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## China's Future as a Low-Cost Nation

### **Introduction**

China has become an immensely powerful player on the global stage in a brief period of time. It went from a nation plagued by civil war and political instability to one of the largest economies in the world, becoming the global capital for manufacturing, responsible for 28.7% of global manufacturing output. Manufacturing's value added was only \$625.22 billion in 2004, it has now exploded to \$4.87 trillion (The World Bank, 2021). As a result, 'Made in China' has become synonymous with cheap goods worldwide, permeating every industry. China is a champion of globalization, taking advantage of its ample supply of cheap labor to make itself look extremely attractive to foreign firms. Its cheap labor meant that it had a comparative advantage in manufacturing. However, it still suffered from a large technology gap and so invited American firms in, thereby marrying cheap labor with advanced technology. Soon China and other East Asian countries learned and developed their own technological capacities.

Manufacturing is a field where producing is the only way to increase productivity, so as China learned how to produce goods at a cheaper rate, foreign firms quickly fell behind, cementing China as the world's foremost manufacturing power (Stiglitz, 2017). It has enjoyed this role for over two decades, especially in labor-intensive manufacturing, but now it may be looking at a new future.

## Wage Increase

There have been academics sounding the alarm bell on China's dominance in manufacturing for more than a decade, and their warnings are ringing more accurately with time. Various sociological and geopolitical factors have influenced China's manufacturing industry, such as the decline in the supply of cheap labor with rural-to-urban migration patterns slowing and the One Child Policy. Despite these external factors, the main reason for concern is rising wages in China. At the beginning of China's transition into manufacturing in 1978, its workers were paid 3% of their American counterparts' wages; this wage was comparatively cheaper than other eastern Asian nations and rose at a relatively low rate until the later parts of the 1990s. In more recent times, Chinese wages across industries and regions have exploded, outpacing labor productivity, due to this, its comparative advantage has disappeared in the modern day, making China expensive globally (Li, Lei, & Yanyan, 2012). This section will use multiple graphical representations to illustrate this wage increase in recent years and how it compares globally to other nations.

