

Dealing with an Economic Slowdown on both Sides of the Pacific

Three US companies with operations in China explain how the slowdown has affected their business.

Karlynn Fronek

Three Minnesota-based companies with China operations—Control Products, Inc., SICO Inc., and Twin City Fan Cos. Ltd.—have managed to keep facilities in both countries open during the economic slowdown, but not without adjustments. The three privately held companies have annual revenues that range from an estimated \$20 million to \$200 million. The companies ventured into China near the advent of the new millennium, and by 2006, all three had established either a wholly foreign-owned enterprise (WFOE) or a joint venture (JV).

Control Products

Established in 1985, Control Products has two factories in Minnesota and offers electronic control solutions with applications for food-service, medical, industrial, residential security, freeze-protection, and heating, ventilation, and air conditioning equipment. The company followed some of its Western customers into China so it could serve those customers at home and in China. It set up a WFOE under the same name in 2006 because the company principals could not find a suitable Chinese partner. That same year, Control Products built a new factory, which has about 100 employees, in Suzhou, Jiangsu. The company produces electronic components in China that are designed for the China market; for multinational customers that build equipment with applications in China, the United States, and the rest of the world; and for companies that manufacture in the United States and China.

The majority of Control Product's customers are still in the United States, but the company hopes to grow its China market and is bringing in new customers. For example, it has attracted the attention of several Chinese companies who have asked Control Products to design electronic products for them—and those products now constitute about 1–2 percent of its business. According to Chris Berghoff, CEO of Control Products, sales in

2009 have been weak, with revenues down in the United States and China. Design engineering is up at both locations for future orders, however. In several cases, the designs that customers inquired about have turned into projects in the United States and China. Based on new orders, the company may add people in China, since it bases its production at the various locations on volume considerations and track record. Nonetheless, Control Products has focused more intently on flexibility in manufacturing operations during the economic slowdown.

Quick Glance

- Flexibility is key to the success of three medium-sized US companies that followed their customers to China.
- The downturn has provided an opportunity for China operations to train staff.

SICO Inc.

SICO began operations in 1951 and has served two major markets—education and hospitality—with mobile folding tables, stages, portable dance floors, and in-wall beds. In 2004, SICO and its Chinese partner, Zhu Jingxi, formed a JV, Beijing SICO-SST Hospitality

Equipment Manufacturing Ltd. The headquarters and sales office in China are housed in Beijing's business district, while a new 60,000 sq ft factory is located near the new international airport. When SICO entered the China market, it chose a partner that produced similar products for the hospitality market. In China, SICO has been able to assist SICO-SST in its standardization of product lines, eliminating unnecessary duplication and cost. At one time, for example, the JV was making trolleys on five production lines. Now SICO-SST does less custom design, which is usually expensive. Operations in China closely resemble those in the United States, with distribution centers, direct sales, dealers or representatives, and wholesalers.

Hal Wilson, CEO of SICO, noted that his company, working in a homogeneous industry, has been developing worldwide patents for more than 50 years, and faces counterfeits in almost every country in which it sells. In general, Wilson notes, "negotiating with the Chinese is different from [negotiating] with Western industrialized

countries with a long history of precedents and contract law. To most Westerners, a contract is a contract; to the Chinese, a contract is okay, but it is always open to negotiation. This requires understanding by both parties and, actually, in some ways, it is better because you don't fall back on a contract that ... might ... be flawed...."

In 2009, SICO's orders from US markets have fallen 25 percent from forecast. For the first four months of the fiscal year beginning December 1, 2008, SICO-SST reported a slowdown of 30 percent, but as of the end of June, sales are on forecast. Prior to the downturn, SICO-SST had been growing rapidly. Now operations in both countries are facing the double challenge of a slowdown in the hospitality industry and the rise of local competitors.

Twin City Fan

Like Control Products, Twin City Fan, in business since 1973, followed some of its US customers, such as 3M Co. and General Motors Corp. (GM), to China. A manufacturer of commercial and industrial fans, Twin City Fan has a plant in Shanghai with 65 employees—Twin City Fan (Shanghai) Co. Ltd.—which was set up as a WFOE in 2006. The company also has manufacturing facilities in several US locations, JVs in India and Singapore, and a manufacturer's agreement in the Czech Republic.

"The business in China is still expanding," said Zika Srejavic, vice chair of the board at Twin City Fan, "but there has been a delay in some projects beginning in late 2008, which coincided with the economic crisis. If a custom project was two-thirds finished, it went ahead. Some cancellation of orders occurred if the customer lacked funds to continue. If a customer in China did not have funds to immediately pay for product, Twin City Fan (Shanghai) stored product temporarily in a warehouse."

The company serves the automotive and petroleum industry in China, and that sector is still doing well with orders from the China operations of Bayerische Motoren Werke AG (BMW), Volkswagen AG, and GM. On the US side, customer orders have lagged. According to Srejavic, Twin City Fan's US operations account for about 30 percent of its sales outside North America. (That figure includes exports to China, but not Canada and Mexico, which account for about 16 percent of sales.) It is more difficult to estimate where the fans made in China end up, but most sales there are to Western or Chinese companies, and the product likely stays in China. For the company as a whole, the United States generates about 55 percent of sales.

