



Florian Butollo

THE END OF CHEAP LABOUR?

*Industrial Transformation and “Social Upgrading”
in China*

campus

The End of Cheap Labour?

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Edited by Klaus Dörre and Stephan Lessenich

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1 Introduction: A leap beyond the global factory model?

During the last decade, Chinese leaders have not been reluctant to point out and criticise the weaknesses of the country's economic development model. Most outspoken about this was China's former premier Wen Jiabao. In 2007, he coined an expression by now known as the "four uns" among China observers when he said that the economy was "unstable, unbalanced, uncoordinated, and unsustainable" (cf. Roach 2009: 229–233). He repeated this critique in almost the same words at a speech at the National Congress in 2012 to underline the urgency of reforms (The Guardian 05.03.2013). In the 12th Five Year Plan, adopted in 2011, the country's structural problems are summed up as follows:

"[I]t is important to have a clear sight of the imbalanced, incompatible and non-sustainable elements within China's development, which mainly turn out to be a tightened constraint between economic growth on one hand and resources and environment on the other, an imbalance between investment and consumption, a relatively large income disparity, uncompetitive technological innovation ability, unreasonable industrial structure, vulnerable agricultural basis, a gap between rural and urban development [...] a significant increase in social conflicts and a still considerable number of institutional obstacles that restrain scientific development" (FYP 2011).

From a European perspective in the year of 2014, such a gloomy assessment appears odd. After all, China's economy has acted as a locomotive of the world economy since the recent crisis whereas the European economy, and with it the project of European economic and political integration, is stuck in grave difficulties that seem endemic.

But China indeed faces mounting contradictions in its recent development model. Unlike it is the case with Europe, these are not the result of sluggish economic growth, but of the very economic success that lets China appear infallible in the eyes of many in the West. The "global factory model" (Ernst 2007), according to which China assumed the role of an assembly platform for consumer goods that were exported to advanced industrial re-

gions, has reached its limits. The economic crisis of 2008/09 graphically demonstrated the risks of an overtly export-oriented growth pattern, and it underlined that high growth rates in the future will barely be sustained through exports of mass consumer goods to Europe and the US alone. And while stagnant growth in the West is putting a strain on China's export performance, domestic consumption up until now has barely generated sufficient demand to act as an alternative source of economic growth. After all, China's success of the last three decades has deepened social inequality which is reflected in a steadily shrinking share of wage incomes as a proportion of GDP and the parallel rise of the GINI co-efficient that measures social inequality (Zhu and Kotz 2011; Guo and N'Diaye 2009). Ecological damages contribute to a rather bleak perspective. They not only compromise the quality of life for hundreds of millions that breathe polluted air, drink contaminated water, and harvest from intoxicated soils, but also turn into an economic risk because of expensive measures that need to be undertaken in order to maintain basic conditions for investment and trade. In short, China is facing a turning point: Chinese political leaders and most international commentators share the view that either there is a reorientation towards a more sustainable and just economic growth pattern based on domestic demand or China's apparently limitless growth engine will lose steam (Eurasia Group 2011; Lardy 2011; World Bank 2012; FYP 2011). The notion that slower growth somehow could turn out to be a desirable alternative is deceptive in the case of China. For if the sources of the country's economic growth run dry, China's historic societal transformation could also get stuck. The result in all likelihood would be growing unemployment, a resurgence of poverty and an escalation of social and political conflict with uncertain outcome. The Chinese leadership therefore is performing the balancing act of achieving the transformation towards a more sustainable growth pattern while avoiding a substantial slowdown of economic growth that could undermine political and social stability.

In response to the contradictions of the current economic growth pattern, the Chinese central government is pursuing the dual target of economic rebalancing and a transformation of China's industrial base. The strategy of rebalancing, a guiding theme in the Eleventh and the Twelfth Five Year Plan, aims at increasing the share of domestic demand in overall economic growth. There are several dimensions to this objective including a rise in the share of wage incomes, the construction of social security systems, and a regional rebalancing between the relatively affluent coastal regions and the poorer regions of the interior. These projects are being pursued with great

fervour, though so far with limited effect in terms of a change in the overall composition of growth.

