

Delta: Pressure to upgrade is mounting

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Her company holds more than 20 patents, including a crucial one for the microchip that controls her bears' actions. Hu employs about 20 people to design, research and market her bears, outsourcing production to factories in the region.

"We are 'created in China,' not just 'made in China.' It's a matter of using your brain and not just relying on manual labor," she said.

A list of challenges

Hu is an example of what authorities and businesses are offering to solve the problems facing Guangdong province's Pearl River Delta region. The delta became an engine of China's economic growth over three decades through its low-cost, labor-intensive and export-oriented manufacturing in industries such as textile, toys, electronics and plastics. Industry figures show that, including Hong Kong players, the region's toymakers account for more than 70 percent of global toy production.

Shenzhen, which borders Hong Kong, became a special economic zone following the country's reform and opening-up in the late 1970s. Guangdong's data are impressive: 104 million people; exports that account for more than a quarter of national total trade volume; growth in gross domestic product exceeding 10 percent a year for three decades; \$21 billion in foreign direct investment last year, one-fifth of the total for China.

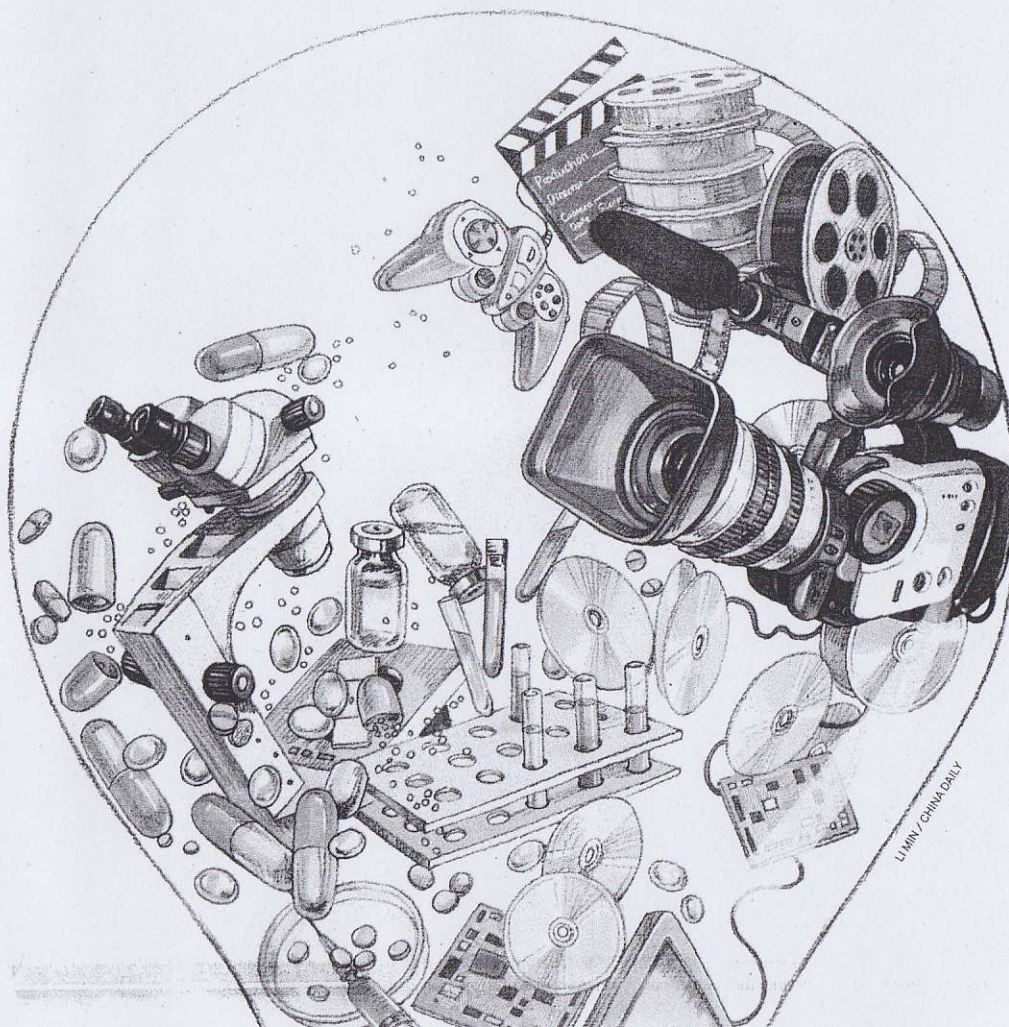
But the factors behind that economic success have also fueled concerns that the Pearl River Delta needs to upgrade to survive the next stage of development.

