

INSIGHT INTO INDUSTRY

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Economic Trends

Our national economy continues to gasp for the fresh air of economic recovery. We may see 1.5% growth this year compared with the 6% coming out of the recession a decade ago. Why?

Internal Forces

Consumer spending ain't what it used to be. Recoveries are fuelled partly by a resumption in consumer spending as companies re-hire workers and increase production. But many of the job losses this time have been permanent. In Ontario, 61% of laid off employees worked for companies that no longer exist. It doesn't take a genius (or her antipode-an economist) to figure out the implications. Adapting to a changed world economy has brought some crushing social and economic costs.

Household debt has increased and housing prices have dropped. Personal savings rates are lower than they were coming out of the 81-82 recession-about 17% then and under 10% today. Many consumers are dipping into savings just to make ends meet and a number have been left holding large mortgages on an asset that has declined in value.

Consumers who are employed are

nervous and this also affects their spending. They don't know if/when the high unemployment rate will become personal! Our economy at the moment is not growing fast enough even to keep up with new entrants to the labour force; it has to grow at almost 3% to do that.

We've made some productivity gains, painful in the short term but good for the future. Preliminary figures show that we've narrowed the gap between Canada and the US in terms of productivity: 1991 showed a 10% improvement in Canadian productivity and 1992 should see another 10%. Unfortunately, the cost in terms of jobs is high.

Fiscal policy has had to be restrictive. Governments have lower revenues from the slow growth, higher "safety net" costs and high debt loads (as we all know) so there is no room for the kind of spending on job creation that could act as a jump start.

Real interest rates are still high: no incentive for business investment especially in the face of slack demand from cash-strapped consumers.

Restructuring in the manufacturing sector has hit the service sector as

well. Everyone is rationalizing, bankruptcies are high. This package of factors makes for a very nervous, sputtering engine of economic growth in search of the right fuel.

External Forces

In the past, we have looked to the US for that fuel. But their recovery has been stumbling badly too. They have the same problems we do--only worse. More severe household debt, even lower personal savings rates (generally lower than Canada but still taking a

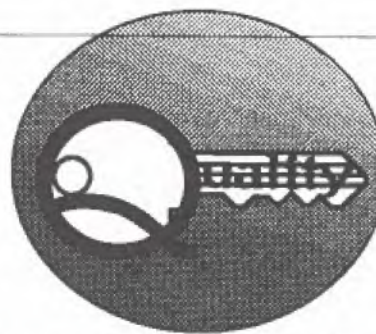


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Quality Cost = Actual Cost - No Failure Cost.

dive from about 8% in 82-83 to around 4% today), corporate indebtedness much worse than in Canada, restrictive fiscal policy and so on. Nothing here to act as a stimulus for Canada.

Similarly, nothing in Europe or Japan will assist North America. Europe is caught in the grip of very tight monetary policy as the Bundestadt seeks to stamp out inflation, so any growth there will certainly be weak. And in Japan, the bubble has definitely burst; real growth is expected to drop to an unprecedented 2% this year, picking up only slightly in '93.

If this explanation can be summarized, it would be that our economy is adapting to globalization and fighting off the lingering world-wide economic malaise. The good news is that our health is improving.

Total Quality: 10 Myths

Quality has become the watchword of the '90s amongst consumers and business. In fact, there is no greater influence on survival and success in business than Quality; and now that consumers (including businesses with their suppliers) have come to believe that Quality is their right, the very nature of the marketplace has changed. But perhaps like any revolution, there are lingering misperceptions about Total Quality: its impact, its methods and its future. Here are some which you may have heard.

Quality is very expensive: actually, it is truer to say that the absence of quality is extremely costly (see box). What about the cost of getting it wrong? The cost of lost opportunity? Doug Anderson of 3M says, "The cost of quality is simply taking the price we pay for error out of the cost of doing business;" i.e. Quality Cost = Actual Cost - No Failure Cost.

