

Chinese Management Style in Question: Foxconn

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1. Introduction

Foxconn Technology Group is one of the world's top suppliers to global computer, communication and consumer-electronics ("3C") leaders. From its beginning as a manufacturer of plastic buttons for TV in the 1970s, Foxconn has developed into a producer of parts for computers such as mainframes, memory expansion boards and graphic cards (other than central processing units and memory). As for the manufacturing of end products, the company rolls out computers, mobile phones, game consoles, MP3-players, monitors and digital cameras.

Foxconn's main clients include global electronics manufacturers: personal computer manufacturers such as Dell, Hewlett-Packard, Lenovo and Sony, consumer electronics companies such as Sony, Apple, Nintendo, and Microsoft, and mobile telecom companies such as Nokia, Motorola and Apple.

At the helm, steers a proponent of top-down leadership, Guo Tai-ming, commonly known as Terry Gou. It is a management style typically seen in Asian companies – and second guessed. While the stellar growth and stature of Foxconn is irrefutable, similar reassessments are being made toward Gou's management style. This report looks at the successful development of Foxconn and Gou's philosophy.

2. Stages of Development

Foxconn has achieved exceptional capabilities in module design and manufacturing in three stages of development that elevated its competitiveness to global standards.

In the first stage (1975-1980) Foxconn fostered workforce agility to produce module through manual work. By doing so, it provided a high quality of services to client companies while enhancing its capabilities in R&D and manufacturing.

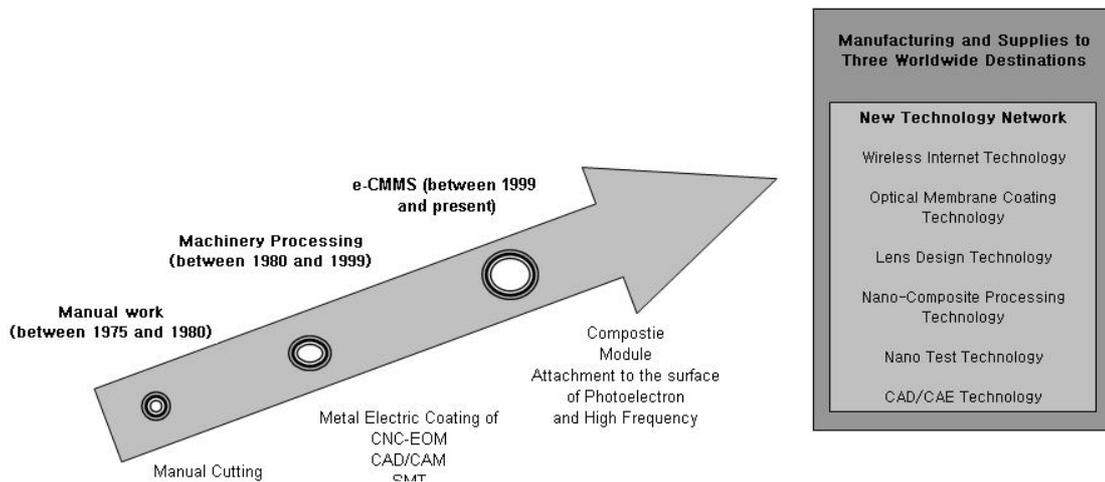
The second stage (1980-1999) overlapped with the emergence of the Information Age. The company shifted from manual production to machinery processing stage. Foxconn started its electro-chemical coating business, pouring massive investments into computer-aided design and computer-aided manufacturing. It also focused on the precision of module devices, yielding modules by item, material, and use.

By 2000, Foxconn had begun with its proprietary eCMMS business model, which redefined the company as a service provider rather than a manufacturer. eCMMS stands for e-enabled Components, Modules, Moves and Services. It integrates mechanical, electrical and optical capabilities into a one-stop system that provides a wide array of solutions to clients, including design, assembly, manufacturing, maintenance and logistics.

Foxconn formed production facilities in three regions (Asia, North America and Europe), consolidating the progress of its purchasing, manufacturing and quality control.

Regarding the delivery of goods globally, Foxconn invested US\$30 million in an ERP¹ system (which guaranteed quality and punctual delivery).

