REEBOK SHOES AND SPECIAL ECONOMIC ZONES: A CASE OF LOCAL AUTONOMY IN CHINA[1]

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It is a common belief among us Filipinos that Marikina shoes are exported all over the world, although under various foreign brand names. Indeed, a report circulated among shoe producers in southern China's Special Economic Zone (SEZ) of Shenzhen showed that Philippine share of world sales for footwear in 1992 was projected to reach 0.56%.

Placing the world's population at six billion, it would mean that 336,000 pairs of shoes will come from the Philippines if only one out of a hundred persons in the world buys a pair of imported shoes a year. At a conservative estimate of ten dollars net per pair of branded shoes, the amount shall easily earn for the Philippines much needed foreign currency amounting to US$3.36M.

Rather than resting on our laurels, however, let us look at our budget coming from our shoestrings. The same source noted that the figures show a decrease of 12.62% in the quantity of 1992 Philippine share in the world market compared to 1991. But the value of Philippine share is expected to increase by 15.03%.

BRANDED AND NOT KUNGFU SHOES

China is the world's largest shoe exporter, with an expected share of 53.10% of the 1992 world market. The figure indicates a quantitative increase of 44.27% compared to last year's. Increase in the value of its branded shoe products, meanwhile, is expected to reach 71.69%. Among the top branded shoes, in order of their world sales, are **Nike, Reebok, L.A. Gear, Keds,** and **Adidas.**

Chinese factories producing **Reebok** brands[2] got 21.36% of January-July 1992 orders from the US mother company, particularly the Reebok Trading (Far East) Company, Ltd. One can compare China's share of **Reebok** orders with South Korea's 29.18%, Indonesia's 24.83%, Thailand's 16.80%, and Taiwan's 3.47%. The low figure for Taiwan is a sign, more than anything else, of the island's shift to high-tech from labor-intensive consumer goods production. The remaining 4.36% of **Reebok** orders are produced by three factories in the Philippines.

The Kong Tai Shoe Manufacturing Company, Ltd. in Baoan, just outside Shenzhen, is one of ten companies in China producing shoes for **Reebok**. A look at Kong Tai's name written in Chinese characters would reveal the source of its capitalization. Kong is for Hong Kong while Tai is for Taiwan. It is, indeed, a Taiwanese factory which was set up in the mainland through its Hong kong corporate office. In short, it is a Hong Kong-based Taiwanese venture in China.

Being an independent shoe factory, Kong Tai takes care of its own product development planning, tooling, and raw material sourcing. Its equipment and machinery are mostly bought from Japan. As such, it may enter into contract with other branded shoe companies. Whenever it does so, Kong Tai chooses to make shoes only for non-**Reebok** competitors. Seven of its production lines,[3] watched over by 18 Taiwanese technicians, are for **Reebok.** Around 2,700 workers coming from China's rural areas man the cutting, lasting (assembly) and stitching lines housed in four five-storey factory buildings. The compound has also its own administration building, sports ground, and men's and women's dormitories.

If **Reebok** does not have its own factory and is but a customer of shoe factories like Kong Tai, how does it maintain the standards it has set for products carrying its name? It does so by keeping a highly paid cadre of management officials and quality assurance engineers under the over-all supervision of an American country manager.

For instance, Larry Mariani, **Reebok's** country manager for China, oversees three factories in the Shenzhen area (one of which is Kong Tai), three in the Zhuhai-Panyu area, and four in the Fuzhou area. He is supported by a management staff composed of a Hong Kong-based production manager for China, China-based area assistant production managers, and quality assurance and quality control (q.a.- q.c.) engineers. It is interesting to note that Mariani's management staff for **Reebok** China is an all-Filipino outfit. A Filipino senior q.a.- q.c. manager for China-Taiwan-Philippines, Alberto Dy, also helps him in his China operations. It was Mariani who, according to our resources, specified to his company that Filipinos should help him manage his operations. But he also hires local inspectors to frequent the production lines and spot check 120 per 500 boxes of finished products.

The Filipinos, besides ensuring that **Reebok** standards are kept at high levels, also serve as consultants to Taiwanese investors on production management. Obviously, while instilling efficiency in Chinese factories, Filipinos make the American management theories they learned in school adapt to an Asian setting. Philippine slogans plastered on factory walls remind workers of the importance of quality products. For example: "Quality means business; Business means jobs, our jobs."

