

# Is China the Factory of the World?

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**Abstract:** That China is a “factory of the world” is a wide spread belief. This article attempts to present an inside look of China’s manufacturing and exports. It first examines China’s current level of industrialization through looking into its status of manufacturing and share of manufactured goods in exports; then by a survey of foreign investments in terms of scale, profitability, wage levels and taxes, the article discloses the contribution of foreign enterprises to China’s manufacturing, exports and income; and finally, through a study of home appliances industry, the article describes the current status of Chinese national brands in the world. In conclusion, the article reveals China’s true power as a so-called “Factory of the World”.

**Keywords:** Factory of the World, exports, manufacturing, foreign investment, national brands

## Introduction

Every Chinese who goes abroad likes to take home something shopped in the foreign country. But nowadays it’s harder and harder to find any consumer goods not made in China. I find Japan is a very good example. If you go to a 100 yen shop, chances are that over half of the goods carry the label “Made in China”. Not only that. A few months ago I went to Yodobashi Camera, a very big Japanese home appliances chain store, to buy a digital camera, knowing that Japan is a leading manufacturer of consumer electronics. I thought all the famous names like Canon, Fuji, Sony, Ricoh, Panasonic, Casio, Olympus, Nikon and etc were all made in Japan, so that I even didn’t think of checking the place of manufacture for the models I liked. But when a friend of mine reminded me, I did the check and found to my surprise that many of the famous cameras WERE actually made in countries like China, Thailand and so on.

Goods made in China are present at almost all the corners of the world. It is a wonder that in Japanese store, all the garments for sale might be made in China. In America and Europe too, Chinese goods prevail. As described in the magazine Design Week:

In the West, however, we experience the profound effect of the Chinese manufacturing behemoth in every aspect of our lives. Products have never been so cheap, and may never be again, as world politics and fuel costs inevitably take their toll. We can buy kettles, toasters, televisions, virtually everything for the home, at rock bottom prices. The intrinsic value of many products has fallen dramatically - they are now almost disposable. Our approach to purchasing is shaped by what we expect to pay for what used to be high value items. Despite our better ecological intentions, when something breaks we are happy to throw it away and buy a new one, because it is cheaper to do so than have the old one fixed (Design Week, 2006).

In the year 2005, China jumped to the 3rd in foreign trade in the world, only after the US and Germany. It exported US\$762 billion and imported US\$660.12 billion of goods and services, with a total value of foreign trade reaching US\$1,422.12 billion, and a trade surplus of US\$101.88 billion. That year its exports accounted for 7.3%, and imports 6.1% of the world's total (WTO, 2006).

In recent years the total Chinese manufacturing output has jumped to the fourth in the world. Up to the year 2003, industry has reached 46% of the whole national economy, whereby manufacturing has reached 34% of China's GDP. This is higher than the average world level and the levels of developed countries like the US, Japan, the UK, Germany and France (Zhao, 2004).

China is now the biggest manufacturer and exporter of consumer goods, overtaking Japan in the past decade. It is now the world's number one producer of more than 100 consumer goods (Ying, 2005: p. 30). For that reason, China is now described by many countries as the "factory of the world" or "manufacturer for the world".

### **How China got the name**

Chinese media report that the name "factory of the world" was given by Japanese Ministry of Economy, Trade and Industry (METI) in its Year 2001 White Paper. After a search in it, I did not find the exact match of the name except the following description:

China is competitive in a broad range of areas, from the comparatively labor-intensive textiles industry to the comparatively technology-intensive electrical machinery industry, becoming in consequence

increasingly important as a world production center (METI White Paper Year 2001: p.27).

Immediately after the name came into being, it was widely echoed by many countries including the US. But the reaction from China is almost all anger. Chinese people from all walks of life – government officials, scholars and entrepreneurs all alike – strongly oppose the name. Many argue that Japan and the US impose the name to China mainly out of strategic considerations. Japan has always been seeing China as its number one rival in Asia, while the “China threat” stance has always been fervently pronounced in America. Others seek factual evidence to argue that China is just a “workshop”, rather than the “factory of the world”, which view originated from the Boao Forum for Asia (BFA) annual conference 2004 held in Hainan, China (Xinhuanet, 2004).

Whether there are strategic considerations behind the naming, or whether China is a “workshop” or a “factory”, it depends on who you are. If you are a diplomat or a politician, you may well make this a topic for argument. But my concern here has nothing to do with diplomacy or national strategy, nor do I think it meaningful in arguing over which name to use. I would like to take a look inside into China’s manufacturing in a global context and disclose the elements that the Western “factory of the world” notion has neglected or chooses to neglect.

