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Hon Hai To Make Bigger Bet in China

Plans to shift some operations out of Shenzhen as company expands inland

This month, wire services reported that **Hon Hai Precision Industry** (Tucheng City, Taiwan) plans to add up to 400,000 workers in China over the next year. This massive hiring effort, which is far beyond what any other company in the outsourcing space could contemplate, will make Hon Hai's Chinese workforce as large as 1.3 million.

In addition, the company intends to downsize operations in Shenzhen, where it endured a series of suicides this year, prompting scrutiny of its management practices (June, p. 1). Over the next five years, the workforce in Shenzhen will shrink by some 170,000, according to wire services, and *Reuters* reported that Hon Hai employs 470,000 people there now. The provider's focus in Shenzhen will shift toward R&D, testing and alternative energy work, reported *Bloomberg.* Hon Hai recently announced two wage increases in Shenzhen that will more than double base pay.

While the shift in production will allow Hon Hai to lessen the effects of labor cost increases in Shenzhen, the company stated that it is responding to "broader societal trends and shifts in China." The idea is to create more jobs, particularly in inland China, that enable employees to work closer to their home towns. In line with this objective, Hon Hai has undertaken factory projects in two inland provinces, Henan and Sichuan. Both offer an abundance of workers. Reportedly, some amount of Shenzhen production will be moved to interior locations.

Hon Hai wasted no time getting production started in Henan. Manufacturing began this month in a temporary facility located within Henan's capital, Zhengzhou, according to published reports. The Zhengzhou operation will mainly assemble **Apple's** iPhone, reported China's official *Xinhua News Agency*, which cited an agreement between Hon Hai and the government of Zhengzhou. Note, however, there have been conflicting reports about whether or not Apple's iPhone and iPad production will be transferred from Shenzhen.

The company has already invested $12 million in this mobile-phone operation, according to information posted on the Taiwan Stock Exchange. *Xinhua* reported that investment in this Zhengzhou operation will amount to $100 million, and a permanent factory is expected to be up and running within a year with an eventual capacity of about 200,000 handsets a day. Hon Hai has also invested $20 million in a second mobile-phone activity in Zhengzhou, and according to *Xinhua*, this facility will involve spending $120 million. At this writing, the status of the second operation is unknown. Together, the two projects will reportedly require an overall investment of $740 million, all things considered, but Hon Hai's contribution has not been disclosed.

Besides cell phones, the new plants will also manufacture base station hardware, core network equipment and

Some articles in this issue

two types of molds, *Xinhua* reported, citing official documents. According a report by the news agency, Hon Hai intends to hire 200,000 workers for its Zhengzhou operations by the end of 2011.

Reportedly, Hon Hai also has its eye on Henan province for its previously reported diversification into the retail sector. The company has been meeting with provincial officials about setting up approximately 2,000 stores in the province, according to *Xinhua*.

Also part of Hon Hai's inland expansion are two operations planned for Chengdu, the capital of Sichuan province. The company has already committed $20 million for a tablet PC unit in the city and $12 million for a set-top box unit there. Hon Hai has begun to recruit 1,000 workers in Chengdu, with the aim of ultimately hiring 100,000 people for its Chengdu activities, reported *China Daily*, citing a local newspaper. It was reported last year that the company had decided to invest $1 billion in a Chengdu production base focusing on optoelectronic products (Oct. 2009, p. 4). According to recent published reports, Hon Hai has also proposed a joint venture to erect an 8.5-generation LCD fabrication plant in Chengdu at a total cost of $4 billion.

Hon Hai's expansion into southwestern China is not limited to Chengdu. Recently, the company began volume manufacturing ahead of schedule at a new notebook plant in the city of Chongqing, *Digitimes* reported (see also April, p. 1). Hon Hai is said to have other projects in mind for its base in Chongqing. The Communist Party's *People's Daily Online* quoted a buyer in Hon Hai's Communication and Network Solution Business Group who said his department in Shenzhen will relocate to Chongqing. Note that **Cisco** has pledged to work with the city government on the development of a telecom manufacturing base in Chongqing (April, p. 1). Although surrounded by Sichuan province, Chongqing is administratively separate from it and reports directly to the central government.

