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From The Desk of CIO

The Pull and Push Factors in Business

A company ventures into a business principally because of profit or potential profit to be earned. The profit motivation is the main driving force of efficient capital allocation. Whenever entrepreneurs see business opportunities, especially in a cyclical uptrend such as the super profits of the rubber glove industry during the pandemic of 2019/20, they will want to ride the bandwagon too. This is the pull factor. There is also a push factor that forces a company to invest, such as backward integration to gain control over the supply of raw materials. China, for example, is forced to produce their own chips as US is forbidding US companies to sell high-end chips to China.

In employment, when an employee resigns it is basically due to the pull or push factor, i.e. better offers elsewhere or unhappiness that forces an employee to leave.

As for companies, the business decision is mainly due to the attractive return on investment (the pull factor). During the pandemic period, the strong demand for medical gloves resulted in glove prices skyrocketing more than four times *(see Exhibit 1).* Glove companies enjoyed profits never seen before. The super profits led to expansions by existing players and also new entrants both in Malaysia and abroad.

From bumper profits in 2020/21, many glove companies are now swimming in red with no indication on when the selling price will recover back to pre-pandemic level. The explosive expansion of China glove producers has now turned into a nightmare for dominant Malaysian glove manufacturers. Looking back, super profits for the glove industry had created new competitors who will be around for many years competing with Malaysian producers.

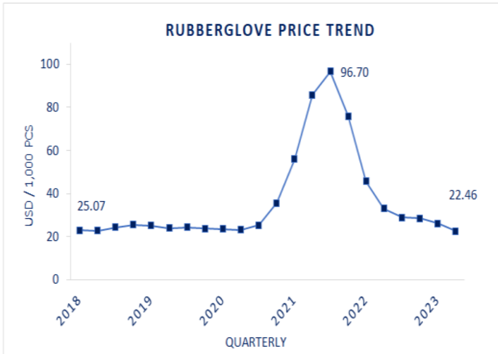
The chip industry in China is a completely different story. China has been a major buyer of chips for their electrical and electronic equipment and appliances (*see Exhibit 2*). They were happy to purchase these chips from various global chip producers where supply has never been an issue. China only produces less than 20% of its chip requirement.

China is the world's largest chip-consuming country as more than 30% of world chip exports ends up in China (*see Exhibit 3*).

With US and its allies cutting off some of the higher-end semi-conductor chips to China, it is forcing China to fast-track its own production of chips. The introduction of the *Huawei Mate 60 Pro* using *Kirin* 7-nm chip is a shock to industry players who thought it would take many years for China to develop top-end chips.

From being a customer, the US sanction has pushed China to become a formidable producer of chips and a worthy competitor.

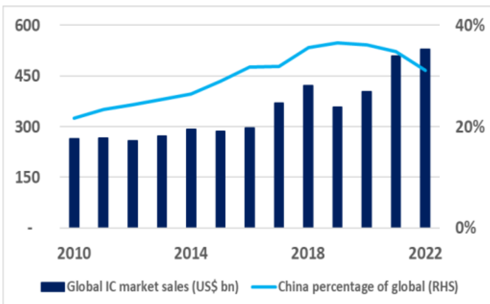
Exhibit 1: Up and down of glove price



Source: Hartalega, PCM, Aug 2023

Exhibit 2: China depends on import of chips

Exhibit 3: China is world largest consumer of chips



Source: The McClean Report

For Phillip Capital Management Sdn Bhd

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