Seeing the Sights of Industrial China: 2 Factories, 2 Futures
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Illustration by The New York Times

"The RMB is killing me," groaned Jin Jue.

Mr. Jin, a hip-looking 35-year-old with spiky hair and an all-black ensemble, describes himself on his business card as the "board chairman" of the Shanghai Jinjue Fashion Company. It was my first full day in China, and Mr. Jin was showing me around his factory on the outskirts of town.

RMB, of course, is shorthand for renminbi, the Chinese currency, also known as the yuan, which, since the beginning of the year, has risen more than 4 percent against the declining dollar. Even as the Chinese economy has become increasingly powerful, the government has kept the yuan artificially low, much to the annoyance of the United States. Truth to tell, it is still not nearly as high as it would be if it were unmoored from government control. When the Treasury secretary, Henry Paulson Jr., was in Beijing this week, he praised the recent rise of the yuan though — as he invariably does when he's in China — he called on Chinese officials to let their currency float freely.

This is my first trip to China and, like most Americans, I had an image of what a Chinese factory looked like. Mr. Jin's operation fit that image almost to a T. It was housed in a run-down building amid a sea of run-down buildings in the Kun Shan industrial zone, just northwest of Shanghai. Except for Mr. Jin's own office, it was really just one cavernous room, filled with rows of tables, on which stood old-fashioned sewing machines. There was a cafeteria with rickety wooden chairs and beaten-up tables where the workers ate their meals, and a sad-looking dormitory where they slept. Behind the building was a dirty-looking river. Debris littered its banks.

Mr. Jin's factory also makes the sort of thing you expect a Chinese factory to make: it churns out inexpensive clothing, aimed at the European market. Mr. Jin is the classic low-cost, tight-margin, squeeze-every-penny manufacturer, the kind of entrepreneur who has been the backbone of China's astounding economic rise — and who has also been the primary beneficiary of the low yuan, which has spurred the market for China's cheap goods. On the day I visited, his work force was making tan jackets under the French brand Camaïeu.

Except ... where were all the workers? I had expected the place to be teeming with people. Instead, only about a quarter of the room was in use; Mr. Jin later confirmed that 60 percent of his work force had either quit or been laid off. Business, clearly, was terrible, and Mr. Jin was losing money.

What the low yuan giveth, the rising yuan taketh away. As China's currency has risen, Mr. Jin's cheap clothes suddenly aren't so cheap anymore. And he had other problems as well. "The business environment in Europe is bad," he said through a translator. Thanks to inflation in China — up 8.7 percent in February alone — his workers wanted more than the several hundred dollars or so a month he says he pays them. The tax rebates he received from the government were shrinking.

Recently, the government passed labor laws that included a series of protections for workers; that was also pushing up his costs. As a result, orders that had once come to him as a matter of course were now gravitating to Vietnam, Mexico and other countries that could undercut him on his only competitive advantage: cost. (I later heard that some Chinese garment manufacturers were putting a "Made in Mexico" tag on their goods and routing them through Mexico to take advantage of Nafta.)

Though he lacked a college education — Mr. Jin had started in business right out of the army, he told me — he had a pretty clear-eyed understanding of what was happening to him. Though factories like his had led the way in China's economic miracle, the government was not all that terribly interested anymore in having the country be the lowest-cost producer of every good imaginable. Factories that played that game sometimes produced toys that were tainted. And they didn't necessarily improve the quality of life of their workers. Ultimately, relying on cheap labor to build an economy was a sucker's game. "If the government lets the RMB keep rising," Mr. Jin said, "all these factories will go out of business."

And so it may turn out. But though it may inflict some pain in the short term, over the long haul, it will almost surely be a good thing for the Chinese economy. And it won't be a lot of fun for the West to watch.

When you travel around China these days and listen to businessmen and analysts, there is a phrase you hear again and again. They all talk about "moving up the value chain." By that they mean they want their businesses to gravitate toward more complex, higher-value goods — the ones that bring in bigger profits, are less dependent on rock-bottom costs and are more immune to currency fluctuations.

