim Euroboard. The primary source for thresholds has been Malaysia since the foundation of the company in 1995. The company that Woodim Euroboard operates with is located on the Penang Island alongside the coast of Malaysia. The quality and overall craftsmanship of the thresholds has always been really good, and the deliveries have been made almost on time, often with the Malaysians working at the peak of their capacity to be able to meet the amounts needed. However, during last years the price of the thresholds has risen to such levels that Woodim Euroboard has sought other countries for possible suppliers, as the price of 1 threshold, depending on the model, has raised 200-300% from 1998 to 2006. The reasoning the Malaysian supplier has given for this price is that it is hard for them to acquire suitable lumber for threshold manufacturing, and the overall material costs have been raising at a steady pace during the last few years. The combining factor among all of these suppliers is, that the natural resources required for production are really close by. Fuma veneer can be acquired from

Ceiba trees that flourish in Ghana and HDF veneer can be made out of European wood mass. Woodim Euroboard sees this as a prime property in their suppliers, as they never need to wait for raw materials to arrive before starting production. Woodim Euroboard has a past business relationship with a Thai manufacturer of wooden components, but due to raw material shortage of several months, this relationship had to be ended because no promises of deliveries could be made to the customers which, in this type of business ruled by large factories operating lengthy production lines, is crucial

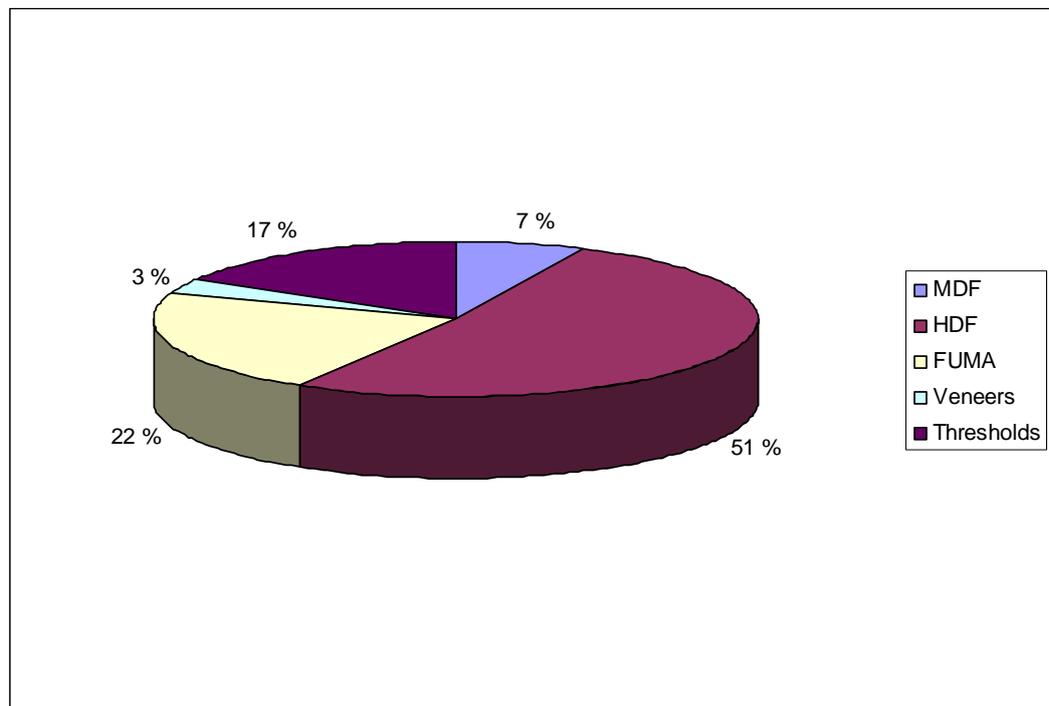


Figure 6: The distribution of different products of Woodim Euroboard's turnover

Figure 6 describes the distribution of different products in Woodim Euroboard's turnover. The threshold sales are almost directly bound to sales of HDF boards. Often a door manufacturing company will first order only HDF boards for door production, and then look into ordering thresholds to cut down on logistics cost in comparison to if they would order the thresholds from another location. The general situation with the thresholds is that there are the major companies that order in bulk, taking almost all of the capacity, thus leaving smaller manufacturers

without thresholds. Because of this situation, the Chinese supplier has been considered.

#### **4.5 Risk Management History**

Woodim Euroboard doesn't have a specific risk management plan, and hasn't done any risk management analyses in the past, apart from very basic ones. The company takes all precautions when doing business long distance however, as the contracts are planned to made so that the seller handles all of the risks until the merchandise has arrived in a Finnish port. This effectively eliminates the company of all logistical risks that might occur. The logistical risk is basically the only risk the company pays attention to. The business transaction is considered a success when the goods arrive intact to Woodim Euroboard's premises. Usually, when problems occur, they are dealt after the damage is done, rather than beforehand with planning and other risk management tools. By concentrating on the logistical risk by leaving all of the transport services to the supplier, the company effectively eliminates itself off any payments due to logistical functions failing in the production country. This, and the usage of forwarders is a major issue in why Woodim Euroboard can run with such a low staff count.

A big part of why the company hasn't paid that much attention to risk management is the sole fact that the company is operating with a 4 person staff, of which 2 are taking care of the warehouse. This leaves 2 people in charge of such functions as marketing, sales, billing etc. so the company basically doesn't have the resources to pay that much attention to risk management. This is why the company uses a forwarder to take care of all of the incoming goods, and to handle the transportation from the harbour to the company's premises in Lahti. Using a forwarder surely is affecting the profit margin of the company, but with the current staff number, there isn't another alternative to be considered.

So it can be said that Woodim Euroboard has focused in avoiding the logistical risks, without paying much attention to other possible risks that might be at hand. However, this might also have been a smart decision, as the company's income relies entirely on the logistical functions and their functionality. Other risk management methods have received little attention, partly because the low amount of staff, and partly because there hasn't been reason to give them any special attention. The risks that have been mentioned before mostly account to concerning personal and political, but, without any reason to give them any more attention them, they have received little so far.

So as a summary it could be said that the company aims in eliminating the logistical risks before anything else, since the success of the logistical procedures marks Woodim Euroboard's performance. When searching for new suppliers the case is almost always such that the previous supplier can't match the quantities required by Woodim Euroboard, and thus a new supplier is needed to fill out the quota. This creates a situation where Woodim Euroboard is not entirely relying on the new supplier, but can, in an emergency situation, rely on the old supplier.

This allows Woodim Euroboard to search for new suppliers quite freely, and they have done so in the past also. For example, Woodim Euroboard uses 2 different kinds of FUMA-veneer from 2 different suppliers, both from Ghana. They use the lower quality one to supply smaller door factories that have a hand-operated assembly line that allows for slight modifications to be done to the veneer on-site to allow a smoother result. The higher quality veneer is used to supply larger door factories that operate an automated supply line that handles the entire door assembly process without much administration. Such occasions require Woodim Euroboard to use several suppliers, as the amount of for is already scarce from the get-go.

#### **4.6 Supplying country**

Woodim Euroboard has always imported thresholds from Asia, partly due to the fact that the results have been positive so far, partly due to extremely suitable natural resources. So far, Woodim Euroboard has imported the thresholds from Malaysia. The selection of China as supplying country was made due to the fact that China, although not the ideal selection when it comes to natural resource, would pose as a better alternative than some of the neighbouring countries due to the fact that the labour force is really affordable and the logistical connection are really competitive.

