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# Impacts of the Financial Crisis on Labour Conditions in China

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*Many academics have said in various occasions that China is not strongly affected by the financial crisis, or some even hold the optimistic view that China could use the financial crisis as an opportunity to expand its power*[1] *or show that state-intervention on economic affairs such as currency value would be, after all, not a bad idea*[2]*. Whether or not their claims are valid, it would take some months, if not years, to be verified. Nevertheless, negative impacts of the financial crisis appeared in the recent months, especially haunting the workers of China. In this article, we are trying to map out the impacts of the crisis, in terms of job losses, labour relations and government's interventions.*

'Factory closure' is a term repeatedly appearing in Chinese newspapers, especially in describing the situation in Pearl River Delta, since October 2008. It seems to be a logical outcome of the financial crisis, to be explained that, as fewer orders coming from the West, on shoes, on toys, on garments and even electronic products. When exports go down, the labour intensive industries would suffer. Yet, if one observes the labour market for a longer time, s/he would notice that 'factory closure' is one of the many impacts of financial crisis. To be more precise, the relation between factory closure and financial crisis is not a matter of cause-and-effect, but a catalyst, an excuse or even a media hype.

The 'credit crunch', as a term for financial market, was first heard in China at the third quarter of 2007 while it came to public attention in August 2007 in the West.[3] For Chinese, at first, it was more a terminology for banking industry, which ordinary people, even some factory owners would be most unlikely to think that they would be subjected to its influence.

The wave of factory closure started in China earlier than the arrival of the term 'credit crunch' in late 2007 and the global financial crisis at the second half of 2008. Back in December 2007, China Central TV (the state-run media) has already broadcast a documentary on "investigation of the closure of thousand factories in Pearl River Delta: rising production costs

1 Chen Zhiwu, professor of Yale University's School of Management, commented that if China could use its foreign currency reserve to invest in foreign resources, e.g minerals in countries which are hit by financial crisis and internal social services, e.g provide better medical care for the lower income groups, then the financial crisis could make China a big winner after all (China Review News, 27 October 2008, http://gb.chinareviewnews.com/doc/1007/8/1/5/100781523.html?coluid=123&kindid=0&docid=100781523&mdate=1027141639).

2 Wu Li, vice-chief of the Institute of Contemporary China Studies of Chinese Academy of Social Science, said: "The Communist Party of China has not predicted the occurrence of financial crisis when it raised the 'Scientific Development Concept'. Yet the Concept has some ideology, which can solve the economic fluctuations, facing by the Chinese economy" (Xinhua Net, 11 December 2008, http://news.xinhuanet.com/politics/2008-12/11/content_10489888.htm).

3 'Credit crisis - how it all began'. In Guardian. In 5 August 2008. Retrieved on 12 December 2008. http://www.guardian.co.uk/business/2008/aug/05/northernrock.banking

leads to factory relocation". By then, Li Peng, General Secretary of Asia Footwear Association already gave some of the shocking statistics. For the 7,000 to 8,000 shoe factories in Guangdong, about 1,000 small-medium size enterprises (SMEs) would be closed by the end of 2007 and the trend would continue[4].

In December 2007, the Federation of Hong Kong Industries predicted that 10,000 to 15,000 of the 60,000-70,000 Hong Kong-owned factories in the delta would close in 2008 and 2009, citing rising labour and materials costs and the currency Yuan[5], instead of financial crisis, as the main cause.[6] Many of the factory owners also described 2007 was the most difficult year for them in the past two decades[7]. China's State Development Planning and Reform Commission also confirmed that 67,000 SMEs shut down in the first six months of 2008 nationwide[8]. The export for toys and garments, for the first nine months of 2008, have growth rates at 3.7% and 1.8% respectively, which are 13.1% and 21.2% lower than the statistics from same time last year[9].

