

## Quality Digest Interview with H. James Harrington

### Subject: Quality in China

***Question Number One – Does the U.S. customer really value price over quality or safety? Why are we content in getting inferior products from China?***

#### **Answer to Question Number One –**

We do not get inferior products from China. We get inferior products from Wal-Mart, Target, Sears, Costco, etc. These are China's customers, not the consumer. Three words have become synonymous with manufacturing. These words are "made in China." What comes to mind when you see these three words are cheap, poor quality, affordable goods. Quality is almost an afterthought in the minds of the Chinese manufacturers' direct customers. Chinese companies are known as OEM's or "original equipment manufacturers." This means that they manufacture parts for foreign brands.

The real question is: Do the Chinese customers (Wal-Mart, Sears, etc.) compete based upon price or quality? Are these Chinese customers pushing the Chinese manufacturers for higher quality products or more volume? The consumers that shop at Wal-Mart, Target, Sears, Costco, etc. make up by far the biggest part of the purchasing economy in the United States and Europe. There is no doubt about it. The fantastic expansion of manufacturing capabilities in China has been driven based upon the fact that the low-cost labor in China allows them to produce products that meet requirements at a very competitive price. As long as the direct customers for Chinese products make their buying decisions based upon cost and not quality,

the Chinese manufacturers will strive to comply with their direct customers' desires and specifications.

We need to question if these distributors desire to sell products that will last, or are they more interested in selling products that have a short lifespan resulting in additional sales opportunities for them in the near future. I believe that these organizations have found out that they make more money by selling low-priced products that consumers purchase more often. These distributors are driven by their consumers' requirements and desires. Based upon actual buying data, it looks like this large population of consumers is more interested in low prices than high quality. They are looking for immediate gratification, not long-term usefulness. They want the newest and latest, not the "Old Faithful." The consumer defines the market and the U.S. consumer is communicating that it is price, not quality, that is driving their buying decisions. Often the consumer's make their buying decisions based upon brand names, not on where the product is manufactured. If the brand name distributors like Sony, IBM, Hewlett-Packard, Canon, Apple, etc. are willing to put their reputation in jeopardy by compromising quality for cost, then that is what the OEM's will provide. We cannot blame the Chinese manufacturers for building products that meet their customers' desires, specifications and requirements.

Foxconn Technology Group, a contract manufacturer for companies like Dell, Hewlett-Packard, and Nokia, employ over one million workers in China. At Foxconn workers' wages have increased so rapidly that Foxconn is moving parts of their manufacturing to inland China cities or other emerging markets. To offset the increased labor costs and to be competitive in

the low-end market, they plan to increase the number of robots used from 10,000 to over one million within the next three years. Demand for Foxconn services and products are continuously growing, but it is not due to high quality; it is low cost that is driving the increased demand. Foxconn plans to buy a set-top plant in Mexico from Cisco Systems this year and is looking into investing more in Brazil where it is already making mobile phone headsets.

It is becoming more and more obvious as labor costs increase in China that it will be necessary for Chinese manufacturers to start competing on the world market based upon value, not cost alone.

To answer your question on cost versus safety, when seat belts were an option on a car, very few people would pay the additional cost even though it was very low. We needed them to become a law before we accepted them and even worse, we needed to pass another law where you were fined if you didn't use them. We have a tendency to believe it will not happen to us.

***Question Number Two – What action does China need to take to get on track with quality? Compare China today with Japan following World War II?***

### **Answer to Question Number Two**

China's manufacturing revolution started with the U.S. opening its market to them when it reestablished diplomatic relationships with China in the early 1980s. My first trip to China was in 1982 and at that time they had many problems:

- Most businesses were managed by the government and were not required to be profitable
- They had a very poor education system
- They were overpopulated based upon what they could produce
- They had an obsolete infrastructure
- They had a major problem because their currency would not be accepted in the developed countries

Their competitive opportunities were:

- They had a vast source of cheap labor
- Japan had moved out of the low-end product market, leaving it open to China

At that point in time Japan was a role model for the rest of the world as far as transforming its manufacturing operations in order to capture the international markets. In analyzing the Japanese performance improvement cycles, it became obvious to the Chinese government that the Chinese environment was very much in line with the Japanese environment in the 1930s. At that time Japan had established a reputation of producing low-quality cheap throwaway products. This approach was profitable enough to greatly improve the living standards within Japan and create enough wealth for the country that enabled them to afford to manufacture a war machine that was large enough to attack the United States.

Following World War II, Japan's focus changed from producing low-quality, inexpensive products to an environment where they established a few brand names that were noted for quality and excellence. This approach was used to allow wages to increase and as a result,

greatly improve the standard of living within Japan. It took Japan 35 years to establish a reputation for building high-quality products. During this 35 years Japan had a number of failures and learning experiences. For example, the first car that Toyota shipped to the United States, the “Toyopet Cown,” was a dismal failure. They sold only 958 cars and had to ship many of them back to Japan.