The investors, meanwhile, are attracted to, among others, the low labor cost and virtual strike ban in China. Power outages, which beset the Shenzhen area now, are expected to ease up when the Daya Bay Nuclear Power Plant nearby is initially commissioned in July. Reliable sources reveal that exactly 115 Filipino nuclear scientists and technicians have been hired by the foreign nuclear plant operator to conduct the high-tech processes of power generation. China's most favored nation (MFN) status in the United States provides an added incentive to investors with an eye for the American market. Some branded shoe traders look at MFN as a very serious matter that they are prepared to transfer their operations in Vietnam in case China loses such a status. The same is true if Europe imposes a quota on China purportedly in support of the new East European states.

Taiwanese investment, Hong Kong corporate laws, Japanese equipment, foreign power-generation, Chinese workmanship, American standard, and Filipino management expertise all combine to come up with a branded shoe. How is it possible to produce such a multi-national shoe in China? Or how is it possible to similarly produce the "Made-in-China" toys, garments, electric appliances, hardware supplies and electronic products that glut the country's compact disks market especially at Christmastime?

The answer may be found in China's highly autonomous, yet centrally well-supported SEZs, and the so-called open coastal cities, open areas, and open industrial zones.

THE SHEKOU EXPERIMENT

The Shekou (Open) Industrial Zone, established in 1979, was the earliest export processing zone in China. Its establishment came on the heels of Chinese President Li Xiannian's March 1978 visit to the Bataan Export Processing Zone.[4] There, President Li had the opportunity to observe the way a foreign factory produced **Bata** shoes.

From a small fishing village with a population of 2000, Shekou has grown into a 10-square kilometer industrial zone with 42,000 people. Its 400 enterprises produce light, medium, and heavy industrial goods from garments, silk cloth, and foodstuff, to glass floats and construction materials. Its industrial output value amounts to RMB¥3.38B,[5] according to Yang Shen of its Public Relations Department. It has a three-jetty port, one of which is the biggest container port in China, maintained and operated by the China Merchants Corporation.[6] Yang Shen explains that Shekou has been divided into three sectors, each of which is maintained and operated by three different entities: a) the China Merchants Corporation; b) the Shekou Fishing Trade Industry Corporation; and c) the Ziwan (Purple Bay) Corporation whose biggest shareholder is also China Merchants. Personalities involved in these operations include Y.K. Pao (Bao Yong-gang), the shipping magnate; and Yuan Geng, China's Hong Kong connection even during the heyday of the cultural revolution.

The Shenzen Top-Tech Electronics Co., Ltd.,[7] one of Shekou's factories, produces black and white security closed circuit TV cameras using Taiwanese investment, Japanese equipment, Philips' imaging technology, and English language-based computer programs. It provides job to 80 Chinese workers who are constantly exhorted with slogans like the so- called four firsts: "Customer first, quality first, reputation first, and service first." Another slogan reads: "Do it right the first time."

It must be noted at this point that Shekou is now but a small part of a large Special Economic Zone. The success of the Shekou experiment prodded Beijing to designate Shenzhen (Shumchum), a small town adjacent to it as China's first SEZ in 1980.

BEIJING-DESIGNATED SEZs AND OPEN COASTAL CITIES

Foreign capital and advanced technology enter China through its special economic zones (SEZ) and open coastal cities. Shenzhen in Guangdong province, where Shekou is located, is the first SEZ established by the central government in 1980. (See Guangdong's Administrative Map.) As Shenzhen's advantages became apparent, three more SEZs were established: Zhuhai and Shantou (Swatow), both in Guangdong, and Xiamen (Amoy) in Fujian (Fookien). In 1988, the whole island province of Hainan, with a land area of 34,189 square kilometers,[8] was also turned into a SEZ. In 1984, Beijing decided to open 14 coastal cities to foreign investment, namely: Tianjin (Tientsin), Shanghai, Dalian (Dairen), Qinhuangdao, Yantai, Qingdao (Tsingtao), Lianyungang, Nantong, Ningbo, Wenzhou, Fuzhou (Foochow), Guangzhou (Canton), Zhanjiang and Beihai.

