
Evolving Your Business Model (1180)

Dr. William K Fung

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Li & Fung is a very old company. We've had 100 years of history. Most people think that it's been fair sailing for 100 years, but that's obviously not the case. I could tell you that there are very critical junctures in the history of the company, where if we hadn't reinvented ourselves, we would be history. One of the things that my father's generation did successfully was to be an intermediary between the buyers from United States, Europe, and Japan, and buying from these labor-intensive consumer products that are manufactured now in the developing parts of the world. By the time Victor

[Fung] and I got back in 1972-73, cracks were already beginning to appear in this business model to the extent that the world was getting smaller, with people now flying around more easily. The language barrier is no longer a barrier. And not only that, but if you think about it, in just the process of putting together a buyer and the right factory, most countries have free services to do that kind of matching. Hong Kong, for example, has its Trade Development Council, which does that. Every country you remember in the '70s and '80s wanted to promote their exports, and every country had some kind of an institutionalized, probably free, service. The role of just an intermediary and saying that I know the market and I can introduce you to the right factories, those days are obviously either over or there is very low value added. Obviously, what we had to do was change. That's why we developed this whole concept, which later on people gave us a name of supply chain management. The idea is not a brokering service; the idea is that you manage the whole process. At first we started with the idea. We went behind the factories and went to the raw material source because the raw materials, by that time, could be in a different place. What happened with the globalization process was that the production didn't just jump from country to country. It was a process where the labor-intensive portions of that manufacturing process were first moved to the place where labor is cheaper. Let's say that instead of Hong Kong, they moved to Taiwan, but the denim fabric was still from Hong Kong, where the textile mills were. Then later on, when Taiwan outgrew day labor--it got too expensive--the labor moved to Indonesia, but the fabric mills were in Taiwan. So there was an extended, at that time, supply chain. What Li & Fung did was say that hey, a big determinant of the cost is not just the labor; it's also the fabric and the raw materials--the whole thing. We developed this whole concept, which later on academics called supply chain management, to what we were doing, and it was on a global scale. The unfortunate thing about this is that that we now call it Supply Chain Management. The problem with Supply Chain Management is that it is such an overused concept that every truck driver now thinks he's a Supply Chain Manager. Li & Fung actually manages very complex supply chains--extending over many parts of the world--and we really seek out what the best place is to do a certain component or raw

material. Then we bring it all together and assemble it in the best place. For example, we have a stuffed toy that talks. For a long time, this stuffed toy product was actually made in Korea, where they had the machinery and the plush fabric. From that we evolved into a situation today where we say, okay, Korea still has the best fabric, the plush fabric---if you want the fabric to last and so on, you get it from Korea. Now we're bringing that plush fabric into Shanghai, near Shanghai, where we're doing the sewing; and we're customizing the sound chip--the talking part of it--in Taiwan. We bring it all together, and now we have the best product because we're taking the best of breed. We're building supply chains that bring it together to produce the best product. That's the evolution, and it's not a simple brokering job of saying that hey, here's a customer, let me find a factory. The whole concept of managing the supply chain rather than managing just the brokering function between the factory and the buyer has evolved, and now Li & Fung is known as one of the world's leading supply chain management companies.

Globalization Leads To Collaboration (1178)

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In the last 20 to 30 years, most of the innovation and growth has been related to the whole process of globalization. I think that it's almost natural that if you're moving out of your comfort zone and your domestic market, when you're seeking these growth opportunities, then you're in an unfamiliar culture and marketplace and you would collaborate with other players in that market. It's a very natural growth for the globalization. For Li & Fung, it is particularly relevant because the whole origin of our company was based on that type of need. To make a long story short, Li & Fung is a company that is a little over 100 years old. When my grandfather first started the company in Canton, China in 1906, his role was to provide Western buyers, who wanted to get China-related products, with things like porcelain, silk, tea, and so on. And they were working in an alien environment. Obviously, there was a need for a local business partner to provide that kind of product. Our whole business actually grew up from that need, within this globalization process, of providing the local expertise, whether it is supplying Chinese products that are unfamiliar in terms of production, quality, and other aspects to the Western buyer or whether it has to do with doing an operation in a land that's far away from your home base. For most business people, the collaboration aspect becomes more and more relevant and pressing the farther you operate from a familiar domestic or local market. I can only see that, with the rate of globalization the world has undertaken in the last 20 to 30 years, this rate of collaborative effort, rather than doing it on your own, will become more and more prevalent. If you look at the whole process of off-shoring production, for example, which is obviously one of the major planks for globalization, you see that many people, when they off-shore their production--let's say they used to have a factory in America and now they want to off-shore their production--

