

# China's Labor Unrest and Implications for Foreign Business in China

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## EXECUTIVE SUMMARY

- Last May's high-profile labor disputes at China-based manufacturing plants disrupted supply chains and shut down production lines. Although the long-term effects of the work stoppages are still emerging, these incidents demonstrate new trends in China's media and labor environments which will impact the overall business climate in Mainland China.
- The increased latitude given to domestic media to report on labor issues suggests a reactive but calculated political move to exert increased pressure on international companies. The Chinese government, emboldened by the nation's rebound from the global financial crisis, sees worker unrest directed at foreign companies as a far more palatable alternative to striking workers at domestic or state-owned companies.
- All-China Federation of Trade Unions (ACFTU)-affiliated unions are the only legal unions in China. Still, many workers see the ACFTU as ineffectual within their organizations or as too imbedded within the government to properly represent workers' interests.
- While the ACFTU still lacks legal authority to force collective bargaining at enterprises, it will likely remain one of ACFTU's clarion calls in coming months and years. However, the ACFTU's mission to support workers does not imply a role as an enabler to striking laborers.
- Against the backdrop of a government emphasis on promoting indigenous innovation and encouraging investment in China's less-developed interior regions, allowing specific types of labor mobilization neatly matches the government's ambitions to move Chinese workers up the value chain.
- By western standards Chinese labor is still incredibly cheap. Nonetheless, steadily rising wages will push companies to adopt alternative strategies like factory relocation to China's interior or increases in automation. There will be pockets within China where low-cost labor will not be the viable option it once was.
- Foreign companies are likely to face more intense government scrutiny than domestic companies, as well as consistent demands to prove corporate value to China and its workers.
- Companies with labor intensive operations in China, as well as companies that depend on China-based supply chains should develop labor-focused crisis response strategies. Such strategies must account for business operations as they intersect with various internal, media and government stakeholders.

## BACKGROUND

Last May, a series of high-profile labor disputes at China-based manufacturing plants disrupted supply chains and shut down production lines in locations across China. Many work stoppages resulted in substantial wage increases for workers, leading analysts to proclaim the political coming-of-age for China's migrant workers while simultaneously sounding the death knell for cheap labor in China. Given that wage increases have not matched China's GDP growth, discontent among Chinese workers is not surprising. According to a [Xinhua news report](#), personal incomes in China currently account for 36.7 percent of GDP, significantly down from 56.5 percent in 1983. Although the long-term effects of the work stoppages are still emerging, these incidents demonstrate new trends in China's media and labor environments which will impact the overall business climate in Mainland China.

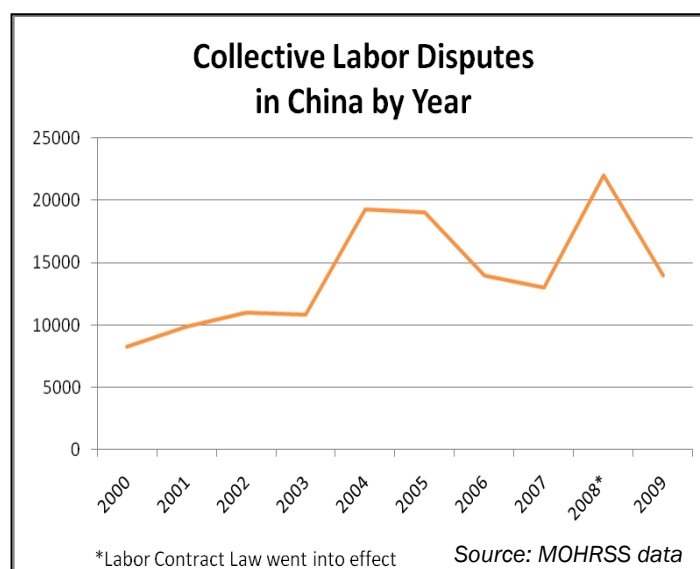
## CHINESE MEDIA RESPONSE TO LABOR UNREST

The uniquely timed occurrence of labor unrest and work stoppages at numerous multinational corporations, including Honda, Toyota and Foxconn, focused the world's attention on emerging labor trends in China. Despite surprisingly strong initial coverage by Chinese media, followed by heavy foreign media attention, it is important to keep in mind that labor disputes in China are not a new phenomenon – thousands are documented every year.