Importers and exporters

With operations in both countries, these three companies import to and export from the United States. Paul Carlson, president of Control Products, remarked that

having production facilities in China allows the company to manufacture the bulk of the product's volume in China at lower cost but also gives it the flexibility to produce the units locally in the United States. In general, the company imports more to the United States, although that can vary from month to month.

SICO's US operation is currently a net exporter, as its Chinese operation imports some products and components the company makes in the United States. Including China, exports to foreign countries amount to about 10 percent of its business. SICO's Chinese partner, which is heavily invested in the hospitality industry, plans to expand into the education market to broaden its base and take advantage of SICO's knowledge and success in that market. The US company hopes that such diversification will increase orders, since a good share of its business has historically been in the hotel industry.

Twin City Fan sources about \$8 million worth of parts from China each year for placement in its US-made fans. Not too many years ago, most custom-designed fans were exported directly from the United States to China, because US-based purchasing departments had brand loyalty to Twin City Fan. Now, the vast majority of custom fans built in China are sold to Chinese and Western companies in China, though some high-end premium fans for China are made in the United States.

Effects of the slowdown

Although sales have slumped, particularly in the United States, the US recession has not slowed production in China for Twin City Fan. Production has dropped at SICO-SST and Control Products but now appears to be on the rebound in China.

Control Products has seen an upturn in potential buyers within the last few months, with some design requests turning into orders. Control Products' Berghoff and Carlson mentioned that large quantities of a custom-designed product may be built in China and shipped to the United States. The company's market in China has been stronger, partly because the Chinese economy is still growing.

Control Products has found that adjusting to the China market requires flexibility. The company has learned to transfer product orders easily between distant locations and can now ramp up production in China just as rapidly as it can in the United States. Control Products' business model shifts production to locations near the product's end use, shortening delivery times. The company made plans when it entered China for production to ebb and flow with economic levels, and those plans have served it well during the current downturn.

The slowdown has not caused changes in Twin City Fan's strategic plans. In fact, the company's China operations have increased production to meet recent demand. Some employees work overtime, and the com-

pany has hired temporary workers to fill additional orders stemming from the government's stimulus package and the World Expo 2010. In the United States, there have been no layoffs, but the number of employ-

United States to reduce costs. The company reported reducing its break-even point by \$1 million when its volume was low. At present, the US company is busy in the educational area and has rehired some personnel.

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ees has fallen more than 5 percent from late 2008 to about 1,300 employees.

For SICO-SST, the slowdown in Chinese production gave the company an opportunity to build cohesiveness among employees through training and education programs. There have been no layoffs. To adjust to the downturn, SICO-SST reduced its work week from six days to five, devoted more time to training factory staff and employees, and allocated time to update and make employees aware of company policies and procedures. The JV has received new orders in the past few months, some of which are likely a result of the PRC government's stimulus package, according to SICO management. Like other companies, SICO laid off factory and other personnel in the

During the economic downturn, there have been signals of growth in the Chinese market, and some of these will create business for US companies on both sides of the Pacific. Despite the fact that China is unlikely to return to long-term double-digit growth, companies like Control Products, SICO, and Twin City Fan believe that its rapidly expanding market will increase exports and opportunities for US companies. 完

Karlynn Fronck (kfrons@comcast.net) is an independent, Minnesota-based communications professional and a member of the US China Business Connections group (UCBC) based in the Twin Cities.

AccessAmerica Connects US Services Firms with Chinese Companies

The US Department of Commerce Commercial Service (CS) will soon release a new online directory to help foreign companies investing in the United States connect with US services providers. The first *AccessAmerica* services provider directory will be launched in Chinese at the 13th China International Fair for Investment and Trade in Xiamen, Fujian, on September 9. The directory will promote US-based firms and economic development agencies that specialize in a range of services, including accounting, advertising and marketing, banking and finance, consulting, event planning, insurance, legal services, logistics, and travel. Kellie Holloway, project manager of the US Commercial Service China Business Information Center said, "While the Department of Commerce initiative to support inbound investment via the Invest in America program has been around since 2007, *AccessAmerica* is the first practical tool to help US service providers

showcase their individual capabilities to a Chinese audience. It enables us to promote US services companies and economic development agencies on a singular basis to prospective buyers of their offerings China-wide and, in turn, boost export sales via service contracts to China."

To be included in the directory for one year, US companies must pay \$400 and submit a company description in English and Chinese, as well as client references, contact info, web address, and logo.

Companies should also select the categories in which they wish to appear.

CS will review each application. Once approved, company listings will appear online 7–10 business days after receipt of the payment. The listings will appear on the websites of the US Department of Commerce, US embassy and consulates, other China-based commercial service offices, and program partners. Each company will have a dedicated webpage

covering its specific expertise and offerings. Listed companies may also submit "how-to" guides, white papers, or case studies to be posted on the *AccessAmerica* resource page for Chinese investors.

If overseas companies and investors inquire about a company in the directory, CS staff will confirm information about the inquiring firm and send sales leads to the US company. If a Chinese firm contacts a listed US company directly, CS can help establish that the inquiry is genuine.

For more information on the new program, see the *AccessAmerica* website (www.buyusa.gov/midwest/access_america.html) or contact Julie Carducci, director of the Commercial Service-Chicago (julie.carducci@mail.doc.gov).

—Paula M. Miller

Paula M. Miller is associate editor of the CBR.