

# Re-evaluating Your China Strategy

A new business and HR deal for foreign-owned companies

By Robert Wesselkamper



power over salaries, bonuses, training and other work-related issues.

Foreign-owned multinational corporations (MNCs) doing business in China are scrambling to comply with the new provisions. But this is just the latest wave in the turbulent Chinese marketplace. These days, savvy companies are rethinking their entire China strategy – looking at not only the changing labor situation but also the shifting business and economic environments in the world's most populous country.

## The New Realities

Historically, the “China price” has been 30 to 50 percent less than the cost of manufacturing the same product in the West. Today, however, production costs in China are increasing due to a variety of factors.

Rising oil prices and competition for other raw materials are driving up manufacturing and transportation costs. And building a manufacturing infrastructure in China is becoming more expensive. The new labor law promises to push costs even higher as the employee/ employer equation tilts in favor of employees, guaranteeing them better working conditions and pay.

The news isn't all bad for foreign MNCs: China's booming economy is creating a middle class with money to spend. What's more, the number of billionaires jumped from 15 in late 2006 to more than 100 today. All this

**C**HINA'S new labor contract law is just 14 pages long, but its impact looms large for any company with employees in that country.

The purpose of the new law, which took effect January, 1, is to strengthen worker protections. It mandates written contracts for workers makes it more difficult to lay off employees and guar-

antees lifetime employment. Employment contracts must now comply with minimum-wage and safety regulations, and short-term employees must become full-time employees with lifetime benefits after a short-term contract is renewed twice. The law also gives the state-run union and other employee representative groups collective bargaining

translates into a burgeoning market for goods and services.

### Home-court Advantage

This is not the first time MNCs have encountered a roadblock in their efforts to take advantage of the “China price” to cut production costs. Foreign-owned companies are accustomed to struggling with a system that favors Chinese firms. When it comes to labor issues, North American and European MNCs for the most part adhere to the letter of the law. Local companies, however, often leverage relationships and ad hoc agreements that differ somewhat from the written law, a long-accepted practice that allows them to reduce costs and gain a competitive advantage.

The new labor law could help level the playing field if Chinese-owned companies are forced to comply with a single law. But an equal and competitive climate won't occur overnight: Many local firms were once state-owned and consequently are bureaucratic and slow to change.

Chinese companies currently enjoy another economic advantage as they move inland to provinces such as Jiangxi, paying lower rates for water, electricity and labor. Foreign-owned companies still tend to operate in the industrialized coastal provinces, where production costs are higher. Following their Chinese counterparts into the interior will challenge these MNCs because of obstacles related to geography, culture, infrastructure, English language proficiency, and the availability of workers and skill sets.

### The Right Moves

In light of these new realities, foreign MNCs must embrace multiple strategies for success. HR executives can contribute to this effort by developing the capacity to differentiate compensation packages and HR services based on geography, function and strategic imperative.

MNCs that seek to expand their presence in China by acquiring Chinese-owned companies face unique challenges. A newly acquired company, for example, might have withheld employee and employer contributions to social programs but failed to remit those contributions to the government. Or withholdings and remittances might have been adjusted based on ad hoc agreements the MNC might not inherit upon purchase of the business.

The MNC must put its acquired company on a path to compliance with legal mandates, as well as corporate values and codes of conduct. Balancing obligations as a foreign-owned enterprise in China with the realities of a competitive business environment is no easy task.

MNCs also face challenges in dealing with China's phenomenal growth rate, which demands swift action. Companies that take an overly analytical approach or that are slow to make decisions are likely to miss opportunities to attract, retain and motivate workers. Consequently, they will find it harder to compete, particularly with Chinese-owned MNCs.

Finally, foreign-owned companies will need to pursue the “China price” wherever it may be. That means considering a move into the country's more remote and less populated interior provinces — and looking beyond China to other countries for the next center of low-cost production.

### Long-term Success

The impact of the new Chinese labor contract law will be dramatic and far-reaching. What's more, the law takes effect at a time when the business and economic environments in China are undergoing radical shifts.

To navigate these changes, foreign-owned companies need to carefully evaluate the new realities of doing business in China, while moving swiftly to make decisions and take action. Companies that balance those demands effectively will position themselves for long-term success in what promises to


be one of the most lucrative markets in the world.

### New Horizons

Chinese companies are already addressing the new realities of doing business in their country. They are turning to regions where raw material and labor costs are low and the legislative environment is hospitable — not only China's interior provinces, but also other countries, including Bangladesh, Cambodia and Malaysia.

Their aggressive pursuit of low-cost production has proven successful. China National Offshore Oil Corporation, for example, has surpassed Exxon Mobil Corporation in terms of market capitalization. China has become a major incubator for homegrown MNCs.

To compete and succeed in China's current business environment, foreign-owned companies will need to be ready to act quickly and decisively. Companies that demonstrate extreme flexibility and the capacity to readily implement new programs will achieve greater growth and higher revenues.

HR professionals can support corporate strategies by exploring lessons learned from their experiences in China and applying them in interior provinces as well as in new national locales. By helping the organization address compliance issues and historical compliance gaps, HR can smooth the transition to a compliant position. 



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