Although such disputes are not new, this recent cycle of unrest may represent something qualitatively different from the past, for the following three reasons:

- (1) Changing demographics of the work force: There are fewer workers aged 15-24, but the number of factories continues to grow. At the same time, the household registration system ("hukou") restricts labor mobility.
- (2) Changing social background of the work force: Younger workers are better educated, more aware of their rights and less likely to return to the countryside.
- (3) Changing political backdrop: The central government was sympathetic to some of the workers' complaints, given its focus on income inequality, desire to stimulate domestic consumption and build a "harmonious society." In addition, with the worst of the financial crisis now in the past, the government has returned to its labor reform agenda.

The high-profile nature of the recent labor unrest is to some extent also the result of increased reporting by the Chinese media. News of Foxconn working conditions was highlighted in reports from undercover *China Daily* and *Southern Weekend* journalists. These reports focused on the rigid schedules, hiring procedures and difficult working conditions for young, mostly rural, migrants. Both series of articles are examples of a



### High-profile labor disputes: June-September 2010

Numerous instances of labor unrest have afflicted foreign and domestic enterprises in 2010. June saw the highest level of strike action in recent months.

- **September 7:** Several hundred workers went on strike at Japanese Brother Industries' Shenzhen plant, complaining of rising workloads and stagnant wages. The strike lasted four days and was resolved when Brother offered workers a monthly wage increase of RMB 100, a workload reduction, and other benefits.
- **August 6:** Around 80 workers (out of a total of 700) went on strike at Panasonic's subsidiary Shanghai factory. The strike lasted only one day, and there was little impact on output, according to Panasonic.
- **July 21:** Workers went on strike at Japanese electronics manufacturer Omron's Guangzhou factory. The strike lasted just one day, after the company agreed to pay workers an additional RMB 300 per month, a raise of approximately 24%.
- **July 12:** Workers at Honda Motor Co.'s affiliated parts maker Atsumitec's Foshan plant went on strike, when management tried to fire 90 workers who demanded higher pay and better working conditions. The strike lasted for ten days, and was resolved when management offered workers a 45% basic wage increase, from RMB 980 to 1,420 per month.
- **June 29:** 3,000 workers at Japanese-owned Tianjin Mitsumi Electric Co, in Tianjin strike.
- **June 22:** Workers at Guangzhou-based Toyota and Honda supplier, Denso Co, Ltd, go on strike.
- **June 17:** Work stoppage at Toyota Tianjin assembly plant.
- **June 10:** 3,000 workers strike at Zhuhai Weichuangli, a large-scale U.S.-invested electronics factory.
- **June 9:** 2000 workers go on strike at Shanghai Tongbao Light & Electricity Co, Ltd. (an affiliate of Taiwanese-owned QiMei), demanding increased wages and back pay. On the same day, workers at Honda Lock, a Sino-Japanese joint venture, strike in Guangdong province. The strike is suspended on June 15 with some concessions and hiring of replacement workers.
- **June 5:** Honda workers at Honda Auto Part Manufacturing Co, in Foshan return to work with 34 percent salary increase after May 17 strike. A second strike on June 7 again halts production.
- **June 3:** 900 workers from two Japanese Brother Industry Co, Ltd, factories in Xi'an strike for wage increase.
- **June 1:** Foxconn institutes 30% pay raise to workers after a series of worker suicides. On June 6, Foxconn increases workers' raises to 66%.

growing, if still somewhat suppressed, trend in investigative reporting in China.

While initial accounts describing the Honda strikes and Foxconn suicides first appeared in Chinese media, journalists' ability to report strike-related news was later curtailed by government censors or media self-censorship. This was most notable following what many perceived as copycat strikes at a Toyota parts supplier. Subsequent strike-related news was heavily censored on well-known Chinese news portals, while previous reports were retracted online. By then, international media had begun to run with the snowballing story.

