

## THE INFLUENCE OF LOWER MANUFACTURING COSTS IN SOUTHEAST ASIAN COUNTRIES ON CHINESE MANUFACTURING



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**Abstract:**—The study focused on the scenario that a major part of the Chinese manufacturing industries are gradually using their comparative advantages when it comes to providing low labor cost over the other Southeast Asian countries who offer much lower prices. Statistical analysis on the volumes of investments made by European countries in China and other Southeast Asian countries in the last five (5) years had been done in order to determine its impact on various manufacturing industries of these countries such as clothing, leather, textiles and electronics. Findings revealed that in the recent years, foreign merchants or investors had been gradually shifting their investment to South East Asian countries and based on the merits of low labor costs this creates effects on the plight of the manufacturing industries inside China. This paper then proposes relative counter-measures that will maintain the edge and influence of Chinese manufacturing in the global production of goods.

**Keywords:** Southeast Asian countries; the status of low manufacturing costs; Chinese manufacturing; influence.

## INTRODUCTION :

Manufacturing remains to be the most common factor of economic growth in China considering that its growth had doubled the size of the country's middle class in the last 12 years (Brown, 2013). Such growth is a manifestation of the so called "East Asian Miracles" or the rise of the four tigers rooted from its history (Kwee Hui Kian, 2013) paving then the way from China's transition into a high-tech manufacturing hub (Liu et al, 2012).

The emerging South East Asian countries had become the new hot spots favored by capital investors in the recent years (Sjoholm, 2013) slighting then the spot of China being considered to be the second largest hub of direct foreign investment (Liu, et al 2012). China's comparative advantages is said to be gradually declining and being replaced by South East Asian countries as evidenced by the patterns of exodus by foreign-funded enterprises out of China and into the realm of these emerging South East Asian countries who offers much lower prices of manufacturing cost. At some point, this kind of South East Asian comparative advantage had also driven some China-based companies to relocate to these countries in order to save costs. These scenarios then offers a great interest of study and analysis that will point towards the creation of countermeasures and strategies for the issue of manufacturing industries in China and the impact of the rising comparative advantage of South east Asian countries to it.

At present, countries around the world measures product manufacturing cost by adding-up together the direct material cost, direct labor cost and manufacturing expenses during the course of production. With the exception of Singapore, the difference between the direct material costs and direct manufacturing expenses between China and South East Asian countries when producing or manufacturing goods is minimal. The manufacturing cost mentioned in the research process mainly refers to direct charges which is labor costs. And so, this paper then examines the influence of low labor cost offered by South East Asian countries such as the Philippines, Indonesia, Vietnam, Burma, Thailand and Cambodia in relation to the labor cost in China specifically in the clothing, leather, textile and electronics manufacturing industries and the impact of the decisions of the investors from the European Union, USA and Japan into the manufacturing industries/economy of China. It has to be noted that the government of China considers the electronic industry to be very important and vital to its economy and so, its success would be related to the cluster strategy (Fang and Guo, 2013), while Hussin and Chin (2013) stated that China's spectacular GDP growth must also be attributed to the massive progress of the agricultural and service sector.

### 1 The current situation of labor costs in China and part countries in Southeast Asia

Statistic on the 2013 minimum wage revealed that the monthly minimum wage in China's per capita is between \$150-267 (US dollars) from which Shanghai falls at the \$267 category. Though the minimum wage in South East Asian countries are also considered to be increasing, they are still considered to be lower as compared to China. The average daily minimum wage in the Philippines is only about 6.8 to 10 US dollars or roughly 240 US dollars per month. In Indonesia, the monthly minimum wage is 72-127 US dollars while Vietnam is 80-117 US dollars. Burma's daily minimum wage is 2-4 US dollars or around 48-96 US dollars per month. For Thailand, the daily minimum wage is 5.8-to 7 US dollars or 168 US dollars per month; while the monthly minimum wage of Cambodia is 60-80 US dollars. Taking all these data, it can be concluded that the monthly minimum wage of the Philippines, Indonesia, Vietnam, Burma, Thailand and Cambodia are generally lower than that of China.

