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An Explorative Study on Functional Upgrading and Export Development of Vietnam Wood Furniture Producers

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AN EXPLORATIVE STUDY
ON FUNCTIONAL UPGRADING AND EXPORT DEVELOPMENT OF VIETNAM WOOD FURNITURE PRODUCERS

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Abstract

The academic debate about whether developing country producers should involve in design and marketing functions through which developed country firms hold strong positions triggers research idea for this research. The research applies global value chain perspective to analyze the relationship between functional upgrading and firm's export development in the context of Vietnam wood furniture industry. It employs qualitative analysis methods including indepth interview, direct observation and case study analysis. The results from this research indicate the positive impact of functional upgrading on firm's export development and the combination of different functions in different value chains enables developing country firms to develop well in the long term. This paper suggests that firms should combine both transactional and relationship marketing approach.

1. Introduction

In an increasingly globalizing economy, too many enterprises from low labor cost economies are compressing into the manufacturing stage, leading to the price and profit squeeze in manufacturing. Schmitz (2006, p 563) point out that:

> "Many producers, especially those of small and medium size, find that participating in and gaining from the global economy do not always go together. This then gives rise to the question whether other nodes of the value chain (such as logistics, design, marketing) offer higher returns. On this critical question there is little information."

In fact, the critical question of whether developing country producers should involve in design and marketing function through which developed country firms hold strong positions has been theoretically debated among different literature streams.

Competitive advantage theory suggests that a firm should focus on what it does well and give away activities in which it has a less competitive advantage. The argument for international specialization is based on the comparative advantage of nations which recommends that firms in labor abundance countries should focus on producing labor intensive products. Compared to sourcing firms from high income countries, developing country firms have more advantage in producing labor- intensive product due to low labor cost while they also are not as advantaged in marketing since there is a lack of managerial skills, marketing knowledge as well as the capacity to brand in consuming markets. According to this reasoning, for economic efficiency, developing country firms should specialize in producing and delegating export marketing responsibility to foreign partners.

On the contrary, value chain literatures recommend a move toward a design and marketing function. The underlying idea of this literature stream is that competing in today's intensified competitive global market, a market where buyers demand many more attributes in addition to price – such as product variety, quality, customization – firms in low income countries need to develop competencies that go beyond the traditional factor of low labor cost. These capabilities include skills, management practices, and productive relationships that allow firms to combine speed and scale with higher order functions such as design and marketing to build more dynamic comparative advantages (Tewari, 2006). GVC literatures (Gereffi 1999; Kaplinsky& Readman, 2001; Schmitz, 2004; Bair and Dussel, 2006) indicate the inequality in value distribution among the chain leader and producers. Thanks to the advantage of being closer to the consuming market, sourcing firms often make decisions about from whom to source, what qualification products have to be met, and the price of the finished product. Due to the lack of branding activities in consuming markets, many developing country producers work as processors, having to accept term and conditions set up by sourcing firms, unable to set up a better price, and even accepting a price lower than that of competitor's contracts. Gereffi (1999) argues that to get higher income, a developing country firm needs to move to more value added activities including marketing and design. Gereffi (1999) names the process in which a firm moves beyond the manufacturing function to other functions in the downstream and upstream end as a functional upgrading. Some global value chain studies (Gereffi,1999; Kaplinsky et.al, 2003; Humphrey, 2004) have brought to the debate their arguments on functional upgrading as a determinant of a firm's sustainable development.

Notably, the recent GVC studies (Bazan and Navas-Aleman, 2003, 2004, Schmitz, 2006) begin their query by asking whether functional upgrading really makes developing country firms better off. In an empirical study on the Brazilian shoe industry, Bazan and Navas-Aleman (2003, 2004) find that the profitability of manufacturers who embarked on selling their own design and established their own marketing channel is not higher than the profitability of those who kept to manufacturing only.

In fact, the debate is two faces of a coin. On the one side, for economic efficiency, a developing country firm should not involve themselves in design and marketing functions through which developed country firms keep strong positions. On the other side, such an international division of labor creates the opportunity for powerful actors to act as leaders, taking the authority in deciding economic returns for other members of the value chain, possibly furthering the inequality in value distribution among the chain leader and producers. Improving market power is only one way for developing country firms to balance asymmetrical power. Developing higher skilled functions such as design and marketing, that is, accomplishing 'functional upgrading' (Gereffi,1999; Kaplinsky et.al, 2003; Humphrey, 2004) is a way for developing country firms to increase economic returns.

The research aims at providing empirical evidence to this theoretical debate. The question set up for study is **"**How does functional upgrading link to firms' export development".

The research employs global value chain perspective to analyze the relationship between functional upgrading and firm's export development.

Qualitative research methodology is employed in this research. Empirical study is to be done on Vietnam's wooden furniture industry. There are several reasons for this option. Firstly, the wood furniture industry is a traditional manufacturing sector employing large amount of labor. The study of such industry has wide sectoral significance. At the same time it also flourishes in high-wage economies, suggesting that there is a potential upgrading path which allows firms in low-wage countries to pursue to develop. Secondly, I believe that by focusing on Vietnam, an emerging economy, we can shed light on the development pathway for firms in other developing economies with similar context. In the context of an emerging market where international players come to source for suppliers, the empirical study on firms' ability to utilise existing relationships to upgrade may provide fruitful managerial implications.