Wuhan in the central province of Hubei has surfaced as another location reported to have a role to play in Hon Hai's inland migration. Some news sources have said Wuhan will take over Shenzhen's production of desktops. In particular, Hon Hai has entered into an agreement with the government of Wuhan to send the company's desktop assembly lines, whose capacity is 68 million PCs a year, plus printer and monitor lines to the city, reported *Digitimes*, which relied on a *Xinhuanet* report in Chinese. By the end of the year, the company will hire an additional 15,000 workers for its Wuhan site, according to *ShanghaiDaily.com*, which cited a Wuhan newspaper.

While Hon Hai, the parent company, has not said which Shenzhen activities will be sent where, its majority-owned cell-phone subsidiary, **Foxconn International Holdings**, reportedly has addressed a production transfer. Citing a spokesman for FIH, *The Wall Street Journal* reported that FIH plans to finish moving its principal manufacturing lines this year from Shenzhen to Langfang in the northern province of Hebei.

Other cities also appear in some reports of Hon Hai's effort to rearrange its China operations. A *Xinhuanet* report quoted a Hon Hai group employee in Shenzhen as saying that workers and manufacturing lines had moved to Tianjin and Wuhan in June. Another worker told *Xinhua* that half of his department in the Communication and Network Solution Business Group will relocate to Tianjin. Anecdotal reports aside, Hon Hai is expanding in Tianjin. According to a posting on the Taiwan Stock Exchange, the company has made an $18-million investment in a new server unit in Tianjin.

A report originating from the *China Business News* and circulating online said Hon Hai will transfer iPad manufacturing to Taiyuan in Shanxi province from Shenzhen. However, as mentioned before, earlier reports did not agree.

Finally, the company will move PCB fabrication to Qinhuangdao in Hebei province, solar equipment production to Jincheng in Shanxi province, and video game work to Yantai in Shandong province, according to a website under China's Ministry of Commerce. Note that Hon Hai recently put $14.1 million into a Qinhuangdao manufacturer of PCB products out of a $33-million planned investment in the business, of which Hon Hai owns 43% indirectly. Both Hebei and Shandong provinces are coastal as is the city of Tianjin. So not all of the Hon Hai group's expansion is inland.

Still, the build-up in inland provinces will allow Hon Hai to employ more people working nearer to their home towns. *MMI* believes that Hon Hai will benefit on several levels. The company can tap large pools of local workers in areas where labor and other costs are lower than on the coast. These workers will be attracted to Hon Hai because they can live near their families and enjoy a cost of living that is lower than in coastal cities. With young workers more connected to their families, Hon Hai is at least somewhat relieved of the 24-hour "parental" responsibility that comes with employing a migrant workforce. Hon Hai also gains a more stable workforce less subject to the churn that results when migrant workers do not return after Chinese New Year.

Hon Hai is sending a clear message that it wants to depend far less on migrant workers. Is the rest of the industry listening?

Market Data

OEM Survey Results Offer Some Surprises

A new OEM survey by **Riverwood Solutions** (Menlo Park, CA), an operations consulting and managed services provider, has produced some unexpected findings. These and other results from the survey reflect OEM attitudes and activities associated with outsourcing.

Completed in mid-May, Riverwood's annual survey of senior operations and supply chain professionals covered OEMs that spent more than $100 billion in the global electronics supply chain in 2009. Respondents reported spending on average between $101 million and $250 million on EMS last year.

With the rising costs of manufacturing in China, one might have expected a decidedly smaller proportion of OEMs to take a positive view of the country this year. But surprisingly, the new survey says just the opposite: 66.7% of OEM respondents agree or strongly agree that China is the best location for building their company's product over the next few years. In contrast, only 23.5% held that belief last year. The shift in attitudes toward China is not only positive, it is unexpectedly large. This result agrees with another of the survey's findings. Just 9.5% of 2010 respondents report that they are actively investigating alternative locations for product that they currently have manufactured in China.

Another unexpected result concerns manufacturing in the region where a product is sold. Popular wisdom says this is a major trend. But only 14.3% of respondents say they are more likely to look at near-shore and on-shore manufacturing options than a year ago. (See Last Word, p. 8 for more on this subject.)

On the other hand, 50% of respondents say it is very likely or extremely likely that they will relocate some or all of their production to another geography. That's up slightly from 47.1% in 2009.