Anecdotal evidence of numerous strikes at Chinese enterprises abounds on the Internet, but little coverage has made it to mainstream Chinese media. Instead, limited reports have been presented by English-language state media like Xinhua and *China Daily*. The publication of such reports falls under the discretion of the General Administration of Press and Publications (which monitors government line reports) and the Propaganda Department (which monitors the Party line reports). Together they form a propaganda apparatus that regularly issues directives to set the boundaries for acceptable coverage.

#### A shifting domestic media mandate?

It is possible that the Chinese media's early response to labor unrest represents a slow reaction by the government to rein in reporting on this sensitive issue. More likely, the increased latitude enjoyed by domestic media suggests a degree of sympathy for the workers on the part of the government and a calculated political move to exert increased pressure on international companies.

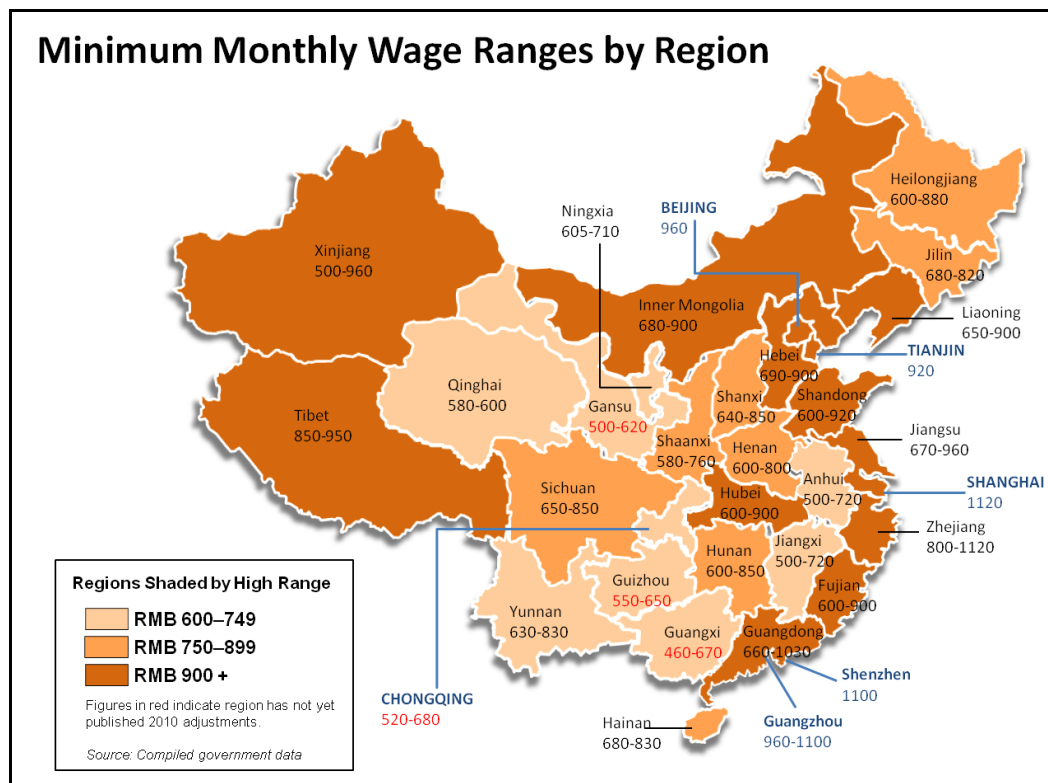
The Chinese government, emboldened by the nation's rebound from the global financial crisis, sees worker unrest directed at foreign companies as a far more palatable and less exigent alternative

to striking workers at domestic or state-owned companies. As a result, the fact that emergency response police forces were deployed to, but not inside, the gates of foreign factories is not an indication of widening press freedoms. Instead it can be seen as tacit acceptance of labor activity at foreign enterprises, particularly those that are Japanese- and Taiwanese-owned.