*Figure 1*

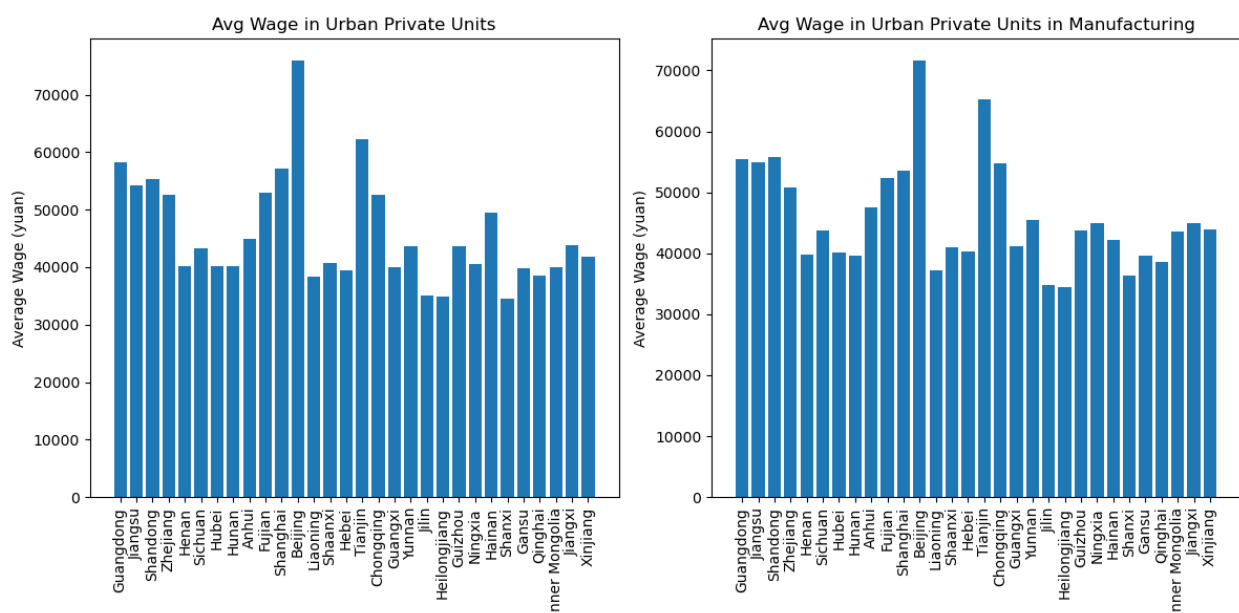
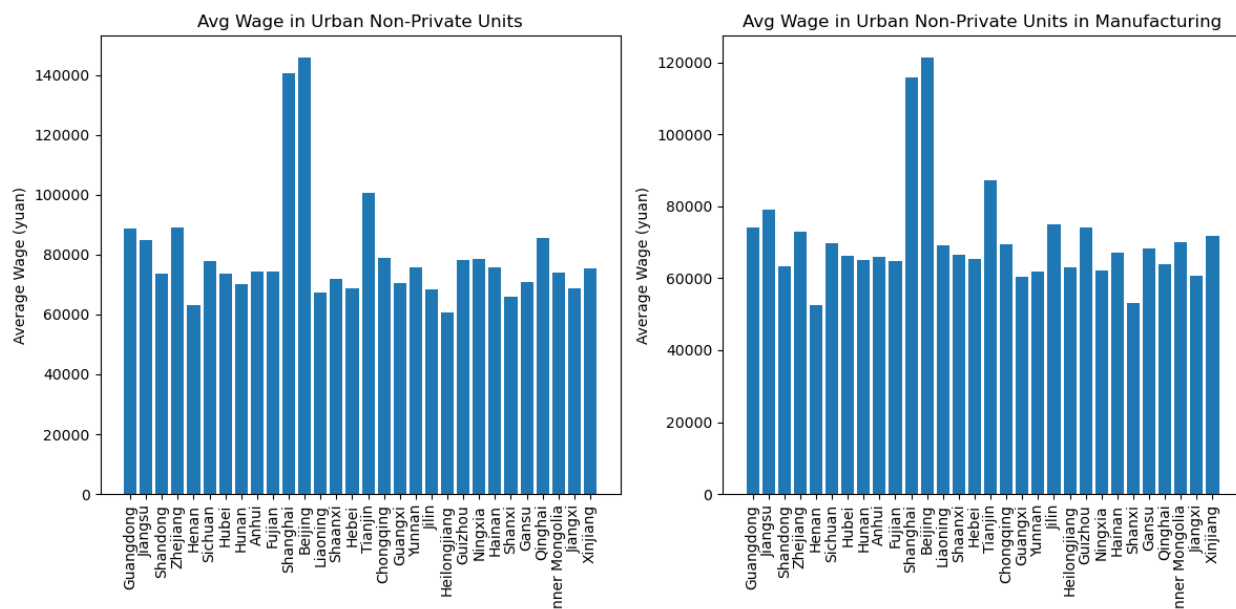
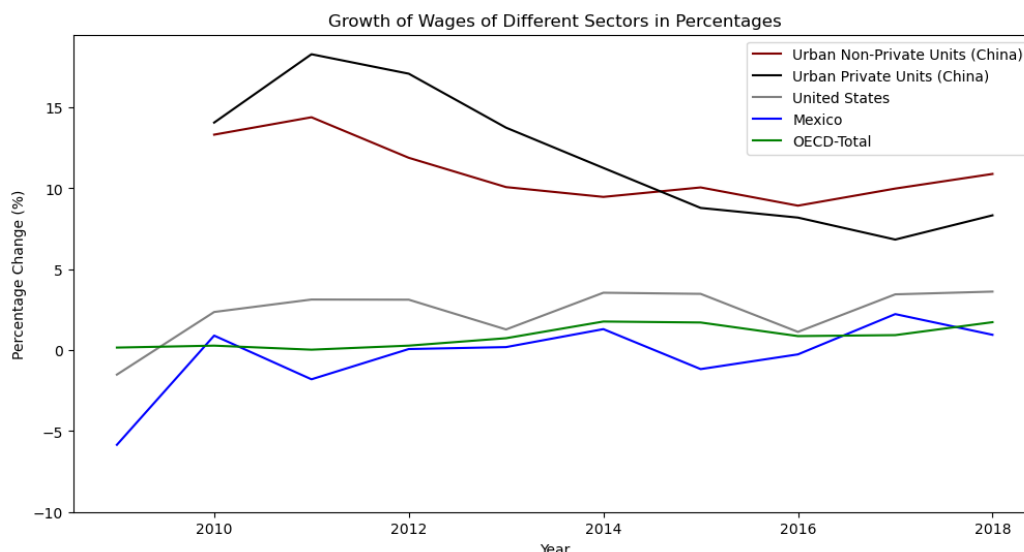