Interviews conducted with the managing director reveal that there was no real intention in searching for a supplier in China specifically, but rather the possibility appeared at a suitable time. The company just searches for companies that have a suitable machine base and are thus able to withstand the challenges that the ever-changing market that Woodim Euroboard deals with, offers. However, due to the somewhat long distance between Finland and China, Woodim Euroboard has considered it to be fit to research the possibilities of perhaps producing the thresholds in a production facility in a country closer to Finland. This would be done to enhance the controlling of the production process, and to reduce the month-long delivery times that they now have with Asian suppliers

#### 4. 7 SWOT Analysis: Woodim Euroboard

Table 1: SWOT analysis of Woodim Euroboard

<p><b>Strengths</b></p> <p>Good financial situation</p> <p>Good product lineup</p> <p>Solid customer base</p>	<p><b>Weaknesses</b></p> <p>Staff shortage</p> <p>Unreliable suppliers</p>
<p><b>Opportunities</b></p> <p>Selling to other Scandinavian countries</p> <p>Expanding product line up</p>	<p><b>Threats</b></p> <p>Swedish suppliers selling to Finland</p>

Good financial situation and product line up have been marked down as the strengths tab. Woodim Euroboard has received the Kauppalehti “Maakunnan Menestyjä” diploma every year since 2004. This diploma is given to companies that have been outstanding in terms of revenue gains and profits. The company is on solid ground and is constantly expanding in terms of new products and warehouse space. Solid customer base is also marked down as strength, as Woodim Euroboard doesn’t boast an exceptionally large amount of customers, but the customers almost always buy in bulk.

The weaknesses, obviously, is the staff shortage the company has. Although the managing director doesn’t feel that they have need for additional crew, the situation is told to be quite hectic during business trips, when the staff can narrow down as low as 2 people. This is obviously a problem, since one person can’t be considered to be enough to manage the office of a company of such size. Unreliable suppliers are also marked down as a weakness. This applies largely to only products arriving from exotic countries, such as Ghana and Malaysia. While

there might be no real unreliability from the supplier, the products are however shipped large distances, and schedules and harbour arrangements can always take a surprisingly big chunk of time.

In opportunities, selling to other Scandinavian countries is marked down. This is largely an item that requires much larger production capacity from suppliers. At this rate of products arriving, Woodim Euroboard can't think of expanding to supply any other countries. However, this is seen as a future prospect, but no real action has been taken in terms of customer analysis. Also in opportunities, expanding product line up is mentioned. At the moment, Woodim Euroboard is supplying quite a variety of wooden products, but there's always room for expanding according to the management.

Only a single threat is marked down, but this threat is a major one. Since the amount of goods Woodim Euroboard can take in monthly is not enough to supply everyone, and because of the unpredictability of the door manufacturing industry, there have been cases where a certain size of fibreboard has run out entirely, and Swedish companies have been supplying the customer until Woodim Euroboard has regained stock. This has been an ongoing phenomenon for a several years, and Swedish suppliers seem to be running into the Finnish markets excessively.

## **5. OUTSOURCING THRESHOLD PRODUCTION**

### **5.1 Prospects of outsourcing in China**

This part of the thesis will go through the risk-management terms of outsourcing production in China Woodim Euroboard has, since the foundation of the company, been outsourcing the production of all its products. This is done because the demands of the Finnish door industry are of such products that demand immense facilities to produce. The case with thresholds is that they have been imported from Asia so far, because of the vast amount of raw material for threshold manufacturing. Centering production in Asia however creates a lot of risks that are not present when producing domestically or even abroad in a geographically closer country. At the moment, Woodim Euroboard has already started production at a Nanning-based threshold manufacturer. This chapter will look into the risks that are present in such production.

China, with 1,3 billion inhabitants is experiencing major growth, and thus it has become a major economical force. The following graph is from the World Bank Group database. World Bank Group announces China's GNI per capita as 1740 US\$ per capita, and the general income level to be lower and middle income. The ranking are conducted by WBC:s ranking system that changes on yearly basis.

Table 2: World Bank Group's ranking on China © WBC Group

Ease of...	2006 rank	2005 rank	Change in rank
Doing Business	93	108	15
Starting a Business	128	141	13
Dealing with Licenses	153	151	-2
Employing Workers	78	77	-1
Registering Property	21	21	0
Getting Credit	101	117	16
Protecting Investors	83	114	31
Paying Taxes	168	169	1
Trading Across Borders	38	35	-3
Enforcing Contracts	63	59	-4
Closing a Business	75	69	-6

Table 2 represents the facts already mentioned before. China is ranking exceptionally well on doing business, starting a business, getting credit and protecting investors. These are all signals of China experiencing tremendous growth. These are also reasons why western investment has been flowing to China for years now. However, China doesn't excel in for example trading across borders and dealing with licenses, also really important factors to foreign trade. It is evident that China is putting great effort on rising up the grid in terms of protecting investors, since the rank gain has been the best there. However, other poorly ranked stats such as paying taxes and dealing with licenses have experienced little to no growth what so ever.

Concluding, China is basically experiencing growth in all areas. This table is displaying the ease of doing certain action in Chinese ground for a foreign company, and all the right stats are facing upwards from a company like Woodim Euroboard's point of view. There is of course the slight downwardness with the trading across borders, but in that stat China already has a far better rank than in the other stats.

Table 3 (Woodim Euroboard's preferred stats in a producer)

Quality	5
Price	3
Production maintenance	2
Fast deliveries	4
Working communication	1

This graph represents the emphasis that Woodim Euroboard has towards different elements required from the supplier with a higher number representing more emphasis, and a smaller number representing smaller emphasis. The graph clearly shows that Woodim Euroboard expects the producer to do good quality products at a fast pace. However, matters such as working communication and production maintenance play a smaller role in Woodim Euroboard's production strategy. This is undoubtedly a sign, that makes China a suitable production country. However, fast deliveries are also represented as the second most important issue when selecting a supplier. This would be a sign of leaning towards a closer supplying country. However, it can also be assumed that as Woodim Euroboard has always bought their thresholds from Asia, that they want fast delivery times in such terms that the production country will undoubtedly be an Asian one.

## **5.2 China as a production country**

“Country economic risk is analogous to business or operating risk. It refers to the volatility of macroeconomic performance, which is often measured by real gross national product (GNP) or real gross domestic product (GDP)” (Clark, Marois, 1996).

The macroeconomic performance of China has been tremendous during the past few years, resulting in an average of 10 per cent per year rise in real GDP alone. This, along with the very low amount of political risk, makes China a prime alternative when selecting a production country.

As Woodim Euroboard has always considered Asia to be the prime source for thresholds since its foundation in 1995, it was only logical that they would eventually venture in to Chinese ground in search for a supplier. There were doubts in the beginning from Woodim Euroboard’s behalf of the availability of suitable natural resources, namely lumber, for adequate quality with the thresholds, but it seems that China, albeit not a country with immense forestry in terms of hardwood, seems to hold enough lumber for effective production of thresholds to be possible. As thresholds pose no requirements for it to be constructed out of a single piece of lumber, different techniques such as gluing several pieces of wood together seem to work fine with the production, and this sort of technique seems to be in use in Chinese factories.

Currently the production facilities are located in Nanning, which, albeit not being the ideal location logistically, the lumber and additional resources for threshold production are within reach, and while the production facilities are in Nanning, the thresholds will be transported in to Shanghai for shipping with the company’s own logistical ways, which, while making the situation easier for Woodim

Euroboard as the transporting is more secure this way, also contributes to the already long delivery times.

### **5.3 The Chinese Supplier**

Woodim Euroboard is using a large-sized company with several factories all over China. However, partly due to the anti-transparent nature of Chinese business culture, and partly due to the reluctant attitude of the company's personnel towards handing out "business secrets", the accurate number of the factories, and for that matter, the total number of the company's employees could not be presented. It is, however known that due to the deliveries they make to Korea and North America that consist largely of wooden floors and doorjambs that they must have several production facilities, since the requirements for doorjamb and wooden floor production differ greatly from requirements for threshold production.



Figure 7 (The location of the supplier on the map of China, and the location of the port where the goods will be shipped (Shanghai) © www-chaos.umd.edu)

As seen in figure 7, the company produces the thresholds in Nanning, and then transports them roadways to Shanghai. When questioned about this arrangement, the producer responded that they have better machinery in Nanning that is suitable for threshold production. Also, different tools and other equipment can, according to the producer, be acquired more easily from Nanning than any other of their establishments. The biggest reason for production in Nanning is, however, the amount of raw material that threshold production requires. Nanning has a semi-tropical atmosphere and lumber resources in such trees that are suitable for threshold production are plentiful.

The company does, however, do business with Korean and American counterparts, to which the company produces various wooden components, mainly wooden floors and door jambs. This is a sign of routine when it comes to overseas trade, and it has, according to Woodim Euroboard, been a major bonus when doing logistical planning with the company compared to a company that has never operates overseas. This also seems to affect the ways the supplier handles the payments. There seems to be great emphasis on the fact that the payments are handled via on sight letter of credit. This is a payment method that Woodim Euroboard regularly uses in Asian trade, so no arguments have been had in that part.

