Hong Kong Manufacturing SMEs: Preparing for the Future

Industry Situation Report

GARMENTS

Funded by SME Development Fund

Made in PRD Research Series III
The Garment Industry

The garment industry consists of fashion design, apparel manufacturing, clothes wholesale, and retailing. The global garment industry’s total revenue in 2006 was US$1,253 billion. This is estimated to reach a value of US$1,782 billion by the end of 2010.¹

China is the largest producer and consumer of garments, producing over 50 per cent of the world’s total in 2008. Guangdong Province is the largest garment producer in China, accounting for 18.3 per cent of total reported Gross Industrial Output (GIO) in garments in China in 2008 (ahead of Zhejiang, Jiangsu, Shandong, and Fujian). It is reported that there are over 30,000 garment enterprises in Guangdong in 2009 and about 80 per cent of these enterprises are mainly export-oriented.² The 2009 Guangdong Statistical Yearbook reports that the garment sector in Guangdong accounted for 1.1 million workers, GIO of RMB 172.5 billion, exports of US$23.9 billion, imports of US$823.5 million, and VAT of RMB 5.6 billion in 2008. Garment manufacturing is concentrated in the PRD, especially in Dongguan, Zhongshan, and Foshan.

Hong Kong firms are a leading global force in the industry. Several of the world’s leading garment firms are headquartered in Hong Kong and it has been estimated that Hong Kong firms control on the order of a quarter or more of world garment trade. Hong Kong companies generally look after strategy, coordination, marketing, and finance from Hong Kong, while producing in the Pearl River Delta and elsewhere. Hong Kong companies started moving production into the PRD in the 1980s and little production remains in Hong Kong. The vast majority of Hong Kong garment companies, large as well as small, are engaged in OEM production for well-known brands and retailers such as Armani, Hugo Boss, and Banana Republic. Hong Kong companies have benefited from Hong Kong’s openness, managerial skills, financial sector, international linkages, transportation system, and communications infrastructure, while offsetting disadvantages in labour and other costs by shifting production into the Chinese Mainland.

The end of the global garment quota system in January 2005 led to a tremendous spike in Hong Kong’s garment re-exports from China in the first six months of 2005. Since then, the global garment trade has steadied, with China’s share significantly higher than before. Hong Kong and other international garment exporters have invested heavily in capacity in the Chinese Mainland.

² gcontent.nddaily.com.
Some developing countries such as Bangladesh, India, Vietnam, Cambodia, and Thailand are growing their low-end garment industry. These countries have lower operating costs than China. Some garment companies in the PRD have considered moving their manufacturing factories to one or more of these countries, though few have done so to date. While industry participants expect that South Asia in particular will become a larger player in the low end segments of the industry, and that even Africa may become a more significant producer, China will remain the dominant production location in the garment industry for the foreseeable future. Thus it is key for Hong Kong firms to be able to continue to leverage Chinese production locations, and to compete against competitors from the Mainland if they are to succeed. While companies that are not able to distinguish themselves in terms of technology, design, flexibility, reliability, and quality will face a tough time, there are enough Hong Kong firms that do distinguish themselves on one or more of these dimensions to indicate that Hong Kong will retain a strong position in the industry.

Basic Facts about the Industry
GIO and employment in the garment sector in Hong Kong decreased from HK$23 billion and 24,000 people in 2004 to HK$8 billion and 13,000 people in 2008. Average wages for the garment sector in Hong Kong are six times those for wages in the sector for China as a whole. This is likely explained by general wage disparities between Hong Kong and China, the employment of more senior staff in Hong Kong, and the fact that higher value end products are produced in the sector in Hong Kong with corresponding higher quality and more costly labour inputs. Wages were approximately 23 per cent of total costs for the sector.