Quality is very complicated: the quality principles are simple really - listen to your customers, meet their needs, measure what matters not what's easy, value and involve your employees, minimize waste. And the practices aren't mythological - communication, training, recognition, teamwork. The subject has been complicated by a swirl of jargon. Vincent Sarni of PPG Industries says, in a demystifying phrase, "Quality is simply conformance to requirements".

Quality is the pinnacle of performance: total quality has little to do with providing the "Cadillac" of service or products. It has more to do with consistency; doing the right thing right the first time every time. It's meeting needs. Does MacDonalds succeed because it has the best food, or because it meets customer expectations? Quality is not perfection. Rather, it's an agreement between the firm (including public agencies) and its customer on expectations

and meeting them all the time.

Quality can be designated (e.g., ISO9000): don't discount their value but, gaining a quality certification may not be sufficient depending on the nature of your work. Certification doesn't ensure a motivated workforce, improved productivity, total company commitment. It often is focused on product characteristics like failure rates. But non-product features are very significant like delivery time, after sales service, correct billing. Total quality goes beyond competence; it permeates the organization and affects every process.

Quality does not apply to small companies: BC firms like Aitken Wreglesworth (architects), and Capilano RV Park wouldn't agree. Neither would Wallace Company the Houston-based petrochemical supply firm with 170 employees which won a 1990 Baldrige Award. These firms all operate on the belief that for small firms, quality is every bit the issue it is for larger firms. For them, all employees are in direct, daily contact with customers and they feel more vulnerable to the short term judgement of the marketplace.

Quality? We're doing it already: the Quality Council of BC released a survey earlier this year suggesting that close to 80% of BC organizations had adopted some form of quality initiative. But the emphasis varied across sectors: resource-based and transportation, communication, manufacturing and construction sectors were much

Management Practices

less likely to have formal quality initiatives in place. For over a quarter of the firms which had quality measures in place, these measures were informal and limited; among firms with a formal quality program, almost 30% had not decided what to name it.

The report notes that, "many organizations claiming to have quality initiatives in place do not necessarily have the degree of involvement

or philosophy consistent with a complete quality management approach throughout the organization."

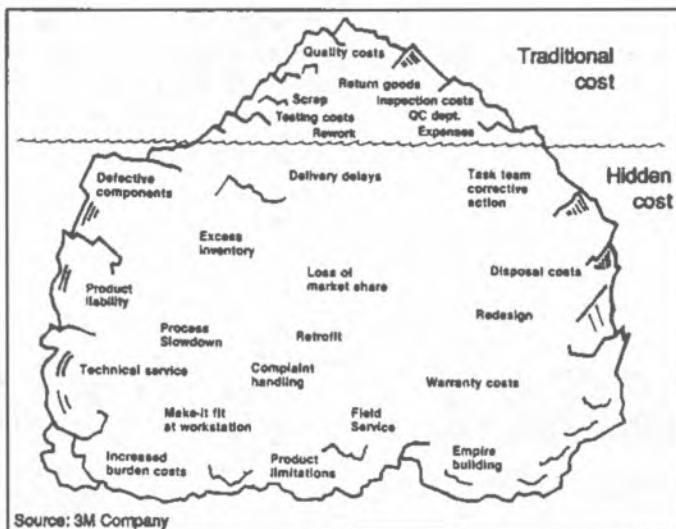
Quality, once achieved, remains: not so. Since quality is an attitude, a process--not a product--it needs tending and nurturing. It's the customer who decides what's good enough.

Quality is just another flavour of the month: the jargon may be, but the principles are not. Customers welcome quality: 90% say they will pay more for superior quality. Busi-

ness ignores it at its peril: you need look no further than the US semiconductor industry to see the long-term impact of quality deficiencies.

Quality is a cure-all: it can contribute to productivity, profit, market share, corporate pride..., in a word,

competitive-ness. It will not remedy strategic mistakes; it will not solve short term cash flow problems. Even



for firms which have been recognized for their achievements in quality, the future is not always guaranteed.

Quality can be bought: quality requires investment, but more than a quality manual and more than a consultant. The quality initiative is featured by innovation involving customers and suppliers, creative leadership, shared goal-setting; have you ever seen a sale on these? Instinctive quality behaviour can be nurtured; it cannot be hired.