As mentioned before, the supplier used in-house logistics to get the thresholds from Nanning to Shanghai for shipping. This was a major part in the selection of the supplier from Woodim Euroboard's part. Although later on it was discovered that the supplier has found out that the most suitable way to get the thresholds from Nanning to Shanghai is by far, rail, and thus, the use of in house logistics, in this case, trucks, have been discarded. Other issues included the overall affordability of the thresholds in comparison to other threshold suppliers currently used by the company. Woodim Euroboard was also prepared for as high reject-numbers as 50%. This was because they already have a threshold producer who is handling a major part of Woodim Euroboard's threshold intake. The supplier is currently only used for production of such thresholds that are easier to produce, or do not fit into the schedule of the main supplier in Malaysia.

#### 5.4 SWOT: The Chinese supplier.

Conducting a SWOT analysis of the supplier is, given the fact that facts are really scarce, really difficult. However, material and information gathered from Woodim Euroboard acts as the basis of this analysis. It can not be said that the SWOT analysis is entirely accurate, but it's based on the information at hand. In Chinese business culture it's considered not suitable to give out any information about your company, apparently even when in a seller-buyer relationship.

It was also unclear whether the company produces a part of the thresholds in a different location, since there were clear changes in product quality between 2 different threshold models. The supplier then suggested that a part of the thresholds were actually produced in another factory, but its whereabouts were left unclear. The SWOT analysis is conducted assuming that the thresholds are produced in a single or 2 factory setup in Nanning, China.

Table 4 (SWOT Analysis of the supplier)

<p><b>Strengths</b></p> <ul style="list-style-type: none"> <li>- Price level is affordable</li> <li>-Good production facilities</li> <li>-Good raw material resources</li> </ul>	<p><b>Weaknesses</b></p> <ul style="list-style-type: none"> <li>-Poor English skills</li> <li>-Far away from major ports</li> </ul>
<p><b>Opportunities</b></p> <ul style="list-style-type: none"> <li>-Widening the scale of thresholds produced</li> <li>- Producing other wooden products</li> </ul>	<p><b>Threats</b></p> <ul style="list-style-type: none"> <li>-Labor force shifting towards the coast</li> <li>-New supplier better equipped for overseas trade</li> </ul>

The biggest strength with the supplier is obviously the price level that has been a major factor in Western companies shifting their manufacturing functions in China. This is also the case with Woodim Euroboard. Production facilities have also been said to be adequate by Woodim Euroboard. The information that was received

about the production facilities in general was really scarce, whether if it was considering the amount of production facilities, nor the production equipment. The producer also has excellent raw material resources. As Nanning is supposedly of sub-tropic atmosphere, the supplier can easily acquire lumber suitable for threshold manufacturing. This lumber has no specific requirements, apart from the ability to take extreme usage, and its ability to be lacquered as to resemble teakwood or similar hardwoods. This seems to be no problem to the supplier. The supplier also uses a technique quite unconventional to thresholds manufacturer; they glue several pieces of wood together with a special glue that no specifications were available of. However, this technique allows the company to sell at a more affordable price, since it allows smaller pieces to be glued together to form one threshold. Also, the thresholds often feature aluminum lining, but the producer hasn't seen this as a problem. In fact, according to Woodim Euroboard, they acquire the aluminum lining as in-house manufacturing, but this question, when asked, was quickly dismissed by the supplier as inquiring about business secrets. The bottom-line however is that the supplier should have no difficulties with production of thresholds, on paper.

The most obvious weakness is the lack of English skills. There is only one person who speaks English in the entire organization, being a female of middle/lower level management. As this hasn't sparked any real problems as of now, there's bound to be problems in the future. For one, reaching the English-speaking person can be hard at times. Woodim Euroboard has marked communication as one of the lesser-valued properties in a supplier, but however the managing director has already made 6 business trips into China, trying to explain the correct manufacturing methods and expectations of quality.

In opportunities there's the possibility of producing other thresholds for Woodim Euroboard. Currently the Chinese company is only producing one threshold model because the troubles in explaining details in the blueprints. If these

difficulties are overcome, and the quality is set right, Woodim Euroboard is prepared to implement several other threshold models. Also marked down as an opportunity, is the production of other wooden products. Woodim Euroboard has expressed interest in also other wooden products, such as custom-made door components, but due to the language barrier, these plans have not proceeded past the preliminary phase.

In threats, the shifting of the labor force is marked down. This is a major issue in China generally, and with the supplier holding premises in a relatively remote region, the capable labor force can seek work closer up the coastline, closer up to special economic zones, where the pay is better.

Also marked down in threats, is the threat of a new supplier better equipped for such trade. Nanning isn't actually the business centre of China, and despite the supplier having business into U.S.A and Korea, the fact still remains that doing business with a company that only employs one English-speaking employee does not categorize it as being well equipped for overseas trade, no matter how capable the person might be.

## **5.5 The current situation**

Woodim Euroboard is set to buy thresholds off the Chinese supplier on a monthly basis. The ideal situation would be such that Woodim Euroboard announces the thresholds they need, and they are produced and shipped out so that there will be about 1 month in between the order and the shipment. Also, an ideal situation would result in as little rejected thresholds as possible. The amount of rejections should be kept as low as possible because Woodim Euroboard operates with clients that often use an automated production system that demands the flow of thresholds to be fluent. The thresholds would be transported rail or roadways to Shanghai for shipping, and from there on they would be shipped in 40 foot

containers on to Finland through a European port such as Frankfurt. Frankfurt is used currently solely because the supplier handles the logistical process entirely.

The optimal situation would also mean that the supplier would not raise their pricing level. The price issue has risen to be a deciding factor in past ordeals with threshold producers. At the moment the supplier is only producing 2 different thresholds and is shipping the same amount each month, but the ideal situation would also include that the supplier would be able to react to changes in the product lineup and would be able to start production of a new model of threshold shortly after receiving the plans.

The current situation is relatively close to the optimal situation. As the business relationship is only in the beginning, and not much is demanded of the Chinese producer in terms of product lineup changes, the business relationship seems to be acting out as planned. Woodim Euroboard likes to see the immense amount of rejection as a result of too hasty production and the over-excitement of the Chinese production, and sees that these problems will be fixed when the business relationship evolves. However, implementations of new threshold models have been started, and it is unknown whether the producer is capable to include new models into the product lineup with just the help of blueprints and threshold models. The implementation is expected to require several visits to the site of production.

Woodim Euroboard has so far received 2 shipments of thresholds from China. which will be discussed further on. While there are some differences in the manufacturing of the thresholds, all models are still seemingly similar when it comes to design, and the largest differences are, counting off length, the sockets that connect the threshold to the doorframe, a property that is often specific to door manufacturers. In table 4.2.1 the 2 shipments are represented, and especially the major amount of rejected thresholds both of these shipments had. Thresholds A and B are basically the same threshold when it comes to design, but A is 10

centimeters longer than B. Thresholds A and B are produced for a major Finnish door manufacturer, and are high in demand on a monthly basis. Threshold C is a new model implemented only recently, and it is sold specifically to a medium-sized door manufacturer that uses only this single threshold at this specific length. Only the number of rejections and the type of thresholds are marked down as variables for this table, but it must also be said that the transporting of these thresholds was problem free. There were no delays what so ever with preset schedules, and the containers arrived at Woodim Euroboard's premises within the agreed timeframe, and there were no signs of thresholds getting damaged while transporting, and the packaging was also adequate.

Table 5 Shipments made from China to Woodim Euroboard

Shipment no	Type of thresholds	Number of rejections
1	A & B	A 0 %, B 40 %
2	C	20 %

Table 5 represents the shipments received so far from the Chinese supplier. The current situation indeed still poses way too much reject thresholds, but according to Woodim Euroboard, they were prepared for as high rate of rejections as 50%, so this isn't considered an entirely bad result. Also, the rejections of threshold B have been told to have been produced in a different production facility from threshold A. However, currently the Chinese producer is used only as a secondary threshold producer to the main producer operating in Malaysia. The 2 shipments have posed results that have been "to be expected" according to Woodim Euroboard. Although they aren't entirely satisfied with the performance of the supplier, they do not seem that shocked by even 40% rejection rate in threshold B.