<table>
<thead>
<tr>
<th>Region</th>
<th>Average Monthly Wages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hong Kong</td>
<td>9,034</td>
</tr>
<tr>
<td>YRD</td>
<td>1,605</td>
</tr>
<tr>
<td>PRD</td>
<td>1,710</td>
</tr>
<tr>
<td>China</td>
<td>1,559</td>
</tr>
</tbody>
</table>


The total exports from Hong Kong for the textile and clothing sector in 2009 were HK$254.5 billion or 10.4 per cent of total exports. Total domestic garment exports for Hong Kong were HK$4.4 billion, a decrease of 80 per cent from the previous year. Re-exports from Hong Kong for the textile and clothing sector were HK$247.8 billion or 10.3 per cent of total re-exports. Mainland based processing trade re-exports through Hong Kong accounted for HK$118.4 billion of this total, while Mainland based non-processing trade accounted for a further HK$45.6 billion. Total re-exports originating from the Chinese Mainland were HK$164 billion or 6.8 per cent of Hong Kong's total re-exports, and 66 per cent of garment re-exports.

In 2009, Hong Kong imported textile and clothing sector traded goods of HK$197.7 billion or 7.3 per cent of total imports. This was down 17.8 per cent from 2008.
### Exhibit 2. Textiles and Clothing Exports from Hong Kong, HK$ millions

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>World</td>
<td>329,269</td>
<td>0.1%</td>
<td></td>
<td>313,024</td>
<td>-4.9%</td>
<td></td>
<td>254,532</td>
<td>-18.7%</td>
<td></td>
</tr>
<tr>
<td>US</td>
<td>83,925</td>
<td>1.3%</td>
<td></td>
<td>77,383</td>
<td>-7.8%</td>
<td></td>
<td>63,083</td>
<td>-18.5%</td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>16,674</td>
<td>5.7%</td>
<td></td>
<td>18,148</td>
<td>8.8%</td>
<td></td>
<td>15,384</td>
<td>-15.2%</td>
<td></td>
</tr>
<tr>
<td>UK</td>
<td>24,092</td>
<td>5.7%</td>
<td></td>
<td>23,811</td>
<td>-1.2%</td>
<td></td>
<td>18,722</td>
<td>-21.4%</td>
<td></td>
</tr>
</tbody>
</table>

Source: Hong Kong Census and Statistics Department.

### Exhibit 3. Textiles and Clothing Re-exported from Hong Kong, HK$ millions

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>World</td>
<td>286,772</td>
<td>5.2%</td>
<td></td>
<td>287,611</td>
<td>0.3%</td>
<td></td>
<td>247,881</td>
<td>-13.8%</td>
<td></td>
</tr>
<tr>
<td>US</td>
<td>68,562</td>
<td>10.7%</td>
<td></td>
<td>66,037</td>
<td>-3.7%</td>
<td></td>
<td>61,517</td>
<td>-6.8%</td>
<td></td>
</tr>
<tr>
<td>UK</td>
<td>19,749</td>
<td>13.3%</td>
<td></td>
<td>22,578</td>
<td>14.3%</td>
<td></td>
<td>18,400</td>
<td>-18.5%</td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>14,376</td>
<td>20.6%</td>
<td></td>
<td>17,366</td>
<td>20.8%</td>
<td></td>
<td>15,281</td>
<td>-12.0%</td>
<td></td>
</tr>
</tbody>
</table>

Source: Hong Kong Census and Statistics Department.

### Exhibit 4. Chinese Mainland Process Industry Garments Re-exported from Hong Kong, HK$ millions

<table>
<thead>
<tr>
<th>Hong Kong’s Garments Re-exports of the Export Processing Products Manufactured in the Chinese Mainland</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>125,952</td>
<td>141,669</td>
<td>135,230</td>
<td>118,446</td>
</tr>
</tbody>
</table>

Source: Hong Kong Census and Statistics Department.