Invest For Success

Your perception may be that the US market is pretty much the same as Canada's, only they are packed closer together and don't much enjoy lacrosse. Those who believe this, may also believe that the marketing, sales and service techniques which work well in Canada will work just as well in the US. The reality however may be very different.

Recent work by Neil Abramson of Simon Fraser University has researched the export strategies and performance of some 76 Canadian software firms. Prof. Abramson has identified the relationship between how companies conducted their US operations and the success they achieved. And it is reasonable to believe that the conclusions are relevant to other sectors, both goods and service exporters.

At the root of success seems to be this: **companies performed better the more closely they were aligned with their customer.** Radical!

Some features which stand out about the US market: US customers (business and consumers alike) expect products and services to be **designed to suit the local market**; they show a thinly veiled **preference for doing business with US rather than foreign firms**; and, they **expect ready access to after-sales service.** A high-performance business



strategy will be built around these characteristics.

Here are some specific strategic factors which led to higher performance: a) having marketing, sales and after-sales activities delivered from a US base of operations; this implies a direct foreign investment by firms because these activities have to be located in the US -- investment could mean wholly owned US offices, acquisitions or joint ventures; b) hiring and listening to bonafide US market experts; c) creating a learning culture in the firm -through broad-based team work among other things - which enables a progressively better understanding of the business practices and culture found in the US; and d) thereby not assuming Canadian experience will apply to circumstances (opportunities or problems) encountered in the US.

From the high-performance achieved by some firms, a number of other useful messages emerge concerning US market entry:

- have *growth in mind* as a strategy; your specialized market niche could be surprisingly large in the US;
- *don't be afraid of a high-priced niche strategy*; for many companies this was more effective than a low-priced higher-volume approach;

- *consultative decision making* processes (leading to shared goals, trust and commitment) were very much linked to market success;
- *collect as much information as you can*; companies were

...high performing companies retained their research and development, production and management in Canada. Their's was not a re-location strategy, but an investment one!

often not able to predict which information about an unfamiliar market would be valuable;

- *be persistent in the search* for just the right US marketing and sales help; it often was not available straightaway.

It is revealing that the high performing companies retained their research and development, production and management in Canada. Their's was not a re-location strategy, but an *investment* one!

The results of this work have encouraged similar research into software firms doing business in the Pacific Rim. Prof. Abramson would be happy to talk further about the details of his research and can be reached at (604) 291-5891.

Do you sell services to other companies?

Attend "Quality Service: The Business to Business Imperative", a one-day quality conference co-sponsored by ISTC and the American Society of Quality Control. November 20th at the Waterfront Centre Hotel.

Cost: \$170/\$195. Call: ASQC at 451-0150

Perception vs Reality in Asian Business

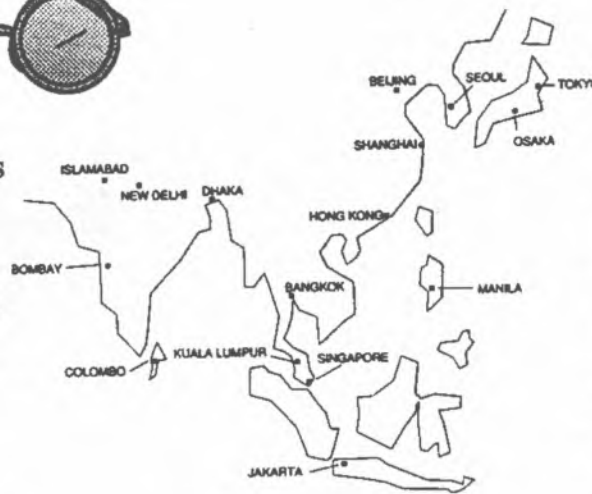
Export Markets



Too many Western companies develop their Asian business strategy around wrong perceptions. Reality, when it hits home, can hurt. Here are some interesting cases that point out lessons Canadians can use:

Perception: that another country's legal framework can be taken for granted. Fatal! Fusion Systems Corp. patented a high-power microwave ultraviolet lamp in Japan. It assumed that Japan's patent process worked the same way as the US process: on a first-to-invent basis. In fact, Japan's is a first-to-file patent process, and Fusions Systems eventually wound up in a legal dustup with mammoth Mitsubishi -- ouch! This is just the start. In Asia there are legal systems with elements of the British codes circa 1940 (Sri Lanka), Islamic law (Bangladesh), and a packet of other surprises for the unwary.