As illustrated in figure 1 which is a comparative presentation of the monthly average minimum wages in the capital cities of South East Asian countries, the cities of Ho Chi Minh, Pnom Penh and Naypyitaw offers the lowest cost of labor, while Shanghai is considered to be the highest.

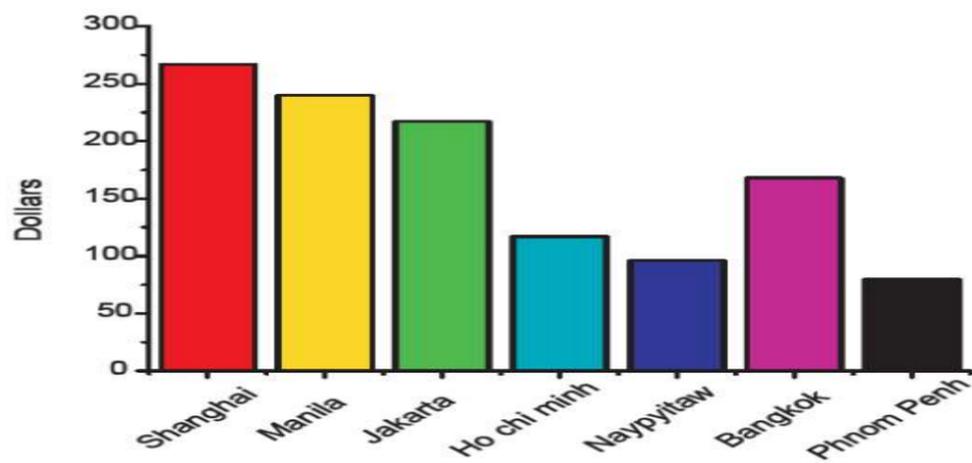


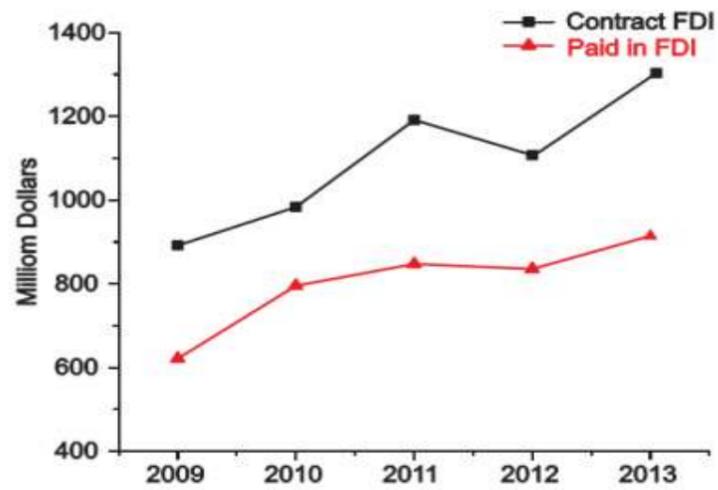
Fig.1 Comparative presentation of the monthly average minimum wage between the selected South East Asian cities and Shanghai, China as of 2013.

**2. Foreign direct investment and low labor cost in South East Asia**

It has been said that China had gained its prominence in the case of inviting in foreign direct investment into its economy in the recent years. But based on the growth or increase of its minimum wage while other South East Asian countries had kept theirs low, such level had been affected with the redirecting of foreign direct investments to countries that offers them much lower labor or manufacturing cost. Labor-intensive industries such as clothing and leather, textile, electronics and other similar industries were not spared from its impact.