### CHINESE GOVERNMENT RESPONSE

Despite concerns over social stability, the outcome of the recent labor unrest, chiefly increased wages for workers, is aligned with the long-term objectives of the Chinese government. The Chinese Communist Party (CCP) built its revolutionary movement from ideological support of the peasant, and recent years have seen worker rights surface as a major priority for the government, particularly at foreign enterprises.

The 2008 Labor Contract Law was primarily designed to level the balance of power between employer and employee by significantly raising worker protections under contract. In part due to increased recognition of workers' rights under the Labor Contract Law, officially reported labor disputes in China have dramatically risen in recent years – 280,000 labor complaints made it to Chinese courts in 2008. This has tested the capacity of China's formal channels for legal redress, but also allowed the government to diffuse potential political instability generated by dissatisfied, non-unionized workers.



The strains of the financial crisis in 2008 led the government to temporarily scale back its action on this issue. This included instituting a temporary suppression of minimum wage increases by many local and provincial governments hoping to minimize overhead for already struggling producers.

Now, with an economic rebound seemingly well in hand, the government is actively promoting wage boosts, and at least 27 provinces and municipalities have instituted mandatory increases thus far in 2010, with average increases exceeding 20 percent. Skepticism remains regarding whether mandated minimum wages are implemented in practice, suggesting that the government standards are less important than market factors.

### THE ACFTU'S CALL TO ARMS

The ACFTU, a quasi-Party organ that controls officially sanctioned unions, has seized upon the public relations opportunity created by the strikes at foreign companies to call for better treatment of workers and the establishment of authorized union representation at foreign and private domestic companies.

Claiming nearly 170 million members, the ACFTU is the coordinating body for all 31 provincial-level trade unions, as well as 10 national-level industrial trade unions and two trade unions for employees of state-owned enterprises, Party and government departments. ACFTU-affiliated unions are the only legal unions in China.

China's Trade Union Law, established shortly after the founding of the PRC and revised in 2001, is the legal basis for unions in China. The law compels companies to recognize union representation when petitioned by 25 or more workers. Additional options exist for organizations with few workers, including the right to merge unions with a second organization, or appoint a representative to organize union activities.

### Perceptions of the ACFTU

Still, many workers see the ACFTU as ineffectual within their organizations or as too imbedded within the government to properly represent workers' interests. This was particularly evident when employees called for the formation of an independent union during the highly publicized Honda strike in May and June. Workers recognized that ACFTU's mandate to support President Hu Jintao's calls for stability and a "harmonious society" removed striking as a viable tactic for addressing grievances under ACFTU membership. Ultimately, the Honda strike was significant because employees, by acting independently, voiced their dissatisfaction with their compensation and also with their alternatives for union representation.



Companies in China have also been hesitant to build relationships with local-level ACFTU leadership, preferring to stay under the radar for fear that outreach might be perceived as a show of weakness or draw unwanted attention compelling companies to unionize. Furthermore, companies are required under the Trade Union Law to finance local trade union operations with a monthly contribution equal to 2 percent of its payroll.

Aware of negative perceptions, particularly among workers, ACFTU leadership leveraged the challenges of the 2008 financial crisis to accelerate its public image campaign, urging workers to unionize and condemning foreign companies forced to lay off workers or adjust scheduling. This initiative ongoing, ACFTU and the Ministry of Human Resources and Social Security (MOHRSS) announced the “Rainbow Plan” (彩虹计划) in May. The plan calls for progressive increases in collective bargaining power through 2011, as well as wage increases that are proportional to companies’ revenue growth. It also aims to expand collective bargaining in multiple industries to 60 percent by 2010 and 80 percent by 2011.

Various regional plans calling for collective bargaining rights at companies are taking shape at the draft policy level. In mid-August, Shenzhen’s Municipal People’s Congress released a set of draft rules regulating collective bargaining. According to the draft, workers will be able to negotiate collective contracts with companies on a range of labor issues, including working hours, working conditions, wage levels and increases, social insurance, overtime compensation and annual leave. Articles 55 and 57 of the draft regulations also outline penalties in the form of fines for non-complying companies. Similar draft regulations have been released in Shanghai – in the form of a set of opinions – and Guangdong Province. The draft released in Guangdong is notable in that it opens the door for strike action against companies; in the event that an employer does not respond to a legitimate collective bargaining request, employees may not be terminated for work stoppages.