### Exhibit 5. Textiles and Clothing Imports to Hong Kong, HK$ millions

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>World</td>
<td>255,439</td>
<td>0.0%</td>
<td></td>
<td>240,646</td>
<td>-5.8%</td>
<td></td>
<td>197,740</td>
<td>-17.8%</td>
<td></td>
</tr>
<tr>
<td>Mainland China</td>
<td>135,343</td>
<td>1.0%</td>
<td></td>
<td>128,247</td>
<td>-5.2%</td>
<td></td>
<td>106,932</td>
<td>-16.6%</td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td>18,863</td>
<td>1.2%</td>
<td></td>
<td>17,762</td>
<td>-6.2%</td>
<td></td>
<td>15,027</td>
<td>-18.2%</td>
<td></td>
</tr>
</tbody>
</table>

Source: Hong Kong Census and Statistics Department.
Issues for Hong Kong Garment Manufacturers

The major issues facing Hong Kong garment firms operating in the PRD are rising operating costs, a shortage of skilled workers, a decrease in orders from overseas buyers, competition from other developing countries, increased order frequency, reduced individual order volume, changing styles, a demand for speedier delivery, higher quality demands from end customers, and the appreciation in the RMB. Competition in the garment industry within China and between China and other locations is intensified by low entry barriers.

The impact of the global economic slowdown can be seen in that Chinese Customs reported that the garment exports from China fell by 9.8 per cent from US$185.3 billion in 2008 to US$167.1 billion in 2009. Hong Kong’s garment business was greatly affected by the downturn, with total exports, total imports, and re-exports of textiles and clothing seeing double digit declines in 2009. China’s garment exports started to grow again during the latter part of 2009. However, retailers’ confidence remained fragile, and they have been reducing their working capital by placing smaller order volumes and demanding quicker delivery times at cheaper prices.\(^5\)

The garment industry is labour-intensive. This means that it is hit disproportionately by increases in labour costs in China and is more subject to competition from low wage nations than other sectors. China has had a labour cost advantage that helped it compete in the industry. Increasingly, however, lower labour costs can be found in other developing nations, though China still benefits from massive scale, a huge home market, and established garment and textile production chains.

In addition, there is a shortage of skilled workers in the sector in the PRD. The manpower shortage across the economy in areas such as Guangzhou, Shenzhen, and Zhuhai was estimated at more than two million in early 2010,\(^6\) forcing garment factories to reduce production. The Guangdong Labour and Social Security Bureau increased the minimum wage effective from 1 May 2010. Most of the Hong Kong factory owners we interviewed thought the new measure would be of little help in attracting more migrant workers as many manufacturers still face labour shortages even after paying their employees more than the amount that the government requires.\(^7\) Further, increases in labour costs have a significant impact on profitability and even the viability of the business, and on the competitiveness of the PRD in the industry.

The garment industry was one of the industries singled out for greater restrictions on export processing and reduced VAT rebates in China in 2006 and 2007 on the grounds that the garment industry was too labour and resource intensive. The dyeing sector, a key component of the garment sector, has been singled out as a polluting industry that also requires restrictions. This has the potential to disrupt a key step in the supply chain.

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5 “HK exporters in Pearl River Delta win more orders,” South China Morning Post, 27 May 2009.
6 english.tianhechem.com.
7 Interview with the leadership of Federation of Hong Kong Industries, 31 March 2010.
China’s Labour Contract Law is not differentially applicable at an industry level, but it is clear that the new law will increase manufacturing costs because of the requirement that firms provide additional worker benefits. This will have the greatest impact on labour intensive industries, meaning that the effect on the garment sector is likely to be more pronounced than on many others.\(^8\)

At the end of 2008 the State Council introduced a “Plan on Adjusting and Revitalising the Textiles and Garment Industry” to help the Chinese garment industry to overcome the global economic downturn.\(^9\) This Plan has helped the industry in Mainland China raise finances and improve their technological capabilities. Raising the tax rebate rate for textile exports, providing subsidies, and postponing social insurance payments has improved the textile companies’ cash flows.

The NDRC Plan for the PRD and related policies have put pressure on garment firms, particularly those that do contract manufacturing, to move elsewhere in Guangdong, move out of Guangdong altogether, and/or move into ODM and OBM as a means of adding greater value. The Guangdong Government introduced a “double-transfer initiative” in 2008\(^10\) to encourage companies in the Pearl River Delta region to relocate their labour-intensive production facilities to less developed regions in the East, West, and North of the Province where there is readily available local labour.