One understandable reason for the title is apparently China’s huge trade surplus. As shown above, China ran a total trade surplus of US\$101.88 billion in 2005. Its surplus with US alone was US\$114.1 billion, and US\$61.1 billion with EU. It ran a trade deficit of US\$16.5 billion with Japan (Ministry of Commerce, 2005).

The trade surplus has caused bad blood from China’s trading partners, who say that China not only takes away their jobs, but jobs in countries exporting to the same markets.

Jobs are going overseas at an increasingly rapid rate, mostly to China. A look at what has occurred in the textile industry alone is instructive. According to the National Council of Textile Organizations, China now controls half of the U.S. apparel market in product areas where quotas have been removed (McManus, 2006).

In the same article (McManus, 2006), William Greider, the national affairs correspondent for the magazine *The Nation* was quoted as saying: “The ‘giant sucking sound’ ... is back, only this time it is not Mexico sucking away American jobs. It is

China sucking away Mexico’s jobs.” Another article (Marquand, 2003) says “shifting from a US-centric view of global economics, it is Latin America, Malaysia, and Thailand that are losing jobs and plants to China.”

Taking a look at the composition of Chinese exports to the US, the EU and Japan in 2005, you are easily convinced of China’s status as “manufacturer for the world”. Table 1 shows that in 2005, manufactures make up 96.3% of China’s exports to the US, 95.8% of that to the EU, and 85.8% of that to Japan.

**Table 1. Merchandise imports of the United States, the European Union (25) and Japan from China by major product, 2005** (Billion dollars and percentage)

	Value	Share in economy's				Annual percentage change			
		total merchandise imports		total imports by product group					
		2000	2005	2000	2005	2000-05	2003	2004	2005
United States									
<b>Total merchandise imports</b>	<b>259.8</b>	<b>100.0</b>	<b>100.0</b>	<b>8.6</b>	<b>15.0</b>	<b>19</b>	<b>22</b>	<b>29</b>	<b>23</b>
Agricultural products	4.2	1.5	1.6	2.3	4.4	21	32	22	21
Food	3.1	1.1	1.2	2.3	4.3	22	33	18	17
Fuels and mining products	2.6	1.3	1.0	0.8	0.8	13	11	93	24
Manufactures	250.1	96.1	96.3	10.7	20.2	19	22	29	23
Chemicals	5.6	1.8	2.2	2.6	4.3	23	26	24	38
Other semi-manufactures	21.6	7.9	8.3	10.1	18.2	21	20	28	24
Machinery and transport equipment	113.4	34.1	43.6	6.5	17.1	25	32	42	26
Office and telecom equipment	80.2	21.0	30.9	10.5	34.4	29	37	47	27
EDP and office equipment	43.3	10.6	16.7	12.1	43.1	31	54	50	18
Telecommunications equipment	35.0	9.6	13.5	14.4	33.1	28	19	43	40
Integrated circuits	1.9	0.7	0.7	1.6	6.9	18	15	53	31
Textiles	6.1	1.8	2.3	12.2	26.9	26	35	27	32
Clothing	21.1	8.3	8.1	13.3	26.4	19	19	20	47
Other manufactures	79.8	41.6	30.7	31.4	41.5	12	14	15	14
Personal and household goods	33.9	16.2	13.1	42.4	56.8	14	15	17	16
Scientific and controlling instruments	2.6	1.0	1.0	4.9	8.5	19	28	31	14
Miscellaneous manufactures	43.2	24.4	16.6	33.2	42.5	10	12	13	12
European Union (25)									
<b>Total merchandise imports</b>	<b>195.8</b>	<b>100.0</b>	<b>100.0</b>	<b>2.7</b>	<b>4.7</b>	<b>23</b>	<b>41</b>	<b>33</b>	<b>24</b>
Agricultural products	4.5	3.6	2.3	1.0	1.1	13	29	21	25
Food	3.1	2.3	1.6	0.8	0.9	14	34	16	25
Fuels and mining products	3.1	1.9	1.6	0.4	0.5	20	43	72	-1
Manufactures	187.6	94.3	95.8	3.3	6.2	24	41	32	24
Chemicals	6.3	3.8	3.2	1.0	1.2	20	37	17	26
Other semi-manufactures	15.5	7.7	7.9	2.6	4.9	24	33	38	30
Machinery and transport equipment	91.3	37.4	46.7	2.5	6.0	29	54	41	19
Office and telecom equipment	61.2	21.2	31.3	4.2	13.8	33	61	41	22
EDP and office equipment	31.6	11.1	16.2	5.0	16.2	33	64	38	21
Telecommunications equipment	26.7	9.2	13.7	5.5	14.8	33	56	44	25
Integrated circuits	2.8	0.9	1.4	0.8	4.1	37	70	52	13
Textiles	4.9	2.8	2.5	3.5	7.5	20	32	29	25
Clothing	23.0	12.4	11.8	10.3	17.9	22	27	22	43