Foxconn's Stages of Development



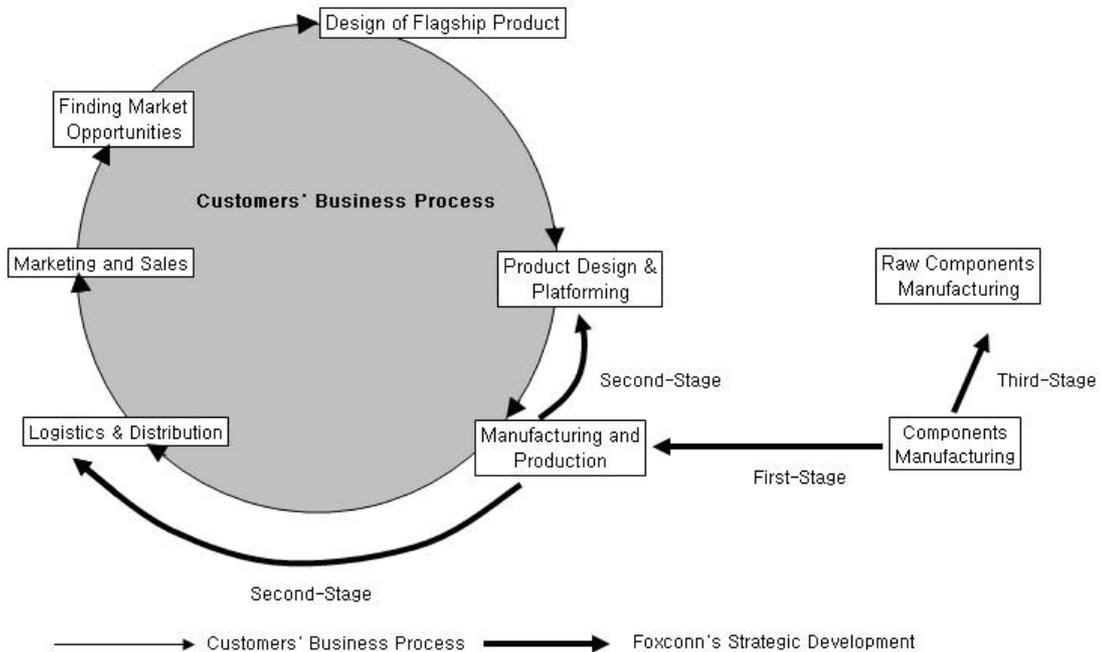
Foxconn shifted its emphasis to joint-design manufacturing or joint-development manufacturer (JDM) from original equipment manufacturer (OEM) and original development manufacturer (ODM).

Foxconn applied its cost leadership (derived from its vertical integration of production) and efficient customer response to consumer electronics (PCs) and telecommunications. At that point in time, Foxconn's products included computers, cell-phones, Internet telecommunications equipment, and game consoles. Swift customer service and support and high-quality products have satisfied customer needs.

Most of the client companies consigned product processing to Foxconn because the company was hardly regarded as a competitor. Orders from Nokia (Nokia branded itself as an Internet company in 2007) reportedly accounted for 50% of Foxconn's total mobile-phone substitute processing, mainly due to its strengthened cost leadership in the manufacturing sector.

¹ ERP is the enterprise resource planning.

Foxconn's Adaptability to Client Business Process



Foxconn modified its strategy after latecomers began copying its business model. Bydauto is a prime example. The company emerged as Foxconn's major competitor when Bydauto entered the mobile-phone substitute processing market equipped with its cost competitiveness. Motorola and Nokia relied more heavily on Bydauto for manufacturing to prevent Foxconn's potential domination in the market.

Bydauto Emulating Foxconn's Growth Model

- ※ Bydauto, which started business as a mobile-phone battery manufacturer in 1995, copied Foxconn's vertical integration strategies in 2003, entering the mobile-phone substitute manufacturing market.
- ※ Bydauto began producing the substitute production of all mobile-phone parts (batteries, buttons, and chips exclusively).
- ※ Total profits for mobile-phone substitute processing amounted to 5.1 billion yuan in 2006, skyrocketing 179.2% from the previous year.
- ※ The number of employees who departed from Foxconn to start work at Bydauto in 2003 reached about 400. Most of them were high-skilled employees and high-ranking executives.
- ※ The continuous drain of Foxconn's core workforce and Bydauto's rapid growth in the mobile-phone substitute processing business was a wake-up call that revealed Foxconn's complacency.

Foxconn also encouraged M&A activity and cooperation to realize business diversification. In addition, the company used intellectual property rights to build entry barriers.

3. Production bases & HR Policy

Foxconn has realized economies of scale through cheap labor and cost advantages found in China. It has acquired large-scale production capabilities in developing modules, assembling bare-bone computers, and releasing finished products. Also, Foxconn adjusted production to fall in-line with its relatively less-educated Chinese workers.

Foxconn is one of many exemplary companies which have realized co-growth with Shenzhen, its base in southern China. Shenzhen, a small fishing town near Hong Kong, was designated a free economic zone in the 1980s and since then has turned into a teeming metropolis. In 2007, Foxconn accounted for 20% of Shenzhen's exports and paid five billion yuan in taxes.

Foxconn's presence also has bolstered indirect economic activity in Shenzhen by implementing municipal support programs. In 2001, Shenzhen custom's office introduced a network-based management system to simplify custom procedures. Also, the government of Wuhan made a 2.8 billion yuan investment in 2007 to construct a 13 km-long railroad for Foxconn's exclusive use in order to attract further investments into the city.