Reasons for factory closure and relocation include labour shortage[10], higher labour costs (in order to keep workers from leaving), electricity control, oil shortage, heavier taxes on the low-technology industries[11], stricter laws to be imposed on labour and environmental standards, order price remains low in USD, despite the rise on RMB, which leads to a narrowing profit

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4 "Concerns on safety, tariffs hurt Chinese shoemakers", in *AFP,* 13 December 2007 (retrieved from Taipeh Times on 9 December 2008, http://www.taipeitimes.com/News/biz/archives/2007/12/13/2003392390).

In another interview, Li commented: "About 50% of the shoemakers that have closed down in Guangdong have moved their factories to China's hinterland, setting up in Hunan and Henan in the center of the country, in Jiangxi in the east, and in Guangxi, which lies between Guangdong and Vietnam. A quarter have moved to other Asian countries such as Vietnam, India and Myanmar, while the remaining 25% have shut up shop but are undecided about their next move." ("Last call for Guangdong shoemakers", in Asia Times, 5 February 2008, http://www.atimes.com/atimes/China_Business/JB05Cb01.html).

5 The Chinese government maintained a peg of 8.27 Yuan per USD from 1997 to 2005. On 21 July 2005, the peg was finally lifted. The Yuan is now moved to a managed floating exchange rate based on market supply and demand with reference to a group of foreign currencies. On 10 April 2008, it traded at 6.9920 Yuan per U.S. dollar, which is the first time in more than a decade that a dollar bought less than seven Yuan. On 15 October 2008, it was traded at 6.83170 Yuan per USD, which is a 21.8% increase and the highest rate since the removal of the peg.

6 "More than 10,000 Hong Kong-owned Factories facing Relocation or Closure", in Yangcheng Evening News, 28 December 2007.

7 Same as above.

8 "Cold Winter of Lay-offs", in China Newsweek*,* 29 October 2008 (http://news.sina.com.cn/c/2008-10-29/120216548971.shtml). However the scale of these 67,000 factories which closed down are not declared, which makes it difficult to judge, how big the impact on China's economy and labour market it would be. According to statistics from State Administration of Industry and Commerce by end of September 2008, China has 9.6 million registered businesses. The numbers for 2006 and 2007 are 9.19 million and 9.63 million respectively (People's Daily*,* 30 October 2008, http://www.gov.cn/jrzg/2008-10/30/content_1135295.htm).

9 "Statistics on Foreign Trade for the First Three Quarters of 2008", in Ministry of Commerce*,* 17 November 2008 (http://zhs.mofcom.gov.cn/aarticle/Nocategory/200811/20081105897283.html).

10 Since 2005, better rural policies and higher inflation rates in cities have kept some migrant workers, who would prefer to stay with their families in the rural areas, not to return to work in the cities. It is reported that "Around 1.7 million migrant workers in the region who took annual leave in January during the Chinese New Year holiday didn't return afterward (to Shenzhen city)" ("China's factories hit an unlikely shortage: labor", in The Christian Science Monitor, 1 May 2006, http://www.csmonitor.com/2006/0501/p01s03-woap.html).

11 When announcing the 11th Five-Year-Plan in late 2006, Guangdong Government has said clearly that "moving to services industries is its priority". In 2007, it started by pushing the low-end industries out of the province, by cutting their tax rebates, such as in textiles and garments. However a new tax rebate was re-introduced in October 2008, when factories close down at a rapider rate than the government expected and wished (cf "China to raise export tax rebates for textile, garment products", in China View, 22 October 2008, http://www.newsgd.com/news/china1/content/2008-10/22/content_4662027.htm).

margin[12].