For China to follow the Japanese model of brand recognition, it would require a great deal more capital investment, hiring and time to design new, innovative products. There would be no immediate return as it would be a new product and building a brand name alone is a massive undertaking. The Chinese market in this case has not been the engine of innovation; in fact it has been a tremendous hindrance. As a result the manufacturing model that the Chinese selected was product recognition rather than brand recognition. By working with products like toys and athletic shoes, the customer base was limited to a dozen companies rather than trying to understand the needs of millions of people and promoting their products to the mass populations. The Chinese focus has been on selling their products to foreign firms, not to foreign consumers.

What does China need to do to get on track with quality? I believe that the concept held by most quality professionals that there is a set of international best practices is a fallacy. Based upon surveys I've seen and my personal experiences I believe there are at least three sets of best practices. There is a set of best practices for the organization that is struggling to grow and/or stay alive. There is another different set of best practices for the midrange companies –

the ones that are serving the general needs of the biggest portion of our population. Then there is still a third set of best practices that pertain to the top 20% of the companies in the world, the ones that are recognized by winning national awards like the Malcolm Baldrige award.

Some of the best practices recognized in the high-end companies are absolutely disastrous when applied to the low-end companies. It is obvious to me that a company that is struggling to keep from going bankrupt has to do very different things than companies like Wal-Mart, GE, IBM, etc. The majority of the manufacturing industries in China have migrated from the low-end performance companies to the midrange and now they have to change their strategy and practices to progress up to the next higher performance level. Wages in China have increased at a rate of 20 to 30% a year. They are losing their competitive advantage of low-cost labor. It is now time for them to focus on establishing brand recognition and competing in a high quality marketplace.

With wages increasing in mainland China, a group of affluent Chinese buyers has been established. They are now buying high-end quality brand names produced in Europe and in the United States. This will become a major sector in the Chinese marketplace and one that is ripe for Chinese manufacturers.

***Question number three-- What is the status of the Chinese auto industry. Will they be able to compete on quality? Do they care?***

**Answer to Question Number Three—**

In 2010 China sold 18 million vehicles. That is a new world record for any country including the United States and Japan. They wisely have focused their sales campaigns to the Asian market, allowing them to gain experience and debug their products without tarnishing their reputations. The Buick production plant located just outside Shanghai is an excellent example of a quality car that is sought after in the Chinese market. At the component level tires manufactured in China is an excellent example of a quality product that is impacting the total auto industry.

Will China be able to compete in the auto industry from a quality standpoint? If quality is what their customers want, they have the capabilities to deliver it to them. Just look at South Korea. They are producing higher-quality cars than GM can produce. Their initial quality level is as good as or better than Toyota is delivering to its customers. In South Korea's case they were able to accomplish this amazing transition in less than 20 years. If South Korea can do it, certainly China can.

***Question Number Four – In your visits to China, you have seen the explosive growth in industry. Is there any sense that the Chinese care about the environmental impact of that growth?***

**Answer to Question Number Four:**

One of China's foremost priorities was obtaining quantities of foreign currency that could be used to upgrade their obsolete infrastructure. This meant producing a large quantity of goods with a minimum amount of investment. In this massive expansion less thought was given to the

environment than the more developed countries were able to be involved in. At the end of March 2011, China has accumulated US\$3.04 trillion in foreign currency reserves. This is the largest stockpile of foreign currency in the world. At this point in time environmental issues are important to the government and the people in China. But as a manufacturing center for the world, environmental controls are a major problem that has to be addressed without hindering their manufacturing capabilities. China has 18% of the world's population but consumes:

- 53% of the world's cement
- 48% of the world's iron ore
- 47% of the world's coal
- and has produced 11 times more steel than the United States

China is focusing on using technology to have a homogeneous balance between the environment and their manufacturing commitments. China currently has the world's fastest train and the world's largest high-speed rail network. China now possesses the world's fastest supercomputer. In the past 15 years, China has moved from 14th place to 2nd place in the world in the number of published scientific research articles. Many of these focus on the environmental challenges. From an electronic technology standpoint China, finds itself in a very good controlling position as it currently controls more than 90% of the total global supply of rare earth elements.

From a manufacturing standpoint, China currently is the number one producer in the world of wind and solar power. They have extensive research going on related to cutting pollution in

the use of coal. Environmental and green technology is important to the Chinese people but their progress will only be made if it does not slow down progress in the total economy.

As a final thought we may say many negative things about the Chinese but being stupid is not one of them. There certainly are a lot of good things that we can share with the Chinese people and the Chinese government. But in return there are a lot of good things that we can learn from China; living within our income and not spending more money than we have is one of them.

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