

Comparative advantage: The boomerang effect

The Economist

Apr 21, 2012

- Shenzhen (深圳) — China's first **Special Economic Zone** established in early 1980s
- Population now around 12m, including perhaps 6m migration workers
- Foxconn City (富士康), owned by Hon Hai Precision Industry, employing some 230,000 people
- Some of iPhones and iPads are assembled here

Make things more cheaply

- Countries that make things more cheaply than others are often accused of running sweatshops, and labour in China was undoubtedly cheap.
- That was why Hong Kong's clothing and toy factories moved to the mainland.

Labor costs are rising

- However, labor costs have been growing by around 20% a year.
- Some **labour-intensive** businesses are now moving from the coastal regions to inland China, where costs are lower, though the infrastructure may not be up to the mark.
- Some are moving to overseas.

Moves again

- In 2010, Vietnam became Nike's biggest production base worldwide.
- Unless some way of making shoes and clothing without manual labour emerges (which is entirely possible), these businesses will move again in the future.

Low wages less important

- For some manufacturers low wages are becoming less important because labour represents a small part of overall cost of making their products.
- For a 16G iPad (\$499), total labor costs is \$33, of which China's share was just \$8.
- If China accounts for such a small share of the overall labour costs, surely Apple could afford to make iPads in America?

Low wages

- It turns out that low wages are **not** the only attraction.
- It has **a network of firms** with sophisticated **supply chains**, multiple design and engineering skills, intimate knowledge of their production processes and the willingness to leap into action if asked to scale up production.
- What Shenzhen provides, in other words, is a successful industrial cluster.

- Another successful cluster is Silicon Valley—
real innovation in designing the product and creating smart software

Returning to developed countries

- Yet some jobs are returning to developed countries.
- Robots are used to reduce labor costs.
- Having a research and development facility nears production plant allows the company to respond to new trends much faster.
- Protect intellectual property.