The relocation of a garment factory is less difficult than other industries due to the simple nature of the machinery and production processes involved. Their requirement for local services is also lower than other industries and their simpler supply chain means that may not also be necessary to move their upstream suppliers as well. Nevertheless, the garment industry has a long processing and supply chain where the PRD still has advantages. The PRD can provide fast and reliable delivery for garments products as it has established a very good supply chain and flexible services system. The logistics costs will increase if the garment factories move outside of the garment manufacturing cluster.

While Hong Kong firms’ ability to manage production in South China is still an advantage, competition with other areas of China will heat up. There will be challenges associated with moving production into new areas of China. Moving deeper into China’s interior dilutes executive control from Hong Kong. It also may bring executives into more direct competition with strong local manufacturers, and require them to deal with local governments less aligned with their export oriented activities. In addition, international sourcing operations traditionally focused on Hong Kong and the Pearl River Delta will diversify their supply locations in China.

\(^8\) China Statistical Yearbook 2009, calculated ratio of GIO to Employment
Response Strategies of Hong Kong SMEs

The sharp decline in Hong Kong domestic garment exports suggests that the industry in Hong Kong suffered greater losses than in many other locations as a result of the global economic crisis and it may also point to an acceleration of moves by remaining firms to relocate garment manufacturing to the Chinese Mainland. For firms already in the PRD, moving to less developed parts of Guangdong may reduce labour costs and allow them to find semi-skilled workers, but may impose difficulties in finding and retaining skilled technicians and management, as well as increase supply costs and the cost of shipping finished products.

The end of the international garment quota system has changed the industry’s competitive landscape. One major impact was competition on price rather than on quota. Several Hong Kong firms that had set up production in multiple locations (or at least in locations other than Hong Kong or the Chinese Mainland) to get around quota restrictions focused their production more and more in the PRD and YRD. With recent cost and regulatory changes in China, however, some have started opening new facilities in interior provinces. Others have opened or considered facilities in Vietnam, Bangladesh, India, and other countries. Still others have supplemented or even replaced their own production activities with outsourced production. In more extreme cases, companies have shifted from manufacturing to sourcing and trading.

Another impact of the end of the quota regime and increased cost and competitive pressure has been on the range of products and services offered by some garment companies. Under the quota regime, companies often focused on one or two products for which they had quota. The lifting of restrictions has allowed some companies to produce and sell a variety of garment products, since the production and support activities across products in the garment industry are similar. A wider product range, in turn, can help increase scale efficiency in some activities while allowing the firm to supply a larger portion of a buyer’s needs. A wider product range and greater scale, in turn, has allowed some companies to invest more in design and has allowed them to provide additional support services to customers that would not have been efficient for a company supplying only a single product.
As regulatory and policy pressure mounts for garment production to relocate from the PRD, companies that are identified as developing new products, new designs, and their own brands may be able to receive more favourable treatment than other companies. While there are no guarantees, a company being able to show it is moving up the value-added ladder may receive more flexible treatment going forward.

Finally, rising costs of operation in the PRD during the 2004 to 2007 had already driven some factories to close down or to relocate outside the PRD even before the economic downturn of 2008-2009. More closed during the downturn. We expect that tough competition in the industry will lead to more closures and consolidations going forward.

Case Study – Lever Style Incorporated
Lever Style Inc. was founded in Hong Kong in 1956 as Lever Shirt G.W.B & D. Factory Ltd. In 2007 Lever Shirt merged with Trinity’s outerwear manufacturing division to form Lever Style Inc. (Lever Style). The company is led by a third generation family member, Mr Stanley Szeto. In 1981 Lever Shirt was one of the first garment manufacturers to open production facilities in China and the company now has a significant presence in Guangdong, while retaining corporate headquarters in Hong Kong.