Illuminating the OEM-EMS relationship

It is industry gospel that OEMs are generally adverse to switching suppliers because of the costs and risk involved. But again, the survey says otherwise. In the new survey, 68.2% of OEM respondents report it was at least very likely that they would relocate some or all of their production to another supplier. By comparison, 47.1% of respondents were so inclined in 2009. Riverwood believes that far less than 10% of programs will actually be moved from one supplier to another as the costs and risk of a transfer generally outweigh the other factors causing this sentiment.

One reason why an OEM would move a program to another supplier is to consolidate its supply base. And the survey presents evidence that OEMs are increasingly planning to do this. Of the 2010 respondents, 59.1% are very or extremely likely to consolidate key suppliers to reduce cost. That's up from 35.3% in the 2009 survey.

Yet the survey found much more interest in new suppliers. That is, 68.2% of respondents are very or extremely likely to evaluate new EMS/ ODM or CDM suppliers, compared with just 23.5% last year.

Another survey question looked at the appeal of ODM companies alone. Of the 2010 respondents, 72.7% say they are very or extremely likely to engage an ODM company on a new program. This figure, which is more than twice the 35.3% of OEM professionals with the same intentions in 2009, offers an indication of the current interest in the ODM model.

The Riverwood survey also discovered less emphasis on cost as the number-one performance metric. Respondents were asked how they felt about cost as the single most important factor they use in measuring and managing their EMS providers. Only 14.3% believe that cost is the primary metric for measuring EMS performance. This result amounts to a substantial drop from the comparable figure of 41.2% in the 2009 survey.

Nevertheless, the 2010 survey shows a significant increase in the number of OEMs that report being concerned that their EMS provider will raise prices or add new charges. The survey found that 40.9% are concerned, compared with 11.8% in 2009.

OEMs are also increasingly worried that their EMS providers are not investing enough on the OEMs' behalf. In the 2010 survey, 40.9% of respondents are concerned that underinvestment by their EMS provider will hurt performance on their account over the next year. Last year, 25% expressed this concern. It is not surprising that more OEMs have this concern in a year when EMS investment is required to support customers' growth, as opposed to last year when there was little or no need to add EMS capacity.

Supply chain constraints, of course, are another source of OEM unease. Of those who responded, 45.5% are at least very concerned that their product shipments will be seriously impacted over the next two quarters based on some major unforeseen event in the supply chain. In 2009, only 11.8% had such worries about supply disruptions.

The new survey reveals that 52.4% of OEMs feel at least somewhat better about their EMS supplier relationships than they did last year. But satisfied EMS customers are still reported as a minority. Of the OEM respondents, 38.1% are satisfied with the overall value they get from their EMS provider(s). The good news is that this percentage represents a substantial increase from 2009's paltry 18.8%. So the EMS industry has been making some progress in this regard.

Vertical integration is another issue addressed by the survey. When polled, 52.4% of respondents say vertical integration and a broad service offering are important to them in selecting or using an EMS or ODM partner. However, the appeal of these capabilities was less widespread in 2010 than in 2009, when 70.6% of respondents voted in favor of vertical integration and a broad services offering, for which some of the largest EMS providers are known.

The survey paints a picture of OEMs who for the most part are not thrilled with their supply chain. Only 14.3% of respondents believe that their company's supply chain is more nimble than that of their competitors. Similarly, 61.9% agree or strongly agree that their supply chain is more complex than it needs to be. Furthermore, just 14.3% believe their company does a very good of identifying and managing indirect costs associated with managing its product manufacturing and supply chain.

In addition, the survey finds a smaller proportion professionals reporting that their CEO views operations and supply chain as a competitive advantage for their company. Of the 2010 respondents, 42.9% held this view versus 64.7% in 2009.

Insourcing, a hot topic in 2009, was also covered in the survey, whose results showed little change in OEM attitudes toward the practice. For 22.7% of respondents, it is likely that their company will internalize some operations activities that are currently outsourced. In the 2009 survey, a slightly higher proportion, 29.4%, submitted such positive answers to the insourcing question.

Another question asked whether OEMs would be willing to pay a quality premium. Of OEM respondents, 47.6% say they would be willing to pay their EMS provider 2% more if product returns were cut in half. Affirmative responses to this question more than doubled versus last year, up from just 23.5% in 2009.

Finally, 63.6% of respondents say they are likely to hire remote operations staff located near their EMS provider. Only 29.4% of respondents reported the likelihood of remote hiring plans in 2009.