## 5.6 Risk assessment on China

The basis of the risk assessment is to map out the risks that are present in the process that goes on after an order has been placed and the production started. It is also assumed that all of the thresholds are produced in Nanning, or neighbouring cities, albeit direct answer was not received whether this is true or not. The risk assessment is done by first analyzing the issues that have appeared during the time Woodim Euroboard has ordered thresholds from China. Second, a source and scenario analysis is done. And third, a table of risks and their chance of occurring is done. Such a business, which involves a great deal of logistics, is bound to be influenced by the logistical risk already present in even intra-China trade. The infrastructure isn't up to date with today's requirements, which appears as poorly conditioned roads and rail tracks.

With people moving towards the eastern coast in search of work it shifts the government's development-scope towards the coastline and the inland transport infrastructure is left seemingly unattended. With these facts at hand, it is safe to say that the risk in Chinese inland transport is immense. The producer in this case uses railroad transport because the immense weight of the goods and that is generally considered the right alternative, especially concerning the hazardous 50% overloading the truck companies often do in China. But even with the usage of rail transport, the risk is still huge. While the risk isn't on Woodim Euroboard's side financially in intra-Chinese transport, the financial damage of losing an entire container because of a railroad accident would be enormous. Woodim Euroboard would be left without thresholds for another month, and the information about the possible accident might not reach the supplier and thus Woodim Euroboard in a weeks time, due to poor delivery-tracking system currently in a very poor state, albeit in development, in China.

The tracking system is seemingly poor, especially when it comes to administrating the shipments, and their current position. In this case the shipments are sent from relatively far away, through several provinces, to the port of shipping. If anything should go wrong during this trip, there would be almost no way of finding out what has happened to the shipment, largely because of the already mentioned communication difficulties with the producer, and largely because the producer is unlikely to know about the position of the coast bound wagonload of thresholds.

Probably the most important thing in this case is the immense distance that the products need to travel inland before they can be shipped. The production facilities are located in Nanning and yet the deliveries are made from Shanghai. This alone is really risky. With above-mentioned poor condition of the road and rail network, the smaller the distance inland, the better. The producer insists that the shipping is made from Shanghai, because the producer has a factory/warehouse there, which will cut down on logistical costs from their part.

This is reasonable, considering it lowers the end price for Woodim Euroboard. However, this factory/warehouse is of little use to Woodim Euroboard, since there is no transaction with the warehouse in terms of when the shipment is ready to go. All information is looped through Nanning and doing so, it usually takes a few days for the information about the shipping to reach Woodim Euroboard. The question why doesn't the producer allow communication between Finland and Shanghai remains unanswered. Woodim Euroboard is using air freight services in tight situations if a customer needs thresholds in a 5 day interval instead of the 1 month waiting period they have when the thresholds are transported seaways. This is impossible without an effective communication link between Finland and Shanghai. It can be argued that this could be done by first contacting Nanning and telling them to ship threshold model X airways, but in reality, as the company only employs one person who understands English, this is impossible.

The logistical risk doesn't only amount to inland transportations. Albeit overseas transport is relatively low in terms of risk, but usually the hazards happening with overseas transportation also pose greater losses financially. Overseas transport also, when used with such huge distances, is really risky in terms of delivery times. There might be moments when a certain product is needed on a 1 week interval instead of the 4 weeks a ship is going to take to get from Shanghai to Finland, and there's no way of getting into the container while its traveling. The risk level is the same for any countries in Asia, as the distances and the time it takes for a container to reach European ports, is evidently the same. Woodim Euroboard acknowledges this risk, as transaction with various Asian counterparts, namely Thai and Malaysian, have been done with the past and overseas transport has always been seen as the safest and best option for threshold transportation.

The possibility of using the Siberian railroad tracks was also quickly assessed during the means of transportation –discussion, but it was quickly dismissed due to the fact that Nanning is located near the Vietnamese border, and the Siberian railroad track would pose to be too expensive. This in mind, both of the parties were more satisfied and comfortable with seaways transport.

Also, the cultural risks are a major part of the risks occurring in such a business. To begin with, only one person of the entire (estimated) several hundred people –employing company knows English. Woodim Euroboard handles all of the business directly through this person. This has led to problems with production. During the production of the 2 shipments Woodim Euroboard has received from China, several 2-week visits have been required to China to solve some, sometimes pretty simple, issues with threshold design and other issues that could have been easily resolved via phone or email, without the language barrier.

Also, amounting to the cultural risks is the immense amount of rejects the company has produced during the time. With 40% rejects in the first shipment and 20% in the second shipment, it can be safely assumed that the labor force isn't capable of production at a steady level. Woodim Euroboard revealed that during these business visits, the producer's machine base was found adequate, and production of the thresholds would not be an issue. However, every time they receive a shipment from China, a large amount is of no use. It was first suspected that the thresholds break down in transport, but since the crates were found intact, it was evident that poor production was the reason for the amount of rejects.

The rejected thresholds were inspected after they were rejected by the door manufacturer they were sent to, and it was found out that most of the problems with the thresholds came down to them being slightly curved. A fault invisible to the naked eye, but one deeming them useless to the door factory they were ordered by.

The managing director of Woodim Euroboard said in an interview that he got the feeling the Chinese producer was trying to learn everything too fast, and directions and remarks about the blueprints, often important ones, were acknowledged by a swift "yes, yes", while in fact, the level of quality demanded by Woodim Euroboard was still, obviously, a mystery to the producer at that point. Although Intellectual Property Rights risks are not really applicable to such custom products, still it seems that production of the thresholds was largely handled not according to the blueprints and specifications, but more to imitate the original threshold samples given to the producer. This assessment might seem harsh, but is done because all of the thresholds seemed perfect to the naked eye, but yet in a test of true craftsmanship, they failed. A thing very common among Chinese infringed products. Of course, with thresholds, it would be out of line to talk about infringements, but the differences between the quality of the 2 producing factories give a hint of such activity.

Now that the scenario and the production details have been explained, we can map out the risk sources. This was done by examining the data received from Woodim Euroboard and combining it with the likely and not so likely, albeit risky, events that might occur during the transport and production. This was done by analyzing statements given out by Woodim Euroboard and the low amount of data received from the supplier. In the following table, the risk sources are mapped out, receiving a score that reflects the intensity of the risk (Table 6).

Table 6: Risk source analysis on the Chinese supplier

Risk source	Risk level (1-5, 5 being max)
Manufacturing department	5
Management	4
Logistics (Nanning-Shanghai)	3
Weather conditions	1
Environmental issues	2
Other	2

“To prioritize, administrate and compare risks, measurement is needed. Probability, or chances of occurring are the prime properties of a risk” (Hallikas & Pulkkinen, 2001). In this case, a 5 point system of used, where 1 marks a low chance of occurring and thus a low risk rating, and 5 marks the highest risk rating possible.

The reasoning behind the manufacturing department receiving such a high risk rating is the sole fact that the high amount of rejects Woodim Euroboard received during the first 2 shipments could not be explained by the manufacturing. As Woodim Euroboard has stated, the company has really good machinery for thresholds production, so that shouldn't be the case. This leaves us with the conclusion that the machine operators lack the needed skills for constant high

quality threshold production. This is why they are also marked down as the highest risk source in this operation. The producer has stated that they use 2 different factories for production of different kinds of thresholds. This has been explained to Woodim Euroboard by the manufacturer by stating that manufacturing of different lengths of thresholds requires machinery that are only available at these specific factories. However, when complaining about the quality, Woodim Euroboard received a statement that the production could easily be moved to the factory that producer lesser amount of rejections. These sort of crossed statements are a sign of unreliability, relating to both the management and the manufacturing.

The second highest risk is the management of the producer. There is no-one who speaks English in the management, so the only possible way to contact the management is via the contact person. This creates various risks, because all of the new plans and blueprints that need to be given to the management first need to be translated by the contact person, increasing the risk of something getting lost in translation. The core reason for the management's high risk marking is the lack of information. As many companies in China, also the supplier sees it fit to reveal as little about itself as possible. Woodim Euroboard's visits on the production site have been relatively brief, and very little information in general is given out about the company itself in terms of number and general data. This seems to be the way of operation of Chinese companies, especially in the inland. This is really risky for Woodim Euroboard, as they can't do effective risk management planning without knowing for example the size of the company. During the time of research an accurate amount of premises in China, nor an accurate amount of employees could not be presented, even after rigorous amounts of attempts.

