

SCI China Market Update – July 2019

Dear friends,

Soon after my delivery of a challenging due diligence report on a targeted Chinese manufacturer for our client's M&A project, I visited Taiwan and Vietnam for business.

In Vietnam I met with SCI's partner in Hanoi. This is a well-established business consulting firm with legal services as well, and offices in Ho Chi Minh City (HCMC) and Da Nang.

Vietnam business is heating up thanks to the U.S.–China trade war. However, my visit to HCMC and Hanoi gave me the impression that Vietnam is still truly a developing nation with a history of war and more war. HCMC traffic suggests strongly that this is a 'no-rule-is-the-rule' country. Quite different from Taiwan and Mainland China, I didn't see any universities or high tech industrial parks.

HCMC has no subway and a poor bus system with millions motorcycles and motorcycle taxis mixed in with imported Japanese cars speeding along roads with no traffic lights. I found it shocking. This city's traffic helped me to understand what "the law of jungle" really means.

Can this nation attract major foreign investment? Can these laborers be trained and educated to become qualified workers to make quality higher end parts and components that would compete with major Chinese suppliers? I doubt it will happen in the near future. Finding loyal, hardworking, experienced and English speaking engineers, CFOs and senior management is a big question mark. At the low end of products, Vietnam may already be starting to replace some Chinese suppliers along the East Coast, e.g. in textiles, casting, powder coating, basic engineering, electroplating, etc. Yes, cellphone and home electronics export from Vietnam to the U.S. has been increased sharply this year.

In any case, Vietnam left me with the impression that it is rich in water and labor resources, but its talent pool is still very small and not yet competitive. Thus, for higher end and higher quality production and supply, Vietnam cannot yet compete with China. But, it seems this post-Vietnam War nation is already becoming a sizable marketplace for companies like Toyota and KFC.

Because of the U.S.-China trade war, many Western companies are re-thinking their international sourcing and sales strategy, eyeing new sources of supply and profitable markets outside of China. It seems that Taiwan, Vietnam, Thailand, Korea and Bangladesh are gaining the most from the uncertainty of the trade war. However, Taiwan and Korea are too expensive for many U.S. manufacturers while their markets are too small and too difficult to invest in heavily. From skilled labor to quality production capability, they are all too small compared to China. This is probably why Tesla is investing more than \$7 billion to build its first overseas Gigafactory in Shanghai. Mr. Musk expects that the Shanghai plant will produce 3,000 Model 3 vehicles per week by the end of this year.

But if you leave China, where can you really turn in Asia today to find qualified back-up and alternative vendors and suppliers as well as sales outlets? Japan? Singapore? Korea? Hong Kong? Taiwan? Vietnam? Indonesia? India? Cambodia? Malaysia? Thailand? It's truly difficult to make a good choice.

Of course, Japan, Singapore and Korea are capable, and Taiwan is cheaper. Unfortunately, Japan and Singapore are too expensive for most U.S. companies whose purpose is to source from Asia to reduce costs. Labor costs in Japan and Singapore can be more expensive than in the U.S. Korea is good but no longer low cost. Taiwan is a relatively small island and its production capability is very limited.

Taiwan enjoys better trade treatment from the White House in terms of tariffs and stable trading relationships. Taiwan's manufacturing capability and level of technology are good, perhaps even much better than Hong Kong's - from semiconductors to auto parts to plastics to textiles, etc.

Importantly, for U.S. companies considering alternative sourcing or manufacturing outside of China, Taiwan's talent pool is attractive. From Taipei's National Taiwan University to Taichung University to Kaohsiung's National Sun Yat-sen University, Taiwan's higher education system produces a lot of quality talent every year. Taiwan's infrastructure is good - from airports to high-speed trains to subways to highways to seaports. Unfortunately, as an island, Taiwan's raw materials and parts supply rely heavily on Mainland China. And Taiwan's labor and overhead costs are no longer low.

Regarding Indonesia and Malaysia, there may be a higher political risk than in other Asian nations. Economically, Japan, Singapore and Korea are no longer low cost. So, Taiwan, Vietnam, Thailand, Bangladesh and Korea are getting increasing attention as a result of the US-China trade war. Taiwanese and Korean companies are winning more and more purchase orders for higher end products from electronics to auto parts.

There was one mishap on this trip - I broke my right arm in Hanoi due to a road accident. I managed to get to my hometown in China, Tianjin, where I had surgery timely. Now I must complete this issue of the SCI newsletter typing with my left hand. But don't worry. If you need help in China or other Asian countries, SCI is here to help!

For more information about today's China market and opportunities please visit our website at www.s-c-i.com or call me at (610) 457 8380.

Best regards,

Shiqiang Gu
President & CEO

Sino Consulting (SCI)
Phone: (610) 457 8380
Email: sgu@s-c-i.com