Perception: that the right business partner for you in an Asian country is (easy, check them off) available, aggressive, well-connected and experienced. Reality: the right business partner in Asia is somebody you pains-



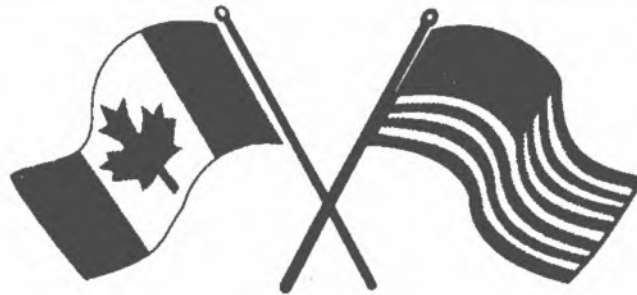
takingly research, carefully select and only slowly develop business with. Asians do this, for good reasons -- in a region where the law is not much used to clear up business disputes, your business depends on how straight your partner is. Lured into a joint venture for a manufacturing plant with a well-connected and experienced family business in the Philippines, *one American electronics firm was "wined, dined and robbed blind."* In the end, it pulled out with nothing.

Perception: that you should use your usual management selection process to pick your Asia business manager: find someone at the right level with the right experience in a product or functional area, who

says he/she wants to go to Asia. Reality: you might be better off putting knowledge and personal skills relevant to Asia at the top of the criteria for selection. Your Asia manager must be more sensitive to the different cultural realities of the Asian market, and build business by nurturing personal contacts and relationships. Language skills may be key -- as a well-known American research organization found to its cost when it posted a non-Japanese-speaker in Tokyo. You also might want to carefully check out people's motivation for saying they want to go to Asia. One multinational bank manager only wanted a foreign assignment for the money -- high alimony, you know.

Perception: if it'll sell here, it'll sell there. Reality: oops! With its whopping 60% share of the Japanese instant-coffee market, giant Nestlé felt confident as it turned to the Japanese chocolate market. After all, it knew what chocolate was, and how to market it -- by targeting adults in supermarkets as it does successfully in other countries. *But to Japanese consumers, chocolate was cheap kid's candy sold in small stores;* they had little yen for it any other way. Nestlé suffered for its wrong perception. Or try this one. *General Foods had no luck trying to sell its well-known Tang to Indians* -- too sour (that's what the Indians felt!), too expensive, and breakfast drinks were unfamiliar to the Indians.

Special Feature



Perception: (opposite from above) Asia is so different a market that absolutely none of a company's home experience applies. Reality: a company should always remember its best strengths. Trying to adapt its Barbie doll for Japan --- girls there have usually dressed up their dolls for display rather than play -- Mattel stiffened her, thinned her and knocked years off her age. The new Barbie had little glamour and mystique. Worse, since she couldn't bend or move, all her accessories like cars, houses and furniture that drive North American parents into the poorhouse couldn't be used or peddled with her. Needless to say, in 1991 Mattel re-thought its whole strategy and reintroduced the standard doll.

Canadian companies can certainly find some lessons in these tales of how our American compadres have gone wrong in Asia. If you want to read more of them, you might ask your library to chase the study we cite here. It's "Asia: Strategic Blunders and Tactical Errors", which is report 810 by SRI International's Business Intelligence Program.

By L. Peach

Cross Border Misperceptions

SAVINGS GALORE!!! Isn't that the general perception that Canadians hold about doing business, be it shopping, manufacturing, investing or paying taxes, in the US? It seems as if everyone these days is touting the US as the place to locate. But is it really such a mecca of profit pleasure, does the perception equal reality?