This is of course extremely risky. The company could go bankrupt at any moment, or the contact person could be moved to another unit in China, leaving Woodim Euroboard without a contact. Of course this would also affect the company's

businesses with the Koreans and Americans, but it is assumed that these non-Chinese companies either operate with a translator or a hired Chinese-capable buyer, or they operate with another section of the company, other than the one operating in Nanning. This assumption is made on the grounds of negotiations with Woodim Euroboard, where they mentioned that the translator doesn't seem to have any other foreign connections than the one with Woodim Euroboard, along with the fact that most of the English vocabulary relating to wood working, was totally new to the translator/contact person.

The logistics functions between Nanning and Shanghai have received a 3. This is because first of all, the distance between the 2 cities is immense. There is no visible reason of first transporting the products to Shanghai, apart from the warehouse the company has in Shanghai. However, usually the shipments are, according to Woodim Euroboard, handled so that when the Chinese supplier gets all the products done for a container, they ship them to Shanghai and load them on to the ship without even overnight warehousing. This would make the usage of the warehouse in Shanghai questionable, as it has no real meaning in the logistical equation. With the questionable condition of the Chinese transport infrastructure, it is safe to assume that the smaller distance the goods travel within road boundaries, the safer.

The weather conditions receive such a low risk largely because of the low probability of the weather conditions having effect on the logistical functions. Admitted, China goes through some altering weather conditions during the year, but in general, the weather seems to be suitable for road and rail transport, as Nanning is located in southern China, which does not normally experience any high alterations in weather. However, because of the unreliability of weather conditions in general, it receives a 2, because weather conditions in a country with such a huge landmass always pose greater risk than in a country with lesser land.

Environmental issues are also marked down as a risk source. This is mainly because of raw material issues. Chinese business culture aims to not show any negative issues facing the company. Woodim Euroboard has experienced raw material shortages with threshold supplier in the past, which have always lead to price of the product increasing immensely. China is not a country with huge natural resources in terms of lumber, but still the supplier says to have unlimited resources when it comes to raw material. This kind of statement needs to be taken with precautions, and as raw material resource pose as a threat in such a lumber-rich nation as Malaysia, they are bound to affect China also. It must be noted though that the Chinese supplier constructs the thresholds from several pieces instead of the Malaysian manufacturer's one piece method. Despite the raw material, of course China is facing other environmental issues also. The non-existent garbage handling system and the recycling of waste is bound to rise as an issue in the future. The government is receiving pressure from international organizations to tighten the environmental regulations for better nature reservation, and when these regulations are tightened, it is unclear whether production will be as affordable anymore, with increased costs from waste handling. Under "other" are basically gathered all other issues that could occur in such a business transaction. These are basically problems with customs procedures or other bureaucratic procedures common in. The possibilities of these kinds of issues surfacing are quite low though, since the local supplier handles all issues concerning inland transport and customs. Also, a scenario assessment is in place after the sources are known. The scenarios are an estimation of the most common risks source –related scenarios that will have occurred and will occur in the future with the Chinese supplier. The scenarios are based on Woodim Euroboard's experiences, and analysis made on the supplier, in addition to factors that are likely to occur in China. The use of a such analysis helps in minimizing hazards such as ignorance of counter-measures. (Oyama 2006)

Table 7: Risk scenario analysis on the Chinese supplier

Scenario	Occurring chance (1-5)
Manufacturing of faulty products	5
Problems with communication	5
Problems with shipping	1
Problems with inland logistics	3
Weather condition hindering transport	1
Problems with tracking shipments	4
Raw material issues	2

Table 7 illustrates the most probable scenarios to occur. The first scenario that is bound to occur and has occurred both times after the business relationship was started is obviously the manufacturing of faulty products. The supplier hasn't yet grasped the idea of threshold manufacturing, and the quality terms that Woodim Euroboard expects. This, so far, has led to several losses from Woodim Euroboard's part, but the most severe reason for the production faults getting such a high score, is the fact that if Woodim Euroboard shifts to Chinese production entirely, they won't have a backup supplier anymore, as they do now in Malaysia, so they won't be able to take even 5% of rejects.

Problems with communication have also received a 5. Woodim Euroboard doesn't emphasize communication too much but the fact that any information about the true size and amount of premises of the company is enough a reason to suspect that communication isn't at the level it should be in such a business relationship. More effective communication would also cut the amount of business trips the managing director has to do to the production site, which, in a 4-person company would be bound to increase effectiveness.

Problems with shipping have only received a 1, because the shipping agent the Chinese supplier uses, is already a known one for Woodim Euroboard, and is also in use by the Malaysian threshold supplier currently in use. The experiences with this shipping agent have been generally positive and no real problems have ever occurred. Naturally there's always a risk in shipping, if the ship should sink or something else should happen that would render the goods unusable. Thresholds are, however, not easily perishable and the packaging it demands isn't that complicated and the thresholds can be shipped without much concern about the packaging. Also humidity always present in shipping is not a problem since heavily lacquered thresholds, manufactured of hardwood, will not take in any humidity and will not be affected by mold.

Problems with inland logistics rise to a bigger role as a scenario. Of course, the poor logistical infrastructure of China is the main reason here also. Although ever-developing, the infrastructure still can not handle the challenges of increased traffic outside the Special Economic Zones. Nanning-Shanghai isn't the busiest of all rail track lines in China, and can thus be considered a risk, because the maintenance intervals are bound to be bigger than with busier tracks, not to mention the long distance between the cities. As earlier mentioned, the internal governance of provinces is often not so friendly towards traffic arriving from outside that specific province. Although this hasn't been experienced in shipments made thus far, it must still be considered as a risk. The supplier is using railways transport to get the goods from Nanning to Shanghai. While threshold packages are not easily perishable, they can still break if mistreated. The personnel working in the rail yards must also be considered a risk because of the bulk-nature of good often transported in Chinese railways the staff might not be as familiar with such packaging.

Weather conditions have received such a low rating because even with the ever-changing weather conditions in China, and the high variance in altitude along the way from Nanning to Shanghai. However, China's railway system can be considered to be the most reliable inland transport mode in China, with the roadways transport mode still taking its first baby steps if measured in terms of modern day performance, and railways transport is bound to be influenced less by weather conditions than roadways transport. Although it must be mentioned that the supplier handled the first shipment by transporting the thresholds by road and the experience was generally positive, and the weather conditions, albeit being quite unpredictable, proved to pose no threat to the scheduling of the transports. The eventual reason for changing to rail was the costs that were substantially cut by the change. As result, it could be said that weather does not hinder the scheduling of the transport and thus does not prove to be a major risk.

The tracking of shipments, a problem that was already mentioned earlier, is also included in this scenario analysis. The problem with tracking shipments has not been a major issue for Woodim Euroboard, and they have not done a lot of tracking in the past. However, this has lead to uncertainty of arriving shipments, and a lot of occasions where there has been no information what so ever of when a shipment of for example thresholds is going to be shipped. While there is always up-to-date information available about the state of the shipments after the goods have been boarded, information flow about the goods before shipping has been really scarce. Often the Chinese supplier announces when the goods leave Nanning, but the true shipment date from Shanghai might be weeks from that announcement. This will eventually pose as a risk, since Woodim Euroboard's before-mentioned will of using air transport as an emergency tool for shipments that are running late, will be hindered by lack of information of the inland transport's state.

Raw material issues have also been marked down as a relatively low-risk scenario. This is because Woodim Euroboard has experienced such problems already in the past, with the Malaysian supplier, which eventually led to extreme price level rise. China is experiencing major economical growth, which will and has led to extreme demand in raw material in all areas. Although the raw material requirements of threshold production are not as demanding because of the gluing technique, there can still be shortages which, with the current communication style, won't be notified of until it is too late.