Tianjin in the north, which like Shanghai and Beijing does not fall under a province but is directly under the national government, is composed of nine urban districts with an area of 315 square kilometers and an additional area of 10,990 square meters.[10] It has a population of 8.78 million. Its zone for foreign investment, the so-called Tianjin Economic-Technological Development Area (TEDA) occupies an area of 33 square kilometers. **A Guide to Investment,** published by its city government, quotes the United Planning Company of the United States to show how TEDA greatly surpasses total investments in each export processing zone of Taiwan, South Korea, Thailand and the Philippines.

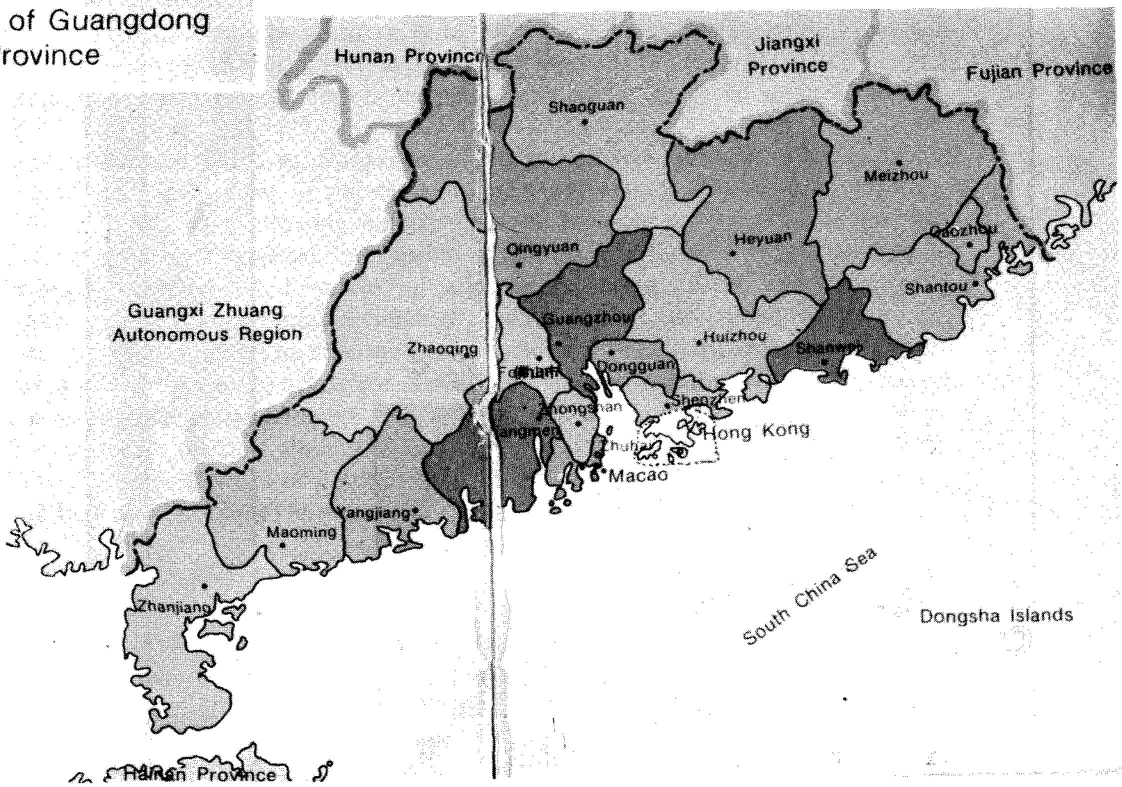
Xiamen in the south, heretofore an isolated island facing the Taiwanese-controlled island of Jinmen (Quemoy), started operating a SEZ in a 2.5 square kilometer area in October 1981. Since then, "an export-oriented economic structure with industry as its mainstay has taken shape."[11] After its initial success, the whole of Xiamen Island, including Gulangyu Islet, was turned in 1984 into a SEZ with an area of 131 square kilometers. In May 1989, Beijing approved the setting up in Xiamen of a Taiwan Investment Zone, with an additional area of 126.64 square kilometers.

Chinese Filipino investments like Henry Sy's Xiamen Plaza and Go Eng Guan's condominium housing units, among many others, greatly contributed to Xiamen's present cosmopolitan ambiance. Indicative of Xiamen's good investment environment is the account that the monosodium glutamate factory in Xiamen of Ajinomoto (Philippines) has recouped its investments in a year's time. Secretary Ye Wende of the Communist Party branch in Caitang Village was very eager to show his visitors a granite mill and a cardboard box factory owned by Taiwanese investors, and an earthen brick workshop owned by a local investor.