Snappy Recovery ...So Far

Forecasts of modest single-digit growth for 2010 have so far been off the mark when it comes to the industry sector consisting of the largest U.S.-traded EMS companies. Indeed, combined sales for this group have snapped back in the first half of this year following a steep decline in recession-mired 2009. First-half revenue for the six U.S.-traded providers increased by 14.7% overall from the year-earlier period, amounting to a brisk recovery from 2009 when group sales fell by 22.7%. Two providers, **Plexus** and **Sanmina-SCI**, grew their first-half sales by more than 30% year over year (Table 1). Aggregate sales for the first six months totaled $27.4 billion, up from $23.9 billion in the same period a year ago.

On a year-over-year basis, the group's Q2 sales rose at a faster rate than its first-half sales. The Q2 increase was 21%, with all six providers in double digits led by Plexus at 41.7% (Table 1). Perhaps more significant, the group's Q2 sales growth easily outpaced the increase in electronic equipment sales for the period. According to a report by **Custer Consulting Group**, worldwide equipment sales in Q2 went up by 12% year over year, a composite value representing the financial results of 70 large OEMs. Thus, the EMS growth rate was nine percentage points higher than the OEM rate in the second quarter as measured against the year-earlier period. While the outsourcing trend's power to increase EMS sales disappeared in demand-starved 2009, the trend once again boosted sales growth above the OEM baseline in the first half of 2010.

Sequentially, combined Q2 sales increased by 10%, with sales growth of **Flextronics** and **Jabil Circuit** in double digits. Aggregate GAAP net income for the quarter improved at a far greater rate. Together, the six U.S.-traded providers produced Q2 net in-

Table 1: Q2 and Six-Month 2010 GAAP Results for the Six Largest U.S.-Traded EMS Providers (M$ or %)

Company (in order of 6-mo. sales)	Q2 '10 sales	Q1 '10 sales	Qtr.-qtr. chg.	Q2 '09 sales	Yr.-yr. chg.	Q2 '10 gross marg.	Q1 '10 gross marg.	Q2 '10 oper. marg.	Q1 '10 oper. marg.	Q2 '10 net inc.	Q1 '10 net inc.	Q2 '09 net inc.	Q1-2 '10 sales	Q1-2 '09 sales	Yr.-yr. chg.	Q1-2 '10 net inc.	Q1-2 '09 net inc.
Flextronics*	6,565.9	5,940.2	10.5	5,782.7	13.5	5.6	5.4	2.4	1.9	118.2	60.1	(154.0)	12,506.1	11,365.2	10.0	178.3	(393.8)
Jabil	3,455.6	3,004.6	15.0	2,615.1	32.1	7.6	7.4	2.8	2.1	52.0	29.8	(28.8)	6,460.2	5,502.5	17.4	81.8	(894.9)
Sanmina-SCI	1,625.2	1,527.5	6.4	1,209.2	34.4	7.6	7.7	3.8	3.0	21.6	10.1	(41.5)	3,152.7	2,404.3	31.1	31.7	(79.4)
Celestica	1,585.4	1,518.1	4.4	1,402.2	13.1	6.8	7.0	1.2**	2.4**	(6.1)	25.9	5.3	3,103.5	2,871.6	8.1	19.8	24.5
Benchmark	589.4	571.9	3.1	481.8	22.3	8.0	7.9	4.1	3.7	20.8	18.3	11.6	1,161.4	978.6	18.7	39.0	20.8
Plexus	536.4	491.0	9.2	378.6	41.7	10.4	10.3	5.0	4.8	24.4	20.7	9.2	1,027.4	767.5	33.9	45.1	14.2
Total/avg.	**14,357.9**	**13,053.3**	**10.0**	**11,869.6**	**21.0**	**6.7**	**6.6**	**2.7**	**2.3**	**230.9**	**164.9**	**(198.2)**	**27,411.3**	**23,889.7**	**14.7**	**395.7**	**(1,308.6)**

*Intangible amortization was subtracted from Flextronics' reported operating income. **MMI calculation.