**2.1 Clothing and leather manufacturing**

As shown at the trending graph of Japan's foreign direct investment in Indonesia, there had been a continuing increase in terms of contracts for foreign direct investment as well as payment made to the foreign direct investors from 2009 to 2013. To wit, the amount of foreign direct investment to Indonesia made by European Union, USA and Japan for the clothing and leather manufacturing alone had been 892 million, 964 million, 1192 million, 1108 million and 1298 million dollars respectively for from year 2009 to 2013. Payments to FDI had been an astounding 622 million, 796 million, 848 million, 836 million and 915 million dollars for the same bracket years.

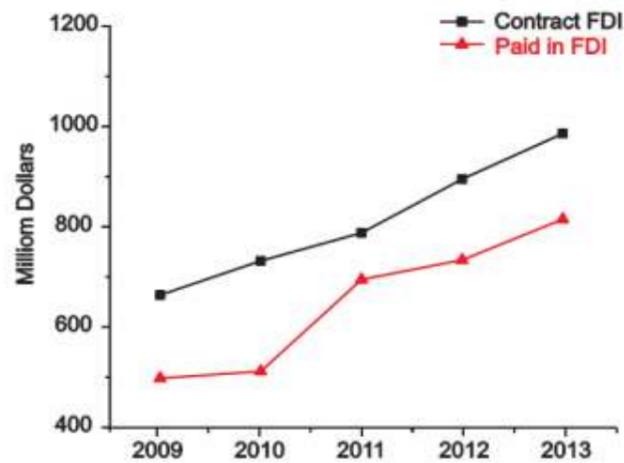


**Fig.2 Characteristics of the clothing and leather manufacturing industry contract FDI and paid in FDI from 2009 to 2013 in Indonesia**

It can be found from the data analysis that the investment volume of European Union, USA and Figure 2. Trends of FDI investment and payment by Japan to Indonesia from 2009-2013

## 2.2 Textile manufacturing

Figure 2 reveals the trends of foreign direct investment made to the textile manufacturing industries of Vietnam by the European Union, USA and Japan. Figures shows that from 2009 to 2013, inclinations for foreign direct investment in this country had been increasing with the following figures: 664 million, 732 million, 788 million, 895 million and 986 million dollars respectively. Payments made for the FDI from these amounts invested had been increasing too with the following proofs from 2009 to 2013: 498 million, 512 million, 659 million, 734 million and 815 million dollars.

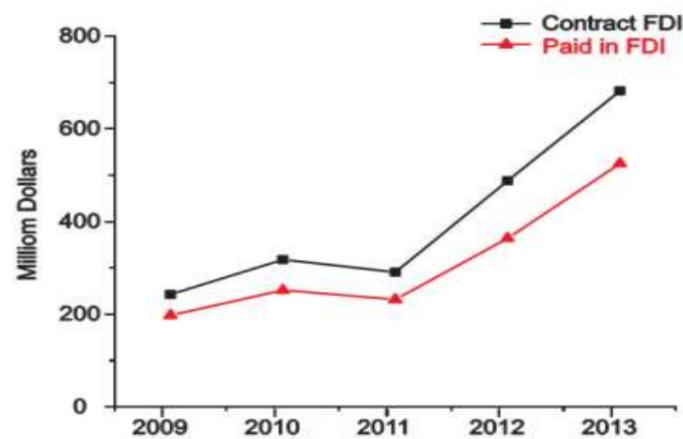


**Fig.3 Trends of foreign direct investment and payment to the textiles manufacturing industry of Vietnam from 2009-2013.**

It can be concluded then that the investment volume of European Union, USA and Japan to the textile manufacturing in Vietnam presents a progressive trend in the last five years.

**2.3 Electronics industry**

With the continuous demand for electronic goods, the electronic manufacturing industry had been enjoying a massive growth and progress in the recent years. The Philippines and Thailand had are two of the South East Asian countries benefitting from these since Japan had shifted to log its foreign direct investment into this countries. To wit, the electronics investments made by the European Union, USA and Japan in Thailand from 2009 to 2013 are as follows: 243 million, 318 million, 291 million, 488 million and 682 million respectively. Payments to FDI from 2009 to 2013 were: 198 million, 252 million, 232 million, 364 million and 525 million dollars. Figure 4 showcases the trends.