2. Theoretical background

Value chain analysis was firstly introduced by Porter (1985), mainly from an intra-firm perspective. Expanding value chain analysis to a system of inter-firm linkages on a global perspective, Gereffi (1994) introduced the term *global commodity chains*, which enabled important advances in the analytical and normative usage of the value chain concept. Based on Gereffi's (1994) analysis of *global commodity chains*, the global value chain (GVC) approach has been extensively developed by several other researchers who consider value chain as the range of link activities which are not confined to within a firm but all those activities between firms in the same country and across countries. Developing from the ideas raised by Gereffi (1999a), Kaplinsky and Morris (2001, p. 4) define a value chain as "the full range of activities which are required to bring a product or service from conception, through the different phases of production.., delivery to final consumers, and final disposal after use." From this definition, a *global value chain can be simply understood as the sequence of all functional activities required in the process of value creation involving more than one country***.**

2.1. Map of value chain.

Generic map of value chain

A typical value chain often comprises production, design, retailing and co-ordination functions, which make it possible to deliver value to the end users. Kaplinsky and Morris (2001) depict a simple value chain in Figure 1, showing linkages between four main functions of the value creating process: design, production, marketing and recycling. By looking at the production function at the center of the value chain, design, R & D, and procurement can be categorized as up-stream activities, while marketing and after-sale services are down-stream activities.

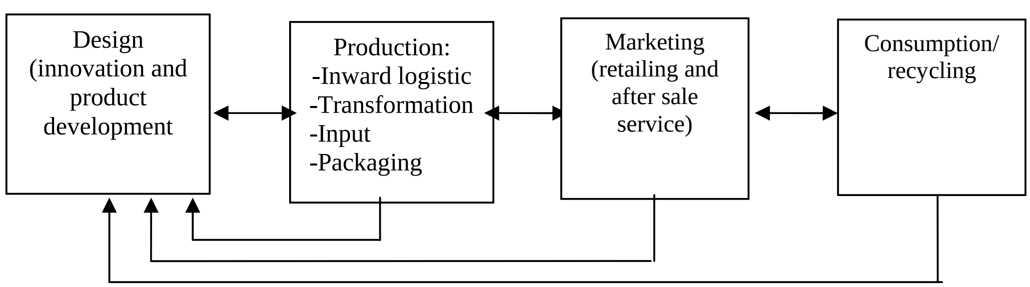

Figure 1: Simple value chain

(*Source: Kaplinsky and Morris 2001, p.4*)

This figure provides a basic picture of the value creating process. It specifies functions and activities along the value chain. However, it does not specify a value chain's actors and their linkages. In fact, the value chain of a finished product is much more complex than this.

Mitsuhashi (2005, p.25) develop more detail map of value chain which include both actors and their linkages as in Figure 2.

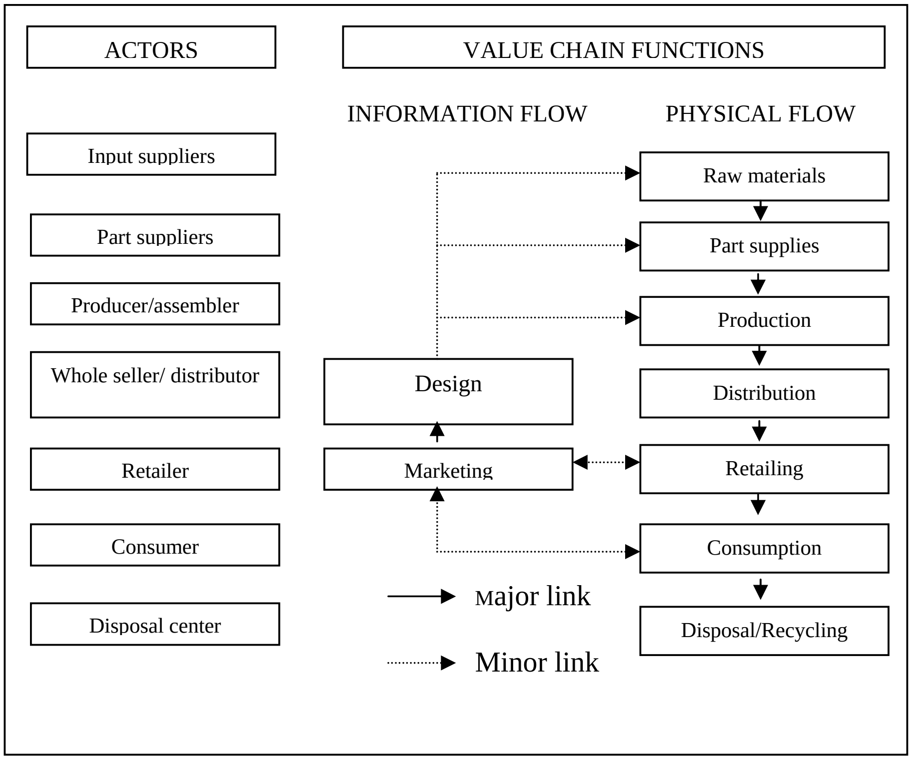

Figure 2: Value chain's functions and actors

(*Source: Mitsuhashi 2005, p.25*)

Mitsuhashi's (2005) value chain figure depicts both value chain functions and actors, making distinction between information flow and physical flow. However, it is inappropriate to assume that whole sellers or distributors are the only ones in charge of design. In many cases, producers regard design and marketing responsibility as illustrated by certain case studies in the Vietnam wood furniture industry. Additionally, marketing function should not be confined to only retail marketing. In the global market, business-to-business marketing also plays a significant role. Therefore, this figure can be applied to maps of the value chain of a finished product, if some modifications are made to overcome the mentioned weaknesses.