Figure 2

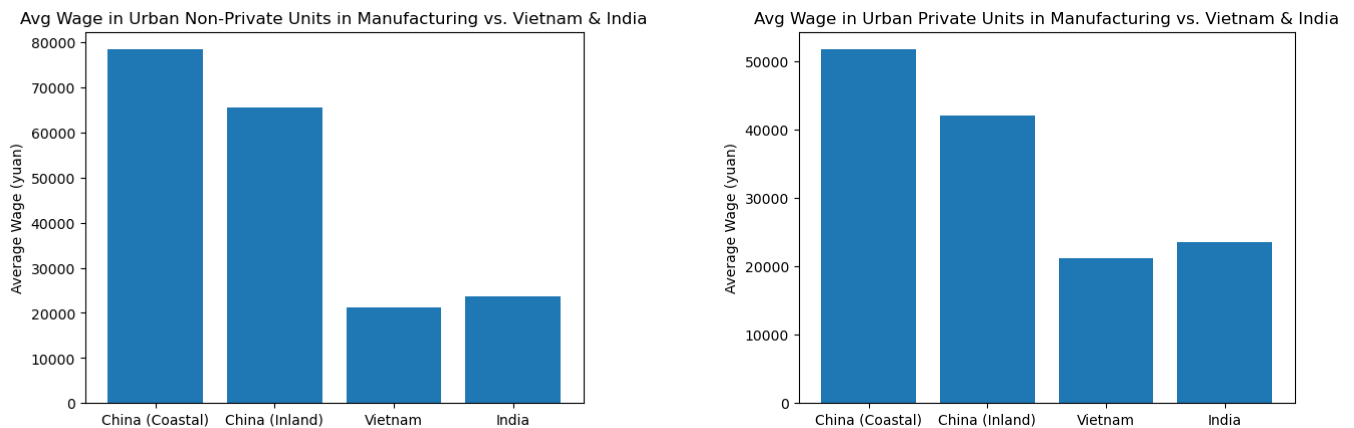


China's rising wages have been a remarkable development across various sectors and regions of the country. In particular, the manufacturing industry has seen an increase in wages, with the average salary in urban private and non-private units reaching record numbers in 2019. Figures 1 & 2 demonstrate this trend in 30 Chinese cities ranked according to nominal GDP, revealing that non-private unit wages have experienced a more significant increase indicating that state-owned companies and government employees have seen the most benefit. While there is a uniform distribution in wages for both sectors, it is evident that all cities have witnessed significant improvements compared to the past. Two decades ago, the average Chinese salary was a mere 9,333 yuan per year, but today even the poorest cities have experienced tremendous average salary increases in the manufacturing industry. The implications of this are significant as it creates a baseline salary that improves the quality of life for the worker. Still, at the same time, it makes China lose its comparative advantage in the global market.

