

Candidate: Francesco Nicoletti
621721

ID:

Supervisor: Professor J. A. Mathews

Assistant Supervisor: Professor M. Quintano

Thesis: “Evolution of contract manufacturing and global value chains with special reference to the continuing sources of competitive advantage of Li & Fung.”

Summary

The reasoning structure of the thesis started recognizing that two interdependent dynamics are transforming international trade and global economy: the reorganization and the relocation of the production of goods and services. These dynamics have led to the emergence of value chains with a global character that involves the coordination and reintegration of production activities along global networks of firms, tied together by non-equity linkages through a variety of relationships as subcontracting, licencing, common standards etc. Globalization, progresses in logistics and information technologies and a simplification in trade regulations have enabled the transformation of over-engineered supply chains into highly fluid and global dispersed marketplaces.

The work followed explaining how the disintegration of supply networks has created an environment of business complexity that has intensified the basic managerial challenge of the coordination of activities along the value chain. This state of complexity and disintegration is creating inefficiency and enhancing coordination costs. Both the buyers side, so for example large Western OEMs, but also the supply side where many small and medium enterprises can be found, have difficulties in repositioning in this new scenario and are not able to sustain a global

competition. This state has called for the emergence of a new typology of economic actors, whose role is managing a process of reintegration of all the players.

This reintegration is a phenomenon still ongoing in many industries and is taking the form of global operational webs or networks, governed mainly through a model that has little to do with a tight management, but resembles more to an orchestration of all its participants. That is why an appropriate definition for this kind of aggregator companies has been found in the term of “network orchestrators”.

The task of configuring and orchestrating these global operational networks is pivotal in allowing businesses to operate with speed and agility, to manufacture in remote low costs regions, to access specialized design talents, to distribute with close to the customer efficiency and to get to the market faster with innovative products and services.

The thesis presented evidence that all these actions are mastered by Li & Fung which represents the purest example of network orchestrator. The company founded 100 years ago in Guangzhou has evolved from a regional sourcing agent to a manager and deliverer of manufacturing programs and from a dispersed manufacturer to a network orchestrator. The specific success of Li & Fung is even more striking because the company does not operate in an high margins or innovative business, but in the textile sector that is one of the oldest and lowest growing industry.

The work has stressed the concept that these emerging aggregate players are not bubble firms, but will become companies of the future because they are intimately linked with the rise and diffusion of these global value chain models.

They play the crucial role of filling the gap in the relations between big and small economic actors spread all over the globe, a necessity that is present not just in the textile industry, but in many others from automotive to electronics. Their nature of neutral third parties that coordinate and align incentives for all the network participants, is becoming more and more fundamental and irreplaceable.

From its side Li & Fung has benefitted particularly from the historical advantage of its location, in the middle of the East Asian region and from a broad and always expanding network of suppliers. Nowadays it is the leader in global sourcing and I explained that its competitive advantage is based on the unique capacity of creating customized supply chains for its clients and being a “one stop shop” for them taking up not just some portions of their value chain, but the overall process. It does so implementing an innovative managerial approach called network orchestration that consists in creating loosely coupled relations with all the independent actors of the chain and establishing a system of incentives to reward them and to make their participation in the network attractive.

Finally I reasoned on the fact that Li & Fung destiny is not too much tied to the persistence of this regions as a cheap labor source, because its network of suppliers is well diversified and already covers keys areas such as the Indian subcontinent, the Caribbean, South America and the Mediterranean basin. Even though China remains its major sourcing country Li & Fung can count on a comprehensive supplier base whose strenght is not just being an alternative source for those looking for cheap production places, but being a global reservoir of specialized suppliers. That is also why eventual future wage increases in East Asian countries will not dismantle the competitive advantage of Li & Fung’s business model. Conversely as a future perspective I foresee that the potential upgrade of China and other developing countries and their gradual transformation into consumer markets, will offer to Li & Fung incredible growth potentials for “selling to the source”.