Other manufactures	44.8	29.6	22.9	8.7	12.0	17	31	20	23
Personal and household goods	15.6	8.3	8.0	10.2	16.8	22	34	32	36
Scientific and controlling instruments	2.2	1.0	1.1	1.5	3.0	25	20	29	37
Miscellaneous manufactures	27.1	20.3	13.8	10.6	13.0	14	31	15	16
Japan									
<b>Total merchandise imports</b>	<b>108.4</b>	<b>100.0</b>	<b>100.0</b>	<b>14.5</b>	<b>21.1</b>	<b>14</b>	<b>22</b>	<b>25</b>	<b>15</b>
Agricultural products	8.9	12.8	8.3	11.3	13.6	5	4	19	5
Food	8.0	10.8	7.4	12.3	14.9	6	4	21	7
Fuels and mining products	5.7	5.9	5.2	3.3	3.5	12	33	38	8
Manufactures	93.0	80.5	85.8	20.9	33.7	16	24	25	17
Chemicals	4.2	2.9	3.8	6.1	11.0	21	27	35	39
Other semi-manufactures	6.6	5.1	6.1	18.2	31.4	19	23	29	20
Machinery and transport equipment	40.7	23.6	37.5	12.2	30.7	26	35	32	20
Office and telecom equipment	24.9	11.6	22.9	10.5	37.1	31	39	35	21
EDP and office equipment	14.3	5.5	13.2	11.0	51.5	36	53	30	19
Telecommunications equipment	8.9	5.1	8.2	20.8	49.2	26	22	37	25
Integrated circuits	1.8	1.1	1.6	3.0	8.2	24	25	82	16
Textiles	3.0	3.7	2.8	41.2	52.2	8	13	14	9
Clothing	18.2	26.7	16.8	74.7	80.9	4	13	13	4
Other manufactures	18.6	17.5	17.2	26.1	37.5	14	18	20	19
Personal and household goods	6.9	7.8	6.4	44.1	56.0	10	12	15	13
Scientific and controlling instruments	1.9	0.8	1.8	5.3	14.9	33	66	41	19
Miscellaneous manufactures	9.8	8.9	9.0	26.5	40.1	15	18	19	23

It now seems a hard fact, as every figure points out, that China has become a “factory of the world”. Figures and facts speak and usually go together. However this time in China’s case, they don’t.

### **China’s level of industrialization and strength of manufacturing**

According to a world-wide accepted standard, a country becomes industrialized if it meets all the following conditions:

1. Agricultural value-added accounts for less than 15% of the GDP;
2. Employment in agriculture is reduced to less than 20% of the total; and
3. Urban population rises to 60% of the whole population (Ren and Wang, 2003).

In 2004, agriculture accounted for 15.2% of China’s GDP, employment in agriculture was 46.9% of the national total, and urban population accounted only for 41.76% (China Statistic Year Book, 2005: Chapter 3). These figures are self-evident.

The first country that is considered the “factory of the world” is the Great Britain. Leading the industrialization process, Britain’s manufacturing started to increase in its share in the world from 1.9% in 1760 to as high as 19.9% in 1860. In 1860 Britain produced 53% of the world’s iron and 50% of coal. The second country gaining the title is Japan. From 1950 to 1973, Japan registered annual economic

growth of 7.5%, even surviving the 1973 oil shock. Since then it has been leading the world in many areas. It rivals Switzerland, the US and Germany in watch-making, automobile and optics industries respectively. It is at the cutting edge of many commodities like cameras, motorcycles and electronics. Its ship-building capacity once accounted for half of the world's total. Its industry already amounted to 10% of the world's total in mid-1980s (Wang, 2002).

Let's look at China. In 2002, its manufacturing generated US\$1.27 trillion; though ranking 6th in the world, it's only 11.5% of the US level and 20% of the Japanese level. In comparison, America's manufacturing has already amounted to 20% of the world in the 20th century (Zhuang, 2004).