**Fig.4 Trends of foreign direct investments and payments to the electronics manufacturing industry in Thailand from 2009-2013**

Based from the data presented on the trends of foreign direct investment in Thailand, it can be attributed then that the trend is unsteadily progressive in the past five years, and that countries in South East Asia are turning to be moving ahead in terms of attracting foreign direct investment into their manufacturing industries specifically electronics, textiles and leather. This is brought about by first: the steadily low labor cost offered by a number of countries in the South East Asian Area with the exception of Singapore. Second is the presence of foreign-direct-investors- friendly policies in the South East Asian zone which in turn reduced or had loosen their tariff policies. Third, there is also the steadiness of its labor-market promising then a steady supply of much needed low-cost labor force. All in all, these kind of perks in the industries of the South East Asia promised the feasibility of an increased profit margin and thus results in the decisions of foreign direct investors to shift gears towards the South east.

**3. Foreign investment's shift to Southeast Asia and its effects on Chinese manufacturing industries.**

**3.1 The garment manufacturing industry**

Figure 5 below illustrates the trend of foreign direct investment by the European Union, USA and Japan in the garment industries of China from 2009-2013. To wit, such amount of investments from 2009-

2013 had been 1278 million, 1166 million, 1125 million, 1096 million and 983 million dollars respectively. Note that such figures draws a downward sloping line. The actual paid FDI were 1052 million, 996 million, 838 million, 709 million and 616 million dollars which also exhibits a downward or decreasing slope.

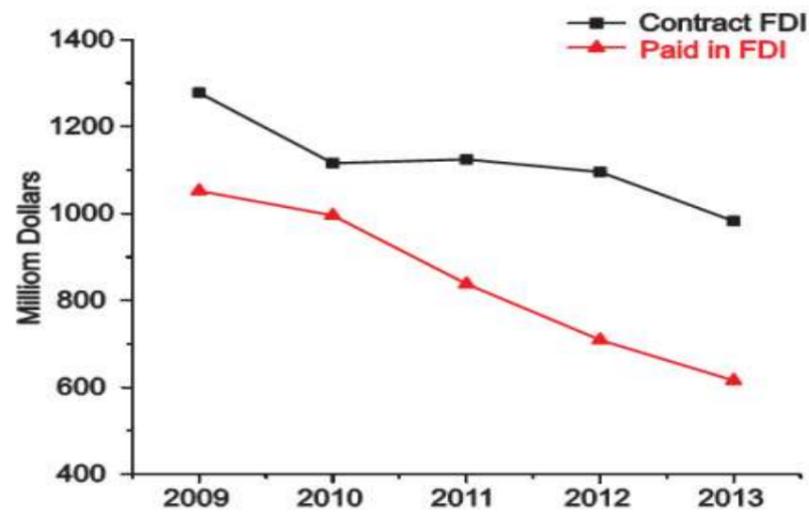
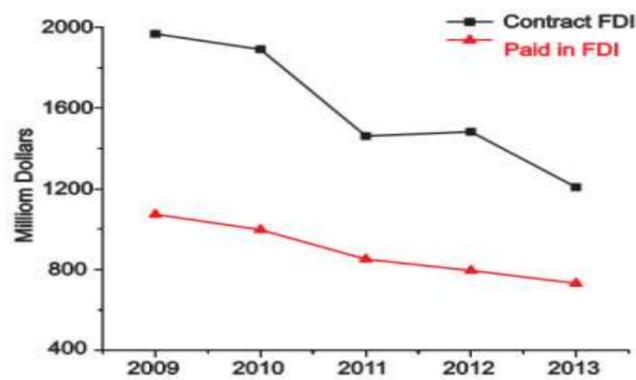


Fig.5 Trend line of the foreign direct investment in the clothing and leather manufacturing industry of China from 2009-2013

Based from the data presented, the investment volume of the European Union, USA and Japan in the clothing and leather manufacturing industries in China had been gradually decreasing in the last five years which can be attributed to the emerging availability of low labor cost in the South East Asian zone.