Lever Style’s traditional line of business was Original Equipment Manufacturing (OEM) for established western brand companies but the company has since extended into Original Design Manufacturing (ODM). The company’s focus is on high-end branded products for clients such as Armani Collezioni, Armani Exchange, Banana Republic, Calvin Klein, Country Road, Hugo Boss, Paul Smith, Ralph Lauren, and Reiss. They also produce mid-range products for the Japanese mass fashion retail company UNIQLO. Lever Style tends to deal with a relatively small number of customers that have size and scale globally (Hugo Boss) or within a significant market (Country Road). The US is the largest market accounting for 40 per cent of revenue, the European Union, Japan, Australia, and other locations account for a further 40 per cent of revenue, with Mainland China making up the final 20 per cent.

The company currently has approximately 7,000 staff with the majority of them based in Mainland China. Product design, customer service, merchandising, and sales are coordinated out of the Hong Kong and New York offices, while production is located in Guangdong. Lever Style manufactures more than 10 million garments a year for men and women across a wide range of garment types and finishes.

Lever Style is highly regarded by relevant players in the garment industry for its creativity, innovation, and clever management.

Issues and Challenges
Presently, cost pressure is the major issue for the company. Given its emphasis on designs and sales to high-end brands, Lever Style is a relatively high-cost producer. The company manufactures in Guangdong, which the company claims is the second highest cost location (to Italy) among major garment producing locations. Competition can also be tough in the sector. Barriers to entry are low in the garment sector. In addition, there are suspicions that some competitors do not fully comply with laws and regulations. This makes the competitive pressures more difficult.

The most difficult aspect of operating in Mainland China for Lever is having to explain to customers that certain issues are hard to address due to regulatory uncertainty and bureaucratic obstacles, while its main regulatory concern is protectionism in the West.

Mr Szeto notes that “there are always new entrants who try to do things cheaper.” The regulatory issue that most troubles Mr Szeto, however, is protectionism in the West. He comments that the quota system was protectionist in nature and that with its abolition, and with China’s accession to the WTO, the world seems generally to be heading towards freer trade.

Company Strategy
Mr Szeto admits that he “doesn’t have a crystal ball”. This means that the uncertainty brought on by the various business challenges confronting Lever Style must be dealt with proactively by having strategies in place to fit the business environment.

Lever Style has responded to cost pressure by reengineering its processes to be leaner, more flexible, and more efficient. Lever Style’s move into China in the early 1980s, long before many other Hong Kong firms, meant that when branded garment retailers and brand owners from outside markets came to Mainland China looking for manufacturers, Lever Style already had a track-record in China most Hong Kong garment manufacturers did not. More recently, Lever Style has tried to avoid fiercely competitive segments such as low-value mass produced unbranded garments. According to Mr Szeto, “We don’t compete based on price. We compete based on our servicing, on our product development capability, on our reliability and on our reputation. We use those things to differentiate ourselves from the guys who grab a hundred workers and start in the business in the hope of making it. Those people are always going to exist, but the customers that we work with may not have confidence on somebody like that.”

Central to Lever Style’s approach is differentiation through a combination of offering value-added services, providing superior service across all activities that the company performs, being responsive to customer needs, and by maintaining an excellent company reputation. Mr Szeto cites the relationship with Country Road, a company that used to simply tell Lever Style to buy a particular fabric from an Italian mill, buy other garment components from a Japanese supplier, and then “just stitch the garment for us.” These days, Lever Style proposes both designs and fabrics to Country Road and sources the fabrics that Lever Style thinks will suit their customer. Lever Style is involved in ODM rather than just OEM and there is deep cooperation between the two companies.
The company is selective in choosing customers, targeting high volume business and seeking to grow as its customers grow. This often means turning away potential business that is small in scale and piecemeal. This is something that many firms are reluctant to do, particularly when they have spare capacity, but as Mr Szeto notes, spare capacity is an asset that once given away is harder to fill with other high-value adding orders. Low-value, patchy, and unpredictable orders are a distraction that Lever Style attempts to avoid. Lever Style has made some strategic acquisitions and it now runs a multi-product operation that allows it to cross-sell its products. For example, the company used to sell only shirts to Banana Republic, but it now also sells them suits. Mr Szeto notes that Lever Style’s “multi-product capability” has helped it to generate more sales with its existing customers.

