

Fuel tankers on the road in Ladakh, India — one of numerous developing countries now seen as alternative source markets for Australian business

# The road from China

Australian companies are turning to Vietnam, India, Philippines and Thailand as alternative-source markets. *Carter McNabb* writes

**C**HINA IS a crucial trading partner for Australia, particularly with regard to our mineral exports and the range of imports from food staples, through electronics, household goods, automotive parts and even complex heavy-engineering items.

There is, however, a growing set of sourcing alternatives to China that can provide both competition against rising Chinese prices and the comfort of a second set of suppliers.

Within the normal constraints of overseas sourcing, Chinese imports provide a source of low-cost goods that are delivered on time and to a specified level of quality.

For Australian merchants used to trading with local and overseas niche suppliers, prices and trading terms, Chinese capabilities seem almost limitless. From basic offerings to high tolerance make-to-plan items, the Chinese cost advantage based on low labour and material costs blew away the competition.

Times change and so do market dynamics.

China is now experiencing a rapid rise in costs, and other Asian and Pacific countries are modelling their industries on its success.

China's new competitors are also leveraging cost differential as their advantage over Australian manufacturers, and many are becoming increasingly competitive against the Chinese.

Development of manufacturing capable of meeting Australian market needs in some of these countries has brought to light some other competitive advantages that now have to be weighed against the 'export infrastructure' that has matured in China.

Because of issues around the repeatable quality of imported goods, competitors to China have taken time to develop but are now becoming increasingly competitive in terms of cost, quality and supply dependability.

As that hurdle has been overcome, other factors

such as time zones, languages and ability to consolidate shipments are coming into consideration.

China might become less attractive because of lessening cost differential, and it is equally likely that other countries will become more attractive if their export infrastructure can be developed to provide a 'complete' cost-competitive alternate source of goods and thus some competitive tension and 'hedges'.

One of the maxims of good sourcing has always been to have 'not too many and not too few' suppliers. The rise of China as the 'world factory' has resulted in a lot of Australian companies placing all their eggs in one basket and buying solely from it as the least expensive, yet still reliable, source.

Of course, while supply is sustained that approach is fine, but as soon as supply disruptions or rapid price hikes occur, so a second supplier has clear value.

Generally, we recommend diversification to Australian and other global customers to reduce supply side risk. Traditionally, that policy has been relatively easy to implement but, in recent years, China has stood out as the 'sole affordable source' and the two-supplier policy has been traded off in favour of cost considerations.

The rise of other viable sources brings that policy back into play but raises issues of increased freight costs from multiple sources — again cost/performance trade-offs that have to be treated case by case and which are influenced heavily by the supply-disruption risks Australian companies are willing to accept.

Categories are country-specific and currently most sources bring their own set of advantages and risks.

At the very real risk of generalisation, Vietnam offers low-cost labour as a plus, however, currency volatility is a key risk. Categories being sourced are textiles and auto components.

In Thailand, labour costs are also low, and there is good availability of agricultural land resources. But

political instability is stopping Australian companies creating critical supply chain dependencies into Thailand's auto components and textiles markets.

India has the largest low-cost workforce and a very large pool of engineers, so it is a natural source of engineered items and equipment. English is the predominant business language in India and western-style business culture is also strong.

Another real source option is the Philippines, which has a significant English-speaking workforce and is being preferred to China and India for outsourcing. Political risk is, however, a key issue in the Philippines.

The time difference to Australia is one reason why the Philippines is getting preference, but India's capability to replicate the Chinese export infrastructure — consolidation centres and so forth — might reduce its 'total cost to serve' and thus out-compete the smaller Philippines.

And, of course, we've all heard the stories about China buying up assets and infrastructure in Africa, so that's another place to watch over the longer term.

Given that there is an increasing number of price-competitive source countries, buyer considerations must also include the advantages of the existing Chinese export infrastructure. Most Australian importers are becoming more sophisticated in dealing with multiple vendors in China. More and more importers are consolidating shipments in China to optimise shipping costs to Australia.

## Times change and so do market dynamics.

There is now a question about the practicality of operating consolidation centres regionally, rather than just in China, and to thereby include other regional sources within the shipping consolidation umbrella. Perhaps that will be the role of yet another country.

This is a complex topic and more companies need to consider it at a strategic level. Procurement teams are often locked into China-based sources and are



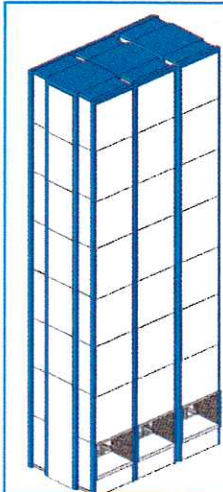
watching a rise in costs and a reduction in cost differential between Australian sources and Chinese sources. However, strategic evaluation of China versus other countries is often difficult at sourcing levels.

Another interesting perspective which we don't have room to discuss here is that Europe sources its lower-cost goods from different regions altogether; Europe's 'China' is in eastern Europe, South America, the Caribbean and some parts of Africa.

At any rate, there are big changes afoot in global sourcing. Now is the time to revisit sourcing strategies and have a look around. Don't get caught playing catch-up. ||

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The Port of Nha Trang, Vietnam: increasingly a source of textiles and auto components for Australia



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