### 3.2 Textile manufacturing

The trend lines of figure 5 describes the plight of the foreign direct investment in the textile manufacturing industry of China made by the countries of the European Union, USA and Japan from 2009-2013 with the following amount of investment flow in separate years: 1968 million, 1891 million, 1462



From the presentation of the trends, it can be concluded that the investment volume of the European Unions, USA and Japan in the textile manufacturing industries of China had been slowing down or decreasing in the last five years.

### 3.3 Electronics manufacturing industry

The curves of figure 7 presents the nature of the foreign direct investment of the European Union, USA and Japan into the electronics manufacturing industry of China in the last five years with the following figures in separate years from 2009-2013: 878 million, 710 million, 696 million, 608 million and 527 million dollars with payments for FDI in the following amounts also in separate years from 2009-2013: 629 million, 588 million, 493 million, 452 million and 396 million dollars.

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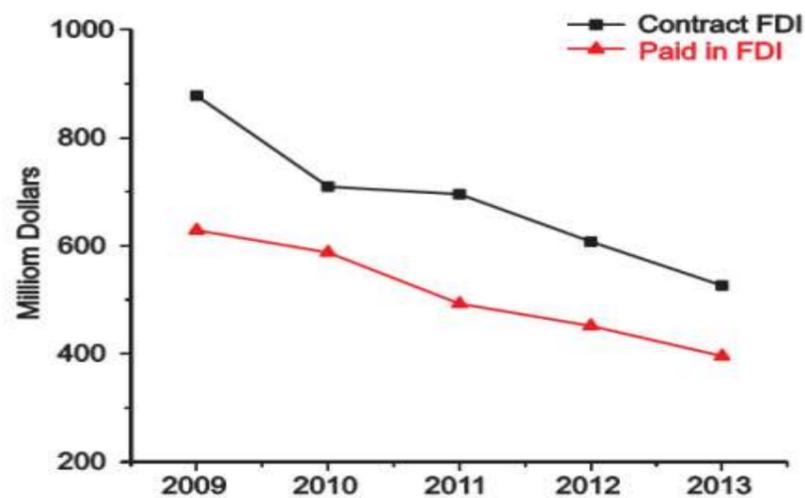


Fig.7 Trend line of the foreign direct investment in the electronics manufacturing in China from 2009-2013

It can be found from the data analysis that the investment volume of European Union, USA and Japan to the electronics manufacturing in China presents a trend of unsteady decrease in the recent five years which is not optimistic.

It can be concluded then that based from the 2009-2013 trend lines, the volume of investments made by the countries of the European Union, USA and Japan into the electronics manufacturing industry of China had been unsteady and downward sloping or decreasing.

The over-all presentation of the various trend lines on the different industries in China that are deemed to be dependent on foreign direct investment speaks of the negative impact of the rising labor cost in China as compared to the steadily low cost and supply of labor in the different countries of the South East Asia. This kind of scenario created an exodus of the various investing countries to China to finally transfer or move their investment to South East Asia with the promise of a much lower manufacturing cost and thus increasing their profit margins. Such scenario creates a very challenging impact to the plight of foreign investment dependent industries in China such as textile and leather, electronics and clothing while countries in the South East Asian zones starts to gain positively. Another concern to be considered too is the decision of some enterprises in the Guangdong province to shift their production workshops to South East Asia.