Company (in order of 6-mo. sales)	Q2 '10 inventory	Q1 '10 inventory	Qtr.-qtr. change	Q2 '09 inventory	Yr.-yr. change
Flextronics	3,320.9	2,875.8	15.5%	2,671.4	24.3%
Jabil	1,781.8	1,565.3	13.8%	1,255.5	41.9%
Sanmina-SCI	855.1	815.7	4.8%	696.2	22.8%
Celestica	676.8	724.3	-6.6%	634.3	6.7%
Benchmark	389.0	362.0	7.5%	322.2	20.7%
Plexus	468.9	430.9	8.8%	313.5	49.6%
Total/avg.	**7,492.5**	**6,774.0**	**10.6%**	**5,893.1**	**27.1%**

Table 2: Inventory for the Six Largest U.S.-Traded Providers (M US$)

come of $230.9 million, up 40% from the prior quarter (Table 1). Composite net margin for Q2 rose sequentially by 30 basis points to 1.6%.

Q2 GAAP gross margin overall stood at 6.7%, up 10 basis points from the prior quarter and 150 basis points from the year earlier period (the latter not apparent from the table). Plexus posted the highest Q2 gross margin at 10.4%, followed by **Benchmark Electronics** at 8%. The group's GAAP operating margin for Q2 amounted to 2.7%, a sequential improvement of 40 basis points. Again, Plexus and Benchmark were first and second respectively in the order of margin results. The provider that showed the greatest sequential gain in operating margin was Sanmina-SCI with an 80-basis point increase.

For the first half, the six providers earned a combined net income of $395.7 million (GAAP), representing a bottom-line swing of $1.7 billion from the year-earlier period. First-half net margin (GAAP) for the group was 1.4%.

The six U.S.-traded providers reported Q2-end inventories totaling $7.49 billion. Compared with the prior quarter, overall inventory grew by $719 million, or 10.6% (Table 2). Program ramps contributed to this increase, and component supply constraints played a role as well. Only **Celestica** managed to reduce its inventory sequentially. On a year-over-year basis, inventory was up 27.1%, with two providers, Jabil and Plexus, posting increases of over 40%.

Results for two providers in brief

Last month's issue contained brief summaries of Q2 results for four of the U.S.-traded providers (July, p. 4-5). Q2 financials for the remaining two companies are described below in the same manner.

Benchmark Electronics. The provider's Q2 sales of $589.4 million fell short of its guidance of $600 million to $630 million. Benchmark blamed the miss on a lack of demand from one computer customer in addition to supply chain challenges coupled with changes in product mix from customer forecasts. Supply chain constraints resulted in an impact of about $30 million on Q2 revenue. Compared with the prior quarter, Benchmark saw stronger shipments from all of its sectors except for medical, where product transitions and crossovers caused a 20% drop in sales.

Gross margin for Q2 was 8.0% (no restructuring charges), up from a non-GAAP margin of 7.9% in Q1. Operating margin of 4.0% equaled the non-GAAP result of Q1.

With Q3 sales guidance of $590 million to $630 million, Benchmark expects Q3 sales from all of its sectors to increase over Q2 levels.

Sanmina-SCI. Revenue for its fiscal Q3 ended July 3 rose 6% sequentially thanks to a 28% increase in its communications segment. Sales from the multimedia and enterprise computing and storage segments fell from the prior quarter, while industrial/defense/medical business was flat.

Non-GAAP gross margin was 7.9%, up 10 basis points from the prior quarter, while non-GAAP operating margin stood at 3.9%, a sequential improvement of 20 basis points. For the first time in several years, the gross margin (non-GAAP) for the company's component businesses exceeded its corporate average gross margin for the quarter.

The provider reported an embezzlement of $3 million in Asia, which appears to have occurred over the course of several years.

For fiscal Q4, Sanmina-SCI expects continued improvement in non-GAAP operating margin, and guidance calls for a range of 3.9% to 4.2%. Projected sales growth for fiscal 2010 is about 20%.

Q3 Projected for Strong Growth

Q3 sales estimates for the six largest EMS providers in the U.S.-traded sector indicate strong year-over-year growth for the group despite a recently sputtering U.S. economy. With Q3 estimates set equal to guidance midpoints, the group's Q3 revenue would grow by 23.2% from the year-earlier period if providers hit their midpoints. What's more, Q3 growth is projected to reach robust double-digit levels in five out of six cases, where the estimated increases range from 19.5% to 39.3% (table, p. 6).

At guidance midpoints, all six providers would experience sequential growth in their Q3 sales. Only **Jabil Circuit** would achieve a double-digit increase. Versus the prior quarter, composite growth for the group's Q3 revenue is estimated at 6.8%.