In contrast with the US and Japan, which lead the world in technology- and capital-intensive goods, China is mainly a producer of labor-intensive or resource-intensive goods. China's manufacturing falls into three major categories: 1) light industrials and textiles, accounting for 30.2%, including foods and beverages, tobacco, apparel, textiles, leather, timber processing, furniture, printing and etc; 2) resource-based processing, accounting for 33%, including petrol-chemicals, chemical fibres, pharmaceuticals, rubber, plastics, ferrous metal and etc; and 3) machinery and electronics, accounting for 35.5%, including machine tools, special-purpose equipment, transportation tools, electronic communications equipment, instruments and etc (Investing in China, 2005).

On the import and export front, a look at the major commodities that China exported and imported in 2006 reveals that the proportion of labor-intensive goods in China's exports is still high. Commodities like "Accessories of garment and dress", "Yarn, fabric and products", "Footwear", "Furniture and parts" and "Travel goods and bags" are among the major items of exports. By contrast, the import list is made up of two kinds of commodities only: one is materials of extreme importance to the economy (oil, plastics, iron ore, steel and copper), and the rest are all technology-intensive commodities. It's not difficult to see that although China exports a whopping amount of goods, no one of them has gained a position that British and Japanese goods did in their time of being "factory of the world".

**Table 2: China's Export Value by Major Commodities, Jan-Oct, 2006** (Unit: US\$10,000)

Commodity	Value
Electromechanical products	43,970,987

Primary electromechanical products	4,484,657
High and new technology products	22,266,766
Accessories of garment and dress	7,777,971
Automatic data processing equipment and components	7,254,786
Yarn, fabric and products	4,014,868
Spare parts for automatic data processing equipment	2,614,525
Wireless telephone, handset or vehicle mounted	2,445,160
Components of TV, radio and telecommunication equipment	2,028,889
Steel	1,967,837
Footwear	1,810,716
Integrate circuit and micro-electronics components	1,711,234
Furniture and parts	1,383,997
Plastic products	1,098,346
TV sets	997,461
Auto parts	722,198
Travel goods and bags	718,308
Game machine	667,448
Video tape recorder and reproducer	620,186
Printing circuitry	615,931
Ship	610,336
Device and parts for circuitry	598,618

Source: Ministry of Commerce, 2006

**Table 3: China's Import Value by Major Commodities, Jan-Oct, 2006** (Unit: US\$10,000)

Commodity	Value
Electromechanical products	34,710,793
High and new technology products	20,043,907
Integrate circuit and micro-electronics components	8,492,510
Crude oil	5,609,034
LCD board	2,607,578
Plastics in primary forms	2,199,163
Iron ore and fine mine	1,697,863
Steel	1,626,670
Components of television, radio and telecommunication equipment	1,608,127
Automatic data processing Equipment and components	1,605,746
Spare parts for automatic data processing equipment	1,442,111
Finished oil	1,359,481
Device and parts for circuitry	1,076,260
Parts of handset wireless telephone	1,022,017
Unwrought coppers and copper products	979,580
Automatic apparatus and instrument for measuring inspecting and analyzing	940,646
Airplane	847,612
Diode and similar semiconductor's parts	813,258
Auto parts	750,443
Printing circuitry	698,569



Source: Ministry of Commerce, 2006

But you may see that there ARE many products with high-tech content on the export list. Yes, China makes and exports a lot of high-tech products like mobile phones and automatic data processing equipment. But observe the ranking of “Integrate circuit and micro-electronics components” on the import list and you will see how these high-tech products are made: they are made with imported chips. This is China’s position in the high-end industries. It has produced 400 million cell phones for the first three quarters this year, but all the chips are imported. It has been making its own cars for 40 years, but no one brand is known abroad (Li, 2006). By contrast, foreign brand cars are flooding the Chinese markets. There is a well-known saying in Chinese that high-tech goods made by China lacks a “Chinese heart”.<sup>1</sup>

In a word, China’s level of industrialization is still low, and its manufacturing is only big but not strong.

### **Foreign contribution to China’s production**

In the mindset of many people, “Made in China” equals “Made by China”. This might be true 30 years ago, when China locked itself away from the rest of the world. But in context of today’s economic globalization, it doesn’t hold true any more, for many goods are made by FOREIGN companies in China but still bear a “Made in China” tag.

With the opening policy initiated in late 1970s, China opened its door to foreign capitals with an aim to boost its economy. In the past 30 years, foreign capital keeps streaming in like crazy. By the end of 2004, 242,284 foreign-funded companies were registered in China. Table 4 shows the value of foreign investments from 1978 to 2004 (China Statistic Yearbook 2005: Chapter 18).