As a conclusion it could be said that the majority of the risk sources and scenarios amount to the thresholds company's production capabilities and the ability to communicate with the manufacturing department. The risk of faulty products being produced is the highest one, relating tightly with the communication with Woodim Euroboard, the management and the manufacturing department. The transport part also provides numerous risks, but they are more related to time, rather than money, since the producer handles all freight-related costs and thus also the risk. China's poor logistical infrastructure is the reason for these risks, and while it is improving at a surging speed, it will still pose risks for years to come. Especially with this kind of transport happening from a more remote inland zone to Shanghai, a special economic zone, the risks are always more numerous than with transport in more widely used areas.

#### **4.7 Risk analysis on China**

This part of the thesis will analyze the risks presented in the previous chapter, and determine what sort of threat these risks pose to the business and what does the situation look like for Woodim Euroboard.

Generally, China is a country where the risk level is generally high. Antti Sillanpää argues that a company's own willingness to risk taking determines the environment in which it can act (Kuusela & Ollikainen 1998). This is especially true with Woodim Euroboard. Since the foundation, Woodim Euroboard has directed the manufacturing of such products as thresholds with relatively cheap manufacturing costs, towards Asia. The company has decided that only the manufacturing of complex products such as HDF boards should be done in Europe. This is done because these low production costs in Asia outweigh the better communication levels available in a closer up production country.

Woodim Euroboard's current ventures in China have been shadowed by poor product quality, and lack of information flow in almost every aspect. The manufacturer is excited about producing thresholds, and possesses the needed machinery and has produced doorjambes and flooring in the past. Yet several visits are required for explanation of relatively simple production details. The contact person's English skills are not up to par with the level required for effective communication of detail-intensive production details. There are all facts that speak for searching another supplier. However, Woodim Euroboard's willingness of risk taking is seemingly high.

The highest amount of risk relates to the production meeting the required standards. The quality standards are obviously not entirely clear to the supplier, and the Chinese producer is still far away from quality standards Woodim Euroboard expects from its main supplier.

Leaving manufacturing aside, the rest of the problems appear in the logistics sector. First of all, the huge distance between Nanning and Shanghai seems ridiculous. With no special reason given for transporting the goods to Shanghai before shipping than the warehouse located there, it can be assumed that the company does this because Shanghai is used as a shipping port with their Korea and North America –contacts. As mentioned before, it would be better for Woodim Euroboard the shorter distance the goods travel via land. This because, first of all, the lacking tracking systems of local logistics providers are a liability to Woodim Euroboard, often operating with low amounts of safety stock in thresholds because of production capacity. Information about threshold shipments would be crucial already before they are shipped from Shanghai.

As a conclusion it can be said than the risks present it China for Woodim Euroboard are largely cultural. Action needs to be taken to ensure better communication with the producer to prevent excessive amount of rejected thresholds that have been a standard of at least 20% in shipments so far. Logistically, the risks lie in unreliability in delivery times. There is a logistical risk present, but as the supplier handles the shipping, this only contributes to delays in delivery times for Woodim Euroboard's part if a shipment might break down before or after shipping in Shanghai.

## **6. PROSPECTS OF CHANGING THE PRODUCTION COUNTRY**

### **6.1 Selection of alternative production country**

Woodim Euroboard has mentioned in interviews that they have always mapped out the production country according to the raw material resources nearby, without much emphasis on the controllability of production. With thresholds however, they were eager to know whether production in would be possible in a closer country, with reasonable production expenses. This effectively left out a large portion of Scandinavian countries, with Estonia rising up as competitive alternative. Estonia's real GDP growth rate shows as a good 10% in 2006, similar levels to China.

### **6.2 Estonia's prospects**

Woodim Euroboard was interested in shifting at least a part of the production to Estonia because of logistical reasons, and this part of the thesis will deal with the risks that such an ordeal would produce. Estonia is, obviously, separated from Finland only by the Gulf of Finland and thus offers an excellent location logistically. Also as a hypothesis, the language barrier would not prove to be such big an issue with the Estonians, as Finnish is largely understood among the exporting companies, at least in Woodim Euroboard's experience operating with Estonian woodworking companies.

Woodim Euroboard is also interested in the production maintenance capabilities of production in Estonia. The current situation with Asia makes it hard to do any maintenance during production. With Estonia, business trips would be much shorter, and could be done during a single day.

Table 8: World Bank Group's ranking of Estonia

Ease of...	2006 rank	2005 rank	Change in rank
Doing Business	17	17	0
Starting a Business	51	50	-1
Dealing with Licenses	13	13	0
Employing Workers	151	151	0
Registering Property	23	23	0
Getting Credit	48	41	-7
Protecting Investors	33	33	0
Paying Taxes	29	25	-4
Trading Across Borders	6	5	-1
Enforcing Contracts	20	20	0
Closing a Business	47	46	-1

As can be seen from table 8, Estonia has good rankings in relatively all of the stats, with trading across borders and ease of doing business rising as the best ones. This is to be expected, as Estonia has experienced major growth since it left the Soviet Union. The World Bank Group categorizes Estonia to be in the upper middle income class, which reflects to the high ratings in relatively every possible stat. When comparing to China, it can be seen that Estonia ranks the highest in every part except for “employing workers” which isn’t going to be of Woodim Euroboard’s concern. The difference is somewhat expected, since Estonia ranks at 9100 US\$ GNI per capita against China’s 1940. The difference is immense, but so is the expected difference in production costs also.

Before comparing production in Estonia to production in China, it’s imperative to say that Woodim Euroboard has never produced thresholds outside Asia, and has been really satisfied with the results. However, communication issues along with the fact that a closer production facility would benefit the company in the form of quicker deliveries and better production maintenance, made Woodim Euroboard curious about their options.

It must also be said that no analysis could be made on the price level of Estonian production, since the product is a custom made one, and price estimates would have needed blueprints and further investigation on the product. Also, sample thresholds would have been needed to produce and excessive testing would have been needed to determine whether the thresholds can take enough punishment. It is also unclear whether Estonian (or an easily attainable) wood could be used, but the requirements of threshold-using door factories usually state that the lumber needs to handle hardwood-like pressure. Because of these facts, it's suspected that the lumber would need to be brought in from a country that sells affordable hardwood. Also, no specific producer could be chosen because of above reasons. However, a swift survey of the market revealed that there are several factories that operate either in the business of doorjamb or wooden floor production, which have similar requirements to threshold production.

Estonia was chosen because of its close location and the fact that while the production is affordable, Estonia is an EU country which eases the customs procedures from Woodim Euroboard's part. At the moment there are sales made to Estonia in the form of HDF boards for door production, but no thresholds are sold to Estonia. In Estonia's case, apart from China, the business would be handled with Euros or Estonian Kroon. Woodim Euroboard's representatives said in interviews that this is not going to be a problem, since a lot of their Central European suppliers use Euros and they do not desire to do only EU/US dollar trade, although this is, considering the exchange rates, preferred at the time of the research. It must also be mentioned that the Estonian currency, Kroon, is pegged to the Euro at 15.64664 Kroons to one Euro. This, suspecting that trade will be handled in Kroon to Euro, reduces the currency risk greatly for Woodim Euroboard. With China, currency risk was not taken in to account since all of the transactions are done with dollars, so the risk wasn't country specific with the currency.

As mentioned before, because of the custom nature of the product, a supplier could not be chosen. However, a large amount of Estonian woodworking shops seem to be located near the coastline and Tallinn. This is the optimal location logistics wise, because all of the deliveries would be made seaways, with the operating ports being most likely Tallinn and Helsinki. The risk assessment and analysis is conducted by assuming that the supplier would be close to the coastline. This is a relatively safe assumption, not only because the majority of the producers seem to be located so, but also because Woodim Euroboard has mentioned that if production of such sort should happen, ideal logistical location would be one of the first items on their requirement list.

### **6.3 Risk assessment on Estonia**

Because the risk assessment for China was done largely on the basis of already ongoing ventures, the assessment for Estonia will be a briefer one, concentrating largely on the general country-specific risks a company operating with an Estonian producer will face, and more specifically the risks Woodim Euroboard will face if it starts production in Estonia. It will be based on comparison between the risks occurring in China and Estonia, and a further on analysis of country-specific risks occurring in Estonia.

Basically, the same source and scenario analysis will be done than the one with China, but without the deep analysis of the country specific risks in general, but rather concentrating on the issues that generated the most risks in China, and comparing them to Estonia.