The second strategy, industrial upgrading, aims at developing innovative capabilities of domestic enterprises in order to enable their emancipation from a subordinate role of low-tech assemblers in global production networks (GPN). By enriching the enterprises' functions, as is the assumption behind this strategy, Chinese entrepreneurs could siphon off higher revenues from advanced manufacturing as well as from design and marketing activities. It is widely agreed that this is the only perspective of escaping the trap of a profit squeeze in manufacturing industries triggered by sluggish export performance, rising prices for the most important factors of production, and the continuous appreciation of the Renminbi (RMB) that is undermining the competitiveness of Chinese exporters of low-end goods (Yu and Zhang 2009; World Bank 2012; HKTDC 2011a). In fact, the desire to overcome low-end production and to reach a higher level of economic development has shaped Chinese industrial policy not only in recent years, but effectively since the beginnings of the reform era in 1978 (Naughton 2007, 349–351). But in the course of mounting economic problems of low-end assemblers and the temporary breakdown of many export-oriented companies with low technological capabilities, such efforts are undertaken with a new urgency. No one expressed this more clearly than the former secretary of Guangdong's Communist Party, Wang Yang, who stressed that the economic crisis of 2008/09 was an opportunity for change and said at the height of the virtual breakdown of much of Guangdong's export industry that it was "time to open the bird cages for new birds to settle down", implying that the economic crisis was an opportunity for a sweeping replacement of low-end industries by more advanced successors (cf. *Businessweek* 15.06.2009).

This study addresses the interrelatedness of both issues, the challenge of rebalancing on the one hand, and the goal of industrial upgrading on the other hand. A transformation of industries that leads them beyond production models based on cheap labour is a precondition for eventually raising the level of domestic consumption and thereby bringing about economic rebalancing. But industrial transformation in itself does not necessarily imply more just patterns of labour relations or income redistribution. In fact, as a growing body of empirical studies in the field of economic sociology has analysed in great detail (Barrientos et al 2010; Bernhardt and Milberg 2011; Bernhardt 2013; Lüthje et al 2013a), much of the literature on industrial upgrading in developing countries proved to be too naïve in assuming such a

direct relationship between industrial transformation and what has come to be known as “social upgrading” of wages and working conditions.

Hence, the principal aim of this study is to analyse recent transformations of industries in China with special regard to the question as to how far the chosen strategies for industrial upgrading lead to improvements for workers in terms of wage levels and working conditions. It approaches this issue by means of case studies from factories in the Pearl River Delta (PRD), China’s main hub for export production and at the same time the site of an unmatched conglomeration of those enterprises that were labelled as “old birds” in Wang Yang’s metaphor. The case studies investigate two industries in this region. The first is the LED lighting sector, a rapidly transforming industry which belongs to the so-called Strategic Emerging Industries (SEI) that are particularly supported by the Chinese authorities. The second is the textile and garment industry, which has a centuries-old history in China and constituted one of the pillars of the country’s recent period of rapid industrialisation from the early 1980s on. By choosing two industrial sectors with remarkably different characteristics, the investigation highlights the diversity of industrial upgrading strategies and their effects. A comparison of differences and parallels of industrial transformation in these industries provides ample insights for a discussion of general development tendencies in the region.

The Pearl River Delta was chosen as the site for the empirical investigation not only because it is presumably the largest industrial area in the world with a particularly long history of low value-added manufacturing for overseas markets, but also because it has emerged as a laboratory for economic and political reform. Nowhere else in China has the economic crisis been felt as intimately, the scale of labour conflict been as high, and the reform programmes of the government been as ambitious as in this region. It is therefore assumed that an in-depth study of economic and social relations in the PRD will offer particularly valuable insights about the future of Chinese industrial and social development.

1.1 Rebalancing, industrial upgrading, and social upgrading in academic literature

By viewing economic rebalancing, industrial upgrading, and social upgrading as combined issues, this investigation pursues an innovative approach

and links debates from different disciplines that have barely been put into dialogue so far. In particular, this study covers new ground by (1) identifying the issue of “social upgrading” as a key issue for economic rebalancing, (2) developing an operable concept for the analysis of social upgrading which can be used for empirical case studies on an enterprise and industry level and (3) delivering rich case studies of two relevant Chinese industrial sectors the upgrading dynamics and labour relations of which have scarcely been investigated to this day.