**Table 4. Total amount of foreign capital contracted and actually utilized, 1978~2004** (billion US\$)

Year	Contracted			Actually Utilized		
	FDI	Other	Total	FDI	Other	Total
1979-1984	9.75	1.398	11.148	4.10	1.04	5.15
1985	6.333	0.402	6.735	1.96	0.30	2.25

<sup>1</sup> The Chinese pronunciations of “chip” and “heart” are the same. The expression “Chinese heart” came from a very popular patriotic song “My Chinese heart” by Zhang Mingmin, a Hong Kong singer.

1989	5.6	0.694	6.294	3.39	0.38	3.77
1990	6.596	0.391	6.987	3.49	0.27	3.76
1995	91.282	0.635	91.917	37.52	0.29	37.81
1996	73.276	0.371	73.647	41.73	0.41	42.14
1997	51.003	4.182	55.185	45.26	7.13	52.39
1998	52.102	2.714	54.816	45.46	2.09	47.56
1999	41.223	2.426	43.649	40.32	2.13	42.45
2000	62.38	8.75	71.13	40.72	8.64	49.36
2001	69.195	2.781	71.976	46.88	2.79	49.67
2002	82.768	1.982	84.75	52.74	2.27	55.01
2003	115.069	1.832	116.901	53.51	2.64	56.14
2004	153.479	3.109	156.588	60.63	3.44	64.07

Source: China Statistic Yearbook 2005

According to China's terminology, enterprises with foreign funds fall into three categories: foreign-capital enterprises (completely owned by foreign investors), equity joint ventures and contractual joint ventures. (For sake of convenience, I use "enterprises with foreign funds" or "foreign-funded enterprises" for all three)

Most of them are manufacturing enterprises. From 2001 to 2005, their industrial value-added kept growing at an annual rate of 30%, and has made up one-third of China's total industrial output. On a list of top 500 enterprises with foreign funds published by the Ministry of Commerce (MOFCOM) based on their sales in 2004 and 2005, 405 are manufacturing enterprises, accounting for 81% (Lan, 2006).

At the early stages of China's introduction of foreign investment, enterprises with foreign funds were virtually not allowed to sell their products in the domestic market. Article 3 of the Law of the People's Republic of China on Foreign-Capital Enterprises, taking effect on April 12, 1986, says:

Enterprises with foreign capital shall be established in such a manner as to help the development of China's national economy; they shall use advanced technology and equipment or market all or most of their products outside China.

But as part of its effort for the WTO membership, China revised the law on Oct 31, 2000, and the same article was amended to read:

Foreign-funded enterprises shall be established in such a manner as to help the development of China's national economy. The state encourages the establishment of foreign-funded enterprises that export their products or have advanced technologies.

Despite this, enterprises with foreign funds have taken advantage of the competitiveness of Chinese products in foreign markets to expand their export sales. As a result, their share in China's exports has been on a steady rise. Table 5 shows the export volumes of different sectors from 2001 to 2006 (Jan ~ Oct).

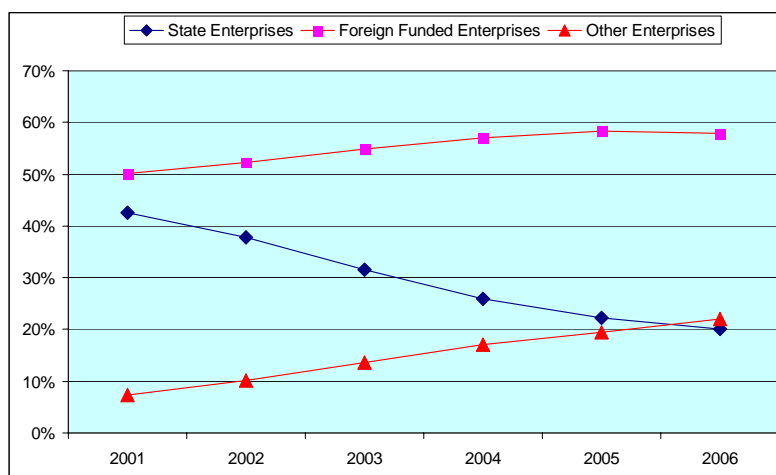
**Table 5. Export sales of different sectors from 2001 to Oct 2006** (billion US\$)

Year	Total	State enterprises	Foreign-funded enterprises	Other enterprises
2001	266.15	113.23	133.24	19.69
2002	325.57	122.86	169.94	32.77
2003	438.37	138.03	240.34	60
2004	593.37	153.59	338.61	101.17
2005	762	168.81	444.21	148.98
2006	779.29	155.82	451.96	171.51

Source: Ministry of Commerce, 2006

Figure 1 shows the percentages converted from Table 5.