Table 9: Risk sources in Estonia

Risk source	Risk level (1-5, 5 being max)
Manufacturing	2
Management	1
Logistics	1
Weather conditions	1
Environmental risks	1
Other	2

Table 9 describes the risk sources present in Estonia. The sources are the same ones that were marked down for China, and this analysis acts as a comparison. The risk with manufacturing department being so low is solely because the communication is expected to be far better than it currently is with the Chinese supplier. A large portion of especially export-oriented Estonian companies know Finnish, and if their Finnish is not up to par, English can almost always be used anyway. Because of this, production maintenance is also expected to be much easier than with the Chinese counterpart. There is, however going to be difficulties if suitable lumber can't be found from Estonia. In this case, lumber will have to be shipped from foreign sources, and with the requirements for the lumber being so extreme, suitable raw material might be found no closer than Central Europe. The thresholds are preferably produced from dark hardwood which can be lacquered even darker to resemble teakwood or similar hardwoods. Such lumber is found in Central Europe and possibly from northern regions of Europe also, in the form of Mahogany and such trees, but the price level in these cases often rises above the price roof.

This would basically mean that raw material would have to be shipped from as far as Africa or Asia, and this would raise the cost and reaction time of production in Estonia considerably. These kind of assessments cannot however be made until Estonian lumber market is analyzed for suitable lumber. The fact however is that in Finland, hardwood thresholds are not produced from domestic lumber, because it is often too soft to take the kind of usage thresholds are put through. This in mind, manufacturing receives a 2, because of the expected unreliability with the raw material supply.

Management, a major problem with the Chinese company, mainly because the inability to communicate with them, will most likely also be within communication reach because of before-mentioned reasons. The business culture of Estonia is very much like the Finnish one, which would cause no issues like the transparency/information flow –one with the Chinese. Generally Estonia is very similar to Finland business culture –wise so it is expected that the communication and more specifically Woodim Euroboard's wishes concerning threshold blueprints, dimensions and other specific features of thresholds would be implemented without much concern. This would mean that a 2-week business trip could be replaced by a swift 2 day visit on the production site.

Logistics have also received a low risk rating. This is mainly because first of all, Estonia has an immensely sophisticated logistical infrastructure. The road network along with the rail one is in excellent condition, and the coastline boasts over 60 harbors. The logistical risks, when operating with such a modern system, are minimal. The deliveries from Estonia would not only be quicker, but also more easily manageable. The system Woodim Euroboard uses now with threshold production, namely announcing the thresholds they need in a monthly spreadsheet, could be changed to a more Just in Time –based system, given there would be enough raw material in Estonia. Woodim Euroboard isn't currently using a JIT based model with any of their products, but is sticking to rather large safety stocks.

This is mainly because none of the producers are located nearby, and the deliveries can sometimes be unreliable. With an Estonian producer, prospects for a JIT experiment would be optimal. This would also make warehousing easier for Woodim Euroboard.

Weather conditions, which were marked down as a risk in China, are also marked down here. Weather conditions usually are combined with logistical risks, but in they are assessed separated here, since this was done also in China's part, and the weather conditions aren't affecting the logistical risks as much in China-Finland logistics as in Estonia-Finland logistics, mainly because the ships that carry containers are not that vulnerable to delays caused for example by extreme wind conditions.

Weather conditions, especially in the winter, are a risk in Estonia-Finland traffic, since the weather can be really cold and windy, hindering traffic across the Gulf of Finland. In case of selecting Estonia as a production country, the deliveries would most likely be made by roadways transport, with the trucks loaded into the cargo bay of cruise ships. This would mean that if traffic across the Gulf would be cut down because of extreme weather conditions, there would be no way Woodim Euroboard would get their goods in time. This would, however, only pose as a problem if the before-mentioned JIT system would be taken to use, and it is generally not that common for traffic across the gulf would be cut down completely. This is the reasoning behind the low risk rating of weather conditions hindering transport.

Environmental issues have also received a low risk rating. It is unlikely that environmental issues will hinder the business ordeal, since Estonia is an EU country and thus environmental issues are bound to be of lesser trouble than with China, and the country generally embraces its reputation as an environment-aware one.

Table 10: Risk scenarios in Estonia

Scenario	Occurring chance (1-5)
Manufacturing of faulty products	1
Problems with communication	1
Problems with shipping	2
Problems with inland logistics	3
Weather condition hindering transport	1
Problems with tracking shipments	1
Raw material issues	3

Table 10 illustrates the risk source ratings for Estonia. The manufacturing of faulty products, the main risk scenario with production in China, is expected to produce way less risk with Estonia as a production country. With lesser distance between the companies, the maintenance of productions is deemed to be much easier, and frequent business visits could be done to the production site to guide the production more efficiently. Because of the absence of the language barrier, guidance on manufacturing of the products could also be directed to the manufacturers directly, in stead of using the management and translators as a mediator.

Communication problems are also expected not to rise as such a huge issue than with the Chinese. Woodim Euroboard stated that if they are going to start production in Estonia, one of the first properties in the producer they are going to use is going to be adequate Finnish or English skills, to ensure production of high quality goods.

Problems with shipping are also estimated to be low, since Estonia, as mentioned before, has a good logistical infrastructure which also amounts to dock facilities. Shipments are expected to be made from Tallinn, which is by far the largest port in Estonia. Infrastructure risk is generally low in Estonia. Inland logistics are also

marked down as a low risk ratio stat, because it is estimated that the possible producer of thresholds would be found from an area close to Tallinn, and thus the amount of road transport made would be as slim as possible, which would cut down the risk also. It is also expected that Woodim Euroboard would use a Incoterm that would leave the logistical procedures to the supplier, which would further on cut down the risk involving transport. Weather conditions mentioned earlier are also not expected to hinder the transport apart from occasions when traffic across the Gulf of Finland will be cut down, but these occasions can't be taken as high-risk, because the chance of occurring is relatively small.

The problems with tracking the shipments in China are also estimated to be non-existent in Estonia. Logistical service providers in Estonia are good in terms of tracking in terms of Finnish standards, and it is expected that information about the state of shipments would be received at steady intervals. Although tracking of shipments with such low distances is bound not to rise in such a commanding role as with business transactions made with China, it is still bound to affect the planning of for example Just in Time type of ordeals possibly being implemented in the future.

#### **6.4 Risk analysis on Estonia**

Estonia, when compared to China, is a much lower risk nation even with just comparing real GDP values. The logistical risk, a major issue when ordering thresholds from China, is almost non-existent when ordering from Estonia. Estonia boasts a highly developed logistical infrastructure, with good connections to both Central Europe, and to Finland through the Gulf of Finland. These issues speak for Estonia as a production country. Also, the communication issues are also expected to be non-existent when operating with an Estonian supplier. Finnish could undoubtedly be used as a business language, which would greatly decrease the risk of information getting lost in translation, leading to production of hundreds of faulty products.

It is unclear whether Estonian lumber could be used in production of thresholds. It is expected that it can not be used, because of the distinct requirements in lumber qualities. This would lead to lumber getting imported to Estonia from probably Africa or Asia. This would basically lead to Woodim Euroboard facing the same kind of challenges than with the Chinese supplier. This would mean that the same kind of risks would be present logistically than with the Chinese supplier, only this time regarding raw material, not the end product. It is also expected that such an ordeal would raise the pricing of the already expected-to-be expensive Estonian produced thresholds. Woodim Euroboard emphasizes price level to a great extent. It is expected that production in Estonia will be more expensive than production in China. It can, however be said about Estonia that the price level is not that prone to changes in for example in environmental regulations, as the price level in China.

Concluding, with Estonia, the risks of production are minimal. The same goes for logistical risks. Estonia has already gone through great reform, and can be considered as one of the world's top 20 easiest countries to do business in. Concerning Woodim Euroboard's production, the tradeoffs are more than visible. With Estonian production, the company would dodge many of the risks that are present with production in such a remote destination as China. The production would also be more easily manageable and differences in the organizational culture would not be as big, resulting in smaller amount of cultural risk. Also politically the country is no different from Finland basically. From a risk-management point of view, Estonia is a far better alternative than China, at least for a company with such small resources for risk management, as Woodim Euroboard.

