

# WHY CHINA? ASIA AFTER 1990

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The consumer electronics industry is moving to Asia and the three countries of greatest interest are China, China and China. Many people are under the impression that manufacturing and new product development are moving to China because of low wages and salaries alone. Wages in China are low; however, not the lowest in Asia. The low cost of both artisan and technical labor can be identified as the first reason for the movement of product development and manufacturing to China but not the only reason. Let's look at Asia starting in 1990 with the historic trends in growth of wages and salaries within Asia, concentrating on China and the Pacific Rim countries. The table and graphs below are courtesy of the Japan External Trade Organization.

	1990	1991	1992	1993	1994	1995
Asian NIEs						
Republic of Korea	100.0	107.5	116.6	124.7	132.3	140.8
Taiwan	100.0	106.8	111.8	117.0	119.3	121.0
Hong Kong	100.0	99.9	98.5	100.0	103.0	103.3
Singapore	100.0	105.6	111.6	116.0	122.4	127.9
ASEAN4						
Malaysia	100.0	103.0	108.2	107.6	112.4	118.6
Thailand	100.0	109.7	120.2	126.7	111.5	120.0
Indonesia	100.0	109.5	130.4	121.6	121.2	
Philippines	100.0	98.4	96.7	96.2	101.5	
China	100.0	105.8	115.2	124.9	135.5	140.2

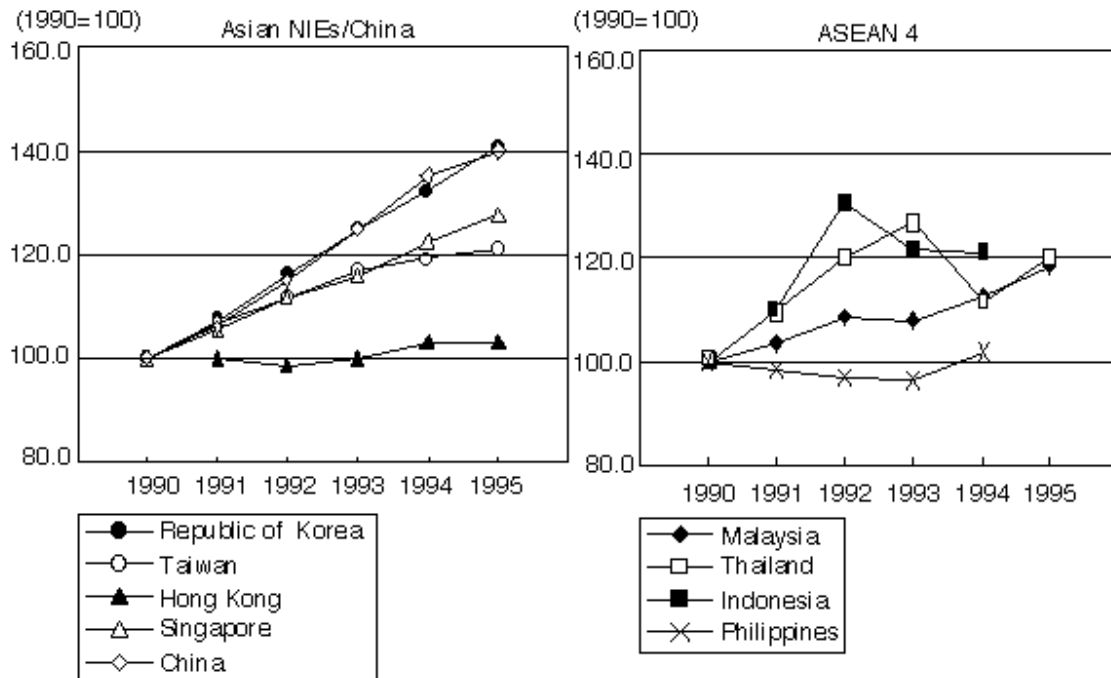


Figure 1.

Southeast Asia was doing well in 1995, foreign investments grew year by year, and exports expanded; however, 'The Asian Crisis' plunged Southeast Asia into political and economic uncertainties in 1997 and real wages declined in all crisis countries. Subsequently, the US recession marked the end of the long boom, and the start of a new

period of slower growth. After the infamous attack on United States on September 11<sup>th</sup> the discovery of terrorist groups in Southeast Asia linked to Al Qaeda brought new worries that will stay with us for many years.

The decline in real wages most affected Viet Nam, Indonesia and the Korean urban sector. Malaysia and Thailand experienced limited declines in real wages. Singapore's rapid economic growth stalled. Almost miraculously China came through the crisis relatively unscathed and real wages actually grew due to the 3% increase in value of the RMB, China's currency. This can be identified as the second reason that China is the frontrunner in the competition for foreign investment within Asia. The economy has demonstrated a robustness that is second to none in Asia.