Despite these regional developments, collective bargaining is not addressed in the 2008 Labor Contract Law, and the ACFTU still lacks legal authority to force collective bargaining at enterprises. However, FIEs operating in China do have cause for concern. In July, the ACFTU announced that it would invest RMB 10 million in trial professional collective bargaining agencies in 10 provinces and cities this year. Additionally, there are signs that foreign companies – especially large retailers and fast food chains – will be targeted for collective bargaining. The Shenyang Municipal Trade Union negotiated collective labor contracts in June for local employees of a major US fast food multinational.

Collective bargaining will likely remain one of ACFTU’s clarion calls in coming months and years. Although service and financial sector unionization has not yet come to the fore in China given the comparatively safe, comfortable and highly sought-after working conditions, the ACFTU also expressed its intent to incorporate major financial and service sector players into its unionization and collective bargaining plans.

### **Balancing act: social stability and workers’ rights**

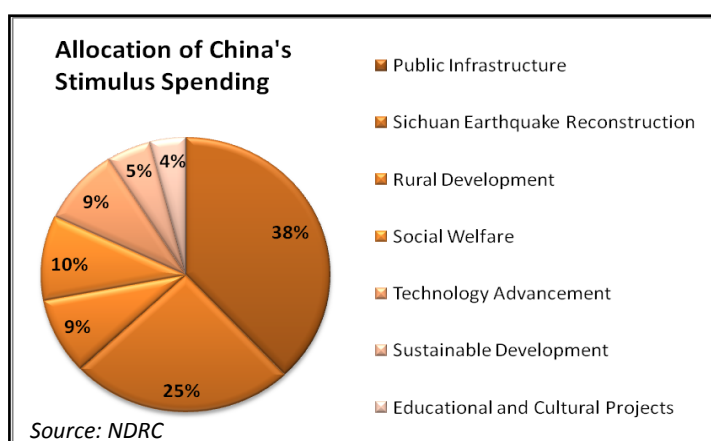
There is an ideological conflict between the ACFTU’s theoretical mandate to protect workers interests and its Party-controlled apparatus that fear social instability. As such, the ACFTU’s support for workers does not imply a role as an enabler to the recent wave of striking laborers. In a [June 21 research report](#), the ACFTU suggests that mounting appeals from workers is a risk to China’s political stability and economic development. This enunciation suggests that local chapters of the ACFTU, historically loath to enable strikes, are still highly unlikely to encourage organized labor stoppages within enterprises.

However, against the backdrop of the government’s emphasis on promoting indigenous innovation and encouraging increased investment in China’s interior

regions, allowing this type of labor mobilization neatly matches the government's ambitions to move Chinese workers up the value chain. Boosting wages also means stronger consumption power for China's laborers, good news for leaders in Beijing as they try to spur domestic consumption in initial steps to transition out of an export-driven development model.

### CONSTRAINTS ON LABOR SUPPLY

While labor in China is not yet in tight supply, China is currently experiencing a shortage in skilled labor. The extent of this shortage and how long it will last has been the focus of considerable debate. The latest batch of strikes indicates that Chinese workers, if not increasingly aware of China's tightening labor conditions, are less willing than previous generations to endure harsh labor conditions indefinitely. They also benefit enormously from social media and mobile phone technology in sharing employment information and in coordinating labor actions, luxuries their parents never had.



Many experts view government stimulus funds being funneled to rural infrastructure development projects as a major driver of the tightening labor market. Though much of the stimulus announced in 2008 was previously planned investment, 72 percent of China's original RMB 4 trillion package was designated for infrastructure development, Sichuan

earthquake reconstruction and rural development. Resulting projects create alternative but temporary jobs for migrant laborers. These jobs are generally outside of the manufacturing sector and often away from the coastal provinces and Pearl River Delta region, the ground zero of China's manufacturing, export-driven economy. China's demographics are also contributing to the tightening labor market, with fewer young workers to replace a steadily aging migrant work force.