## **7. RECOMMENDATIONS FOR WOODIM EUROBOARD**

Keep primary production of thresholds outside of China for the time being, until the Chinese supplier can produce steady quality of thresholds in each of the required models. Keeping China as a secondary production country for now ensures the careful development of production methods needed for larger scale production.

Market research needs to be done in terms of mapping out the supplier base in China. Albeit Nanning being a location that has good natural resources for thresholds production, but communication needs to be emphasized to the extent of mapping out the suppliers in the area capable of handling transactions in English without translators.

Hiring a translator with such high risks in cultural terms, would be paramount and would decrease the possibility of such high amount of rejects, and would also enhance the communication capabilities between the 2 companies, and also make it possible to cut down on business trips to the production site.

If possible, the distance that the goods travel on land could be cut down, first of all to enhance the logistical performance by shifting pressure off China's already crowded rail network, and secondly, to get the goods shipped from a closer destination to cut down on delivery time. There are many port cities, for example Guangzhou, that are close to Nanning.

If possible financially, Estonia should be considered a viable option considering thresholds production if raw materials can be acquired from close by.

## 8. CONCLUSION

China is a country on the brink of a tremendous business revolution. This creates instability in a lot of terms, and reflects upon risk management also. The risks present in China trade are numerous, but so are the rewards of a successful business relationship, a reason that has for years now attracted Western investment like wildfire.

Discoveries were made in all fields of risk management. Logistical, environmental, cultural, political and legal risks were mapped and the discoveries told that companies thinking of expanding to China need to be aware of specific risks on all the before-mentioned fields.

First off, China's logistical infrastructure was found to be out of date. Road and rail transport systems, while being the most popular ones, still lack standardization and tracking systems, often expected by Western companies, but considered a luxury among Chinese operators. In general, China's logistical network can be considered to be in a much better condition in areas where the government pushes investments, namely the coastline. Parts of the infrastructure receiving lesser amount of attention can be considered to be of higher risk.

Environmental risk in China was considered to be a ticking time bomb so to speak. The government is pushing major building developments, especially in Special Economic Zones (SEZ) to enhance competitiveness, almost always at the cost of environmental issues. Companies thinking of operating in China need to pay special attention to environmental issues, bearing in mind that China need to assess the environmental problems they are going to face in the future someday.

Cultural risk in China is a high one, already because the low amount of people being English-skilled, communication is bound to be difficult and the services of third-party translation services are recommended in almost any case. Chinese business culture is also a rather conservative one, revealing as little as possible can be considered a trend among Chinese organizations. Adoption of new production methods can also be challenging, if not because of language barrier, then because of old methods always considered to be better.

With political risks the situation is considerably better. The Chinese government is embracing foreign investment and the risk of facing difficulties politically is relatively small. Naturally, careful research on local policies and laws needs to be done before investing in China.

All in all it could be said that the risks in China are manageable, depending on the risk taking willingness of the company willing to invest. For a company that is willing to face the challenges of unreliable logistical infrastructure, and somewhat eccentric business culture, China will bear fruit in the form of low production costs and cheap labor.

This thesis set to analyze the ongoing business venture of Woodim Euroboard, producing thresholds in Nanning, China. The findings were largely following the same pattern as the facts presented in the above findings. The Chinese company was reluctant to cooperate, so the data extracted was largely collected by Woodim Euroboard themselves.

The findings suggested that the producing company has poor human resources for such trade, as only one English-speaking person was available in the entire company. The company also faced difficulties in producing steady quality in thresholds, which was determined to be a combined effort of poor production management and poor instructions. It was also found that the company does little

to no optimizing of the logistical chain, as the goods traveled ridiculous distances before finally being shipped. All in, the supplying company was determined to be extremely risky to order from, but also it was determined that by hiring a translator, the risks could be cut down on all grounds considerably. The plan was also to construct a base for a risk management plan, but with the surprisingly low participation of the Chinese company in the process, the goal wasn't entirely achieved.

As a conclusion it can be said that certainly the risk taking willingness of a company determines its operating environment, and thus its ability to operate on Chinese soil. The requirements and the ability of preliminary work is immense, but the perks that come with it are often worth the trouble. In this case, Woodim Euroboard is a company with a high risk taking willingness and high hopes in the supplier despite the almost 50% reject rates the company is currently producing. For a company expecting a lesser number of rejects, such business transaction can not, in any case, be recommended.

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Legal differences	法制差异	0	1	2	3
International treaties	国际合约	0	1	2	3
Other: 其它					

2. Political 政治因素

Trade barriers	贸易壁垒	0	1	2	3
Dealing with officials	应对政府官员	0	1	2	3
Government policies	政府政策	0	1	2	3
Political situations	政治环境	0	1	2	3
Other: 其它					

3. Cultural differences 文化差异

Language	语言	0	1	2	3
Communication	交流与沟通	0	1	2	3
Religion	宗教	0	1	2	3
Values and attitudes	价值观和态度	0	1	2	3
Manners and customs	风俗习惯	0	1	2	3
Other: 其它					

4. Environment 环境

Sufficiency of environmental protection	充分的环境保护	0	1	2	3
Sufficiency of natural resources	充足的自然资源	0	1	2	3
Pollution	污染	0	1	2	3
Level of technology	技术水平	0	1	2	3
Quality standards	质量标准	0	1	2	3
Other: 其它					

5. Transportation and logistics 交通与物流

Transport by rail	铁路运输	0	1	2	3
Transport by road	公路运输	0	1	2	3
Transport by sea	海路运输	0	1	2	3
Transport by air	空运	0	1	2	3
Goods lost or damaged in transport	在运输中物资的丢失或损耗	0	1	2	3
Transit times	过境时间	0	1	2	3
Transport regulations	交通法规	0	1	2	3
Communication difficulties	沟通困难	0	1	2	3
Logistics infrastructure	物流基础	0	1	2	3
Cost of transportation	运输费用	0	1	2	3
Inventory control	库存控制	0	1	2	3

Documentation and customs 文件证明及海关 0 1 2 3

Warehousing 仓储 0 1 2 3  
Other: 其它

### 3. Managing the risks 风险管理

Please select the best measures to manage the risks mentioned above. You can choose as many as you like, and also input your own measures.

请选择管理以上所提到的风险的最佳方式。可以多选，也可以输入你自己认为的方式。

#### 1. Legal 法制

- Careful study of laws and regulations  
仔细研究法律、法规
  - More international cooperation on legal issues  
在法制问题上有更多国际合作
  - Help from a third party 第三方帮助
  - Abolishment of legal restrictions 废除法律限制
  - Closer ties to legal entities  
与法人实体更加紧密地联系
- Other: 其它

#### 2. Political 政治

- Better understanding of political procedures  
更好地理解政治程序
  - Help from a third part 第三方的帮助
  - Closer relations with the government and officials  
与政府官员建立更加密切的关系
- Other: 其它

#### 3. Cultural differences 文化差异

- Increased level of communication 提高交流水平
  - More frequent communication 更加自由的交流
  - Studying of foreign culture 学习外国文化
  - Improved translation services 改善、提高翻译服务
  - Increased awareness of religions 提高宗教意识
  - Focus on ethics (rights of workers etc.)  
关注人权（工人权利等）
- Other: 其它

#### 4. Environment 环境

Participation in international treaties

加入国际合约

Investment on technology 技术投资

Focus on more environment-friendly production

注重更加环保的生产方式

New sources of resources 资源的新来源

Other: 其它

#### 5. Transportation and logistics 交通与物流

Improved communication methods 改善交流方式

Improved inventory management 改进库存管理

Alternate transportation methods 交替运输方式

Outsourcing 外包

Supply-chain efficiency 有效的供应链

Investments 投资

Other:其它

#### 4. Open questions 问题

1. In addition, do you have suggestions for the foreign company, what other aspects are important to consider when doing business with a Chinese company?

另外，你对外资公司在与中国公司做生意时还有什么重要方面应予考虑有无建议？

2. Also, if you have any other suggestions or comments to me personally, about this research subject or this particular questionnaire, please feel free to write them here.

如果你对我个人，对这个研究题目或对这次问卷调查有什么建议或评价，请不要有任何顾虑，把这些建议或评价写在这里。

Thank you! 谢谢!