Industries in the coastal region are facing challenges that include the rising costs of labor and raw materials, a shortage of workers, calls for better worker welfare and benefits, industrial impact on the environment, a shift of focus to domestic consumption to avoid an overdependence on exports and exposure to the vagaries of the global market, and policies

15
percent
annual minimum wage increase set by the central government

1,300
yuan
minimum monthly wage in Guangzhou

70
percent
share of global toy production that comes from the Pearl River Delta



Conshing Group alone hires about 3,000 workers on its 32-hectare site and can produce more than 50,000 pairs of jeans a day. The company reaps about 300 million yuan a year from the domestic market.

But Landy Wu, the human resources and administration manager, said the company is also focusing on worker welfare and the environment as part of efforts to upgrade its business.

"We have increased investment in our water treatment facilities, for example, because of the huge amounts of water we use to wash our jeans," Wu said. "We need to think about how we can keep our business sustainable, beyond short-term economic gains."

Chen Guanghan, an economics professor and delta specialist at Sun Yat-Sen University, said it is inevitable that the delta fully upgrade its industries but it could take about 20 years.

"It took us three decades to get here, so it will also be some time before we can change," he said. "But we should not totally dismantle or abandon the industries that our success is built on. The idea is to improve and innovate from these sectors. Some of the businesses are already doing this in the electronics and even furniture industries."

"The government must be very careful in directing the change. It should just provide the framework and necessary support. It is still best to let the businesses and the market make the changes and the upgrade."

Education, migrants

The delta lacks the centers of learning, like Beijing's Peking and Tsinghua universities and Shanghai's Jiao Tong, that are needed to attract top talent to work in the area, Vettoretti said.

"Most of the jobs for such talent are lacking across many industries here. Most of our members (in the European Chamber of Commerce in China) will say that getting and retaining top talent is one of their most important priorities. If you want to change the spots of your

LI MIN / CHINA DAILY

to move growth from the coast to poorer inland areas.

Analysts and businesses say that many of the delta's economic changes must be considered together with the country's 12th Five-Year Plan (2011-2015), a central economic blueprint that trickles down to the provincial and local levels. What happens in the prosperous province is often also a bellwether for other areas nationwide.

According to the central government's plan, new strategic and high-tech industries should be developed and supported by policies to wean the economy away from previous production models. The focus should also be on developing products and brands with international stature.

To that end, Guangdong's authorities have set specific targets in their own five-year plan. These include increased expenditure on research and development for science and technology, a 36 percent increase in patent filings and expansion of high-tech manufacturing. Industries targeted for growth include information technology, biomedicine, new energy, LED and new materials.

Provincial capital Guangzhou as well as Shenzhen, Zhuhai and Dongguan have also been earmarked to set aside sites for national high-tech industrial bases.

'It will take time'

Alberto Vettoretti, managing partner of the China and Vietnam practice at business advisory Dezan Shira & Associates in Shenzhen, says it won't be easy to move away from the perception of the delta as the hub of low-cost manufacturing.

"It has been doing extremely well in terms of growth and the low-end export economy. But now that the decision has been taken, with the Guangdong government quite clear in saying that it has to 'clean the cage to change the birds', what they want to do is very clear but it will take some time," he said.

As part of the country's five-year plan, central authorities plan to gradually increase the minimum wage by an average of more than 15 percent annually. In Guangzhou, the minimum wage has already been raised to 1,300 yuan a month.

Tony Chen, chairman of Shunde Uyork Furniture Co in Foshan's Shunde district, said, "Wage hikes are definitely a concern for us, together

with higher cost of materials. But that also means we need to find new avenues for growth, particularly in a 'bricks-and-mortar' industry like ours."