**Figure 1. Export sales of different sectors from 2001 to Oct 2006**



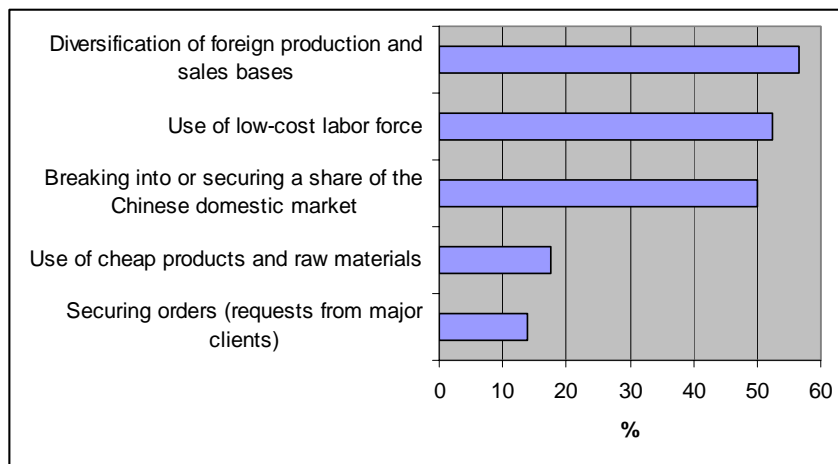
As we can see, in 2005 and 2006, 58% of China's exports are products made by enterprises with foreign funds operating in China. According to Mr Yi Xiaozhun, Deputy Minister of MOFCOM, in the US\$101.88 billion trade surplus of 2005, US\$84.4 billion was contributed by enterprises with foreign funds. Deduct that figure and we have the net surplus made by Chinese enterprises only: US\$17.48 billion! (Liu, 2006)

This can be a big surprise, and is the other side of the "factory of the world" story that Western countries have failed to disclose. You may argue that it's unfair to put all the blame on foreign-funded enterprises. Yes, I agree. As mentioned above,

there are three kinds of enterprises with foreign funds, and two of them involve Chinese capitals. Yet even with this factor adjusted, the contribution of foreign capitals to China’s trade surplus is still huge, but it has never been acknowledged by the “factory of the world” believers.

It can be of more help to have a look at the incentives for foreign capitals to come into China. Figure 2 shows the reasons that Japanese companies enter China:

**Figure 2. Reasons for entering Chinese market**



Source: METI White Paper Year 2001: P. 28

Summarizing their reasons, we see that they enter China because it’s too expensive for them to produce in their own country, and in China they not only can take advantage of the low labor cost and materials cost, but also can grab a share of the huge Chinese domestic market.

The same holds true with all the investors, including Americans. As the McManus article puts:

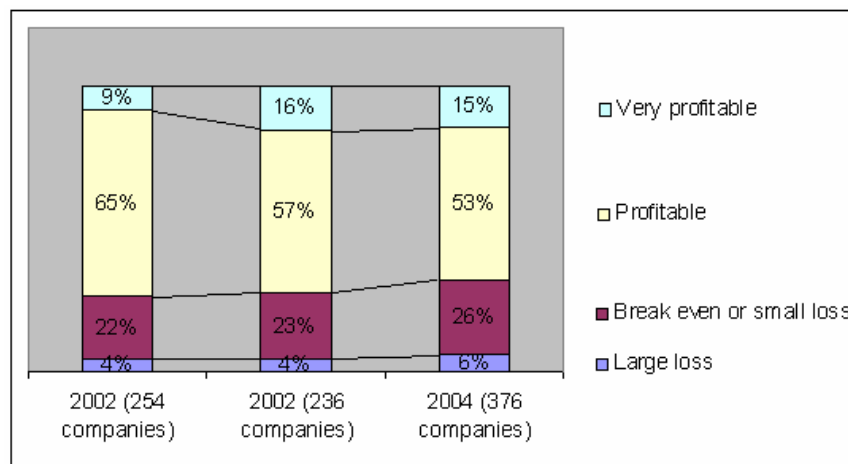
It’s reasonable to wonder how a communist-led nation could become an economic power. The answer is that, by itself, it could never have accomplished what it has done. China has become a significant producer because U.S.-based corporate interests have infused it with money, infrastructure, technology, and business savvy. They have even moved their plants to China (McManus, 2006).