Furthermore, Foxconn established a mobile-phone factory in Langfang, Hebei Province, and integrated it with its wireless communications handset business in Yantai. It also formed an industrial belt related to laptop parts around the area of the Yantze river delta.

In 2007, Foxconn also increased its investments in Shenyang to advance itself into the auto parts and computer numerical control system industries in three provinces of Northeast China (Liaoning, Jilin, and Heilongjiang provinces). Lastly, Foxconn is to complete its construction of a magnalium and module production site in Shanxi province this year that will produce 50% of the world's magnesium.

Foxconn's Production Sites in China

Location	Establishing Year	Products
Kunshan County of Jiangsu Province	1995	PC Connector
Shenzhen in Guangdong Province	1996	Barebone computer, consumer electronics
Beijing	2002	Wireless communication products
Shanghai	2002	PC parts, semiconductor facilities
Hangzhou of Zhejiang province	2003	Wireless communication products (Personal Access System)
TaiYuan, ShanXi province	2004	Components of 3C products, alloy materials
Yantai in Shandong province	2004	Computer cards
Tianjin	2005	Wireless communication products
Jincheng city, Shanxi Province	2006	Optical products, broadband communication products
Huai ' an, Jiangsu Province	2006	Computer peripherals

Langfang City, Hebei Province	2007	Components of cell phones, high-precision modules
Wuhan, Hubei Province	2007	Electronic products integrated with optical technology and machinery
Shenyang in Liaoning Province	2007	Computer numeric control system
Qinhuangdao Hebei Province	2007	High-tech electronics (cable system for signal transmissions)
Nanjingof Jiangsu Province	2007	Software and design development
Jiashan, Zhejiang Province	2008	Products related to high-precision modules

Foxconn’s human resources management operates through strict supervision and a control system based on military management. It urges employees to make use of production know-how quickly and to introduce a system abiding by “Management by Objective,” which is directly connected to employee wages.

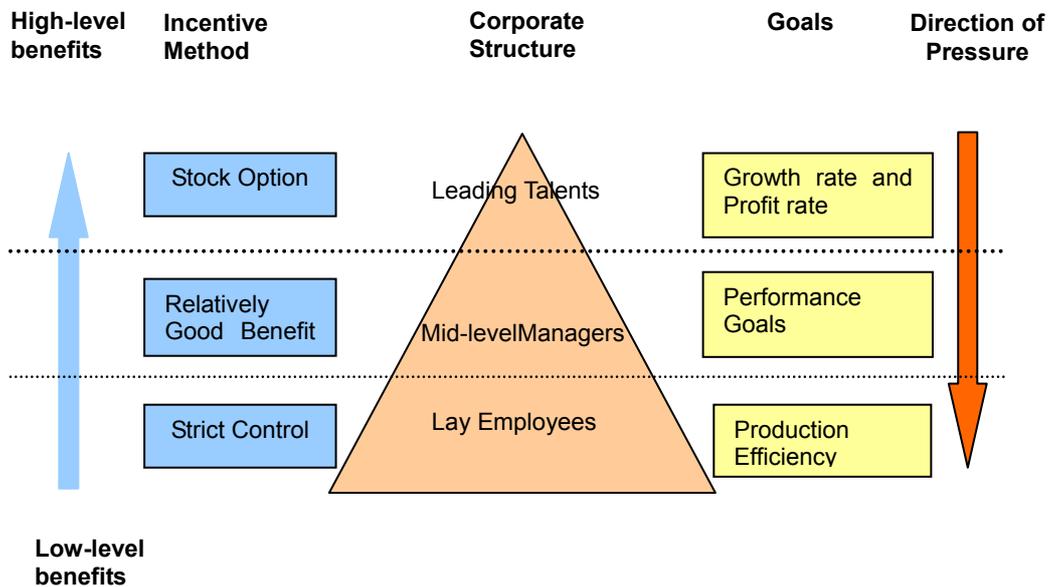
Mid- and high-level managers participate in setting up overall strategy, executing them and reducing costs. They offer products at lower prices than their competitors. They try to meet target profits through strict business management and efficient production processes.

Foxconn adopted a performance-based salary system and incentive mechanism. Foxconn’s mid- and high-level managers are granted stock options to help boost morale. Mid-level managers can enjoy competitive benefit plans that include on- and off-site leisure facilities and the ‘138 home plan².’ The company is even planning to build golf fields for senior managers.

Foxconn hires people, who are competent but less educated and less experienced, and pay them according to their performance. 75% of Foxconn’s employees are vocational high-school graduates.

² Selected employees with superior performance evaluations after a year of employment are given benefits such as subsidies and incentive pay if they sign a three-year contract. Additional benefits accrue if sign up for eight years.