2.2. Industrial upgrading

Typologies of industrial upgrading

The GVC literature provides a view of the industrial upgrading in a wider perspective, which is systemic in nature and involves groups of firms linked together in value chains. This relates both to the achievement of new product and process development, and in the functional reconfiguration of who does what in the chain as a whole (Kaplinsky, R. and Morris, M. 2001). The concept of upgrading—making better products, making them more efficiently, or moving into more skilled activities—has often been used in studies on competitiveness (Porter 1990 and Kaplinsky 2001). Summarizing GVC literature's idea on upgrading, Giuliani, et al. (2005, p. 9) represent a clear description of four upgrading typology of as below:

> (i) Process upgrading is transforming inputs into outputs more efficiently by re-organizing the production system or introducing superior technology…
>
> (ii) Product upgrading is moving into more sophisticated product lines in terms of increased unit values. ..
>
> (iii) Functional upgrading is acquiring new, superior functions in the chain, such as design or marketing or abandoning existing low-value added functions to focus on higher value added activities…
>
> (iv) Intersectoral upgrading is applying the competence acquired in a particular function to move into a new sector…

Gereffi (1999a) and Humphrey (2004) provide discussion on functional upgrading as a hierarchy mechanism, in which developing country firms transform from OEA production (original equipment assembling under contract to a global buyer) to OEM (original equipment-manufacturing manufacturer that is manufacturing a product under a buyer's brand), to ODM (own design manufacturer) to OBM (own brand manufacturing).

Upgrading and economic returns

The aim of upgrading, as suggested by GVC literature, is to increase economic returns. Summarizing key ideas in GVC literature on the relationship between economic returns and functional activities, Mitsuhashi (2005, p.28) draws a figure describing the link between upgrading and economic returns in Figure 5:

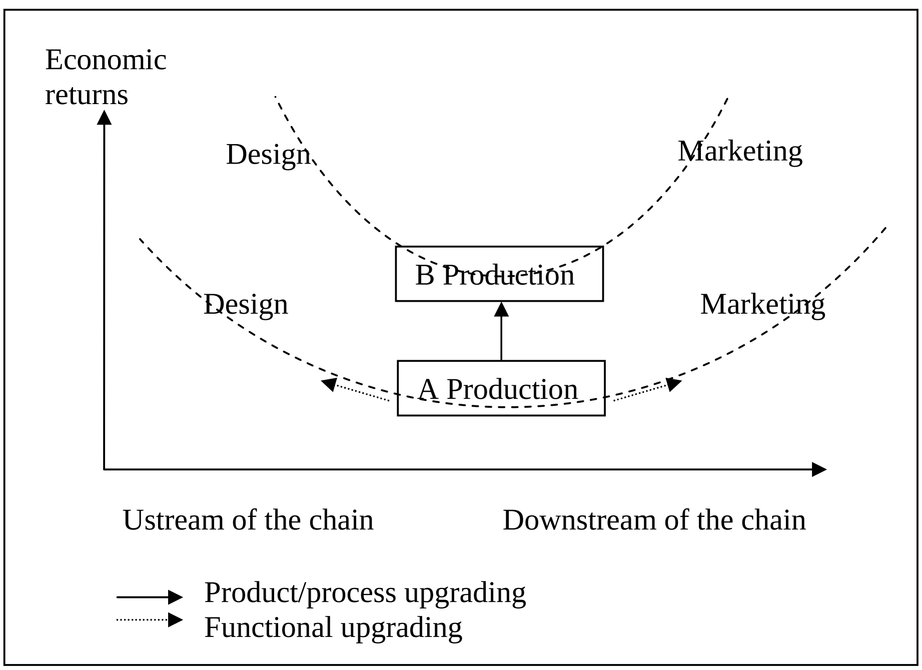

Figure 5: Upgrading and economic returns

(*Source: Mitsuhashi 2005, p.28*)

Mitsuhashi (2005) explains that the process and product upgrading are indicated as an upward shift of production activities from A to B, which allows the industry or firm to take part in a higher level value chain. In contrast, functional upgrading is denoted as movement or expansion along the value chain by acquiring design and marketing function, which is expected to yield higher returns, especially in a buyer-driven chain. The previous key research, Gereffi (1999a), proposes that the participant in global commodity chains enables local industry and firms to obtain both the upward shift and movement/expansion along the value chain.

3. Research methodology

The units of analysis in this chapter are two: the industry and the firms in the industry. The research uses qualitative research methods including in-depth interviews, direct observation and case study analysis. Primary and secondary data are used in this chapter. Secondary data is collected through official statistical sources and published researches. Primary data is collected from the researcher's field work that included interviews and observations in Dong Ky, Quy Nhon, Binh Duong clusters. The researcher visited four firms in each of the three clusters[1] and had twelve interviews with entrepreneurs. In addition to interviews with entrepreneurs, the researcher had interviews with three local authority leaders in the three clusters and two leaders of two associations (Vietforest and HAWA). Data obtained from these interviews and observations was note taken and then transcripted right after each interview and observation. *The in-depth interview method* is employed in order to do analysis at the firm level. Key informants include two types: managers of association and local governments as well as firms' export managers. The interviews were semi-structured[2] and designed in two formats. The interviews with association and local government leaders were based on questions relating to institutional factors and the export development of firms in the industry. The interviews with firms' export managers were based on questions relating to that firm's export activities including design and marketing activities, and its business relationships. In total, seventeen interviews were conducted. Each interviews lasted for more than an hour. *The direct observation* method employed in this study was limited to what the researcher could see when the researcher was present during the interviews. The presence of the researcher in the case study firms created the opportunity for direct observations of some management behavior, and such observations served as another source of evidence in the case study (Yin, 1994). *Case study analysis* was based on both primary data collected during interviews and observation by the researcher at selected firms as well as secondary data provided in the firms' materials. Among twelve firms visited by the researcher, only four firms with notable features relating to functional upgrading and relational capability were opted to develop into case studies.