Figure 3



Over the last decade, China has closed the wage gap that exists between itself and the US by multiple magnitudes going from 30 times smaller in 2000 to only 3.5 times in 2021. This trend will continue into 2023 and the future, dwarfing any developing country and competitor (Ezrati, 2023). Figure 3 shows China's percent change in wages in two sectors: urban non-private and urban private units, along with the US, Mexico, and the average of all OECD countries. It shows that China is leagues ahead, with both sectors consistently seeing significant increases, with private units averaging slightly more growth per year. At the same time, the other nations struggle to see more than a 3% increase and routinely see a negative change, especially Mexico, a direct competitor to China in terms of cheap labor-intensive manufacturing. The accumulation of an enormous amount of capital in such a short period of time has allowed for an unprecedented increase in wages. Figures 1-3 have shown the growth in average wages and manufacturing wages, but the next thing to look at is the distribution of this increase across regions in China.

*Figure 4*

China has a well-known inland-coastal inequality as most of its economic centers are based on the coast. This inequality in economic growth has grown in recent years, so it is crucial and necessary to isolate these regions and see if the trends from before hold true (Felice, Odoardi, & D’Ingiullo, 2021). From the list of 30 Chinese cities listed in Figures 1 & 2, a ‘Coastal’ and ‘Inland’ group was created, each comprised of the average wage their respective cities had in 2019. Figure 4 shows that the gap between the Coastal and Inland groups is noticeable but not significant, especially when viewed in the context of historic economic inequality between the two groups. These two groups, in non-private and private units, were compared to the manufacturing wages of Vietnam and India - nations that China once had a comparative advantage over in terms of cheap labor. This is not to say that all workers are benefiting from this increase. The rise of gig manufacturing, born from relocating production lines inland, circumvents these wage increases by using short-term contracts, low wages, and limited job security. Companies such as Foxconn may increase the wages for a minority of its workers while a majority still see low payments, in a sense, ‘hoarding overtime.’ They and other inland companies have also been using dormitory systems in which workers are closer to the

factories, isolated, and their daily lives are controlled. But because these workers gain housing, many workers come back to these factories despite hard hours and low pay. Many manufacturers within China are still attempting to exploit workers for as long as they can (Dong, 2022). These types of practices are another reason why wages for private urban units are so much lower than their non-urban counterparts (see Figures 1 & 2). Still, the general trend that these graphical representations show is that wages as a whole everywhere, coastal and inland, have been increasing. It is clear that Chinese wages are now multiple times larger than their competitors. Still, because their labor force is mainly unskilled and has never been the high school, it is easy to lose manufacturing ground to other nations (Rozelle & Hell, 2020).

A common trend seen in Figures 1, 2, and 4 is that non-private units often see a more considerable wage increase than their private counterparts. This may be due, in part, to the Chinese government prioritizing rising wages. The government has a history of raising wages for government employees, a much easier and more consistent process than protesting and striking against multinational corporations; foreign firms always attempt to play as little as possible in order to take as much surplus as possible from their laborers (Reuters, 2015 & Chua, 2018). More recently, in 2020, China's President Xi Jinping launched the "common prosperity" campaign by raising minimum wages nationwide to benefit rural migrants working in cities. This program and others like it are vital for Xi's public acceptance and the strength of the communist party as a whole (Kawakami, 2021). These types of programs and the rapid development of China have led to a radical increase in wages to the point where manufacturing workers in China are not only making several times more than their competitors in Mexico, Vietnam, and India but also have their wages growing at a rate these nations have never seen.

### **Movement of Manufacturing**

In the age of globalization, companies will continue to operate in a way where their costs are the lowest, and their profits are the highest. They originally came to China due to cheap labor, at the cost of millions of Western jobs, and now that is changing (Yan, 2017). As wages and costs for firms have grown along with rising concerns about cross-border dependencies, companies have been leaving China and seeking cheaper alternatives.

From the perspective of companies, rising wages have been a growing issue in China for a decade but are now too large to ignore. Large technology companies have been aiming to get out of China for a while now, but Samsung was the first and largest to do it successfully. Samsung had been working for a decade to diversify its manufacturing bases, finally closing its last Chinese smartphone plant in 2019. China no longer has the cost advantage for assembly labor, rather it now belongs to nations such as Vietnam and India (see Figure 4). Due to this, Samsung has built new plants in Vietnam and has announced plans to build the largest smartphone factory in India (Jung-a, Yang, & Bradshaw, 2019). Samsung was the first but is certainly not the last, companies such as Apple have followed suit, pushing their suppliers to nations such as India instead. These companies are also influenced by greater consumer awareness and demand for ethically sourced products and well-treated workers (Jim & Standing, 2012). Operating in China for a while has been more expensive, but now the cost is so significant that it is cheaper to leave China altogether (Wong, 2023).

