Practice Case 5 (VieTire)

Question

A tire manufacturer in Vietnam, VieTire, has been the only player in that market due to high tariffs on imports. They dominate the tire industry. As it stands, the tariff is 50% of the total cost to produce and ship a tire to Vietnam. Because of the forces of globalization and lower consumer prices, the Vietnamese government decided to lower the tariff by 5% a year for the next ten years. VieTire is very concerned about this change, as it will radically alter the landscape of the industry in Vietnam. They hire you to assess the situation and advise them on what steps to take.

Recommended Solution

High Level Plan of Attack

- The first thing we need to understand is the current cost structure of VieTire's product.
- Next, we must determine the impending competitive situation.
- Then, Calculate the impact the reduction of tariff will have.
- Finally, recommend specific steps that VieTire can take to protect themselves from increased competition.

Lay Out Your Thoughts

- Specify what steps we must take to understand the cost differences now, and in the future, of VieTire and its competitors

Dig Deeper: Gather Facts/Make Calculations

- What would you say are the major costs associated with making a tire? *Raw material comprise about 20% of the cost, labor 40%, and all other costs such as overhead 40%. The average tire cost about $40 to make.*
- It seems that labor is a major cost, $16 per tire. Why? *Things are done more manually. Most of technological advances in the industry have not yet been implemented in Vietnam.* What about the cost structure of the competition? *An average tire manufacturer in the US produces tires at a cost of $30 each.*

- Assuming shipping cost to Vietnam of $4 each tire, and a tariff of 50%, the average cost of an imported tire in Vietnam amounts to $51. So currently, even though the cost to produce a tire in the U.S. is much cheaper due to technological advances, foreign competitors are out of luck because of the tariff.

Year	Tariff	Cost	Result of Competition
Now	50%	$50.00	Will not enter
1	45%	$47.90	Will not enter
2	40%	$46.00	Will not enter
3	35%	$44.50	Will not enter
4	30%	$43.00	Consideration of entrance if willing to take a cut on price
5	25%	$41.30	Preparing to enter
6	20%	$39.60	Entered the market
7	15%	$38.00	Competing on the market

Key Findings

- Depending on what price they are willing to set, the competition will start to think about entering the market in year four. In year six, the competition will surely enter as their prices become lower than domestically produced tires.
- This analysis assumes that the cost structure for the competition will remain constant. It is important to note that because of the rapid advances in technology, chances are that the costs of producing tires will decrease resulting in competitors entering the market even sooner.

Recommendations

- VieTire needs to benchmark against word class tire manufacturers and reengineer production methods and cost structures.
- They must invest in the latest advances in order to reduce their labor/operations costs.
- The company should focus on increasing the skills of labor while at the same time contain their hourly wage.
- Need to develop loyalty from their customers/consumers in order to lock in a certain percentage of the market share.