| Some examples of relocation plans and reasons | | | | |
|---|---|---|---|---|
| **Company** | **Location in China** | **Relocating to** | **Reasons** | **When** |
| Yue Yuen (Taiwanese capital, the biggest shoe producer in the world for brands) | Pearl River Delta | YY moves some of its factories in China to either the northern provinces of Guangdong or expands its investment in Vietnam and Indonesia) | Bigger buyers, such as Adidas, tend to place their orders in YY's factories outside China | A continuous trend over past few years |
| Adidas (German sportswear brand) | 50% of its suppliers are in China | Trend to buy more from SE Asia | Due to rising value of Yuan and labour costs | Over the past years, will continue (same trend for Puma and Nike[13]) |
| Hayidai (Chinese toy producer) | Dongguan city | 90% of workforce to Henan Province. Only R&D remains in Dongguan. | Lower costs in the northern part of China. | April 2008 |
| Avon (US-American cosmetic brand) | Guangdong | Sichuan province | Lower production costs in Sichuan (the plan would continue to proceed, even after the Sichuan earthquake) | June 2008 |
| GST (US-American auto-leather producer) | Guangdong province | Mexico | Low tax rebate in China | Shut down production line for Honda in China and reopens it in Mexico, considering to move more production lines from China to Thailand and Vietnam, reported on 10 November 2008. |
| Olympus (Japanese digital Camera producer) | Shenzhen and Guangzhou (the low-priced products) | Vietnam | Costs in China get higher | By the end of 2008 |
| Hoya Corporation (Japanese camera lens producer) | Guangzhou city | The Philippines | To concentrate its production by combining two factories (one in China and one in the Philippines) into one | March 2009 |

12 See footnote 9.

13 See http://www.sxtvs.com/content/2008-10/25/content_712273.htm

Another reason seldom admitted by factory owners and trade leaders but commonly believed by workers is, that many of the factory closures were attempts to end labour relations before the implementation of Labour Contract Law on 1 January 2008, which makes lay-offs more complicated and expensive. For big companies, such as Wal-Mart China[14] and Huawei Technologies (see Box), which are not closing down, they have been terminating contracts and asking employees to resign before the introduction of the law.

**The Huawei Technologies' example of avoiding the Labour Contract Law**

In late September 2007, Chinese media was reporting that Chinese communications equipment manufacturer Huawei Technologies had internally arranged its more than 7000 of its senior employees, all of whom had reportedly worked for more than eight years in the company, to resign from the company in order to evade China's upcoming Labor Contract Law. One of the employees to resign, according to Huawei, was its own president Ren Zhengfei. They were paid a total of one billion Yuan in compensation but it was unclear how this sum was distributed.

After the senior employees rejoin the company, they will take their previous posts and basic salaries, and the only difference is that their length of service for Huawei is shortened. Because their length of time with the company is shortened, the company doesn't need to contribute as much for their social welfare, pension, and dismissal funds.

The case was then widely reported in China, Huawei put out a statement in China Daily on 6 November 2007, denying its plan to evade the law. It then announced that it had dropped the programme of resignation after some talks with ACFTU. Yet, there was no further comment from Huawei or any mention of what had happened to the workers who had already resigned.

Of course, as a reality, the financial crisis and factory closures do come hand-in-hand (see Diagram on page 5). One of the explanations is that the credit crisis made the banks nervous, which in return cut the credit line, especially for many SMEs by up to 50%[15].

In fact, many enterprises in China invested in more than just one field. Especially when the profit margin has been dropping over the years, as discussed before, they tend to invest in other fields. Therefore, they may go bankruptcy for their other investments due to financial crisis or other reasons. Smart Union, the world's biggest toy producer in Dongguan city which left 6,000 workers jobless in October, was reportedly shut down due to mis-investment and credit reason[16].

No official figures in terms of job-lost and factory closure have been made available (not until next spring), but there are various sources and estimations on the impact on workforce, to offer us a glimpse of the situation:

- Dongguan City's Foreign Investors' Association predicts that by spring 2009, 9,000 factories would shut down in Guangdong province and a loss of 2.7 million jobs[17].

14 “Sackings at Wal-Mart: Global restructuring or avoiding the new Contract Law?”, in IHLO, December 2007, http://www.ihlo.org/LRC/W/101207d.html.