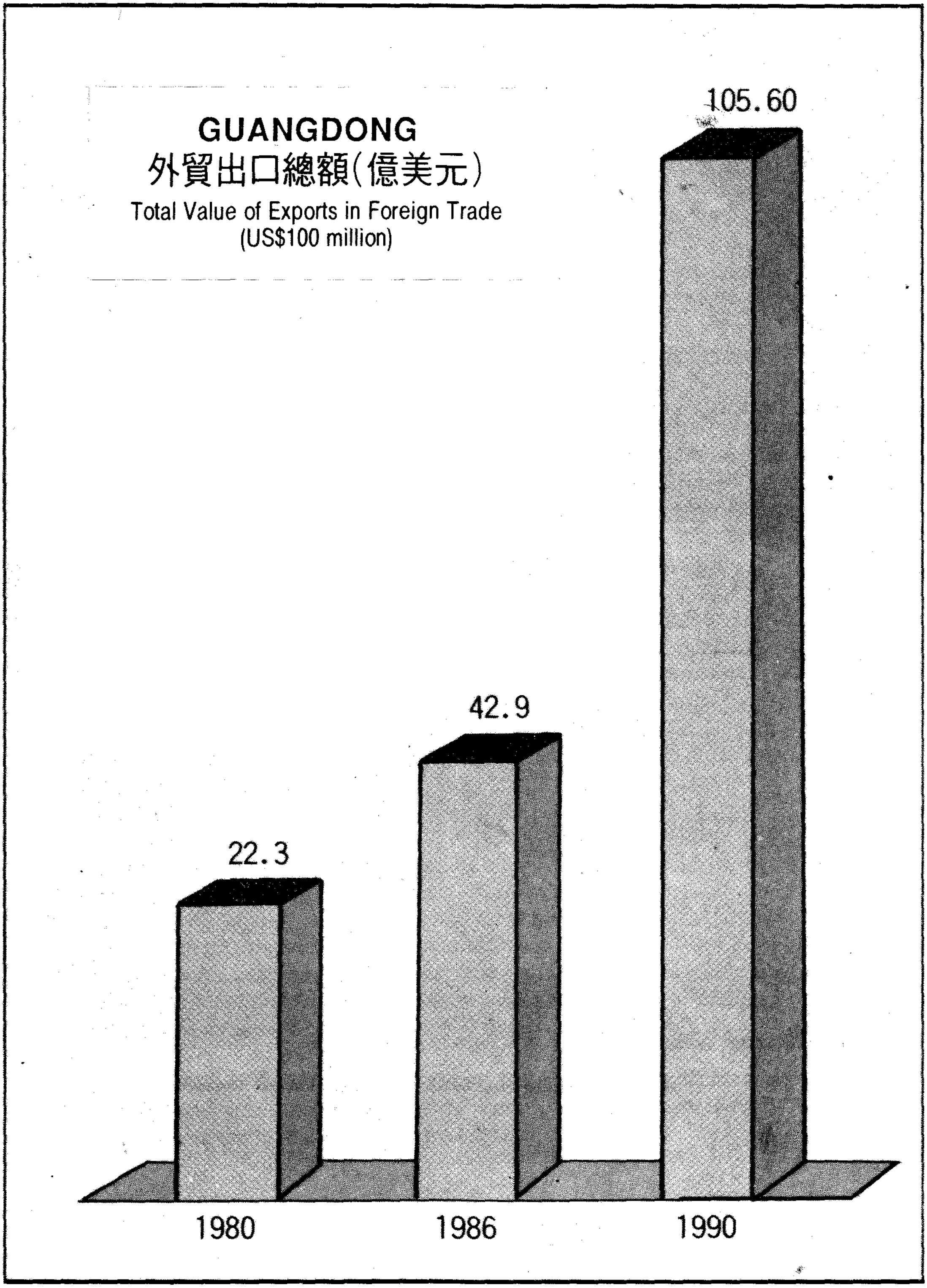
What made them click? What are the factors behind the apparent success stories in China's open cities and SEZs? Tianjin's and Xiamen's are only replications of what is considered the model of them all, Shenzhen.