Ad 1) Social upgrading as key issue for economic rebalancing

In the disciplines of Economy, Economic Sociology and Political Science there is a lively ongoing debate about the contradictions of China’s current growth model and the prospects for its transformation (Zhu and Kotz 2011; Akyüz 2011; Lardy 2011; Breslin 2011; McNally 2013). Academic studies are thereby complemented by analyses from business observers and researchers in international institutions (Eurasia Group 2011; Credit Suisse 2012; World Bank 2012; Ahuja et al 2012). In China, the issue of rebalancing has been the subject of extensive debate and commentary around the release of the 12th Five Year Plan the central theme of which is the transformation of China’s economic growth model (cf. Y.Yu 2009 and 2012; CCCWS 2009; FYP 2011). All of these accounts acknowledge that the sustainability of the Chinese growth model depends on the ability to shift its growth composition from a high share of exports and investment towards household consumption. To a certain extent, they also agree that a rise in wage incomes is a precondition to achieve this task. Yet, none of these accounts discusses the impact of industrial transformation on wage incomes in detail. On the basis of macroeconomic reasoning, there often exists an underlying assumption that industrial transformation is taking place and that this will contribute to a rise in incomes, but there is no attempt to investigate this correlation empirically by looking at changes in remuneration at the enterprise level. While the mentioned macroeconomic analyses are indispensable for monitoring China’s economic imbalances, quantifying recent changes and identifying problems of political reform, the omission of the question how economic change affects labour relations is a serious shortcoming. After all, a rise of wages as a share in national income decisively depends on the question whether the distribution of income within Chinese enterprises takes on

more just forms than has been the case in export-oriented manufacturing industries during the last decades.

Ad 2) Tools for assessing the relationship between industrial upgrading and social upgrading

The neglect of the issue of labour relations is also characteristic for most studies on industrial upgrading in China. Various accounts by Chinese authors and institutions paint an increasingly detailed picture of recent transformations, but usually do not address the impact on labour in their analyses (cf. M.Yu 2011; Qiu 2012; Yu and Zhang 2009; HKTDC 2011a; Schiller 2013). At the same time, there are some studies that deal with the relationship between China's economic growth model and the rise of income inequality in recent years (cf. H.Yu 2009 for the case of Guangdong), yet here again they do not address the character of production models and labour relations on an industry basis. Comprehensive empirical studies that combine an analysis of recent economic changes with the analysis of labour relations are the exception (cf. Lüthje et al 2013b).

These shortcomings mirror the narrow focus on technological changes, which is inherent in theories about industrial upgrading in the discipline of economics (cf. Porter 1985). In the field of economic sociology, the issue of social upgrading, defined in a broad way as “improvements in the rights and entitlements” as well as the “quality of employment” of workers (Barrientos et al 2010, 7), has recently received considerable attention. A broad international network of researchers collaborating under the umbrella of a project entitled “Capturing the Gains” (CTG) is dedicated to investigate how economic¹ and social upgrading “relate, and what strategies can help to combine them” (CTG Website). This project corrects a blind spot

1 The term “economic upgrading” is preferred in the framework of Barrientos et al because it is conceived to provide a broader focus than the term “industrial upgrading”: “in recent years GPNs [Global Production Networks, F.B.] have widened beyond manufacturing to include sectors such as agro-food, and services like call centres, tourism, and business-process outsourcing, where the term ‘industrial upgrading’ is less appropriate. A more generic concept used here is that of economic upgrading which applies across sectors” (Barrientos et al 2010, 6). “Economic upgrading” is defined analogously to “industrial upgrading” as “the process by which economic actors – firms and workers – move from low-value to relatively high-value activities in global production networks” (ibid).

of previous research on industrial upgrading in global value chains which “often implicitly assumed that economic upgrading in GPNs will automatically translate into social upgrading through better wages and working conditions” (Barrientos et al 2010, 7). Under the CTG framework a rich body of literature has already been published, a part of which also addresses the relationship between economic upgrading and social upgrading in China. The available analyses on China, however, are based on a “parsimonious approach” of social upgrading which is methodologically limited to a cross-country comparison of employment and wage figures in different sectors (Bernhardt and Milberg 2011; Bernhardt 2013). While these developments in academic discussion are a suitable point of departure for this investigation, empirical studies need to go beyond the analysis of macro-economic data and must develop a more precise conceptual framework if they are to produce meaningful insights about recent changes within Chinese enterprises and their consequences, as will be discussed in more detail in the chapters 4 and 5. The critical task in this respect is to analyse concrete upgrading strategies that are implemented by enterprises and to assess their impacts on skill requirements, employment patterns and wages. So far, such instruments are missing in analytical frameworks which is why empirical studies either reproduce a bias towards technological changes without thoroughly assessing their impacts on the workforce (cf. Brandt and Thun 2011; Sturgeon and Marakami 2011) or remain limited to swift judgements on the basis of aggregate wage and employment figures which do provide some insights about general development tendencies, but fall short of explaining their profoundness and root causes (cf. Bernhardt and Milberg 2011; Bernhardt 2013; Lee and Gereffi 2013). What is needed therefore is an approach that combines the merits of research on global production networks, which discusses the preconditions for industrial upgrading on enterprise level, on the one hand, and concrete tools developed by industrial sociologists, by which the impact of industrial change on the workforce can be assessed, on the other hand. This study develops such a framework which is used in the analysis of the case studies drawing on important groundwork from, and close dialogue with, a team of researchers at the Institute for Social Research in Frankfurt. Their empirical studies of the “regimes of production” in Chinese key industrial sectors (Lüthje et al 2013b) inspired the development of a set of indicators for the assessment of social upgrading which is introduced in chapter 5.