It goes without saying that all the movements of capital are profit-oriented. How much have foreign investors earned? According to a survey conducted by the World Bank among 12,400 foreign-funded enterprises in 120 Chinese cities, the average rate of returns to their investment in China is as high as 22% (Lan, 2006).

The American Chamber of Commerce People’s Republic of China (AmCham China) published a survey in its White Paper 2005. The Business Climate Survey was responded by 450 AmCham companies. “Given China’s economic growth, it is not surprising that 86 percent of respondents reported higher revenues in 2004 over 2003 and 68 percent reported profitable or very profitable performances.” 48 percent of American companies reported their China profit margin bigger than their worldwide margins, while 30% reported the opposite (AmCham, 2005: p.12).

Figure 3 is taken from the AmCham White Paper, which shows American companies’ profitability in China in 2002-2004.

**Figure 3: Profitability of American companies in China, 2002-2004**



Source: AmCham White Paper 2005: p.13

Where do the profits come from? And where do they go?

Apart from the profitability of the nature of business itself and the management efficiency, one can not deny that their profits are partly a result of cheap raw materials and low-cost labor, which form the reasons for foreign enterprises to enter China, as you may recall from above.

While it is difficult to calculate how much they have saved from cheap materials, labor costs are often available in statistics. According to official Chinese figures, the 2004 average total income of Chinese employees in all sectors is RMB16,024 yuan, and in foreign-funded enterprises it is RMB20,440 yuan (China Statistic Year Book, 2005: Chapter 5). Converted into foreign currencies at the exchange rates of that year, 20,440 yuan is roughly US\$2,350, Sterling £1,360 or JP¥292,000. Don’t forget the figure also covers administrative personnel.

As to Chinese manufacturing workers, BBC reports that they are paid 34 pence per hour, only 7% of the British minimum wage (BBC, 2005). The US Bureau of Labor Statistics reports 57 US cents per hour for Chinese workers in comparison with the US\$16.08 US pay level (McManus, 2006). In Shenzhen in 2003, migrant workers made from US\$60 to US\$150 per month (Marquand, 2003). Calculated by the white collar workers' 8 working hours per day and 20 working days per month (although manufacturing workers work far longer everyday and often 7 days a week), that equals 37 to 90 US cents.

Besides low labor costs, foreign-funded enterprises also enjoy tax breaks. Article 5 of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (April 9, 1991) stipulates a tax rate of 33% for foreign-funded enterprises, same with that for Chinese enterprises. But in contradiction with the National Treatment principle, Article 7 and 8 go as follows:

#### Article 7

The income tax on enterprises with foreign investment established in Special Economic Zones, foreign enterprises which have establishments or places in Special Economic Zones engaged in production or business operations, and on enterprises with foreign investment of a production nature in Economic and Technological Development Zones, shall be levied at the reduced rate of **fifteen percent**.

The income tax on enterprises with foreign investment of a production nature established in coastal economic open zones or in the old urban districts of cities where the Special Economic Zones or the Economic and Technological Development Zones are located, shall be levied at the reduced rate of **twenty-four percent**.

#### Article 8

Any enterprise with foreign investment of a production nature scheduled to operate for a period of not less than ten years shall, from the year beginning to make profit, be exempted from income tax in the first and second years and allowed a fifty percent reduction in the third to fifth years.

In fact, the 33% tax rate is only nominal for both Chinese and foreign enterprises. The actual rate for Chinese enterprises is 22%, and that for foreign enterprises is only 11%. Many have complained about the "Supra-National Treatment" granted to foreign firms (People.com, 2006).

From 1999 to 2005, the total Chinese national tax was 13,219.28 billion yuan, and foreign-funded enterprises contributed 445.81 billion yuan, i.e. 3.37% (State Administration of Taxation, 2006). This is very disproportionate in comparison to