Location of Guangdong Province

DIVISION OF GUANGDONG PROVINCE ADMINISTRATIVE



Map by Guangdong Association for External Cultural Exchanges



Graph by Guangdong Association for External Cultural Exchanges

SHENZHEN'S SPECIAL CHARACTERISTICS

In 1980, Shenzhen was a small town of 30,000 people. The tallest building in its 3 sq. km. land area was five storeys high. Now, 12 years later, it is a 2,200 sq. km. modern metropolis properly zoned into industrial, commercial, tourist, residential, cultural and educational areas. Its population, coming from all over China, has swelled to 2.38M (including Baoan County's one million). Its International Trade Building, built at a rate of a floor in three days, has 53 floors. Soon to be the tallest being built, constructed by Thai investors, is called simply the Shenzhen Building. There are 4,287 foreign industrial and commercial enterprises in Shenzhen whose total investments amount to US$3.8B, or around 15% of all foreign investments in China. Its gross domestic product (GDP) since 1981 has been growing by 45% per annum, a rate that is faster than the fastest growth rate of any of the Asian dragons.

According to Zhang Yi[12], the most important factor in Shenzhen's development is the central government's favorable policy of allowing the SEZ to be as flexible as possible so it may boldly experiment on all forms of investment policies. For instance, Shenzhen now allows foreign investors engaged in processing products for export 100% equity and 100% repatriation of profit. Moreover, corporate income tax has been set at 15%.

Unlike the rest of China, Shenzhen which started from scratch is not burdened by a shift from the traditional Soviet model of a centrally-planned economy to the now more favored policy of allowing market forces to regulate economic development. Traditionally, planning governed all aspects of the Chinese economy from production to distribution, which dictated sourcing of raw materials even when economically non-viable and yielded non-marketable finished products which only found their way to godowns (i.e. warehouses). The Shenzhen policy is to have planning go hand in hand with the market economy, i.e., to allow the central government to intervene in matters of direction-setting, financial policies, and taxation; and where transportation and power rates may be set by the state while 97% of all other sectors rely on market forces. Zhang Yi referred to the examples of Singapore and South Korea where strong government direction helps promote market economy.

Zhang Yi also referred to Shenzhen's proximity to Hong Kong as another advantage for Shenzhen which other cities in China do not enjoy.[13]He expressed the hope that Shenzhen learn from Hong Kong its excellent experiences as one of the finance capitals of the world. In the same breath, he mentioned of an on-going crackdown in Shenzhen on pornography and prostitution as a proof of its "still being socialist" while Hong Kong is capitalist. Other features of Shenzhen's economy include: a) publicly-owned industries coexist with 100% foreign-owned companies, joint ventures, cooperatives, and individual enterprises; b) state-owned banks coexist and compete with sectoral, commercial, industrial, and foreign-owned banks; c) state ownership of all land is offset by a 50 year lease-hold system where favorable prices are set for those designated for industrial use, while commercial lands are open to bidding and options;[14] d) the so-called "iron rice bowl," which provides equal security of tenure to all workers regardless of their varying degrees of competence, is replaced by freedom on the part of management to hire or fire workers who, on their part, are asked to contribute to a kind of social security system hitherto unheard of in China; and e) industries outside the state-designated duty-free areas, which require no tariff for materials used in producing export products, may buy tax-free their requirements from the latter.

For better administrative purposes, it is being proposed that Baoan County, where Kong Tai Shoe Manufacturing Company and scores of other factories are actually located, be officially made part of Shenzhen SEZ.

The proposal may prove disadvantageous to investors. Investors in Baoan make use of the fact that it is not technically part of the SEZ, though geographically part of Shenzhen, to produce highly competitive goods. On the one hand, they make use of the last feature mentioned above to procure duty-free raw materials from the actually designated SEZ. On the other hand, they presently enjoy cheaper labor than if it becomes formally part of Shenzhen SEZ. Such a situation prompted a comment from Liu Yun, assistant director of Shenzhen's Foreign Affairs Office that in some ways, SEZs are no longer that special.