Projections for the first three quarters of 2010 paint a rosy picture for revenue growth in the U.S. traded sector. Estimated nine-month sales for the sector's six largest providers total $42.7 billion, representing growth of 17.6%. If this rate holds up through the fourth quarter, 2010 sales for this group will have not only made a full recovery from 2009 but also attained a double-digit growth level thought to be

Q3 2010 Guidance and Estimates for the Six Largest U.S.-Traded Providers (sales in B$ except as noted)												
Company	Q3 guidance	Q3 midpoint	Q2 '10 sales	Qtr.-qtr. estim. chg.	Q3 '09 sales	Yr.-yr. estim. chg.	Q1-2 '10 sales	Q1-3 '10 estimated sales	Q1-3 '09 sales	estimated change	Q2 EPS Non-GAAP* $	Q3 Guidance Non-GAAP* $
Flextronics	6.8 - 7.2	7.0	6.57	6.6%	5.83	20.0%	12.51	19.51	17.20	13.4%	0.19	0.19 - 0.21
Jabil**	3.8 - 4.0	3.9	3.46	12.9%	2.80	39.3%	6.46	10.36	8.30	24.8%	0.40	0.45 - 0.50
Sanmina-SCI	1.65 - 1.70	1.68	1.63	3.1%	1.35	23.7%	3.15	4.83	3.76	28.5%	0.32	0.35 - 0.41
Celestica	1.55 - 1.65	1.60	1.59	0.9%	1.56	2.8%	3.10	4.70	4.43	6.2%	0.21	0.20 - 0.24
Benchmark	590 - 630 M	610 M	0.59	3.5%	0.51	19.5%	1.16	1.77	1.49	19.0%	0.33	0.33 - 0.36
Plexus	530 - 555 M	542.5 M	0.54	1.1%	0.39	38.0%	1.03	1.57	1.16	35.3%	0.59	0.58 - 0.63
Total/avg.		**15.33**	**14.36**	**6.8%**	**12.45**	**23.2%**	**27.41**	**42.74**	**36.33**	**17.6%**		

Q3 estimates equal midpoint of Q3 guidance. Nine-month 2010 estimates equal six-month sales plus midpoint of Q3 guidance.
*Non-GAAP EPS may not be comparable from company to company. **Q3 data correspond to the quarter ending August 2010.

out of reach for the mature EMS industry. Nine-month growth rates for all providers in the group except one will be in two-digit territory if estimates prove accurate (table). Estimates of nine-month sales equal first-half sales plus Q3 guidance midpoints.

Guidance for Jabil's August quarter and **Sanmina-SCI's** calendar Q3 quarter suggests that in each case non-GAAP EPS will improve over the prior quarter's result. **Flextronics** and **Benchmark Electronics** expect their non-GAAP EPS for calendar Q3 to be equal to or greater than their Q2 result.

News

Catalyst Acquires EMS Operation in NY

Catalyst Manufacturing Services (Endicott, NY), a full-service EMS provider operating in two U.S. locations and Mexico, has acquired **Harvard Custom Manufacturing's** PCBA Division in Owego, NY. The purchase price was not disclosed.

"Catalyst has a manufacturing location a few miles from the HCM site, which made this an attractive situation for both companies on many levels. There are many similarities between our organizations – similar business models as well as target markets," stated Randall Lainhart, executive VP at Catalyst. "The merging of these operations will provide greater engineering depth and advanced capabilities for both the Catalyst and HCM customer base. HCM's advanced capabilities in system level assembly, including engineering and test, were of great interest to Catalyst."

The transaction did not include HCM's Interconnect Systems Division in Salisbury, MD, which serves the aerospace and defense industries.

*Deals done…***Pufin S.p.A.**, an Italian company, has acquired **Flextronics'** operation in Saint Etienne, France. According to translated press reports, the operation has 150 employees. **El.Ital.** (Avellino, Italy), which is held by Pufin, does business in the EMS and energy sectors….**Sunburst EMS** (West Bridgewater, MA) has purchased **Quality Electronics Manufacturing** (Melbourne, FL), which specializes in wire and cable harness assembly….**Sparton** (Schaumburg, IL) has completed its previously announced acquisition of certain assets of **Delphi Medical Systems'** contract manufacturing business in Longmont, CO (July, p. 6).