In terms of cross-border shopping, no doubt about it, Canadians are spending big bucks down south--in the neighborhood of \$2.5 billion in retail sales in 1991, with British Columbians alone contributing about \$650 million to the total.

But, recent studies by the Creative Research Group and Herbert Grubel, an economics professor at Simon Fraser University, show that *while there are some US bargains, it very much depends on what you're buying and what else you do when you're down there.* That's because while a particular product may be cheaper (see chart because not all are), many shoppers turn trips into mini vacations and spend additional money on hotels, food, and travel (approximately 2-7 hours per trip in travel time alone). *Ernst & Young (1991) estimates that for every dollar Canadians spend on US goods, they spend \$1.48 on services-*

-services which aren't necessarily cheaper than at home. For example, a hotel and 3 meals in Vancouver will run you about \$US155, in Calgary--\$US126 and in Edmonton--\$US117. Compare that to \$US143 in Seattle, \$US185 in San Francisco and \$US144 in Denver.

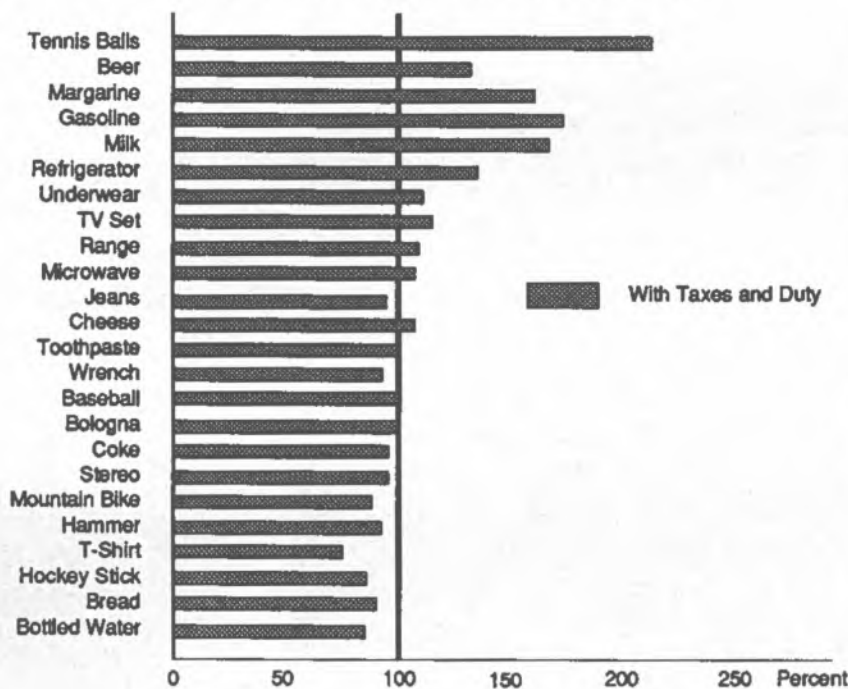
And what about manufacturing? People always seem to be saying "it's cheaper to operate in the US because of the lower taxes and labor costs". But does this apply across the board?

There have been a number of studies recently on this subject, all with varying conclusions as to what the advantages are and where. And although the general (and possibly growing) perception is that the real advantages lie south, this isn't by any means clear or conclusively proven. *What is clear, is that the issue is contentious and that the advantages are not universally or uniformly applicable to all industries, nor even to all firms within one industry.*

For instance, we understand that *in electronics manufacturing generally, BC is cost competitive with Washington State, Oregon and California*, according to a recent study by the BC Government. And, our tax environment is actually more favorable. Consider these facts about electronics manufacturing:

Is It Really Cheaper?

Canadian Prices as a Percent of US Prices



Source: Grubel and Khangura survey of stores in Vancouver, BC and Bellingham, Washington, in March, 1992.

Labor costs in BC...

