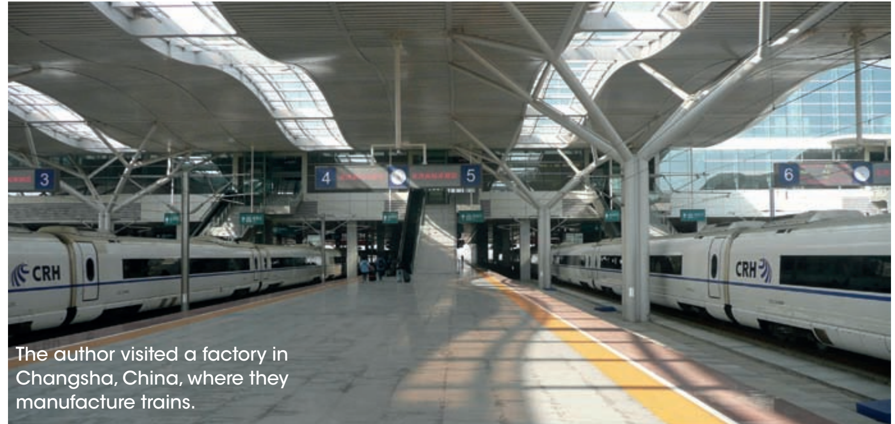
SOME FACTS CONCERNING CHINESE LABOUR

By Alexander List

Delving into what makes Chinese labour different to South African labour.



The author visited a factory in Changsha, China, where they manufacture trains.

Sometimes, if you are lucky, the world gives you a chance to touch it changing. In September, in a factory in the city of Changsha, I had such a chance. The factory assembles trains, and on its finishing line was a set destined for a new subway line in Malaysia, one whose builders I had interviewed only a few months earlier. Running a hand over the cold metal of the train was like feeling the world After the West.

Another change was also prefigured in that factory. It was light and airy, tidy and well managed. Workers moved around with autonomy, working together smoothly. Bosses barking orders were conspicuous by their absence, as were drones on an assembly line. I asked a supervisor about the workers' wages. On average, they made R160 000 per year; the highest, R240 000. Those wages were, by explicit company policy, rising at 15 percent per year. This was some distance from low-cost labour. That factory is not an exception. Wages across China have risen by an average 15 percent for all of the last decade. If, as South African managers protest, rising labour costs decrease competitiveness and increase unemployment, China's exports should have plummeted and it should have an unemployment crisis. Neither has occurred.

This essay will probe this phenomenon, its causes, and its relevance for South Africa. The first section will present the data to substantiate the claim above. The second will probe why wages are rising so fast, and why employment and competitiveness are being maintained regardless. The third will consider the implications for ourselves.

RISING WAGES, RISING EXPORTS, RISING EMPLOYMENT

According to official data, in 2004, the average annual wage across China was 16 000 renminbi (RMB). By early 2014, that had risen to RMB51 000. Over the same period, the renminbi rose from 8.3 to the dollar to 6.1, while the South African rand dropped from 6.5 to 11. In rand terms, the average of wages across China rose from roughly R13 000 per year to roughly R90 000, or around R7 500 per month.

This is official data, so it is likely an overstatement that excludes informal, very low-wage employment. But there is no reason to think that the overstatement would be higher today than ten years ago. If anything, it will be smaller, since data quality in China has improved greatly, and migrant labour in particular is now much better tracked.

Moreover, the data tally with observations across the country. In Shanghai, labour has become so expensive that even KFC has been forced to automate, introducing touch-screen ordering earlier this year. Construction workers with some experience now earn RMB10 000 (R18 000) per month. The rises are not confined to the rich coastal cities. In Changsha, in the historically poor province of Hunan, the rapid increases were not restricted to the train factory. In the plant of a multinational auto company, I was told that interns from vocational colleges were now given RMB1 500 (R2 700) per month, which is what a full worker would have been paid a decade ago. Everyone, from makers of construction machinery to auto companies, said much the same.

The figures also align squarely with policy measures. Ten years ago, the wealthy coastal provinces began raising the official minimum wage, at rates of 15–20 percent per year. A few years ago, the inland provinces followed suit.

The minimum wage in Guangdong, the "workshop of the world", is now RMB1 808 per month (R3 250), having been raised by 19 percent last year.

Though South Africa's Reserve Bank has castigated workers for seeking such wage rises, across the decade inflation in China has barely risen. The consumer price index rose a mere 3 percent per year on average. The producer price index *declined*, even with soaring raw material prices as well.