#### **4 The development tendency of Chinese manufacturing industry in the future and its countermeasures**

##### **4.1 Perfect the mating industry chain for manufacturing industry and actively construct industrial system with characteristics.**

Faced with the challenge of the comparative advantage of the South East Asian countries labor cost, it can be said that there will then be a growing number of enterprises which will decide to move their investment in that part of the world in order to save cost and increase their marginal profits. However, the comparative advantages of the emerging manufacturing industries in China must never be discounted but instead must be strongly re-considered and promoted as their strength and guarantee of a much better option and method of manufacturing. It has to be noted that the Chinese manufacturing industry has its complete mating production chain and system in place for years especially in the coastal areas, where the coordination among industries and supporting facilities within industries are relatively perfect, which cannot be built in some Southeast Asian countries in a short period of time. Thus making the Chinese manufacturing industries better in terms of providing a complete operation of the production and/or manufacturing system for global purposes. One good example is this case in the garment manufacturing which happened after the international financial crisis, when a garment factory in Suzhou, China decided to open a direct sales factory in Vietnam in pursuit of lower labor cost. Such decision were rather been faced with problems that includes the infrastructure construction and availability of the accessories needed to make clothes affecting then the clearance and export process, working schedule and so on. Thus, China must then identify its strength beyond labor-cost when it comes to the entire system of operating a manufacturing industry for offshore clients.

##### **4.2 Promote the optimization and upgrading of industrial structure and actively develop middle and high-end manufacturing**

China may be losing her advantage in low labor cost manufacturing and is being replaced by South East Asian countries, which results into the transfer of the foreign direct investment of the European Union, USA and Japan and also those of some enterprises in China onto the realms of South East Asian countries who owns the comparative advantage of low-labor cost. But Southeast Asian countries mainly absorb low-cost-efficiency-oriented foreign investment. These countries fall behind China in terms of middle and high-end manufacturing infrastructure, and research and development capabilities. The advantage of large-scale production economies in Chinese manufacturing industry wherein a match to the raw material and technology for finished-product conversion affirms its status of being a provider of middle and high-end manufacturing services to the global clientele. And so, China must continuously promote the optimization and upgrading of its industrial infrastructure in order to attract foreign investors and keep track of its competitive alignment as provider of global manufacturing services and technology to offshore clients or investors.

##### **4.3 Increase the productivity of manufacturing, actively cultivate the laborers' Quality**

The low-labor cost in South East Asian countries is undoubtedly attractive and beneficial to offshore investors who are concerned with maximizing their profit by means of lowering their manufacturing cost. It must be noted that the average wages in the South East Asian countries are much lower than China. In the past decade, China has witnessed its average wage increased by 7%-8% year-on-year. Malaysia and Indonesia are similar to China in wages but their bottom labor costs are far lower than that of China. China has the highest labor costs when comparing with other emerging Southeast Asian countries, followed by Malaysia, Thailand, Indonesia, Vietnam and Cambodia. But labor cost only accounts for 5% in the profit and loss statement of corporations while the proportion of labor costs and productivity matters more. But then, it must be noted that labor cost only accounts for about 5% in the profit and loss computation, and it is the proportion of labor cost and productivity that matters most. China's national character of collectivism suffice that Chinese are more suitable in providing high quality manufacturing skills and services than the emerging South East Asian economies. Take the case of Adidas wherein Chinese technical experts were dispatched in Vietnam as instructors to Vietnamese manufacturers and thus guarantee the high-end operations of the Vietnam-based factory. Faced with the challenge of foreign investments being transferred to Southeast Asia, China must further increase the productivity of manufacturing, further cultivate the quality of laborer's output and raise the proportion of labor costs and productivity.

#### **4.4 Speed up the internal transformation of manufacturing and seek breakthrough in promoting product quality**

The transformation of Chinese manufacturing must be given an utmost importance by means of transferring the factories in coastal areas to middle and western areas where labor costs are relatively lower which will eventually reduce costs, expands production scale and improve productivity. On the other hand, robotic technologies maybe introduced that will replace labor in order to improve the levels and quality of productions. By doing such, the Chinese manufacturing industry will definitely keep its competitiveness in large-scale production and manufacturing infrastructure and research and development capabilities

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