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Recently I was looking at the mountain of stuffed toys that my two young children have and was comparing this to the lone, high-cost teddy bear I had when I was the same age in the 1960s. The mountain of stuffed, “made in China” toys of today probably, collectively, did not cost as much as that teddy of yore. Who will make the stuffed toys 40 years from now when the Chinese economy evolves into a higher wage economy than it is today?

While the world will not grind to a halt if teddy bears are once again an expensive item and children are reduced to having one or two, what happens at Gap if a pullover is being produced by someone getting paid \$2 an hour instead of 50 cents an hour? How soon will this moment come and will there be an end to the great era of “cheap”?

The two great sources of “cheap” these days are China and India. China is starting to move, however, into the space once occupied by Taiwan and Korea in more sophisticated components. Why then shouldn't China evolve in the same way that they have into relatively high-cost economies that can no longer compete in some of the categories that made them famous?

Bottomless pit

Many economic commentators see China as a bottomless pit of cheap labour. We suspect the factories will have to go to the workers in the near future rather than vice versa. In the longer term, we could see the Chinese economy increasingly following in the footsteps of the other tigers with a scenario in which it could very rapidly convert from being export-oriented into being a mix of exports and domestic consumption, in much the same way as Japan did in the 1960s.

Some would say that the untold peasant masses will provide permanent factory fodder to sew away for the western world. But this flies in the face of the demographic demon China has finally got under control, with the replacement ratio now negative. It also fails to note that no nation has remained so overwhelmingly such a net exporter for all that long. Eventually the established urban masses will gravitate to higher paid jobs (as shown by the current apocryphal tales of urban labour shortages) and then more of the population will be engaged in servicing domestic demand. China could become a more classic service economy with a powerful external sector.

So in the scenario that the Chinese become too busy to worry about making knick-knacks, then is India the next China? It is about the only nation with such an enormous base of population that could be put to work at rock-bottom rates. The Chinese government felt an imperative to develop the economy in such a way as to keep occupied the heaving masses of the hinterland. Does the Indian government show the same type of propensity to have the Keralan fishermen throw away their nets and head to the outer reaches of Mumbai to make clothing? There has been little sign of that.

Finding a replacement

So where is the inexpensive labour to come from to keep the perpetual motion machine of cheaper goods coming the West's way? Sub-Saharan Africa? Central America? There is not enough labour in these places to fill the Chinese gap and they are not cheap enough compared with China. Maybe the nadir of absolute cheapness in production costs for goods with a high manual labour component has been reached in these most recent times.

If China were to move its currency upwards the move would not be small. The shift could be of the order of 20%-30%. Instantly, "cheap" becomes 25% more expensive. This is a scenario in which "cheap" as we have known it could end within a few months of now. In the longer term, the Chinese economy will evolve into a more expensive place that may forsake making many cheap items.

Goods will still be available for a price, but that price will be higher. There will also probably be more diversity of supply. Those countries now fearful of losing their tenuous grip on maquiladora (assembly line) activities for western consumer markets may find

the balance tipped back slightly in their favour. There will be more made in Myanmar, El Salvador and even some made in Mali. Cheap isn't dead yet, but we should not count on it being around forever.

Christopher Ecclestone, Strategist at Hallgarten & Company LLC, New York