[1] The researcher visited four firms in Dong Ky including Hung Long, Viet Ha, Viet A, Dong Duong, four firms in Quy Nhon including Duc Nhan, Phu Hiep, Tan Duc Duy, My Tai, four firms in Binh Duong including Truong Thanh, AA, Tan Phu, Tan Thanh.

[2] Jones (1985) guides that in preparing for interviews researchers will have, and should have, some broad questions in mind, but argues that although they are to some extent tied to their frameworks they should not be tied up by them

4. A description of the industry's development

In the recent ten years, Vietnam's wood furniture industry has shown remarkable achievements with exceptional growth in scale and production, an increase in foreign investment and export turnover. Export turnover from wood products has reached an annual growth rate of 40 percent, multiplied almost tenfold since 2000 and reached 2.4 USD billion in 2007, officially included in the country's top five products[3] since 2005 (Vietnamese German forestry Program, 2008).

Vietnam has become one of the world's top furniture exporters, ranking the fourth largest wood furniture exporter[4], holding 0.78% of the world's furniture market share since 2005 (UNCTAD, 2007). The main markets of Vietnamese wood furniture are USA, Europe (UK, France, Germany, Netherlands, Denmark, Sweeden), East Asia (China, Japan, South Korea) though currently Vietnam exports to more than 120 countries.

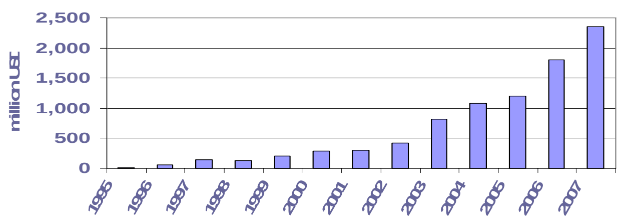

Table 1: Wooden Furniture Exports

(*Sources: General Department of Vietnam Customs*)

According to Vietnamese Ministry of Agriculture and Rural Development, in 2006, there are 1500 companies registered in the wood processing industry, 30% of these are state owned or Joint Stock companies, 60% are private owned, while the remaining 10% are foreign invested companies. Besides the number of registered companies, there are hundreds of thousands of small woodworking manufactures that are not registered across Vietnam.

Wood furniture producers mainly gather in three regions the Northern Red River delta provinces (densely in Dong Ky village- Bac Ninh province), the Central highland provinces (densely in Quy Nhon city), and the Southeast provinces (densely in Binh Duong, Ho Chi Minh, Dong Nai industrial parks). These three main production areas can be notably distinguished from each other in their institutional context, their firms'production scale, the types of products, and their target markets. The institutional context for example in Dong Ky village is a traditional handicraft village with a small production area. Workshops are in living quarters. Dong Ky's infrastructure although being improved by widening the main road is quit poor in comparison to those of the other two clusters. Although the local authority has been open minded on upgrading infrastructure to meet demand for production sites, they still lack the necessary knowledge to manage the industrial park. Meanwhile, industrial parks in Quy Nhon and Binh Duong clusters are quite different from Dong Ky in

3 after crude oil, footwear, garments, and seafood

4 after China, Malaysian.

the sense that they are newly built with good infrastructures, enabled by favorable supporting policies of local governments. Binh Duong cluster is being recognized as the area where local government is the most active in providing the most favorable condition for business, while the Quy Nhon cluster is recongnised as the most favorable geographical location because of its closeness to the sea and Lao where almost all of the wood supplies come from.

Regarding production scale, on the whole, enterprises are relatively small, with the exception some export oriented furniture factories. The companies which employ less than 50 employees are 63% while companies employing more than 500 workers account for only 7%[5] of the total enterprise (General Statistic Office, 2005).

The industry produces four main types of products: exterior furniture, interior furniture, and fine arts products. Firms in the Central highland and Southeast provinces produce western-style furniture mainly for the EU, USA markets and a small minority in the domestic market while firms in the Northern provinces make home accents and traditional solid wood furniture for the domestic market as well as China, Japan, South Korea market.

5. Position of Vietnam wood furniture producers in GVC and their moves towards functional upgrading

5.1. Upstream activities

Upstream activities are examined from the perspective of inputs needed for production.

In regard to machinery, Vietnam wood furniture producers purchase machines mainly from China, Taiwan, Japan or Germany but small tools and equipments from domestic makers. Specifically, Dong Ky producers mainly buy domestically made machines or ones imported from China. Producers in Quy Nhon and Binh Duong mainly import machines and equipments from Taiwan, Japan or Germany.

As far as wood material is concerned, producers rely heavily on imported wood material. 80% of the furniture industry is based on imported supplies (Dawson, 2008). Statistics from Vietforest show that Vietnamese enterprises need between 3-3.5 million cubic meters of wood per year, while the domestic material supplying market only meets 20 percent of that total volume. In 2006, the wood sector imported US$700 million worth of wood materials, accounting for one-third of the export turnover[6].