- Average hourly compensation for production workers is on par with Washington State, 11% higher in Oregon and 8% higher in California;
- Payroll taxes (social insurance, worker's compensation and unemployment insurance) are 60 to 100% greater in the US;

- Medical insurance costs, a common discretionary benefit, are four to six times higher in the west coast states; and,
- Compensation for professional and technical workers is often 10-15% below Washington and Oregon levels and 15 to 30 percent below Silicon Valley norms.

Land and building costs in BC...

- Both construction and land costs in the outer suburbs are roughly equivalent between Vancouver, Seattle and Portland and significantly higher in Silicon Valley;

Energy costs in BC...

- Electricity costs in Vancouver are on par with Seattle, 20% lower than in Portland and almost 50% less than Silicon Valley;
- Natural gas costs are one third higher in San Jose, compared with Vancouver.

Taxation in BC...

- Although difficult to estimate, a BC electronics manufacturing firm has a lower total tax burden (37%) than its counterparts in Washington (41%), Oregon (43%) and California (44%)*;
- Tax savings from research and development are roughly 10% more favourable.

Again, it would be nice if we could generalize and say that a similar

* Tax burden calculation verified by Price Waterhouse

“ *When you actually start looking into operating down in the US, it's not a bed of roses; there are a lot of road blocks and negatives that you wouldn't normally expect or see.*

Ray Goddard, Savolite Corporation

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competitive advantage exists for all industries and all companies, but we can't. *Each case requires its own examination.* If your business is light manufacturing, you may find urban Vancouver costs too high. What we can do, however, is tell you about some companies who have investigated (or experienced) the situation on their own:

Ledalite Architectural Products Inc., a Langley-based manufacturer of interior fluorescent lights for transit systems, hospitals, schools, offices and grocery stores, closed down their Seattle branch plant and shifted 10 jobs to a new plant in Langley. **Peter Murphy, President** says, *“we had a perception that our costs would be lower down there but in reality it's only marginally cheaper. And if you're only saving marginally, then you're going to face the other increased costs.”* The years spent training Canadian workers and the cost of starting that process over were major factors in Murphy's decision to stay in BC. Ledalite employs 110 workers and is forecasting \$14 million in sales this year, with US customers accounting for 70 percent of revenues.

Savolite Corporation, which makes cleaning and sanitizing chemicals, relocated their manufacturing operation from Seattle to Anacis Island last year. Why? **Vice President, Ray Goddard** says, *“when you actually start looking into operating down in the US, it's not a bed of roses; there*

are a lot of road blocks and negatives that you wouldn't normally expect or see.” Savolite found that bank financing for chemical companies was more difficult in the US, permit processes were a nightmare, government assistance was more attractive and flexible in Canada and land values and labor rates were comparable. The Savolite group of companies expects to do about \$65 million in sales throughout Canada and the US in 1992.

David Hubbard, owner of **20/20 Products Inc.**, BC's foremost manufacturer and supplier of optical cleaning products, chooses to operate in Chilliwack because simply put, it makes more sense. Hubbard says, *“in the US, I have to cut my prices to compete with manufacturers with 10 to 20 times the buying power that I have and if I do that, I don't make any money. We thought about opening a branch in Bellingham awhile back, but after seeing how much time, money and red tape was involved in set-up, we decided that it was just more trouble than it was worth.”*

Toronto-based **Magicuts'**, a hairdressing franchise successfully expanded into the US but not without frustration. Credit was harder to get (because American suppliers won't extend 30-day terms to 60 or even 90 days, like some Canadians) and unemployment

insurance is handled differently. *Unaware of the US rules, Magicuts spent more than \$50,000 unnecessarily before it learned how to control its claims.*

Swedish Jeweler Ltd. opened in an upscale shopping mall in a high-income suburb of Seattle, but found that its exclusive European jewellery wasn't as popular with Americans and had to alter its product. **Helen Stewart, President**, says with the benefit of hindsight she's doubtful she would do it again. *“If we had spent the same amount of money and effort in setting up a store in Calgary we may have achieved better results.”*

This newsletter is published quarterly. For more information contact:

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