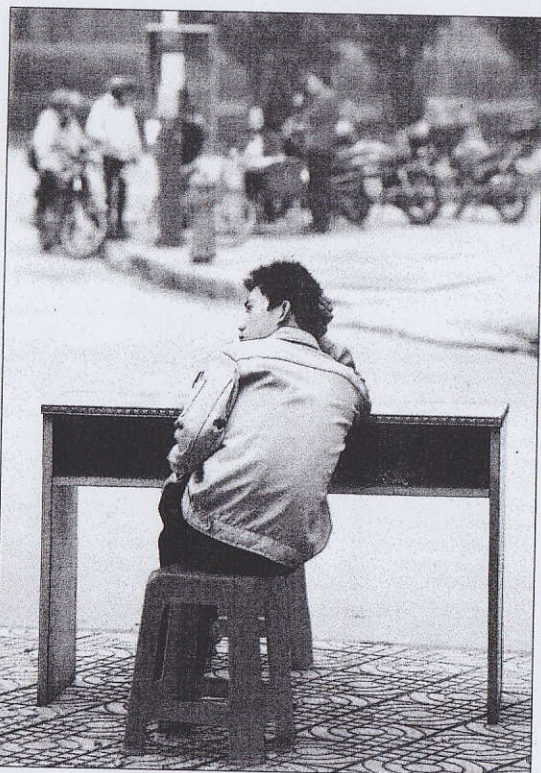
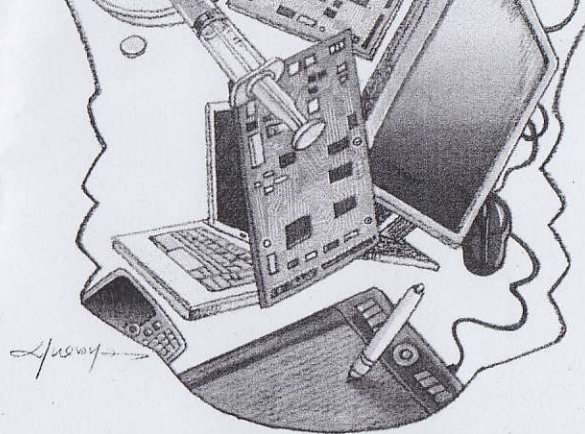
Chen is a major player in Shunde, which has at least 2,000 businesses that help to make Guangdong responsible for one-third of the country's furniture market and half of its furniture exports. Uyork, which Chen started 14 years ago, employs more than 500 workers and rakes in about \$20 million a year.

But the sector slowed in the first half of the year and there could be tough times ahead, he said. To stay on top of the game, he is ramping up ways to promote his brand at home and abroad. These include showrooms linking his brand to "a lifestyle and tapping into Chinese culture, such as the experience of drinking tea in a holistic setting", that go beyond mere tables and chairs.

The investment is also a long-term one that requires government support that balances the need for an open market and level playing field, he said. "That is still the best way to encourage innovation and fuel growth."

Improve, don't abandon

In Zengcheng, a suburb of Guangzhou known for its jeans industry, businesses large and small are also battling rising wages and production costs. More than 3,000 major producers there churn out about 200 million garments annually.



A private factory owner waits to recruit workers in downtown Jiangmen, Guangdong province. Many industries in the Pearl River Delta are having to deal with the rising costs of labor and raw materials.

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HU LANTIAN
TOP EXECUTIVE AT SHENZHEN PP BEAR
INDUSTRY INVESTMENT

"It took us three decades to get here, so it will also be some time before we can change. But we should not totally dismantle or abandon the industries that our success is built on. The idea is to improve and innovate from these sectors. Some of the businesses are already doing this in the electronics and even furniture industries."

CHEN GUANGHAN
AN ECONOMICS PROFESSOR AND DELTA
SPECIALIST AT SUN YAT-SEN UNIVERSITY

those important priorities. If you want to 'change the spots of your skin' and go high-tech, obviously you need top people. Does the Pearl River Delta currently have that? That's a big question mark.

"There are some good universities here and they are also developing joint programs with Hong Kong and Macao, but this is work in progress. For the time being, they are caught in between wanting to be something else and what they have always been."

Chen from Sun Yat-sen University said any development plan for the delta will have to take into account the relations between the migrant population that provides the labor for the region's factories and the resident population that is more well off.

"A small town could have 300,000 workers who have come from other provinces and areas, against a resident population of about 50,000 people," Chen said. "It might not be noticeable in the initial stages, but the differences in lifestyle and access to education or other public services that favor the long-time residents could become more pronounced and that might become problematic."

Changed focus

Nevertheless, many agree that the delta's low-end model is unsustainable in the long run. Factors such as the dependency on exports, environmental degradation, factories moving out to cheaper Asian countries, and rising costs in a fast-urbanizing Guangdong are all indicative of the changing trend, Vettoretti said.

He said the delta will need to invest more in the global market if it wants to upgrade and "to promote all the incentives or new industries and what is available from the government."

Susanne Zhang Pongratz, chief representative of the Austria-based Raiffeisen Bank International's Zhuhai office, said the area still offers many advantages for foreign businesses.

"The Pearl River Delta... was one of the first places to open up to the outside world, and many businesses started here. The region was hit quite badly during the financial crisis because many of its businesses were small enterprises involved in intensive labor with small profit margins. (They) are trying to move away from export-driven financing, to focus on the domestic sector and move up the chain, but these cannot happen overnight."