Due to the COVID-19 pandemic and its interruption of global supply chains, many nations are rethinking their current supply chains - especially China. The pandemic shut down China and the world, and supply shocks happened globally. Due to these supply shocks, trust has weakened between nations, and increasing geopolitical concerns are making China less attractive to foreign firms. The pandemic also revealed breakdowns in logistics related to manufacturing,

such as sending raw materials to China, so nations favor regional alternatives. For example, the U.S. moving away from China and towards Mexico due to lower transport distances, costs, and wages (Shih, 2022). China was also unique with respect to the pandemic, as it had a zero-tolerance policy that constantly started and ended production in an unpredictable manner leaving companies out to dry. Moreover, geopolitical concerns regarding the U.S.-China Trade War, increased aggression towards the West and the South China Sea, and close connections with Moscow all make China unpredictable and toxic for businesses. This, again, mixed with rising wages, explains why Apple, Samsung, Addidas, and Hasbro have all already started or moved out of China to Vietnam and India instead (Braw, 2022). This trend is not isolated to foreign firms, domestic manufacturing companies have started to move their supply chains due to rising wages and geopolitical risks. These companies also have the desire to be near consumer markets, so Chinese companies increasingly move to and finish goods in nations like Mexico. India and Bangladesh are becoming increasingly attractive for manufacturing due to cheap labor and land, while nations such as Vietnam are attracting Chinese solar giants (Tan, 2023). Due to all of these companies moving, China is losing significant amounts of manufacturing ground to Vietnam, India, Mexico, and other Southeast Asian nations. Specifically, China's furniture, apparel, footwear, travel goods and handbags, minerals, and science and technology exports are all declining. In addition, cargo arriving from China to the U.S. is at 40-50% of what it once was, indicating drastic changes.

## **Conclusion**

Low Chinese wages catapulted China to a global power but have been rising at breakneck speeds. China has slowly lost its role as the world's factory to cheaper alternatives such as Mexico, Vietnam, and India. The main reason for this is rising wages, as companies will always



prioritize creating a good for the cheapest amount possible. Companies that want to remain in China, perhaps due to how much they have invested, are resorting to predatory practices to circumvent rising wages. This is a trend that could continue to grow as wages are rising. Concerns about Chinese-based supply chains and geopolitical risks have also influenced companies to seek other nations. This does not spell doom for China, however.

As manufacturing jobs and exports have been on the decline, other industries in China have been booming. Industries such as software and information technology services, information transmission, and finance have all seen a 13% increase in growth in 2021. These same types of high-tech, white-collar jobs also saw the most significant rise in wages, indicating that industry is growing and is the new focus of China (National Bureau of Statistics of China, 2021). The rise in wages across China will induce invention and technology adoption due to more disposable income, a greater incentive to innovate, and a larger number of technology firms. China has been shifting to more significant corporate investment in order to boost innovation as it has become crucial to its economy due to the significant increase in labor costs and labor scarcity (Jianqiang et al., 2020). China may not have enough of these white-collar jobs in the short term, but it is still the largest manufacturer in the world, and many firms remain with them. China can no longer indeed be considered a low-cost nation, but it will remain a staple in the manufacturing industry due to decades of investment. Its transition into technology as a primary sector of its economy indicates its future plans and where the nation aims to go into the future.

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## Appendix: Data & Code

The following sources were used to gather data for this research:

### GitHub Repository:

Chittem, N. (n.d.). GitHub. Retrieved from <https://github.com/NarenChittem?tab=repositories>

This link will take you to the code and data files used in the creation of the graphical models.

Comments within the code isolate each graph, and the README file in the folder will further explain the process of transcribing the data.

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