have skipped the stage of trying to own factories overseas because of the unfamiliar environment, and when it's trading into an outsourcing deal at the same time. They're both off-shoring and outsourcing at the same time. That's only natural because of the environment, the culture, the social norms, and the business ethics. Everything is different when you go into different marketplace that is not your domestic marketplace or when you go overseas. I think that the world is in an era of what I would call radical outsourcing--any function that is not deemed to be a core competence and essential strategically for your company is a candidate for outsourcing. If somebody else in those areas can do it better, faster, and cheaper than you, maybe that's the way to go so that you can focus your energy on areas that are of strategic importance to you. This outsourcing trend, besides the globalization trend, is also going to contribute to the need for cooperation. Your need for local expertise increases exponentially if your product range is very wide. If you're a single product, a very narrowly product line based company, whether you're a brand or a retailer, perhaps it's easier to control the supply chain with your own operation. But if you're selling everything from lawn mowers to silk underwear, chances are you need a partner or partners all over the world to do this. A lot of people talk about buying direct, but they need an intermediation layer. When somebody says that I buy direct from China, chances are they mean that I buy through my buying office from China; or I buy through somebody like a Li & Fung, an agent in China; or I buy through some intermediary. By the same token, if a factory in India says that I sell directly to somebody in America, chances are they're selling to that buying office or Li & Fung. It is not direct just because of the need for expertise on the ground. There's a need to control quality. There's a need to control compliance, which is very important now. There's a need to sort out the numerous suppliers--who the good suppliers are and who the bad suppliers are. There's a whole supply chain that's now offshore. If you're buying apparel, chances are that your fabric is made in country A, and it's shipped to country B or another part of country A for it to be made. It's a very complex for an old-fashioned kind of business, a very complex supply chain. Li & Fung really made its name by managing all these very complex supply chains.

Institutionalizing The Process Of Reinvention (1179)

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Our attitude about change is that, first of all, change is inevitable. Not only is change inevitable, but change is happening faster and faster. The rate of change is actually accelerating. Li & Fung has a very specific way of dealing with management of change. As you know, most companies have planning cycles--3-year plans, 5-plans, 10-year plans, and so on. Our first point about the duration of the planning cycle is that it should be kept relatively short. With the way the world is changing, even five-year plans are probably too short. Again, I'm making a general statement. It depends on the type of

industry you're in and the lead time it takes to set up plans. But in 10 years, certainly, I don't think anybody with any kind of even rough certainty can tell you what's going to happen in 10 years' time. So Li & Fung sticks with a three-year plan. The second aspect of planning is that most business schools teach you about something called the rolling plan. In other words, every year--if you have a three- or five-year plan--every year you redo it. At Li & Fung, we think that moves the goal posts too much. We think that every year the plan changes, and as a result of that, nobody actually pays attention to the plan. We learned something from the Chinese communist central planning system. They have five-year plans that are fixed. Li & Fung adapted and adopted that concept, and we have three-year plans that are fixed. Within that three-year time frame, most of our seasoned executives can foresee the changes coming down the pike with some certainty, or at least with enough certainty to plan properly in the three-year time horizon as compared with a 5- or a 10-year time horizon. That's the first thing. The second thing we do is look at that planning horizon and say that you really must start from zero base. We start from the zero base meaning that at the beginning of every three-year planning cycle, where we actually wipe the slate clean, we say let's start from ground zero; let's start from zero base. If we didn't have our business today, would we go into it? That's the first, most telling question. Most companies just assume that we're in the business, so we have to deal with it. I think that's what happens when CEOs foresee something so momentous coming down the pike. They say that well, maybe, they should get out of this business. But we do that every three years. I'll tell you the reason why we do this every three years. This philosophy really comes from my brother, Victor, who taught at the Harvard Business School. His perception is that if you're a company that cannot change with the times when the change is already upon you, then you're history anyway. You will not survive. But if you're a company that has somebody like a CEO or a group of executives who can look down the pike a bit and foresee the changes that are coming and anticipate change--for him that's only like a primary school level competence in terms of planning--you can foresee change and anticipate change

[and will be in a better position]. If you're a company that is so good that you can not only see what's coming down the pike, but you're willing--and that's a key thing; if you're willing to change yourself so fundamentally and I guess the buzzword for that nowadays is to reinvent yourself--then you're probably secondary school. You're not afraid of change, and you're ready to change yourself quite fundamentally if you see something coming down the pike. What's required of Li & Fung is that what we want to do is to institutionalize the process of reinvention. The way we do that is using our three-year planning cycle. So no matter what, we don't have people there who suddenly jump and say that something is happening and I better do something about it. We systematically, every three years, do it. We get people offsite, and we really spend the time to say that for the next three years, these are the changes we, as a team, collectively foresee coming down the pike. Not only that, but also let's ask the experts. Let's ask some of the people whose job it is to do this kind of forecasting and be visionary, and see what we think the changes are that are coming. Let's do a proper exercise once every three years. And every three years, we do that. What we've done is institutionalized the process of reinvention.