Let's compare engineers' salaries from the USA and developing countries. With regards to salaries of engineers, the IEEE presented the information contained in table 1 on 18 June 2003 to the US House of Representatives. Table 1 lists salaries of engineers within a sample of developing countries. Audio engineers poled in China felt that the salary estimate was overstated.

Country	Purchasing Power Parity	Annual Salary
United States	1.0	\$70,000
Hungary	0.367	\$25,690
China	0.216	\$15,120
Russia	0.206	\$14,420
India	0.194	\$13,580

*Source - Ron Hira, Columbia University*

**Table 1.**

Let's list the countries in Asia that develop new and/or manufacture products that are marketed in the USA, Western Europe and/or Australia in order of typical wages and salaries.

1. Japan
2. Singapore
3. Taiwan
4. South Korea
5. Malaysia
6. Thailand
7. Philippines
8. Indonesia
- 9. China**
10. India
11. Viet Nam
12. Kampuchea / Laos / Myanmar

After 15 years of tough negotiations, the People's Republic of China has joined the World Trade Organization as its 143<sup>rd</sup> Member. Given the size of its economy and its pace of economic liberalization, China can be a very important player in the WTO. China's per capita income is approximately US\$780.00/year and the economy is growing at around 6.5%. It has a share of around 2% in world trade and had an annual average growth rate of 13% for exports during the 1990s. This has strengthened China's position to permanently maintain a Most-Favored-Nation trading status with the United States.

Let's look at population and economic growth projections by Dr. Hal Hill. GDP is the gross domestic product at market value.

	Popul'n	Popul'n est.	GDP	GDP per cap.	GDP est.	GDP per cap. est.
	1995	2020	1995	1995	2020	2020
	mill.	mill.	AUS\$ bill.	AUS\$	AUS\$ bill.	AUS\$
i	ii	iii	iv	v	vi	vii
Indonesia	198	264	197	970	977	3 737
Malaysia	20	30	82	4 010	444	14 834
Singapore	3	3	84	28 570	214	71 258
Thailand	59	72	165	2 713	756	10 449
Philippines	69	100	73	1 105	400	4 004
Vietnam	74	112	19	219	103	915
S. Korea	45	52	416	9 413	1 345	25 859
Taiwan	21	26	256	12 439	863	33 163
China	1 206	1 488	2 024	506	3 511	2 364
Japan	125	123	4 871	39 200	8 032	65 034
Australia	18	24	347	21 524	737	30 712

**Table 2.**

Sources -

Columns ii-iii. United Nations 1995, *World Population Prospects, 1994 Revision*, (New York: UN): projections based on medium-level rates of annual increase.

Columns iv-vi. Asia-Pacific Economic Group, 1966, *Asia-Pacific Profiles 1996*.

Column vii-viii. Projections by Dr. Hal Hill.

The projections made by Dr. Hall in the late 1990s appear to have significant insight; however, he did not predict the political unrest, fanaticism and/or terrorism in Indonesia, Malaysia, Philippines and recently in southern Thailand. Southeast Asia's economic malaise is aggravated by the uncertainty in the regional political and security

environment, particularly the rise of political Islam and the threat from extremist regional terrorist groups linked to Al Qaeda. This uncertainty saps confidence, and deters investors from committing capital. Southeast Asia has essentially slipped off investors' radar screens.

The bombing in Bali, Indonesia; Dr. Mahathir's controversial speech at the Asia Pacific Economic Conference (APEC) 2003 in Thailand which was attended by President George W. Bush, drew criticism from US, European Union, Australian and Israeli government officials; the kidnappings and hostage taking in both the Philippines and Eastern Malaysia and the recent bombings and skirmishes in southern Thailand have given investors good reason to look for a more politically moderate and stable countries in which to invest. The Islamic nations of Asia face prejudice and anger from the West and Australia and are certainly not the first choice of the Taiwanese, Hong Kong and Singaporean investors with the exception of perhaps parts of Malaysia and Thailand. 25% of the population of Malaysia is of Chinese decent and please remember Malaysia and Singapore were united as Malaya a British colony until 1965. Resultantly, most Malays and Singaporeans speak English quite well. Thailand's Muslim population is concentrated in the southern provinces and there is a significant Chinese cultural influence within the predominantly Buddhist population of Bangkok and the northern provinces but the typical Thai cannot speak English nor Chinese. This has left Thailand with agriculture and tourism based economy. Additionally, Thailand has very high import duties, 30-38%. This increases the cost of doing business in the land the smile but please don't count the Thai's out, Thailand is the 'ONLY' country in Asia to have never been colonized. Thailand is clearly the USA's strongest supporter and ally within Asia. This dates back prior to Thailand's support of the USA during the Vietnam Conflict and has added the perception of stability to the political environment in Bangkok. Pattaya is a favorite deepwater port at the mouth of the Gulf of Thailand for the US Navy and the Marines. Joint maneuvers are regularly scheduled between US Marines and the Thai Military.