15 “How will China Weather the Financial Storm?”, in Time, 23 October 2008, http://www.time.com/time/business/article/0,8599,1853112,00.html.

16 According to Chinese media, Smart Union intended to change from simply being a processing manufacturer and since June 2007, it invested more than 400 million Yuan in a silver mine in Fujian Province. Yet it turned out to be a poor investment and with a dropping export on toys, Smart Union ran out of cash and therefore had to announce bankruptcy (Sina Finance, 3 December 2008, http://finance.sina.com.cn/review/observe/20081203/22585587182.shtml).

17 “2.7 million job loss by Spring 2009, said the Foreign Investors Association”, in Liberty Times, 11 November

## Interactions between Workers, Enterprises and Government

Compiled by Tony Fung, Worker Rights Consortium, 30 October 2008

### WORKERS

- being laid off without proper compensation

- going back to inner provinces (e.g. Guangzhou train station reported nearly a *130,000* more departures between 11 to 27 October, compared to the same period of last year; in Chongqing (inner province), journalist found *a large number of returnees*, migrant workers are coming back earlier this year.

- Demonstrations on street, complaints, lockout factory to prevent debt owners to go inside and loading assets (many cases reported in Guangdong regarding toys, shoes and other industries)

### ENTERPRISES (manufactures)

**Problems:**

- banks and finance institutes refuse new loan (capital chain broken);

- enterprise bosses mis-invested in the stock market and also “foreign currency leverage tools”, resulting in big losses (cash flow problem)

- lack of new orders or do not have the confidence to take new order – no future income

- exporters refuse to receive/load the products, income cut

**Reactions**

shutdown immediately, massive bankrupts (e.g. HK, Jiangsu), flexible employment (e.g. in Zhongshan), some factories “rent

### GOVERMENT

**Responses to workers**

- prepay back-wages, (Guangdong for example) on factories' behalf

- persuade workers to “calm down”

**Responses to enterprises**

- loan guarantee program, e.g. national gov’t 19 billion CNY ready; local initiates in Guangdong as well as in HK.

- direct financial aid (?)

*ACFTU's attitude*

*Apart from the usual “defending workers’ rights” view, Guangdong trade*

2008 (http://www.libertytimes.com.tw/2008/new/nov/11/today-e2.htm).

- Federation of Hong Kong Industries says that among the 70,000 Hong Kong owned factories in Pearl River Delta, one fifth would shut down by early 2009, causing 2 million jobs lost[18].

- According to Yangcheng Evening News, the population of Dongguan city, an infamous industrial city, would drop from 12 million (as estimated in early 2007) to 6 million, by next spring[19].

- Foxconn, the world's biggest electronics contract manufacturer, plans to lay off 5% globally of its workforce to cut costs. The job cuts could leave about 30,000 Foxconn workers unemployed in China. The company, with its main plant in Shenzhen city, had already cut production, suspended recruitment of new employees and reduced overtime work since October to cut costs[20].

- For Hong Kong, a city famous for its financial infrastructure, its unemployment rate has gone up from 3.4% (July to September 2008) to 3.8% (September to November 2008).[21] It is estimated by mid-2009, the unemployment rate would reach 6%. Major employers in the banking industry, such as HSBC, Standard Charter have announced lay-offs plans.

**Governments' interventions**

With everyday news of factory closures and workers demonstrating on the street for missing wages, China's Poliburo member Li Changchun was sent to Pearl River Delta for a three-day visit in mid-October 2008. It is believed that the Central government would base on Li's observation and come up with solutions. In mid-November 2008, premier Wen Jiabao also visited Guangdong, promising to help investments from both Taiwan and Hong Kong.