Ad 3) The analysis of industrial and social upgrading in the LED lighting and textile and garment industries

Thorough analyses of the shape and development of Chinese industries remain scarce, be it in the academic world or beyond. Despite the outstanding performance of Chinese manufacturing sectors in recent years, there is often surprisingly little known about their history, their basic structure, the division of labour between companies, and their dominant models of production. To the author's knowledge, this also largely is valid for the literature by Chinese authors. Often the only available general analyses about Chinese industries are provided by business analysts, sold at high prices and sometimes of doubtful quality (cf. BMI 2009; IBISWorld 2011). Beyond that, anyone who wants to find out more about Chinese industries needs to painstakingly collect information from Chinese and international business media, Chinese industry associations and government sources. When it comes to the question of labour relations, labour scholars and NGOs have published extensively about the conditions in typical mass manufacturing industries geared to export such as the IT and the textile and garment industries. Such analyses and the related advocacy work deserve credit for having raised the awareness on frequent labour rights violations in the supply chain of transnational corporations (TNCs) (A.Chan 2001; C.Chan 2010; Egger et al 2013). Especially the studies on working conditions in the IT industry, most recently on the giant electronics contract manufacturer Foxconn, have shown that low wages and bad working conditions are pervasive in this supposedly modern and advanced high-tech industry (Pun 2005; WEED 2008; Pun et al 2012). They thereby demonstrate that there is no linear relationship between industrial and social upgrading, though without explicating this conclusion at a theoretical level. Notwithstanding their merits, most labour scholars also fail to relate their comprehensive analyses about conditions in Chinese enterprises to an assessment about the wider dynamics in global and regional production networks. The debate often focuses on cases of labour rights violations whereas the impact of the profound industrial transformations on labour relations is insufficiently assessed (cf. H.Yu 2011 for an exception). As labour research and labour activism constitute the background of the author's interest in China, the ambition here is to contribute some insights to close the gap between labour studies and structural analyses of economic change in China.

In concrete terms, both of the industrial sectors under consideration have barely been the object of comprehensive analyses that combine an assessment about recent industry dynamics with the monitoring of labour relations. Recent global developments in the textile and garment industry have received extensive coverage (Fernandez-Stark et al 2011; Lopez-Acevedo and Robertson 2012; Frederick and Gereffi 2011), but so far there are few comprehensive analyses of production networks and labour relations in the Chinese industry with the exception of the already mentioned study by Lüthje et al (2013b, 251–314) and an overview provided by the Hong Kong-based NGO Globalization Monitor (GM 2010). The study presented here adds to this knowledge by delivering additional insights about recent dynamics in China, providing more profound findings about the textile segment and contributing a rich set of case studies about industrial and social upgrading at the level of industrial clusters which constitute an important structural characteristic in this sector. Thereby, the case studies also highlight the relationship between government policies and industrial upgrading on an enterprise basis, which is often neglected in analyses on inter-firm networks (cf. Bair 2005 for a critique).

The dynamic developments in the global LED industry are covered in a broad range of studies from business analysts which constitute an important source for this investigation (JPMorgan 2010; HSBC 2011; McKinsey 2011a and 2012a). Some detailed analyses of the Chinese industry do exist, but are barely accessible because they are sold by commercial market research institutes at prohibitive prices. Some preliminary studies about the industry have also been published by Chinese scholars (Li and Qiu 2010). This study combines a groundbreaking analysis of the Chinese LED industry with the first thorough investigation of industrial upgrading strategies and working conditions based on case studies of enterprises in Guangdong.

1.2 Structure of the presentation and research methods

The general point of departure for this investigation is the assumption of a correlation between China's outward-oriented mode of development and its current macroeconomic imbalances. Because China's economy is strongly shaped by export-oriented industrial sectors that grew based on the comparative advantage of a large pool of cheap labour, there has been a wid-