China's exports have also grown rapidly throughout this period. In constant dollars, in 2004 they were USD680 billion per year, tripling to USD1.921 billion in 2013. Its exports to South Africa rose from USD3 billion to USD16.8 billion, or almost six times over, despite its wages now equalling or even surpassing ours. If wage costs were what made our firms uncompetitive, they should have regained market share. They seem to have done no such thing.

It is true that China's global share in some low-value products has, at last, begun to decline. But those declines are almost insignificant. In 2012, China's share of global garment exports remained at 38 percent, almost eight times higher than any other country. It declined in 2014, by a whole 0.1 percent (in the US). At this rate, China will indeed lose its market leadership sometime in the 25th century. It has certainly lost no competitiveness versus South African textile producers. Our imports just of footwear and apparel grew 3.5 times, from USD0.8 billion to USD2.7 billion.

There has also been no discernible decline in employment. China's official unemployment rate is one of its most untrustworthy pieces of data but, except at the peak of the global crisis in 2008, there have been few to no reports about joblessness. No one I have spoken to or read in China recently has reported anything other than a strong jobs market.

In fact, labour activism is rising rapidly across China. Since the workforce has stopped growing due to the "one child" policy, but employment remains high, Chinese workers have realised their own strength. Strikes and labour action have soared. In 2014, there were roughly a hundred strikes per month across China, double the rate of 2013. In September, a major electronics factory faced a strike when it skimped on giving its workers a moon cake for the Mid-Autumn Festival (roughly equivalent to eggs at Easter). A docile and predictable workforce this is not – nor, given that Chinese firms can fire at will, one scared of losing work.

So wages in China are rising rapidly, strike action is intensifying, and yet inflation is low, exports are rising and unemployment is low. But, during wage negotiations, South Africa's employers, echoed by our media, confidently state that such a world is simply impossible. According to them, a living wage, rising rapidly, *must* mean declining market share, rising prices, and rising unemployment. One-fifth of humanity, for a full decade, has achieved the opposite. How?

HOW AND WHY

Some may argue it is "work ethic" or "subsidies". Neither excuse stands up to scrutiny.

Take work ethic. Set aside the ignorant prejudice and, purely for the sake of argument, accept that "the Chinese" work harder than "the South Africans". For this to account for the facts above, this work ethic must have been increasing as fast as wages. If it weren't, the amount of work ethic bought for a rand would be dropping at double digits per year, and exports and unemployment would suffer. In other words, the argument only makes sense if the Chinese today work *four times* harder than the Chinese did ten years ago. If anyone intends to maintain such an absurd claim, one might merely point out that this would require adding a dozen hours to the ordinary human day.

The rebuttal of subsidies is much the same, although it at least has some factual merit as far as *levels* are concerned. The Chinese government provides greater subsidies than our own, or most others. But the argument breaks down on *trends.*

Subsidies can only account for the facts above if they are growing as fast as wages. Neither data nor observation provides evidence of such growth. Free land was available ten years ago, and is no more available today. Capital was cheap, and is no cheaper. Tax rates have been stable, with some rotation among industries. Indeed, once its range of levies and compulsory social security payments are taken into account, China is said by some to have a tax burden second only to France. Electricity and water prices have changed. They have increased rapidly. Ten years ago, the average price of power across China was roughly R0.30 per kWh. Today it is approaching R1.25.

So we must seek causes among those aspects of the Chinese economy that have been changing at roughly the same pace as wages, and which would work to maintain employment and exports. Two changes fit the bill: domestic demand and productivity.

The first has exploded across the decade, rising on average by 16 percent per year. Much of that demand has been for investment, particularly in infrastructure and housing, with overall fixed-asset investment rising at over 20 percent per year over the last decade. However, consumption has also grown rapidly, at 14 percent per year. To give a few indicators: retail sales have grown as much as 18 percent per year; auto sales have exploded from 5 million to 23 million cars per year; and Apple now *sells* (not makes) almost as much in China as it does in all of western Europe.

Rapid wage increases have played a large role in this demand boom. The link to rising consumption is obvious, but rising wages have also supported investment. Though housing has recently become a speculative bubble, the boom in its early years was driven by rapidly increasing incomes as well as policies to unlock investment – rather than consumer – credit for low- to middle-income households. For example, many provinces and cities maintain "housing funds" that guarantee and subsidise mortgages for workers who earn too much to qualify for public housing but too little to easily ➤➤

obtain a mortgage themselves. The funds contain strict rules to ensure workers are not preyed upon with excessive loans. At its peak, Shanghai's fund was said to account for 1–2 percentage points of annual GDP growth.