Producers mainly buy wood material imported from Malaysia, Laos and Cambodia. The dependence on imported materials make Vietnam’s wood processing firms vulnerable to the fluctuation in material supply. Since 2005, when its major suppliers in Southeast Asia like Malaysia halted exporting sawn timber, Vietnamese enterprises felt difficulty in sourcing timber input, leading to a competition for materials. Moreover, the increasing concern in high income markets like Europe, USA, and Japan regarding legality and sustainability will also limit a furniture firms’ choice of wood material suppliers in the future. The fact that

[5] Calculated based on data supplied in Statistic Handbook of Vietnam 2007
[6] Calculated upon figure in Statistic Handbook of Import Export 2007, General Department of Vietnam Customs

Vietnam wood furniture sector has been growing at a rapid rate while its material supply is limited makes Vietnam producers suspect that they may be involved in the illegal trade of wood to global buyers. This is an obstacle for their downstream activities in a market with concerns about the legality and sustainability of wood material used.

In response to the requirements by consuming markets, Vietnamese firms have been paying attention to and source legal wood materials. Many firms deal with the requirements by the European and USA markets for certificates of FSC (Forest Stewardship Council) chain of custodies by sourcing for legal and secure source materials. Some firms like Truong Thanh, Tan Thanh, Duc Nhan, Tan Phu have invested in forestation in Lao to ensure the legal source of their materials. Many firms such as Truong Thanh, and Dai Thanh were applied and accepted as members of the Vietnam Forest and Trade Network (VFTN), meaning that they pass the VFTN membership requirement demonstrating long-term commitment to responsible forest management and trade (Fripp, 2006).

Regarding other sub materials including adhesives, paints and finishing materials, producers often will buy products imported by domestic trading companies because these supporting industries have not been well developed in Vietnam.

5.2. Downstream activities and the moves toward functional upgrading

The industry firstly served the domestic market and began the internationalization process in early 2000s. Presently, Vietnamese wood furniture producers have become very active in downstream activities. Downstream activities are examined in connection to specific value chains with European, American and East Asian partners who are key buyers of these Vietnamese producers.

The European market has been a traditional market of Vietnam furniture producers. The European market is recognised as being a more stringent market in terms of the requirements for legality and sustainability, as compared with markets such as Japan and the USA. Across the EU, different member states are at different levels of awareness and action. Five EU member states – Denmark, France, Germany, the Netherlands and the UK – all currently have a national legal framework which require, as a minimum, proof of legal origin for purchases of wood product (Fripp, 2006, p10). To enter this market, Vietnamese producers had tried their best to comply to all the European Union’s regulations on material origin and environmental standards. Almost all Vietnamese producers are active, with more than 70% coming from certified sources, in a reliable FSC (Forest Stewardship Council) chain of custodies.

Regarding the distribution channel, most Vietnamese producers have not held direct contacts with consumers in this market. They normally sell products to large retailers like IKEA, Carrfour or a medium retailer like Scancom, or even a small specialized retailer like Lapeyre. Some small firms export through other exporting agents. Main exports to Europe are outdoor furniture and western style hard wood indoor furniture. In early times, Vietnamese producers had worked as processors under designs by European buyers, but now they can offer their buyers their own catalogs. In early times, very few producers undertook marketing activities abroad, just producing and waiting for foreign buyers to make orders but now the number of Vietnamese producers undertaking export marketing activities is increasing. With financial support from Vietnam Trade Agency, more and more furniture firms frequently participate in the biggest annual furniture trade fair in Europe, Tendence-lifestyle (Frankfurt, German) and obtain big orders. *This shows that Vietnamese furniture producers are moving toward a design and marketing function in the value chain with European buyers.*

Vietnam wood furniture exports to the USA have greatly expanded since 2004 when USA imposed import duty penalties on Chinese furniture. Vietnam is now the sixth largest exporter of wood furniture and components to USA (Dawson, 2008). This market has been moving towards systems which will require, as a minimum, proof of legal origin for purchases of wood. Although the demand for verified legal timber products in the United States is less pronounced than in Europe, some US-based retailers have announced procurement standards that favour certified wood. For example, Clarke Veneers, responsible for approximately 25 pe cent of tropical plywood imports into the USA, is FSC chain-of-custody certified and prefers to buy FSC from its suppliers (Fripp, 2006, p.13). To enter the USA market, many Vietnamese firms like Truong Thanh, Duc Nhan comply to the requirement and supply USA buyers with FSC chain-of-custody.

Regarding the distribution channel, except the case of AA, almost all Vietnamese producers have not sold directly to American end users. Most of them sells product to large retailers such as Jofran, John-Richards, Wyckes, Stickley, and Wal-mart. Some small firms export through other exporting agents. Furniture exported to the USA includes both outdoor and indoor products which are mainly based on western design style and are mass-produced, flat-pack furniture. Vietnamese producers are mainly producing indoor products based on the samples provided by American buyers. Therefore they can be said to be a Copy-OEM for these indoor products. For outdoors, Vietnamese producers produce their own design which are copied from their designs for Europe with some modifications. They can be said to be Quasi-ODM and ODM. Regarding the marketing function, almost all Vietnamese producers obtain orders when American buyers come to the two annual international Furniture trade fairs held in Vietnam (Expo and VIFA). In addition, under support by the Vietnam Trade Center in New York, many firms have been participating in big furniture trade fairs in the USA (including International Furnishing/Merchandise in Carolina, Houston Furniture & Accessory Market in Texas, International Contemporary Furniture Fair in New York) since 2005 and obtained big orders. *It therefore can be concluded that that Vietnamese producers have been taking steps toward functional upgrading in the downstream value chain with USA buyers.*