Not all initiatives have succeeded. In the 1990s the company set up a branded retail division and licensed several low-end American brands. At the time, it was thought that higher margins could be made through retailing company-owned brands. Initially, the strategy worked and the company made decent profits, but in the late 90s, the division started to suffer significant losses. It was clear that retailing in Hong Kong and in China was going to become even more competitive and that the company did not have the skills or the knowledge to compete in that part of the industry. Lever Style got out of the business and is not looking to take on a similar challenge in the foreseeable future as it sees no natural synergy at an operating level between manufacturing and branding and retail.

Ensuring that the company has a diversified customer base was key in managing during the recent economic downturn. With this in place, Lever Style decided not to aggressively pursue new markets during the downturn but rather to focus on existing markets that were stable and to seek out developing them further for the time being. Lever Style is already well-known in its market. The company does not participate in trade fairs. The space that the company occupies is relatively small and potential customers know of Lever Style and its capabilities. Mr Szeto believes that as long as the company continues to act and think progressively and operate efficiently then new customers are likely to be attracted over time and deeper working relationships with existing customers will also result.

The fragmented nature of the garment industry and Lever’s focused strategy means that the company does not actively monitor its competitors. Instead, it looks to learn from other companies. Mr Szeto states that Lever Style “tracks other companies not because they are competitors, but so we might see where they are doing well and learn from them.” Lever has adopted Toyota production methods with its focus on designing out overburden, reducing inconsistency, eliminating waste, inventory management, and Just-in-Time (JIT) delivery.
Lever tries to remain environmentally and socially conscious. In addition to being careful to follow all appropriate laws and rules, in 2006 Lever Style became one of the first apparel manufacturers in China to be certified for SA8000, one of world’s strictest social responsibility standards. The company has also obtained ISO 9001:2000 certification, as well as being certified by third party compliance audit firms such as CSCC and ITS. In an environment in which pollution and sustainability issues are increasingly in the spotlight, having a reputation for environmental sustainability may lead companies to do business with Lever Style. Mr Szeto notes that “being sustainable doesn’t necessarily cost money in order to save money. It is not like that you have to spend millions of dollars to be sustainable, and being environmentally conscious gives a reputational bump. We would rather be known as a company that is environmentally conscious than as a polluter.” External recognition of Lever Style’s commitment to the environment came when the firm’s factory in Shenzhen was chosen as one of three pilot factories in the Pearl River Delta that was selected to run a WWF low carbon manufacturing programme.

Over the years, Mr Szeto has restructured the family owned business into more of a “modern competitive company.” This involved professionalising its leadership and management teams, and by encouraging a flatter management style to permit more direct and efficient communication, and more autonomous decision making. Mr Szeto believes that knowing his strengths and leaving it to others to do the things that he is not particularly good at has played an important role in Lever Style’s success. Mr Szeto has strong strategic skills, but others have excellent production skills and day-to-day management skills and he leaves these activities to them as much as possible. This frees up his time to add value where his time is best spent.

The company’s growth is evidence of its success in dealing with competitive pressures. Five years ago Lever Style was approximately half its current size. Mr Szeto benchmarks against the best, however, and notes that the company is not yet growing as quickly as Li and Fung which has doubled in size every three years in the past two decades.
**Future Plans**

Mr Szeto is bullish on opportunities in the industry saying that “people will always need to buy clothes. There are sunset companies but this is not a sunset industry.” With this mindset, Lever Style plans to try and double in size every few years and achieve at least double-digit growth annually. If all goes to plan, Mr Szeto hopes that Lever Style will be big enough to consider becoming a publicly listed company in a few years. Achieving this would put the company in a stronger position to continue its growth by using its equity to make strategic acquisitions.

In the long-run Lever Style plans to develop production capability outside of Mainland China, but it may do so by working with partner companies rather than “going it alone.” The idea would be to continue doing the high value-adding work in design, sourcing, and other services, and to subcontract the labour intensive work to companies in Bangladesh or Vietnam, for example. For now, there are plans to open a modern manufacturing facility in Huizhou, Guangdong Province in late 2010, with the prospect of producing 10 million garments annually and employing 8,000 workers, with a further overseas customer service office to be set up in London.