Such a rapid rise in demand would likely have caused rampant inflation were it not for a simultaneous rise in productivity. Over the decade, labour productivity in China grew at around 10 percent per year, peaking above 12 percent. As above, this cannot be explained by "work ethic", since it would require working harder. If anything, hours are dropping. Indeed, Chinese workers must be taking some time to do all that investing, consuming and organising. Two interlinked causes are at work. The first is investment in equipment. That has itself grown at 21 percent per year for ten years. Today's factories in China are unrecognisable from a decade ago. Halls of people manually moving things about have been replaced by great swathes of metal. The trend is not slowing; if anything, it is accelerating. Last year, China became the largest market for production robots in the world, growing by 60 percent per year. (As an aside, then, China also shows that automation is not only inevitable, it need not coincide with rising unemployment, as long as wages and demand rise with it.)

Second, Chinese firms have become continually better managed. Total factor productivity (TFP), which nets out the growth in capital stock to measure how well an economy is organised, has been rising at roughly 4 percent per year. At the top end of the scale, the decade has seen the rise of Chinese firms such as Huawei, Lenovo, Alibaba and Tencent to global prominence in the most demanding of industries. Outside of high-tech, a clutch of lesser known companies are challenging the West, Japan and Korea in high-end machinery. Sunward, a company started in Changsha a mere fifteen years ago, recently won a contract for the drilling machines used for the new subway in Singapore, which is hardly known to compromise on quality.

That word, "quality", might sum up much of the difference between China and the low-cost economies that were supposed to take its jobs. In everything from textiles to printing, firms in Bangladesh, India, or South Africa struggle to match the quality levels and response times of those in China. A printing firm in Shenzhen will have a book in Durban before its competitor in Johannesburg will return a phone call, and will do it with fewer mistakes.

In other words, there are quality thresholds beyond which price competition is irrelevant. When combined with surging productivity, which at the least keeps a lid on prices, this allows Chinese firms to increase wages rapidly while increasing volumes.

Of course, both factors only beg further questions. First, why do Chinese firms invest so much? In part, because of the low cost of capital. But that in itself is a function of inflation staying low. The larger answer is predictability. Chinese firms do not have to fear wild swings in prices with a volatile exchange rate. Conversely, they can expect rapid growth in demand, both investment and consumption. Indeed, that seems their "default" expectation. As evidence, consider the widely used "purchasing manager indices" (PMI), compiled through surveys. In almost all countries, a "neutral" reading on the index indicates no growth in industrial input. In China it indicates growth of almost 10 percent, because Chinese firms consider anything lower a *contraction*.

Chinese firms know what they will pay for their equipment, without fearing that a currency movement between order and delivery will change it, and can count on increasing if not full utilisation of it. Subsidies then turn the obvious into the irresistible.

The sources of management quality are harder to discern. In part it may be the ferocity of competition. In China, not even the giant state-owned enterprises are monopolies (there is always more than one in any sector, and they fight each other). In the private sector, the country is so vast that any manager will know that someone, somewhere, is out for them.

But for that vastness to count, new managers and new firms must be able to emerge from any stratum of society, including workers and the children of workers. Where that is not the case, as in India's highly stratified society, competition is throttled back. In China, assembly-line workers can and do rise within a few years to become production managers. Even if they do not, their children carry no marks, verbal or physical, of their parents' origins.

This requires an absence, or at least an overcoming, of social cleavage. That same overcoming of cleavage then translates into much more effective communication and trust between workers and management. Without such communication and collaboration, the tools of advanced management, such as "lean production" and "total quality management", are next to impossible. Since implementation of those techniques is today a *de facto* pre-requisite for global competitiveness, so too are equity and trust between workers and management.

That introduces a final element, which is the need for continually rising skill levels in the workforce. To that end, China's vocational education system is simple, elegant and – not perfectly, but much better than most – it delivers. In broad strokes, it works as follows: whether started by a local government or a firm, it is extremely hard to start a vocational school. Once licensed, though, the government does not try to set curriculum or force cooperation with firms. Instead, it makes sure that everyone has simple, free access to data about the schools: employment rates, graduation marks and professional certification rates.

It then funds the schools on a strictly per-student basis. If they deliver skills that are not needed, their figures drop, students see that and go elsewhere, and their budgets disappear. The result is a feverish competition among a handful of schools in each city to make their courses

as job-relevant as possible, and to recruit as many trainees as they can. The market does the heavy lifting, but only because the government has intervened strategically to attack the lack of information between workers, schools and firms that scuppers most skills programmes.