Foxconn's Human Resource Management Structure



4. Guo Tai-ming's Leadership

Foxconn leader Guo Tai-ming has repeatedly demonstrated insight and an ability to forecast market trends. Entry into the connector market in 1990, vertical integration, and advancement into the electronics manufacturing industry were all done under his watch.

Guo finds potential customers and forms an alignment with other companies in advance of other competitors. In 1995, he invited Michael Dell, CEO of Dell Computers to visit a Foxconn factory in China. At the time, Dell was not relatively known in China and Foxconn had no business relations with Dell. However, the meeting culminated into a business partnership, paving the way for Foxconn in becoming one of Dell's largest component suppliers.

As for Foxconn's LCD panel business, Guo decided to advance into the market at a time when Japanese LCD makers were on a downward path in tandem with an emergence of Korean companies. He wished to enter the market when the LCD panel supply chain further matured.

His adventurous managerial philosophy paved way for corporate innovation and development at Foxconn. Even though Guo was bold in his decision to kick off risky strategic investment projects, he was prudent in trying to keep risks minimal. In order to improve capacity in Foxconn's mold manufacturing, Guo funneled most of the company's early stage revenues into building mold facilities. With high uncertainty, the decision to invest in mold manufacturing facilities at the time was taken with significant caution.

‘Autocracy for Company Benefit’

The focal point of Guo’s leadership stands on “autocracy for the benefit of the company.” Guo believes corporate decisions relying solely on decisions of the CEO are much more efficient than wasting time and energy in going through inefficient discussions and the collecting ideas. Guo opposes independent directors on Foxconn’s board, saying they lack industry expertise and may not even have experience in running a company.

According to Guo, a leader should possess determination and courage in order to implement his form of autocratic management. “A leader should convey his aspirations thoroughly to subordinates by explaining and deciding firmly matters at hand,” he says. Guo explicitly defines responsibilities, fair rewards and disciplinary action and while he keeps key decision-making to himself, Guo empowers employees. “Foxconn’s management believes supervision can be kept to a minimal when the transfer of responsibility and jurisdiction gives individuals a sense of responsibility in their work. This is our corporate culture,” Guo explains.

Excerpts from Guo Tai-ming’s “Management by Wandering Around”

-Air-conditioners in production facilities for G5 computers in Shenzhen were prohibited due to technical conditions. This was at a time when summer temperatures reached 37 to 38 degrees. To aggravate matters, the refusal by Japan to transfer needed technology and the outbreak of SARS left us carrying out both manufacturing and technological development simultaneously and on our own. Our management team stepped up to the challenge, pulled up their sleeves and began working with field staff. This fostered trust and encouraged company dedication. I call those two months a period of “blood, sweat and tears.” Our employees retained clients through the fulfillment of orders despite the looming threats coming from the SARS epidemic.

- As a leader of a company, where a single action speaks louder than a hundred speeches, taking initiative is much more effectual than one amicable word. Trust in management begins here.

Guo Tai-ming’s words from Taiwanese magazine “Tian Xia”

Guo’s sense of responsibility and his rather imposing reward and punishment system led to a boost in operations through more effective employee performance. He went so far as to bind his business experiences into in-house educational curriculum in order to share his thoughts with company subordinates.

Some high-ranking managers left the company because they could not adapt to Guo’s autocratic leadership. Even Guo Tai-qiang, his brother and head of Taiwan operations, resigned on the eve of attempting to push into the US market because of a conflict in opinion. Chen Yifei, the engineer in charge, and You Xiangfu, the director of connector

business, resigned, only to return with a considerable amount of resentment.

There is no doubt that Guo's full understanding of Foxconn and the business environment along with his managerial style allowed for the timely execution of successful strategies. Unfortunately, Foxconn's manufacturing-centric development strategy poses some latent risks. The company's competitive advantage relies on "manufacturing technology" as well as the cheap cost of labor. New labor laws and tighter regulatory measures, however, would no doubt drive up labor prices. The overall cost advantage strategy can easily be imitated by other competitors.

Military-like management may have worked before but will soon be outdated. Military-style corporate culture has begun to stymie corporate development, it being the root cause behind an outflow of mid-level managers. Likewise, Foxconn's over-the-top managerial controls have begun to arouse discontent with production workers.

If Guo's influence decreases, such hard-line managerial measures may come back to haunt him and/or his predecessor. If the follow-up to Guo shows a relative deficiency in vision or reliability, Foxconn will find it difficult to maintain its coherent developmental strategy.

Clashes with middle management and labor workers may distort the public's corporate image. Unlike executives, who are well compensated and have much respect for Guo, mid-level managers and production workers are less loyal and are less compensated. If employee dissatisfaction is leaked to the media, Foxconn's corporate image may indeed suffer a significant setback.