Vietnamese exports to East Asia which includes China, Taiwan, Singapore, Japan and South Korea, are solid indoor furniture often with some details and decorations, such as eggshells, lacquer, and carvings. Such products to those markets are made mainly by Dong Ky producers who have traditional craftsmanship since the 16th century[7]. Some Vietnamese producers open sale offices in China to sell their products directly to Chinese consumers. A few firms sell directly to Japanese or South Korean consumers. Many firms sell products to specialized retailers in the Japanese market. East Asian buyers seem to be design takers. Vietnamese furniture producers export products to these markets under their own traditional design, dating back to old Chinese dynasties. Some firms (as illustrated by case firm AA, Hung Long thereafter) are very active in undertaking marketing activities in Japanese, Chinese and Singaporean markets. By participating in furniture trade fairs in Singapore (IFFS- International Furniture Fair Singapore) and China since the 2000s, many firms have obtained large orders from not only Singaporeans and the Chinese but also from other global buyers from Japan, Europe, USA, Canada, Australia[8]. It can be concluded that there is a diversification in functions of Vietnamese producers in value chains with East Asian buyers. Some play as ODM while some play as OBM.

5.3. Position of Vietnamese wood furniture producers in GVC

Summing up downstream and upstream activities conducted by Vietnam wood furniture firms, it can be concluded that the Vietnam wood furniture industry is highly internationalized in both the upstream and downstream end of the global wood furniture value chain. The majority of the industry's inputs are imported and the majority of its outputs are exported. Design is mainly supplied by foreigners. Distribution and after sale service in export markets are mainly operated by foreign buyers. However, many Vietnamese firms have taken steps toward functional upgrading, working as ODM and OBM in some value chains. The position of a majority of Vietnam wood furniture firms in the global value chain can be drawn upon the simple value chain figure by Kaplinsky & Morris (2001) introduced earlier as Figure 6 below

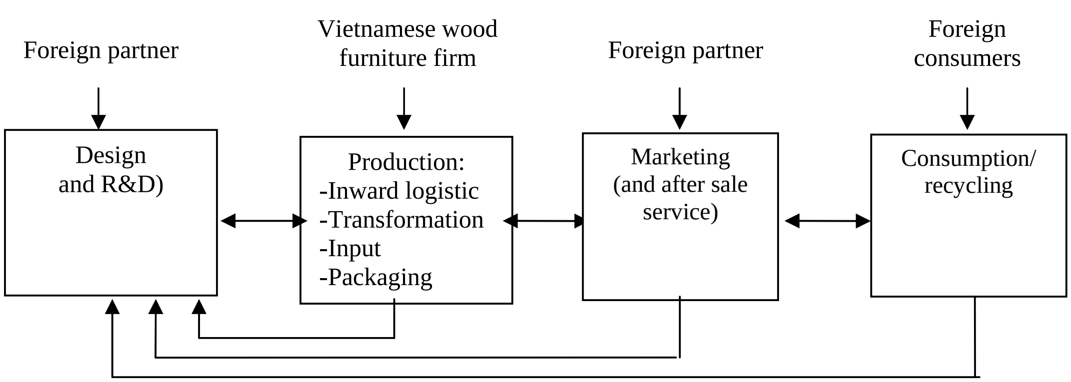

Figure 6: Position of Vietnam wood furniture firms in GVC

This figure shows that most Vietnamese furniture firms are in the manufacturing function, producing under a buyers' design or their own- copied design, delegating distribution and the after sale service function in final markets to foreign partners.

[7] This fact was revealed by Mr.Nguyen Van Sang, the vice chairman of Dong Quang Commune where Dong Ky village is located, during the interview with the author.
[8] http://muasam247.vn/Desktop.aspx/Tin-DN/Thi-Truong/Do_go_VN_thang_lon_tai_Singapore/

6. Cases of successful export development

6.1. Development profile of case firms

The four case firms optioned for study are established firms. All of them were founded in the middle of the 1990s when the Vietnamese government's reform policy began taking into effect. Four firms come from three main wood furniture clusters: Dong Ky; Quy Nhon; Binh Duong province. All firms have demonstrated successful development as a result of their upgrading in the international market.

Hung Long Company[9]

Hung Long Company was founded in 1994 in Dong Ky village with a small workshop. After nearly 15 years in operation, the company business has increased in scope. Its production site has been enlarged 25 times. Besides the old shop on Dong Ky Fine Art, the other three shops of the company have now opened. Its current turnover has increased thirty times compared with the initial year of opening. It firstly served a local market, mainly supplying furniture for local province consumption. Its first export to China was conducted five years after its establishment and now its export market has expanded to South Korea, Japan and Europe. Its initial products are solid wood carving furniture. Together with producing traditional wood carving furniture for a domestic and China market, Hung Long is now producing a western designed product for export to Europe.

Duc Nhan Company[10]

Duc Nhan Company was founded in 1995 with its first factory in Gia Lai, a Central Highland province, opening a second factory in Quy Nhon and planning for a third factory opening in Binh Duong. Its production site has been enlarged 4 times. Its current turnover has increased fifteen times compared with the initial year. It has produced exports since its establishment. Its export market firstly is Scandinavia and has now expanded to other Western European countries and the USA. Its initial products were outdoor furniture. Presently, together with producing outdoor furniture for Scandinavian customers, Duc Nhan is now producing western designed indoor furniture for some other Western European buyers.