Andrew Rothman, a China strategist with the investment firm CLSA, described it as "a deliberate policy to push manufacturing up the value chain."

"It is coming at the same time as rising raw material costs. What the Chinese government is saying is that, 'We don't want to be the world's workshop for junk. We want to make higher-value stuff that creates more wealth and better jobs.' "

For instance, if you open up, say, an iPod, you'll find that many of the higher-value components are made in places outside of China—and then brought into the country to be assembled. And, of course, the biggest profit of all goes to the owner of the brand: Apple. The Chinese are no long content to simply assemble the components. They want to make them as well — and own the brand.

In his own way, Mr. Jin understood that, too. On the flip side of his business card was the word "Tousnosamis." It was, he told me, a fashion brand he had started recently; he had put out several lines of women's clothing that he was selling in the domestic market. Eventually, he said with a small, self-conscious laugh, he hoped it would become "like Armani." At the least, it would allow him to be freed from the

grinding pressure of being a low-cost manufacturer. “Maybe in 10 years,” he said. It was his dream — and China’s.

The next morning, I met someone who had already fulfilled the dream. His name is Li Xian Shou, and he is the founder and chief executive of a company called ReneSola, which makes the silicon wafers that are used in solar panels.

Mr. Li, 39, looks as uncool as Mr. Jin looks cool; his pink tie was slightly askew and the sleeves of his suit were so long they almost covered his hands. His company, however, is as cool as can be: In the fourth quarter of 2007, its revenue was up nearly 200 percent from the fourth quarter of 2006. Last year, it made $53 million, almost double its 2006 profit, and in January it raised $130 million in a stock offering on the New York Stock Exchange.

The ReneSola factories were also on the outskirts of Shanghai, but that’s where the similarities with Mr. Jin’s factory ended. Mr. Li’s company was expanding like crazy, taking over acre after acre of former farmland, and snapping up plants, dormitories and other facilities as fast as it could. As we toured through Mr. Li’s plants, I was a little stunned to discover that some of the buildings were only six months old; the plaster was nicked and scarred, suggesting a lot of wear and tear. Like many Chinese businessmen, Mr. Li is moving so fast he doesn’t have time to worry about whether the plaster on his walls is smooth.

Before giving me the tour, Mr. Li told me his story (again through a translator). A former government official, he had raised $1.5 million from four friends to start his company in 2001. (Government officials who go into business tend to have the crucial advantage of good connections.) At first, the company assembled solar panels; most of his customers were companies in Germany and Japan that made the wafers and then sold the panels once they were assembled. “By 2003,” he said, “revenue was about $10 million.”

But assembling the panels was the lowest-cost, lowest-value part of the solar industry. “It is a commodity business,” he said. “And it can attract a lot of competition.” So in 2005, he decided to take the big leap. He got out of the solar panel business and into the more profitable solar wafer business.

Now instead of competing with other Chinese companies, he is competing with German and Japanese companies — where his cost advantage is huge. His company has created a technology for using recycled wafers and other materials, which is helping him avert the shortage of polysilicon, the material from which the wafers are made. He employs 3,300 people, up from 20 in 2005, and pays his line operators upward of $500 a month. From a standing start three years ago, ReneSola is among the world’s top five suppliers of solar wafers.

When I asked Mr. Li about the effect of the rising yuan, he gave me an indifferent shrug. Because his wafers are shipped to other Chinese companies — the panel assemblers — instead of exported, he can demand payment in yuan. His is a business that relies on complicated machinery at least as much as manual labor, so he can work toward productivity improvements. And because he is making a product with a much higher profit margin than a solar panel’s, he can more easily absorb a currency hit. So far, he said, the money lost from the rise of the yuan was “trivial.”

As we toured his plant, I couldn’t help noticing that much of the machinery ReneSola uses to make wafers came from Germany. A rising yuan helps Mr. Li there, too.

As the Chinese say, Be careful what you wish for, Mr. Paulson.

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