*Ownership change…***EN ElectronicNetwork**, a German EMS provider ranked in the *MMI* Top 50 for 2009, has taken on new ownership. Huub Baren, chairman of the company's supervisory board; Klaus Kroesen, CEO of the company; Dr. Daniel Heinemann, head of Controlling of the EN ElectronicNetwork group; and Rolf Weinreis, GM of the company's Bonn unit, have taken over a majority of the company's shares. Baren holds a 51% interest, and management 24%, with the remaining shares still held by employees. EN ElectronicNetwork will move its headquarters to Bornheim-Hersel, Germany, near Bonn, from Limburg, Germany. The company's Limburg site was divested at the end of 2009.

*Some new business…***Hon Hai Precision Industry** (Tucheng City, Taiwan), considered a newcomer to the notebook outsourcing space, has already made significant inroads in the space. For 2011, Hon Hai will become **HP's** second biggest supplier of notebooks with orders for 9 to 11 million units, *Digitimes* reported, citing notebook industry sources. What's more, Hon Hai will have the third largest portion of **Dell's** notebook orders for 2011, according to *Digitimes* (July, p. 7)….Top 50 EMS provider **LaBarge** (St. Louis, MO) has landed a contract from **Sikorsky Aircraft** to produce wiring harnesses for a Medevac helicopter in the Black Hawk family. The award is valued at about $5 million. Also, LaBarge has received a $4.9-million contract from **United Launch Alliance** to continue to produce complex wiring harnesses for the Atlas V launch vehicle, which takes satellites into orbit. ULA is a joint venture between **Boeing** and **Lockheed Martin**….A portable alarm systems company called **tattletale** (Westerville, OH) has selected **The Morey Corporation** (Woodridge, IL) to manufacture and fulfill what is described as the world's first portable, cellular-based security system for consumers. In addition, tattletale said it will look to Morey to manufacture its complete suite of portable alarm products in the near future….Under a new turnkey agreement, **Enigma Interconnect** (Pointe-Claire, Quebec, Canada) will mass produce an intelligent motion detection device developed by **Lyrtech** (Quebec City, Canada). The agreement is related to a CA$28-million OEM contract that Lyrtech recently won….Publicly-traded **IEC Electronics** (Newark, NY) has received an order from a defense customer valued at more than $6.1 million. IEC will serve as exclusive turnkey supplier for a satellite communications modem used by the U.S. Department of Defense. The program also includes life cycle support. …**Kitron** (Billingstad, Norway), a Top 50 EMS provider, has landed orders worth about NOK 70 million ($11.3 million) from its medical equipment segment and additional business valued at about NOK 55 million ($8.8 million) from the company's offshore/marine segment.

*Adding capacity…*According to press reports from Turkey, Hon Hai signed an agreement this month to build a new factory in Turkey for production of **HP** PCs. If this news creates a feeling of déjà vu, it's warranted. Last year, the two companies announced that Hon Hai would invest about $60 million in a new plant to manufacture desktop PCs for HP in Turkey (March 2009, p. 7). The original schedule called for production to begin in March 2010….Top 50 provider **Creation Technologies** (Burnaby, BC, Canada) has opened a new facility in St. Peter, MN, offering 50,000 ft^2 of manufacturing space. …**Enics** (Zürich, Switzerland), another Top 50 provider, will invest several million euros to increase the capacity of its Beijing, China, plant. Manufacturing area will expand, and SMT capacity will double. The added space will enable Enics to increase the plant's workforce from 600 at present to 900 if needed.

*Entering the U.S. market…*News sources in the Philippines are reporting that **Ionics EMS** (Laguna, Philippines), a subsidiary of Ionics, plans to establish a design and prototyping operation in Silicon Valley.

*Facility consolidation…*As a result of **Sanmina-SCI's** acquisition of **BreconRidge** (May, p. 7), Sanmina-SCI will combine its NPI facility in the Ottawa, Canada, suburb of Kanata with BreconRidge's plant in Ottawa. In addition, BreconRidge's operation in Shenzhen, China, will be combined with a Sanmina-SCI operation in China.

*Facility closures…*The integration of BreconRidge will also involve a facility closure. BreconRidge's logistics and repair center in Ogdensburg, NY, will cease operations, a local newspaper reported….Flextronics intends to shutter its automotive factory in Mór, Hungary, according to a report on *PRW.com*. The company obtained the factory in its 2009 acquisition of **AFL Stribel Production** from **Alcoa**. …**NOTE** (Danderyd, Sweden) recently began closing its Gdansk, Poland, operation. In Q1, the company started plant closures at Skänninge, Sweden, and Tauragé, Lithuania.