Mr Szeto is keen for the company to be recognised for doing things a little differently, for doing things in a better and more creative way. He cites role model companies as being Li and Fung in the garment industry and Dell in terms of changing a business model in a “revolutionary way.”

**Lessons from the Lever Style Case**

There are a number of lessons that can be learned from the Lever Style case.

- It is important for firms to play to their strengths and for owner-managers to do the same. With professional management in the firm, owner-operators can do the tasks that play to their strengths and leave other tasks to others.
- SMEs can successfully undergo generational change as long as succession issues are addressed at the right time.
- To understand where the firm is comparatively weak, the firm should benchmark against the best firms in the industry and to look at what the outside world is doing.
- SMEs can benchmark aspects of their business against leading firms from other industries and can incorporate processes and systems that work in other industries where possible.
- Firms should accept that uncertainty will always exist and they should not be constrained by it. Growth can and does occur in uncertain environments. What is important is that there are strategies to deal with uncertainty by engaging in scenario planning and in forward thinking.
- Companies need to continually adapt to their environment and not keep unthinkingly doing the things that worked for them in the past. Wishing that things would be different won’t change the environment. Adapting is the only way to prosper long-term.
- Costs should be reduced to the extent that this is possible, but most SMEs will not have the scale or the financial firepower to compete with larger firms on a cost leadership basis. Thus they also need to consider differentiation strategies.

SMEs can avoid fierce competition by choosing to do business in segments that have less direct competition. Firms need to identify and focus on value drivers that will insulate them from purely price competition. For most Hong Kong SMEs, this will mean focusing on creativity, innovation, continuous improvement, flexibility, and reduction in lead-times. Being smaller and more nimble, SMEs can often carve out advantages in these areas.

SMEs in the sector should look to add value to their customers by extending their operations to include ODM and OBM if they have the capability to do so. Firms that are able to offer their customers a wider range of services including design, material sourcing, manufacturing, delivery, customer service, and after-sales service are likely to be more attractive.

Doing ODM is likely to be simpler than doing OBM. Building a brand takes a lot of time and is expensive.

If the firm is able to integrate some of its activities or processes with its customers, then the customers are unlikely to give their business to another firm. Such integration requires regular communication to understand the needs of the customer and to coordinate activities.

It is important to choose the right customers and to not just accept any order that is offered to the firm. Companies should target customers that are likely to yield them profits and look to grow alongside their customers.

Building a customer base that is diversified but that places large and regular orders to create scale effects, and which will enable the possible cross-selling of other products, will create significant upside while reducing risk.

Following the abolition of quotas, diversification through the manufacture of multiple products is a more viable option for firms in the sector. Firms that pursue such a strategy will likely already possess many of the capabilities they need to succeed.

A reputation for reliability and having a good reputation in general are vital to SMEs. Doing business with firms with poor or uncertain reputations is just too risky a strategy for many global customers, who are judged not just on profits, but also on the labour and environmental practices of their suppliers. Further, the firm will need to communicate its positive reputation in convincing ways, because customers may not take the time to do sufficient due diligence themselves when they have other known low-risk options.

Firms in the garment sector should invest in staff recruitment and retention policies as much of the value in the industry is added through having the right people (or destroyed by not having the right people).

Success in the industry is dependent on identifying and understanding trends in fashion and producing to cater to that demand more so than it is on an ability to blindly mass produce. Managers who are in touch with the trends and who have foresight regarding the industry are a significant asset.

When in markets that require flexibility, firms should be careful not to overinvest in inflexible automation that is geared toward mass production of goods that may not find a timely market.
Federation of Hong Kong Industries

31/F, Billion Plaza, 8 Cheung Yue Street
Cheung Sha Wan, Kowloon, Hong Kong
Tel: (852) 2732 3188
Fax: (852) 2721 3494

Website: www.industryhk.org
Email: fhki@fhki.org.hk