Truong Thanh Furniture Cooperation[11]

Truong Thanh Furniture Cooperation was founded in 1993 with its first small factory in Dak lac, opening a second factory in Quy Nhon and a third factory in Binh Duong. After 15 years of operation, its production capacity has increased 15 times. Its current turnover has increased by forty times since establishment. Founded as a private Ltd, Truong Thanh now becomes a PLC (public limited) company. Its market price of stock is five times higher than its face value even in the downturn period of the Vietnam stock market in early 2008.

[9] Hung Long Company website http://www.hunglong.com.vn
[10] Duc Nhan Company website http://www.ducnhan.com
[11] Truong Thanh Furniture Cooperation website http://www.truongthanh.com.vn

Truong Thanh firstly served a local market, mainly supplying furniture for local province consumption. Its first export to France was conducted three years after its establishment and now it has expanded its market to many other Western European countries. Currently, besides serving export markets, Truong Thanh is one of the most reputed producers of indoor wood furniture in the domestic market.

AA Cooperation[12]

AA Cooperation was founded in 1993 with its first factory in Ho Chi Minh, opening a second factory in Binh Duong. Founded as an architecture and industrial design company, AA firstly served demand for industrial decoration in a domestic market. It provides design and supplies interior decoration for hotels and apartments. After the three years since their establishment, it shifted its focus to indoor furniture. Its first export furniture was indoor furniture to Japan under the brand name of a Japanese buyer. Its current turnover has increased by twenty five times since its establishment. Currently, besides serving export markets, AA is the most well-known brand producer of indoor wood furniture in the domestic market.

6.2. Functional upgrading and export development

At the beginning of their international business, Duc Nhan, Truong Thanh and AA acted as processors or as an OEM (original equipment manufacturer) for some European and East Asian branded retailers. Specifically, a year after it was established, Duc Nhan began its export business as a processor for Scancom[13]; Truong Thanh firstly worked as a processor for Lapeyre[14] and sold its first OEM furniture to Carrefour[15]; while six years after AA's establishment its first OEM furniture shipment to Japan was exported.

After several years working as processors and OEM, AA and Truong Thanh have been upgraded to ODM (original design manufacturer) as a result of their efforts in production and functional upgrading, including investing in machinery and design teams to maintain their competitiveness, developing their own brand name, and conducting marketing activities in export markets.

Specifically, AA is currently working as an ODM to supply Jadora, a special furniture collection for the US market, and Kecebo, a line of furniture created for the European market. Notably, unlike other export-oriented producers who often ignore the domestic market, AA has developed to become the national leading interior furniture producer with

[12] AA Cooperation website http://www.aacorporation.com/
13 ScanCom International A/S is one of the world's largest manufacturers of outdoor furniture as well as decorative accessories. http://www.scancom.net
[14] Lapeyre is the largest specialized wood furniture retailer in France. http://www.lapeyre.fr/
[15] Carrefour is the world's second-largest retailer and the largest in Europe. http://www.carrefour.com/

the brand name “Nha xinh”[16]. With the desire of branding “Nha xinh” as the world name, AA is conducting a series of marketing activities overseas in both the US and Europe including opening a sales office in both countries. The keys for AA’s success have to do with its investment in designing (hiring a talent foreign designer to work at the company) and its multi-chain strategy (working as an ODM for export market and branded producer for domestic market).

Besides investing in advanced machinery to upgrade production capacity, Truong Thanh has invested in building designing capacity[17] to work as an ODM for three of the largest British distributors[18]. Although similar to AA in upgrading design capacity, Truong Thanh still supplies outdoor furniture which is considered a less design-led product while AA focuses on only interior furniture. At present, Truong Thanh is also conducting a multi-chain strategy: working both as an OEM[19] and as an ODM for the export market as well as a branded producer for the domestic market.

Except for AA and Truong Thanh that have developed a distinctive designing capacity to work as ODMs in export markets, many producers imitate designs ordered by foreign customers or from competitors. Unlike AA and Truong Thanh who have both reached the position of a brand producer in the international market, many other companies like Duc Nhan are still OEM and ODM suppliers. They also use a mix strategy to develop an export market. One the one hand, they work as processors under the name of foreign branded firms while on the other hand they develop their own design to get higher prices.

6.3. Combination of relationship marketing and transactional marketing

Relationship marketing and transactional marketing are the terms used by Grönroos’s (1997) to distinguish between a classical 4P marketing mix tool and relationship building and management which are now considered two marketing approaches composing firm’s marketing strategy continuum.

Four firm cases consider both the combination of relationship marketing and transactional marketing as a key to their success. Transactional marketing tools play an important role in attracting buyers while relationship marketing helps to maintain existing relationships. Personal relationships are considered the most useful marketing tool not only for the small firm like Hung Long but also for the big firm like Truong Thanh. Hung Long represents a typical success case for a micro firm in Dong Ky village that often uses personal relationships (kinship or friendship or acquaintanceship) to get orders. Through kinship and

[16] Nha xinh, meaning beautiful house, is a line of furniture which AA creates for the domestic market. Nha xinh is a well-known brand name for middle and upper class households in cities. Designs of Nha Xinh line look similar to their design in the EU and US market.

[17] Some companies fund potential employees (e.g, daughter and son of the Group’s president Vo Truong Thanh) to study design and marketing in the UK. During their studying in UK, they have worked as the company’s marketing staff, creating business relationships with three of the largest British distributors.