Singapore on the other hand has a multi-cultural and multi-religious based population. Since the caning of a US student, Singapore has maintained a reputation for law and order to say the least. To quote from a conversation was a friendly Singaporean gentleman within the Changi International Airport, "Singapore is a fine country. Whatever you do they fine you". This was said in jest; however, the Singapore and Chinese Governments are well known for their authoritarian social policies.

Historians write that independence was thrust upon Singapore. Singapore was forced to change and has developed rapidly. In the last 15 years, the per capita GDP has more than doubled. The proportion of the workforce with more than 10 years of education has doubled (from 17% 15 years ago to 38% today). So has the fraction of managers, professionals or technicians (from 22% 15 years ago to 42% today). 15 years ago Singapore was manufacturing consumer electronics; today Singapore has wafer fabrication plants, pharmaceuticals and petrochemicals facilities. Singapore is no longer a developing country; it is now a source of capital for investment.

Although this topic is somewhat beyond the scope of this article, Singapore is a shining example of what diligence, freedom and capitalism can achieve. Is it no wonder that Asian Americans have the highest per capita income within the USA of any ethnic group, including European, African, Hispanic and Native populations?

This brings us to the third reason why China is the country of choice for new product development and manufacturing. The Taiwanese, the Hong Kong and the Singaporean

investors typically have little or no language and/or cultural barriers to overcome in comparison to their Western counterparts. Additionally, Hong Kong as a result of British colonization has a population that is typically bilingual, Chinese and English. The same can be said for Singapore. Taiwan has long been heavily involved in audio system development and manufacturing. Taiwan was considered to be the 'capital' of the loudspeaker industry for several years. This transition of audio system development and manufacturing to China from Taiwan was a 'natural transition'. However, there are also historically based political tensions between Taiwan and China. This did not seem to deter the Taiwan investors from investing in factories and outsourcing manufacturing jobs to the low wage Chinese workers.

Let's now look at the policies of China's government economic development plan. The Shenzhen region of China has been designated as an export only product development and manufacturing zone. While the Shanghai region of China has been designated as both an export and domestic product development and manufacturing zone. Facilities within these two economic development zones are typically the result of Taiwanese and Hong Kong investors respectively. However, this is typical but it is not cast in stone. There are investors from other countries including the USA. The government will grant a 50 years lease that is renewable to the investor. The Chinese government retains ownership of the land and therefore the building also.

The Chinese at their discretion also offer tax waivers of the 17% tax, the equivalency of the corporate tax, for a three-year startup period and a waiver of 50% of the tax for an additional three-year period, six years with very little taxation. Some companies have been known to start a facility in the Shenzhen region only to close that factory and invest in a new facility within the Shanghai region, if the tax waivers are approved. The Chinese government has also been known to build a facility for the investor and become a quasi-partner. In this case, the Chinese government typically requires 10% of gross sales to be paid to the government and this will cover customs costs. Again, this partnership is at the discretion of the Chinese government.

The results of the Chinese government's diligent economic development plan has been very effective in attracting investors from Taiwan and Hong Kong with regards to the audio industry, as we all well know. This brings us to reason number four as to why China is the country of choice for audio system and system components development and manufacturing. The factories and facilities are in place. There are more than 1000 audio related facilities in each development and perhaps as many as 2000 in the Shenzhen region. This is why India with lower labor costs and good technical skills among the middle and upper class is not fairing anywhere near as well as China. India has not been able to attract investors from Taiwan and Hong Kong. For reasons that were discussed, these investors have chosen China. The facilities are not in place in India and the typical small to middle sized A/V system manufacturing company cannot or will not invest in India at this time. Viet Nam also has lower labor costs; however, the political climate and stability of the government in Viet Nam leaves something to be desired. While again, the facilities are not in place. Only China has the capacity to supply the industry with sufficient product quantity.

In addition to tapping the technical resources of the investor countries, particularly Taiwan, China also has vast deposits of the raw materials needed for many of the A/V system components. China is a huge country and not just in population. China has the natural resources required for high quantity manufacturing of the A/V system's component parts. Additionally, China does not have the environmental restrictions that

are so common in the West. This can be identified as the fifth reason why China is the country of choice for A/V product development and manufacturing.

Finally, due to the reduced product development and manufacturing costs, the larger consumer electronics companies are literally specifying that their OEM or ODM suppliers build their products in China. This is a result of demanding on a product cost target that can only be met by utilizing the Chinese facilities and resources.

India is unlikely to repeat China's explosive take-off. Growth will not be uniform across that diverse sub-continent. But India will have many high growth pockets and sectors, which will present opportunities. India is stirring, although so far not as vigorously and profoundly as China. In the decade since India started liberalizing its economy, it has significantly lowered its high tariffs and trade barriers. India has been growing at 5-7% per year, higher than the "Hindu growth rate" of 3-4% before the reforms. If India continues to liberalize its economy, and achieves the 7-8% growth it aims for, it will create many more opportunities for investors.

See you in China, Phuket to Hong Kong in 2 hours and 40 minutes by air.

That's the Phuket Report,

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