### Advantages remain

By western standards Chinese labor is still incredibly cheap. One estimate published in a 2009 Monthly Labor Review by the U.S. Bureau of Labor Statistics places Chinese hourly manufacturing wages at only 2.7 percent of American workers' wages. As the steady rise of Chinese wages over the past decade continues, producers will see more parity in nominal terms in manufacturing costs between China and other Southeast Asian countries. This parity will be somewhat offset as Chinese labor productivity outpaces wage growth and ingrained supply chains keep China competitive.

While discussion of the oft-cited Lewisian Turning Point (the threshold at which wages increase as surplus labor supply from rural regions in developing economies begins to shrink) is well merited, it will be some time before manufacturers' China incentive is critically undermined. A widely reported survey released in June by the Hong Kong Trade Development Council revealed more than half of 2,400 surveyed

companies would continue to employ a China coastal-hub manufacturing strategy, while a quarter would seek to move operations inland. Less than 13 percent responded that they would seek other Asian manufacturing-base alternatives. The survey also noted that the top five Asian production regions were all still in mainland China, including the Pearl River Delta (PRD), the Yangtze River Delta, regions in Guangdong Province outside of the PRD and provinces adjacent to Guangdong and the Bohai region.

### **Coping with a tighter labor pool**

Nonetheless, steadily rising wages will push companies to adopt alternative strategies, like factory relocation to China's interior or increases in automation. China's 31 mainland provinces, autonomous regions and municipalities still suffer from vast wage disparities despite the 1994 establishment of regional minimum wage standards

Foxconn, at the center of the recent media coverage on worker unrest, recently announced that it would shift jobs for thousands of workers from Shenzhen to other regions, including Langfang in northern China's Hebei province and Zhengzhou, the capital of central Henan province. Recruitment of up to 200,000 workers has already begun. *China Daily* reported that Dell was considering a shift for its manufacturing facilities in Xiamen to central or western China. Similarly, *The Economist* reported that in 2009 foreign firms invested \$3.8 billion in Anhui province, inland from Shanghai along the Yangtze River.

The inevitable adjustment process for an economy-wide reallocation of human resources has immediate costs for workers and business operations. While China's labor advantage is far from disappearing altogether, in the face of gradual rises in wages nationwide, there will be pockets within China where low-cost labor will not be the viable option it once was. This fact will affect producers differently based on the labor-intensity of their operations, whether down-stream sales strategies can capitalize on the growing consumer market in China and whether supply chains can be effectively managed to mitigate costs of potential work stoppages.

### **WHAT THIS MEANS FOR FOREIGN BUSINESSES**

Chinese leaders in Beijing hope increased costs in more developed coastal areas will draw attention to poorer regions in need of foreign investment where wages are still low. In this sense, their hopes are increasingly being realized. Progressive minimum wage increases, despite their flaws, are also seen as an important step to alleviating the growing wealth disparity in China within government circles. *The People's Daily*, the official newspaper of the Chinese government, ran an article in July acknowledging citizens growing concern over wealth disparity and the tremendous challenge it presents to China's continued development. In conjunction with a tighter market for skilled labor, foreign companies in particular will face increasing pressure from both workers fighting for increased compensation, and the government, which will put greater legal and procedural constraints on labor management operations.