- **Beijing**: to avoid unrest and recession after the Olympics, especially in the Beijing area, the city government, as well as the central government tend to provide more protection for enterprises in Beijing (for example, the first provincial / municipal level of re-insurance company, dedicated for providing fast loans for Beijing SMEs was first set up on 16 November 2008 in Beijing. The 1.5 billion Yuan fund was provided by the Beijing city treasury), to avoid massive lay-offs in Beijing. Also, the city government said that Beijing itself is less likely to be affected by the export drop, as most of the industries in Beijing are for domestic consumption and are relatively services / technology-oriented, when compared with the southern provinces.

- **Hong Kong**: traditionally Hong Kong-owned factories are the most vocal group[22]. There-

18 "How will China Weather the Financial Storm?" in Time, 23 October 2008 (http://www.time.com/time/business/article/0,8599,1853112,00.html).

19 "A Painful Turn for Guangdong. Six million population lost in Dongguan", in Yangcheng Evening News, 13 November 2008.

20 "Foxconn plans to lay off 5% of employees", in Shenzhen Daily, 2 December 2008 (http://paper.sznews.com/szdaily/20081202/ca2905922.htm).

21 'Hong Kong Unemployment Rate Climbs to 1-Year High on Recession'. In Bloomberg. 18 December 2008. http://www.bloomberg.com/apps/news?pid=20601080&sid=aPSU03YXv1Mc&refer=asia Traditionally, the summer unemployment rate in HK is higher than the winter one, as more graduates would enter the labour market in summer time.

22 Many of the prominent Hong Kong businessmen are political figures in the region they invested, e.g. as delegates at the National People's Congress of PRC, legislative council members and political party leaders in Hong Kong. Also they consider themselves as the main contributor of China's economic growth as the first group to invest in China.

fore, since the discussion of labour contract law, the trade associations in Hong Kong have been lobbying the national government to down-play the law or pressuring the Hong Kong government to lobby the national government. The ongoing factory closures serve as another reason for them to lobby the Hong Kong / Guangdong government to suspend the labour contract law, which is blamed for causing the closures. The Chief Executive of Hong Kong, Donald Tsang said openly that “Hong Kong enterprises worry that in complying with the Labour Contract Law labour costs will surge, flexibility in managing human resources will be undermined and labour disputes will arise”. He hoped Mainland authorities can introduce relief measures to address the issue[23].
Given that the main cause of factory closures is tightening credit from banks, especially for small/medium enterprises, on 29 October 2008, Premier Wen Jiabao promised that the Central Government would help Hong Kong to survive the financial crisis, by suggesting banks in Hong Kong with Chinese background to make loans easier for SMEs. Other offers include 1) to give more tax-rebate for exporting goods, 2) to help Hong Kong business to open the domestic market.

- **Local governments in Pearl Rive Delta**:
  *Dongguan* city government has launched a one billion Yuan fund, to help companies in troubles. It includes paying wages arrears to workers affected (especially in factory closures, e.g Smart Union workers), reduce tax and factory rental.
  The *Shenzhen* city's labour and social security bureau reported on 21 Oct, that it had paid out from its overdue wages fund for 10 million Yuan and published a list of 30 enterprises which failed to pay their workers. It has published an urgent notice on “stabilizing jobs for migrant works”, requesting the related authorities to give support, “early intervention” for enterprises which would encounter troubles, on 4 November 2008. Many labour activists in Southern China suspect that it also means to loose its implementation of Labour Contract Law. By 25 November, a researcher from the National Development and Reform Commission called at China Daily that “Employees who are at the most disadvantageous position should lower their expectations of income rise in order to keep their rice bowls”[24].