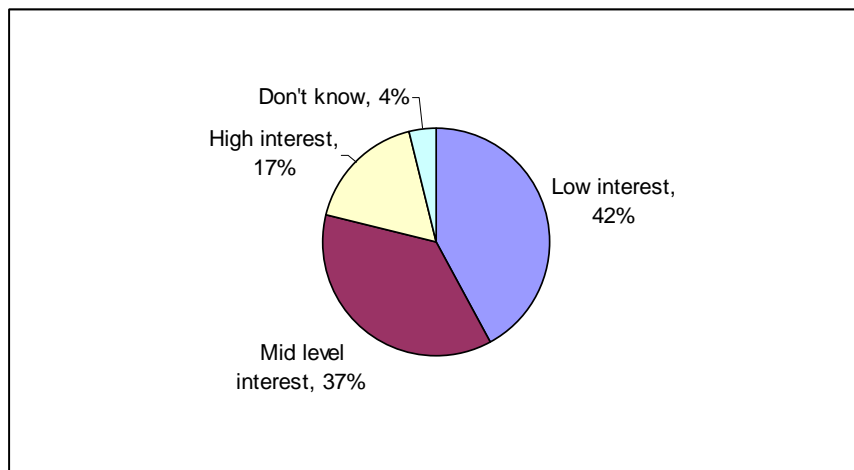
their lion's share in exports value and their share of 1/3 of China's total industrial output. Among the biggest tax-paying enterprises of 2004, the first 10 are all state-owned enterprises. The combined tax contribution of the top 100 foreign-funded enterprises is 62.78 billion yuan, only 2.25 times as big as that of Daqing Oilfield, which paid 27.89 billion yuan alone (Xinhuanet, 2005).

Apart from the low wages paid to Chinese workers and mean tax paid to Chinese government, profits are also distributed to Chinese share-holders in the case of equity joint ventures and contractual joint ventures. In the former case, profits are shared in proportion to the contribution to the registered capital, and in the latter case according to what is agreed in the contract. The above deducted, and all the remainder goes to foreign pockets.

### **Competitive strength of Chinese national brands**

China-made consumer goods wouldn't have been accepted in the West if they did not carry a foreign brand name. While products made by foreign-funded enterprises naturally have foreign brand names, many Chinese home-made products have to do the same in order to sell in the West. This is largely because of the image of poor quality that Chinese brands carry in the eyes of Western consumers. The anti-Communist sentiment is also a consideration. "Most Americans are comfortable buying U.S. brand clothing made in China." (Tucker, 2006: P.13) And "only one in eight respondents from the US and key markets in Europe think highly of the quality of products made in China and Korea" (Baverstock, 2006).

**Figure 4: Level of U.S. interest in Chinese brands**



Source: Tucker, 2006

Take home appliances. Following the approach taken by Japanese and Korean manufacturers in the past, Chinese manufacturers are making products under foreign brand names as OEM manufacturers. For doing so they have to pay high loyal fees. About 90% of Chinese home appliances enterprises have produced for foreign brands on OEM basis. Among them, Galanz (microwave ovens), Midea (air-conditioners), Frestech (refrigerators) and Aucma (refrigerators) are all household names in China, but none of them is known to foreigners.

Galanz takes the OEM lead in China. Its microwave ovens take 70% of the domestic market. And in cooperation with over 240 multi-national corporations, its products bearing different names occupy 50% of the world market in 2005. Yet it succeeds neither in establishing its own brand in the world nor in making profits. In the OEM microwaves market, brand owners take 70~80% of the profits, logistics take 15%, and the OEM manufacturers only take a measly cut of 5~10% (Zheng, 2006).

Despite the accomplishments of Chinese manufacturing firms, “efforts to market uniquely Chinese brands have thus far stalled” (Tucker, 2006: p. 12). So far, there is not a single Chinese brand that is recognized worldwide. Haier – the nation-wide recognized No. 1 national brand – has refused to act as an OEM manufacturer. So far it has the biggest penetration in the world market among Chinese home appliances brands. But its 2002 revenue amounted to only 10% of Sony’s. And the combined profits of all 20 Chinese TV makers are less than that of Sony (Ying, 2005: P. 30).

## **Conclusion**

Now we should be able to see more clearly how the so-called “factory of the world” works. On the one hand, this “factory” is producing lower-end goods that industrialized countries are no longer interested in producing; on the other hand, although goods are statistically made in China, many of them are made by foreigners. So a better interpretation of the “Made in China” label should be that China only provides the venue, opens it to all Chinese and foreign manufacturers, charges them some administration fees and allows their products to carry the “Made in China” tag. But by becoming the “factory of the world”, China imports US\$660.12 billion a year. It’s 6.1% of the world’s total and enough to feed many countries.

With the intensification of globalization, it’s now increasingly difficult to tell who is the actual maker of a product. A product can bear a “Made in ...” label, but its



components and parts may be made in many different countries. So in the context of increasingly globalized world economy, it is hard for any country to become a factory of the world.

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