The SEZ is fenced all around, and one could enter only through checkpoints upon presentation of proper identification documents. Meanwhile, displaced rural workers seeking greener pastures may come to Baoan without going through much formalities. Such being the case, investors could choose to give lower wages and less benefits here than in the SEZ proper, if they are higher than the rest of China. Shenzhen proper may look ultra-modern, but one may find ghettos — the so called "floating population" or migrant workers in Baoan. If the plan pushes through, Baoan will add another 1,692 sq. kms. to the fenced area of Shenzhen.

SOME COMMENTS AND OBSERVATIONS

When asked if he thought Shenzhen could serve as a development model for China, Zhang Yi replied that the SEZ should share its excellent experiences with the whole country for the sake of the common weal, socialist education and the people's spiritual development. One may observe, though, that investments in Shenzhen are mostly concentrated on export-oriented light- and medium-sized industries. It has not built heavy and highly technical industrial bases as have Shanghai, Beijing, Harbin, Wuhan, and Xian. It can only complement, not replace, the contributions of the traditional industrial bases to the national economy. Shenzhen, including the other SEZs in China, is an example of an area within a country tasked with a clearly defined function, i.e., that of providing replicable experiences for a whole economic structure which is undergoing reforms. The flexibility it needs for such a task is provided by a clear-cut central government policy of least interference in its experimentations. The policies it derives from its own experimentations, however, such as those with regard to management, hiring, and social security, although for most parts applicable to other cities, must not be confused with the needs of the whole economy which is still largely agricultural. Zoning it, and making it produce goods almost exclusively for export, helps lessen the adverse impact of rapid development on a largely rural population. Strict control over population movement which characterizes its traditional Soviet model, still serve China in good stead in terms of minimizing social imbalances that arise from what otherwise would be hasty modernization. The very liberal package Shenzhen and the other SEZs offer to foreign investors make them very competitive with Philippine efforts at industrialization. What makes the Shenzhen example relevant to the Philippines, then?

The **Reebok** experience may be an indication.

NOTES

[1]This paper contains observations about the latter part of this researcher's most recent trip to China: first, as deputy head to a UP Asian Center delegation which toured Beijing, Xi'an, Guangzhou, Guilin, and Shenzhen and had discussions with fellow academics and researchers from May 19 to 29, 1992; second, as an individual researcher doing interviews in Baoan County near Shenzhen, and in Guangzhou and Xiamen from May 29 to June 2; and third, as part of another delegation, that of the Philippine Association for Chinese Studies (PACS) headed by Singaporean scholar Theresa Cariño until June 5.

[2]This researcher has gathered that the owners of this shoe trademark which carries the Union Jack in its logo are not British at all, but a US shoe trading firm which owns no factory.

[3]The number had increased to nine September of this year.

[4]Established in 1972.

[5]There are approximately six yuan renminbi (RMBY6.00) to a US dollar, or P5.00 to Y1.00.

[6]Established in 1872.

[7]The UP Asian Center delegation visited the Shenzhen Top-Tech Electronics Co., Ltd. when it toured Shekou on May 27, 1992. The manager of its purchasing department, a local Chinese named Zheng Zhengyu, showed the delegation around its workshops.

[8]Cf. Samar: 13,077 sq. km; Negros: 12,704 sq. km; Panay: 11,512 sq. km; Leyte: 7,213 sq. km; and Cebu: 4,421 sq. km.

[9]See China: A General Survey (Beijing: Foreign Languages Press, 1989) p. 182.

[10]Cf. Manila proper: 37 sq. km; and Metro Manila: 4,338 sq. km.

[11]According to A Guide to Investment in Xiamen Special Economic Zone. Published by the city government in 1991.

[12]Coitang Village was visited by the PACS delegation on June 4, 1992.

[13]This researcher had discussions with Zhang Yi, research assistant to Shenzhen's Foreign Affairs Office on 27 May 1992.

[14]Note also the location of the other SEZs, which happened more by a design to attract international investors rather than by an accident of geography: Xiamen is near Taiwan; Zhuzai, a stone's throw away from Macau; while Hainan is in the South China Sea, in fact the biggest island in all the archipelagos there. The coastal area of Shantou is home to most overseas Chinese, and may attract their capital, too.

[15]Cf. Xiamen's detailed incentives for foreign use of state-owned land: 40 years for industrial; 50 years for commercial, transportation, communication, and public service; 70 years for housing; 60 years for technological, educational, cultural and health care; 30 years for all other uses; and two years for temporary use. (See Xiamen's Guide to Investment, op. cit. p. 17).