Where FIEs once enjoyed tax incentives and the open invitation of government officials, they will increasingly find stronger emphasis on technology transfer, less inviting corporate tax options and mounting pressure to unionize workforces. Many in the foreign business community have argued that this trinity heralds the end of the China heyday for FIEs. The unprecedented acquiescence toward domestic media coverage of recent strikes at foreign companies may be another example of how the

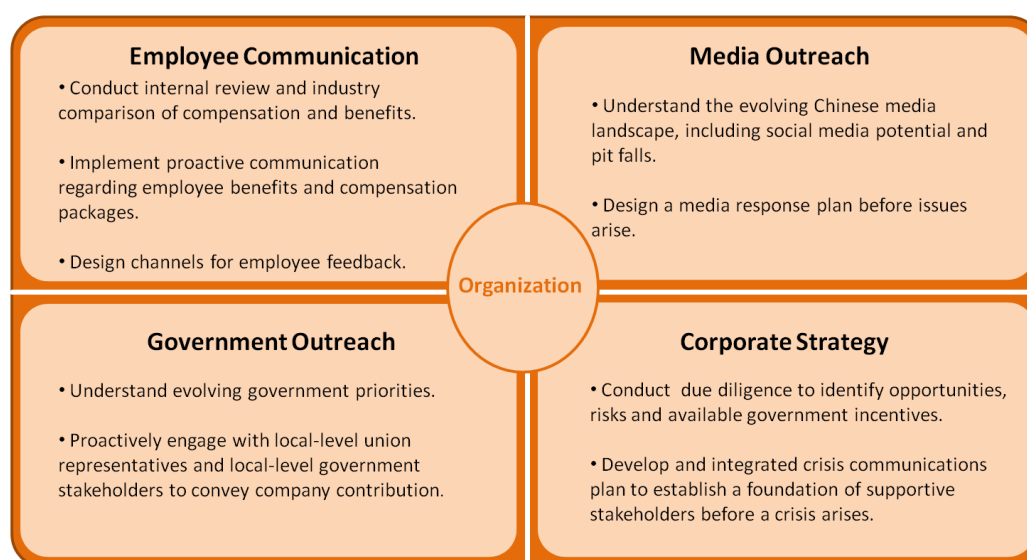
business environment for FIEs in China is becoming increasingly challenging. This would certainly be the case if FIEs face more intense government scrutiny than domestic companies or consistent demands to prove corporate value to China and its workers.

### ADDRESSING RISKS AND OPPORTUNITIES

With increased pressure in China to justify to the government and to workers corporate contributions, FIEs must prepare for the impact of shifting labor demographics and the latitude given to a more vocal labor force. Companies with labor intensive operations in China, as well as companies that depend on China-based supply chains should develop labor-focused and crisis response strategies. Such strategies must account for business operations as they intersect with various internal, media and government stakeholders.

#### Employee communication

A proactive internal review of compensation structures and industry-specific compensation comparisons can help companies anticipate worker complaints and prepare quick and effective responses. Ensuring that employees receive and understand information about the range of employee benefits should be a regular feature of a company's human resources operation. The use of social media has been an increasingly important means for workers to communicate about their experiences and expectations from the company. Companies must understand the pitfalls and opportunities for corporate communication presented by mobile messaging and the Internet. Developing internal feedback channels via social media can open channels for communication and help leaders identify challenges before they transform into crises.



#### Media outreach

Understanding China's evolving media landscape is important in designing an effective media response to a labor dispute or related complications. Given the tentative tolerance for laborers within China's arena for civic debate, companies should ensure that media response strategies and internal communication guidelines are in place before an issue arises. Similarly, developing a media outreach strategy to ensure that appropriate government, labor and public stakeholders are being

reached is critical to establishing a foundation for government and public support that can help a company weather a crisis.

**Government outreach**

Understanding China’s evolving political environment is critical to anticipating trends and coordinating outreach efforts with government agendas. In some instances corporate and local government agendas are in alignment – local governments hope to promote economic development and follow central government precepts for creating a stable a prosperous society, while corporations seek to maintain peaceful and stable working conditions that support business development and institutional objectives. Without the support of local and municipal level government officials, local union leadership is less likely to press for specific action against a company. Companies should make increased efforts to open communication channels and secure the support of local-level government officials and even trade union representation outside of the company, leveraging their corporate contributions to the local economy and communities.

**Corporate strategy**

As companies’ strategies and operations transform to meet China’s dynamic social and political development, proper due diligence and analysis of government plans and incentives can make the difference between failure and success.

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For further information on how APCO Worldwide can help your organization understand China’s labor environment, please contact:

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