

OUTSOURCING TO EASTERN EUROPE ISN'T AS RISKY AS YOU MAY THINK,
ACCORDING TO WIESIEK CHODYNIECKI

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Most OEMs are under constant pressure to review their cost base, particularly manufacturing costs, to stay ahead of the competition in a global economy. Traditionally, since most British OEM capital equipment manufacturers are small or medium size firms, they have evolved over a number of years with in-house manufacturing. Alternatively they have relied on local UK subcontractors. All seems to be “business as normal” except that these OEMs find it more difficult than ever before to compete with their foreign counterparts.

On the continent things have been very different. Since the mid 1990s there has been more of a revolution rather than an evolution. With the former Eastern Bloc collapsing many continental OEMs (in Germany in particular) have ventured eastbound for low cost manufacture. They took a strategic decision to focus on high added-value business, while outsourcing/subcontracting non-core manufacturing to low cost-base countries. Hungary, the Czech Republic or Poland seem an obvious choice in terms of the right balance of potential savings, low commercial risks and short lead times. It was a strategic focus on know-how and steering away from manufacturing components with a commodity based price structure—an area where the developed world cannot really compete long-term.

This move by continental OEMs has not only secured their future but they have started eroding the traditional export market share of many British OEMs. Not all is lost, since many continental OEMs learnt the hard way that subcontractors in Central Europe could be a real challenge and take 3 to 4 years to establish. The key to success has been a structured approach to supplier selection.

It has to be remembered that material costs in open market economies are relatively similar. Therefore unless materials are purchased in wholesale quantities, there are no real savings on materials alone. Savings are mainly on the labour element of manufactured components—on average sub-contract manufacture rates in Central Europe are a third of those of Western states. However when the labour element is less than 50% of total unit cost, the benefits of overseas manufacture can be eroded by additional transport and contract management costs.

It should also be remembered that lead times in Central Europe can be 3 to 4 weeks, UK delivered. No duty is payable on entry to the UK, as long as the component has been manufactured in a preferential country; i.e. from countries that will be joining the EU in 2004.

By manufacturing some components overseas we can secure the future of many British OEMs of capital equipment. As the OEMs grow so do all of their subcontractors, including those based in the UK.

To succeed, OEMs must take into account the subcontractors size, ownership, sales and marketing infrastructure, and capabilities. The OEM must also have a clear understanding of what constitutes “core” and “non-core” business. They must make a long-term commitment in order to succeed. It does take time to search out and work with suitable overseas manufacturers. After all, if it were easy, everybody would be at it.

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