[18] They are Argos&Homebase (UK), KingFisher (UK), Alexander Rose (UK)

[19] Truong Thanh works as OEM for Alexander Rose, , Carrefour and ODM for Lapeyre, Argos&Homebase, KingFisher

friendship, Hung Long gained some contracts to supply furniture for local state organizations. First, foreign buyers came to Hung Long as a result of the recommendation by local officials with whom Hung Long holds good personal relationships. Keeping good personal relationship with buyers is Hung Long's key toward development. Hung Long who is an owner-manager is also the main person taking responsibility for face-to-face communication with foreign customers as well as big domestic customers. Besides satisfying the buyers' requirements on quality, design and delivery time, he possesses good communication and negotiation skills. All of which contribute to the firm's success in keeping buyers. Because Hung Long holds a big share of the carved wood furniture domestic market, Hung Long now has expanded into the export market starting with China, then South Korea, and now to Europe. However, this is expansion is different from the first foreign business transaction brought to the company by local authority, as later foreign buyers come as result of Hung Long effort's in transactional marketing activities including export trade fair participation as well as its name and website address listed on the websites hosted by domestic trade promotion agencies including those by Vietforest and HAWA.

Similar to Hung Long in the North, Duc Nhan in Quy Nhon developed as a result of holding good business relationships with foreign buyers. Established as an export oriented firm, firstly focused on outdoor furniture, Duc Nhan gained its first foreign buyer[20] through the recommendation by a local authority. Keeping cooperative business relationships with Scancom, by meeting quality requirement and delivery time, Duc Nhan has accumulated a lot of production technology and market knowledge. Within additional to these marketing relationships, Duc Nhan has been significantly investing in transactional export marketing activities including participation in international furniture trade fairs annually in Frankfurt and its name and website address listed on the B2B website including Ebay and Alibaba. With effort in marketing activities both relationship and transactional marketing, Duc Nhan has now established itself as one of the leading furniture manufacturers with key buyers not only from Europe but also the USA and Korea.

6.3. Summary of case findings

The process of successful export development of firm cases indicates that successful firms started their export business as pure producers without any export marketing activities, gradually involving in export marketing and then fully taking marketing function. The producers in Dong Ky village (Hung Long) developed from a small family business, starting its business to serve the domestic market. After being sourced by Chinese buyers, Hung Long decided to conduct export marketing to a neighboring country, China and other high income countries in the region like Taiwan, Japan, South Korea. Producers in Quy Nhon (Duc Nhan) and Binh Duong (Truong Thanh) started in the export business from their inception, working as processors or sub-suppliers for export to Europe and America. Many of these firms had to learn to upgrade their quality to meet the requirements in high-income

[20] Scancom is first foreign buyer of Duc Nhan

markets (say the UK, France). Together with working as processors or as an OEM, these firms actively developed their own design and undertook marketing activities to brand their products in the international market. The export success of these firm cases closely link up to the upgrading trajectory. Upgrading trajectory of the selected case firms is summarized in Figure 10 below.

Position in global value chain	--------OEM →-------	------→ ODM-------	-----→ OBM-
Case firms	Duc Nhan, Truong Thanh	AA, Truong Thanh Hung Long,	AA

Figure 8: Upgrading trajectory of the selected case firms

The studies on firm cases reveal the significant contribution of functional upgrading to their export development. By conducting transactional export marketing activities like trade fair participation, the firms make their produce known to more potential buyers. Many buyers which the firms attracted from trade fairs become long term partners as a result of the firms' effort in relationship management. Relationship with buyers plays a significant role for the firms' export development. Besides meeting buyer's requirements on quality and price, the case firms maintain long-term relationships with buyers through personal communication.

7. Conclusion

The explorative study signals that the Vietnam wood furniture sector has been booming as a result of the outsourcing trend from high-income economies. Although, there are a number of firms (in Dong Ky) which develop an export business as an incremental process, many firms engage in the international market as a result of a global buyers' sourcing activities. Some become a part of the captive chain with big buyers like Scancom, some engage in the market-based chain with small specialized retailers like Lapeyre. The majority of the industry's inputs are imported and the majority of its outputs are exported. Design is mainly supplied by foreigners. Foreign buyers still operate distribution and after sale service in export markets; however, some firms are operating their own sale offices in export markets. Many Vietnamese firms have been taking steps toward functional upgrading, working as ODM and OBM in some value chains.

Although it is always hard to draw conclusion from a small number of cases, this explorative study is helpful in answering the research questions by the confirmation that functional upgrading has been implemented but not very popular in the industry. There have been some case firms transforming from OEM to OBM in different chains. The firms undertaking functional upgrading have not experienced economic downturn but instead have demonstrated success in export development. Trade fair participation is the most popular and efficient marketing tool.

The research provides some theoretical and managerial contributions. For theoretical aspects, the research provides an answer to the query that whether moving beyond manufacturing to a marketing function will lead to a firm's export success. The findings challenge the theories of competitive advantage which suggests that a developing country firm should specialize in activities where they would have a competitive advantage which is low labor cost manufacturing activities. Actually, specializing in production helps a developing country firm in the short run to learn to produce better and makes the most use of its current comparative advantage in cheap labor cost. But in the long run, this specialization causes firms to be stuck in the vulnerable position of a threatening price war and profit margins being ever narrowed down. Building new capabilities through functional upgrading is a dynamic process, creating new comparative advantages.

For managerial aspects, the research suggests that to develop in the global market, firms should be more active in design and export marketing. Combining different functions in different value chains is a good strategy for long term development. More specifically, when conducting export marketing, a firm should combine both relationship marketing and transactional marketing. Transactional marketing tools play an important role in attracting buyers while relationship marketing helps to maintain existing relationships.

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