IMPLICATIONS FOR SOUTH AFRICA

All of this raises a range of implications for us. First, it is past time to counter business's arguments about a living wage. When employers state, "We cannot afford to raise wages by 15 percent", the counter must be: "The Chinese can afford it, from a higher base than you. Why can't you do it too?" If the response is "work ethic" or "subsidies", then they must be presented with the facts and asked again, "Why can't you match them? Are you simply less competent than Chinese managers?"

At worst, employers will be exposed as arguing in bad faith. At best, the embarrassment may provoke them to investigate and provide what they believe are the real reasons why they have not been able to reclaim any market share from the Chinese.

Likewise, they must be asked their reasons for not investing. If they retreat to "labour uncertainty", the facts about Chinese strikes must be presented; if they say "red tape", China's position 50 places below South Africa in the "Doing Business" rankings must be presented. That is the principal use of comparative facts: to induce policy dialogue to grow up.

Further implications are more difficult. Obviously, we cannot simply replicate Chinese policies, but it would be equally blind to not suggest anything, on the grounds that we are "different". We are: that is why policy requires thought. Different ideas may then result from a common understanding of Chinese solutions, based on differing understandings of our experience and differing diagnoses of why we are not investing and why our management is sub-par.

On investment, one obvious implication is to reduce uncertainty, in particular by taming exchange rate volatility. This is not about levels, but about predictability. Breaking our vicious cycle of portfolio inflows and volatility may not require a Chinese-style currency peg, but, at the least, it implies substantial reserve accumulation in periods of over-valuation.

A second idea could be an aggressive fiscal rebalancing to subsidise investment in equipment. The large, cumbersome national programmes for such incentives simply do not work. We might replace them by a simple rule, whereby, for example, firms that raised wages by 10 percent per year and raised investment to 30 percent of their earnings before interest and tax would receive a much lower tax rate, on the order of 15 percent. This could be funded through much higher consumption taxes on luxuries, especially luxury imports, and replace the failed wage subsidy.

That points to one of our central dilemmas: raising demand without exacerbating our consumer credit problems. So a third idea might be to supplement our top-down housing provision with new financial-market measures to enable low- to middle-income workers to build, renovate and upgrade their own homes. Housing can be the source of bubbles, but in a period of demographic boom it can easily absorb 10 percent or more of the labour force, not to mention catalysing demand for everything from cement and steel to appliances and services.

A fourth implication is to change our approach to skills. At present, employers who seek training for their staff, workers who seek new skills, and new entrants to the labour market all face a dismal choice between public institutions offering out-of-date curricula and fly-by-night private operators. Massive allocations for skills training disappear into sinkholes created by poor flows of information. Information costs little in money, and is the purest of public goods; on the other hand, it is much more managerially demanding, in both public and private sectors.

That leads to the most difficult factor: management quality and within-plant relations. It may be that, alongside a deliberately unskilled workforce, apartheid's most pernicious economic legacy is a managerial class so coddled that it is able to compete only when paying its workers less than a living wage. Likewise, it may be that the mechanisms chosen for black economic empowerment have resulted in the enculturation of new black managers with old habits, rather than a shake-up of management.

If this is the case, it is not clear what might be done. At the least, our firms need to be shaken out of their complacency by fiscal pressure, but even more by a gale wind of domestic competition. One means to do so is clearly to ramp up the Competition Commission. Another might be a much more aggressive scheme of capital grants for the children of low-income parents. A programme that gave every such child, once at 18 and once at 30, a lump sum of around R50 000 to start a firm or seek additional training, could cost as little as 2 percent of GDP.

The idea is also far from radical. In Europe, an identical scheme, with much larger grants, has been advocated by the former economic advisor to the president of the European Commission, a former Europe editor for the *Economist*. Similar policies are used, in various forms, in a range of social democracies. In Sweden, for example, anyone unemployed is entitled to a capital grant to start a business, alongside subsistence allowances to stay alive while doing so.

Many in our middle class may howl at such ideas. Their self-image is that of a persecuted minority, valiantly keeping the country going in spite of government and labour. The facts may have little impact on such entrenched worldviews. But such ideas would seem, if anything, less radical than some alternate routes to economic freedom that are gaining traction among the young.The question, then, is whether or not our middle class is as incapable of enlightened self-interest as it is of competing with the Chinese. NA

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