

PAINTING A BIGGER PICTURE FOR A SMALL REGION: PEARL RIVER DELTA SUPPLY CHAINS AS ENABLERS FOR THE LONG TERM DEVELOPMENT OF HK

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ABSTRACT

Hong Kong (HK) has suffered a major setback from a severe economic downturn since the Asian financial crisis in 1998. The situation has deteriorated ever since, with the problem being cyclical as well as structural in nature. It has endured a lengthy period of deflation and record high unemployment. This paper proposes that HK can 'stand on its feet' through effectively managing supply chains involving companies in Chinese cities in its hinterland, i.e., the Pearl River Delta region. By leveraging its existing capabilities, it could re-shape its economy for long term gains and ultimately achieve a win-win situation by contributing to the further growth of both the Mainland and HK.

INTRODUCTION

The effective management of supply chains has been instrumental in reshaping HK companies. The relaxation of the travel restrictions on the Mainland China has seen an inflow of cash and possibly hopes for HK to combat its economic downturn. The signing of the Closer Economic Partnership Arrangement (CEPA) is anticipated to add impetus and momentum to some industries. With its superior infrastructure in air cargo and container port services, HK is in close proximity with the world's largest factory base known as the Pearl River Delta (PRD), an area which is one of the fastest growing and most affluent regions in China. Since the 1980s, HK has started to relocate most of its manufacturing assembly lines in the PRD region. This turned PRD into the most significant economic region within China, contributing 40 percent of the nation's export and 30 percent of foreign direct investment. Being at the forefront of PRD, HK's fortune also relies greatly on its successful integration with the emergent growth of its hinterland. However, HK has to face new challenges on creative and flexible supply chain management and logistics strategies to lift its competitiveness.

HK'S CURRENT ROLE IN THE PRD SUPPLY CHAIN

HK is economically closely integrated with the PRD. HK is the leading investor in the region and about 90 percent of HK manufacturers have production facilities in the PRD. The rapid growth of manufacturers in the PRD has been the major impetus behind HK's economic development over the past two decades. Nonetheless, HK's relationship with PRD is not limited to the manufacturing exports arena. HK contributes to the supply chain management of the PRD through its business modelling, product research, design, logistics and marketing.

HK firms gain the reputation as reliable partners in licenses production and distribution for overseas companies targeting China's domestic market. As a service center, HK offers an ideal location for regional offices, in marketing and distribution.

Among the major service groups, trade-related services contributed most significantly to the overall invisible trade surplus at US\$11 billion in 2000. This was followed by transportation at US\$6.5 billion, financial services at US\$2 billion and other services at US\$1.2 billion. These service groups are either directly or indirectly involved in the supply chain management for the PRD region. The services sector is now the principle source of employment in HK. In 2001, 83.5 percent or 2.72 million of the working population of 3.25 million worked in services.

To a large extent, the relocation of HK's factories to the PRD has generated considerable demand for various support services with the key ones being transportation and logistics, insurance and professional services. These come by as a result of HK's enterprises in the supply chain management of the PRD region, and HK's fortune will rely more than ever on its successful integration with the emergent growth of its hinterland.

IMPLICATIONS FOR HK FIRMS: INTEGRATED SUPPLY CHAIN

Whether HK can meet the challenges and maximize the market opportunities including its attractiveness as a business platform for foreign companies and partner for Chinese companies to upgrade their management structure, as well as opportunities ranging from manufacturing to logistics brought about by China's WTO entry, heavily depends on whether individual HK companies are innovative in their supply chain management, especially in integrating the different supply chain activities.

A good example is Li & Fung which is the largest export trading company in HK and an innovator in the development of supply chain management. The company produces global products by optimising each step of the manufacturing value chain. What they have been practicing for the recent years is regarded as a very successful example of integrated supply chain management and a good illustration of the four level integrated supply chain model proposed by De Meyer et al. [1].

Rationalising the Network of Suppliers and Distributors

In the effort to maximize the efficiency of manufacturing process and lower the cost, Li & Fung breaks down the value chain and gets the best supplier for each step. For an order of 10,000 garments received from a European retailer, Li & Fung might buy yarn from a Korean producer and have it shipped, woven and dyed in Taiwan. If the Japanese have the best zipper manufacturing in China, Li & Fung will order the right zippers from their Chinese plants. If Thailand has the cheapest labor, so all the raw products are shipped to Thailand for manufacturing [2].

Sharing Information and Common Problem Solving

As Li & Fung is spread geographically world-wide, they form a 'policy committee' consisting of approximately 30 people. The committee meets once every five to six weeks [2].

Implementing Systems by Common Cost Reduction Programs and Channel-Wide Management of Inventories

Li & Fung applies a low inventory policy to meet the customers' needs. It also implements common systems to reduce costs: a product leaves a factory at a price of \$1, it may end with selling price of \$4 on shelf. As it is hard to decrease the cost of production further down, Li & Fung looks at bigger cost reduction spread throughout the distribution channel [2].

Sharing Risks and Rewards Common Performance Evaluation

Li & Fung hires people whose main objective would be similar to running their own businesses. Li & Fung provides them with the financial resources and the administrative support of a big organisation, but with freedom and independency. All the merchandising decisions are made at the divisional level. To motivate division leaders, they rely on substantial financial incentives by tying their compensation directly to the unit's bottom line [2].

CONCLUSIONS

The advantage of HK relative to other Asian cities is that it is politically, culturally, geographically and economically attached to the largest and fastest growing market in the world – Mainland China. It remains a highly efficient centre for services and fundraising activities, something that China is in desperate need of. To an increasing number of multinationals, HK is also an ideal base for their regional headquarters and offices. HK is attractive because of its location and also the value it adds.

To successfully capture these opportunities, HK has to be able to maintain a strong, transparent and well-regulated financial system; low and predictable taxes; the rule of law; a well-developed transportation and telecommunications infrastructure, the free flow of trade, information and capital facilities, and a level playing field for all corporations. More importantly, it should continue its ability to adjust to changing conditions, from a manufacturing based economy to a service economy. HK must find new ways of strengthening economic synergy with Mainland China and, in particular, the PRD. It will face competition from Shanghai, which benefits from Yangtze River Delta region, but the dynamism in one should help rather hinder the success of the other. Besides, with China's sustainable economic growth, it is possible that there are two economic hubs such as HK and Shanghai in serving their respective business delta regions.

HK's future lies in high-value added activities as opposed to trying to compete in a low cost contest, the latter feature for which it cannot compete with its Chinese counterpart. With a pool of skilled and educated workforce, outstanding infrastructure and most importantly, an agile approach in problem solving, the most preferred option for HK would be to design and implement an effective integrated supply chain management system which is recognized to add value to companies in Mainland China.

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