- The **Guangdong Provincial Government**, suddenly getting all the negative spotlights on factory closures, tried to down-play the scale of this challenge. On 17 November 2008, Liu Huanquan, chief of the SME Bureau of Guangdong Province denied the saying of “some 50,000 enterprises are shutting down in Guangdong”. He provided the number that 7,148 enterprises shut down during the first 9 months of 2008. He also said that during the first 9 months, 62,361 enterprises terminated their business licenses but 100,634 were newly registered (one of the reasons was shutting down and reopening as a way to avoid the responsibility imposed by the new Labour Contract Law).
  The Guangdong Provincial Government is trying to ensure the existence of enterprises by launching a fund of 1 billion Yuan, from the provincial treasury, to set up a re-insurance company, to provide accessible loans to SMEs, as Beijing did.
  The Guangdong Government also commented that for those factories which closed down, most of them were merely too 'low-tech' to exist.

- **Ministry of Human Resources and Social Security** issued a notice on 17 November 2008, demanding all possible measures be taken to help struggling domestic enterprises weather the upcoming economic winter and stabilize employment situations. It also made a decision to put a temporary moratorium on the implementation of the long-overdue

23 “Aid for HK enterprises on the Mainland proposed”, in Hong Kong Government News Website, 12 November 2008 (http://news.gov.hk/en/category/businessandfinance/081112/html/081112en03001.htm).

24 “Joint Efforts Needed to Weather Challenge”, in China Daily, 25 November 2008 (http://www.chinadaily.com.cn/opinion/2008-11/25/content_7236860.htm).

minimum wage levels throughout domestic enterprises[25]. This decision had a great impact on workers, overall inflation rate for 2007 was at 4.8% while food price has gone up 12.3% (the 2008 statistics would be made available in early 2009)[26].

- **Shaanxi Labour and Social Security Bureau** has issued an Eight-point notice to prepare itself for the high number of returnees. Preventive measures on monitoring the situation and reporting to the higher level government to ensure stability and creating jobs, for example to raise a fund of 21 million yuan to create jobs in 21 labour-exporting counties[27].

**Trade unions**

On 22 November 2008, the Guangdong Federation of Trade Unions (GFTU) announced that they would be suspending collective wage negotiations. The Vice-chairman of GFTU, Kong Xianghong also 'praised' factories which did not openly lay off workers but forced them to take unpaid leaves as 'humane employers'. Yet it is not clear how many companies will rehire their former workers and if they do, whether they will pay the same wages or rehire them as ‘junior’ workers at a lower wage level[28].

The impacts of the financial crisis, positive or not, have not shown their full faces yet. While official statistics are not yet made available, workers and factories are still on the move, it is yet too early to conclude how it would affect the so-called 'world factory'. In the coming years we are going to see very different developments of China's labour situation. It would not be only sweatshop stories, we would see industries striving for higher technology production, demanding for well-trained workers, governments investing for internal infrastructure and demands, workers struggling to come, stay or leave the industrial cities and more importantly, what happen to those who have decided to stay in the rural areas? Would China's agricultural policies be able to offer them a living? When they are no longer migrant workers, what would be their new identities?

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25 Same as above.

As it shows in the tables at IHLO's research, the minimum wages (which most migrant workers receive) is much lower than the average wages in the city. To make the ends meet, migrant workers who has the minimum wages as their basic wages, would have to work extreme long hours to earn the over-time wages. Very often their overtime hours is higher than the legal maximum. See the tables at **“**‘Average’ wage versus ‘minimum’ wages in selected cities in China”, in IHLO, October 2008 (http://www.ihlo.org/LRC/WC/071008b.html).

26 “Statistics release for 2007”, in National Bureau of Statistics of China, 28 February 2008 (http://www.stats.gov.cn/was40/gjtjj_detail.jsp?channelid=4362&record=17).

27 “Eight Measures to Actively Deal with the Wave of Returnees”, in Shaanxi Daily, 27 November 2008 (http://big5.gov.cn/gate/big5/www.gov.cn/fwxx/sh/2008-11/27/content_1161513.htm).

28 **“**Guangdong Provincial Trade Union suspends collective wage negotiations”, in *IHLO,* November 2008 (http://www.ihlo.org/LRC/W/271108.html).