*People on the move…*Peter Laveson has taken over the reins as NOTE's new CEO and president. Laveson, who worked as a business developer at **Investment AB Öresund**, has been a member of NOTE's board. He replaces acting CEO and president Göran Jansson….**ESCATEC Group** (Penang, Malaysia) has appointed Michel Van Crombrugge GM of its ESCATEC Electronics and ESCATEC Medical units in Penang. He joins the group from **NXP Semiconductors Germany**, where he held the position of GM and head of NXP's Sensors business line….Creation Technologies has added four directors of business development. Karen Armendariz, whose 20-plus years of experience include **National Semiconductor** and **Intel**, will cover the Dallas area. With more than 10 years of experience in business development, marketing and media, John Earle will be responsible for Eastern Canada. Joe Garcia, who has done business development for several tier-one EMS providers, will handle Northern California and Nevada. And Kathy Thomson, most recently director business of development at a major metal finishing company, will cover North and South Dakota and Iowa….LaBarge recently promoted Mike Foti to director of business development. In this newly created position, Foti leads the company's sales efforts in the defense and government market sectors. …Kitron has made Thomas Löfgren GM for Kitron Sweden in addition to his role as managing director for Kitron Microelectronics. Also, Stefan Tjust has been promoted to managing director of Kitron's unit in Karlskoga, Sweden. Finally, Kitron has named Yvonne Wenzel GM for Kitron's operation in Ningbo, China. Before joining Kitron, she was GM for an automotive supplier in Beijing.…Enics has promoted Sabina Romagnolo to GM of Enics Switzerland.…**Integrated Micro-Electronics Inc.** (Laguna, Philippines), a Top 50 provider, recently appointed Jeremy Cowx sales director in charge of its IMI Japan office. He has experience working with Japanese OEMs.

Some Explaining To Do

It would seem that the time has come for large-scale migration to a regional manufacturing model. Rising labor and other costs in China, potential devaluation of the Chinese yuan, and concerns about carbon emissions are ostensibly acting in concert to provide extra motivation for OEMs to create supply chains capable of supporting manufacturing in or near the region of product sales. It all looks great on paper. By shortening shipping distances, you reduce logistics costs and carbon footprint. You also shrink pipeline inventory, enhance your ability to respond to demand changes, cut travel time, and facilitate engineering changes and communication. But there is no big surge of OEM interest in regional manufacturing, if a recent poll is taken at face value.

Riverwood Solutions' OEM survey found that only 14.3% of respondents say they are more likely to look at near-shore and on-shore manufacturing options than a year ago. (See the article on p. 3-4.) Even *MMI* is surprised about this result, given *MMI's* 2010 outlook (Jan. p, 4). Furthermore, just 9.5% of the survey's respondents report that they are actively investigating alternative locations for product that they currently have manufactured in China.

How can these counterintuitive findings be explained? Although the first result shows that only a small minority of OEM professionals are more likely now to explore near- and on-shore manufacturing, the survey does not identify those who are only looking at near-shore production. It's entirely possible that some additional percentage of respondents fall into this category. Indeed, **Flextronics** during its last earnings conference call reported getting a lot more interest in Mexico and Eastern Europe, two near-shore locations for low-cost regional manufacturing. In addition, the survey does not address whether some portion of the remaining 85.7% could have *already* been looking at near- and on-shore manufacturing. So the survey doesn't necessarily rule out regional manufacturing as a trend.

As for China, it has three things going for it: a well-developed supply base, good infrastructure and a growing domestic market, which just overtook Japan as the world's second largest economy. A 20% or 30% increase in Chinese labor costs this year may not be enough to force many OEMs out of China when direct labor is often under 5% of their providers' sales. On some products, it can be less than 2% or even 1%. Also, many OEMs will be loath to switch their supply chains around as along as component shortages persist.

While some future attrition from China is probably inevitable as increasing labor costs work their into the supply chain and currency effects become palpable, China's supply base, relatively low labor costs and domestic market will likely remain attractive to many OEMs for some years to come. In fact, two-thirds of the survey's respondents say China is the best location for building their company's product over the next few years.

But the continuation of a large production base in China and the rise of regional manufacturing are not mutually exclusive. The OEM universe is large enough to accommodate both. At least that's how *MMI* reads the survey results.

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