

IMPACT OF URBANIZATION ON PERCEIVED LABOR COST CHANGES IN
MANUFACTURING INDUSTRIES IN HEBEI OF CHINA

CHEN LISHA

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To my beloved mother, father and husband

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ABSTRACT

The past five decades have witnessed unprecedented economic growth in China. One of the major elements that accelerated this rapid economic growth, especially in manufacturing sectors, is the relatively low labor cost of China. However, labor cost in manufacturing industries of China continues to rise in recent years. Therefore, this study was designed to investigate the rising labor cost from a new perspective based on urbanization as well as its impact on the change of labor cost. A sequential exploratory design as a mixed method was used. Initially, qualitative data were collected and analyzed, and the results were used to develop the survey questionnaire. The qualitative data comprised document reviews, interviews and expert opinion assessments on the components of the labor cost and the impact factors of urbanization on labor cost. Quantitative data were collected from a survey of 200 manufacturing industries in Hebei province. The results of the qualitative data analysis showed that the major components of labor cost consist of social insurance, wage, job training and welfare costs. Social insurance has the most and fastest rise in cost. In addition, six factors of urbanization proposed by the experts are policy factor, human capital investment factor, living costs factor, population factor, economic factor, and individual factor. However, based on the quantitative data analysis, only the first three factors are statistically significant. From the study, it is concluded that there are three implications: model development to address the theoretical contribution, recommendations for the government on policy making and living cost control, and proposals for the employers to minimize negative impact of increasing labor cost.

ABSTRAK

Lima dekad yang lalu telah menjadi saksi kepada pertumbuhan ekonomi yang belum pernah berlaku di China. Salah satu elemen utama yang mempercepat pertumbuhan ekonomi yang pesat ini, terutamanya dalam sektor-sektor pembuatan, ialah kos buruh yang rendah di China. Walau bagaimanapun, kos buruh dalam industri pembuatan di China terus meningkat sejak mutakhir ini. Justeru itu, kajian ini dilakukan untuk mengkaji peningkatan kos buruh dari perspektif baharu berasaskan perbandingan dan kesannya kepada perubahan kos buruh. Reka bentuk pemerolehan berjujukan sebagai kaedah gabungan telah digunakan. Pada mulanya data kualitatif dikumpulkan dan dianalisis dan kemudian dapatannya digunakan untuk membangunkan soal selidik kajian ini. Data kualitatif terdiri daripada tinjauan dokumen, temu bual dan penilaian pendapat pakar tentang komponen kos buruh dan faktor-faktor kesan perbandingan kepada kos buruh. Data kuantitatif diperolehi daripada kajian selidik ke atas 200 buah industri pembuatan di wilayah Hebei. Dapatan analisis data kualitatif menunjukkan bahawa komponen utama kos buruh terdiri daripada insurans sosial, penggajian, latihan kerja dan kos kebajikan. Insurans sosial mengalami kenaikan dan peningkatan paling cepat dari segi kos. Selain itu, enam faktor perbandingan yang dicadangkan oleh pakar-pakar turut mengalami kenaikan dan peningkatan, iaitu faktor polisi, faktor pelaburan modal insan, faktor kos sara hidup, faktor penduduk, faktor ekonomi dan faktor individu. Namun demikian, berdasarkan analisis data kuantitatif hanya tiga faktor yang pertama secara statistiknya adalah signifikan. Kajian ini merumuskan tiga implikasi, iaitu model pembangunan untuk memenuhi sumbangan teori, cadangan kepada kerajaan tentang dasar dan kawalan kos sara hidup dan cadangan kepada majikan untuk meminimumkan kesan negatif daripada peningkatan kos buruh.

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CHAPTER 1

INTRODUCTION

1.1 Background

The past five decades have witnessed unprecedented economic growth of China (Lett and Banister, 2009; Zhang, 2013). One of the major elements that accelerated this rapid economic growth, especially in manufacturing sectors, is the relatively low labor cost of China (Waldman, 2004; Ang, 2010). However, in recent years, labor cost in manufacturing industries of China continues to rise. People began to wonder what had impacted the rising labor cost. Undoubtedly, there are many possible impact factors, such as government's macro-control, economic globalization, and currency exchange rate (Banister and Cook, 2011; Liao, 2008; Zhang, 2009). But, in this study, the researcher tries to explain the reason of the rising labor cost from a new perspective – urbanization. To begin with, it is necessary to have a systematic introduction on the background information of the study: the labor cost in manufacturing industries and the urbanization process in China.

1.1.1 Labor Cost in Manufacturing Industries of China

In 2010, China overtook the U.S. as the world's largest manufacturing nation with an annually output of 2.9 trillion USD, accounting for 19.8% of the manufacturing output in the whole world. Value-added of the manufacturing industry accounted for nearly 30% of the GDP of China in 2010 (National Bureau of Statistics of China, 2012). In terms of employment, according to official data, almost 30% (40.88 million people in 2011) of the employed persons in urban units engaged in manufacturing industries (National Bureau of Statistics of China, 2012). As a matter of fact, considering the many small scaled enterprises and enterprises in rural areas that are not included in the official data, the number of employed people in manufacturing industries could be over 100 million (China Council for the Promotion of International Trade, 2014). Therefore, the development of manufacturing industries is essential to both the economic growth and the population employment in China.

The relatively low labor cost is the key for the growing of manufacturing industries and keeping international competitiveness for the Chinese economy during the past three decades. With the proliferation of Chinese products on the international market, there has been increasing interest in the statistics of China's manufacturing industry, particularly for the labor costs in manufacturing industries (Lett and Banister, 2009). The concept of labor cost defined by China is similar to the international practice, it includes wage of employees, social insurance contribution, company welfare, training outlay, labor protection expenditure, residence of employees and other labor cost expenditure. Briefly speaking, labor cost in China mainly has the following features:

Firstly, compared with other developed countries and newly developing countries, labor costs of China are still at a low level. In 2008, with reference to

Figure 1.1, the average hourly compensation of manufacturing industries was only 1.36 dollars per hour in China, while Japan was 27.8 dollars/hour and Taiwan was 8.68 dollar/hour (U.S. Bureaus of Labors Statistics, 2010).

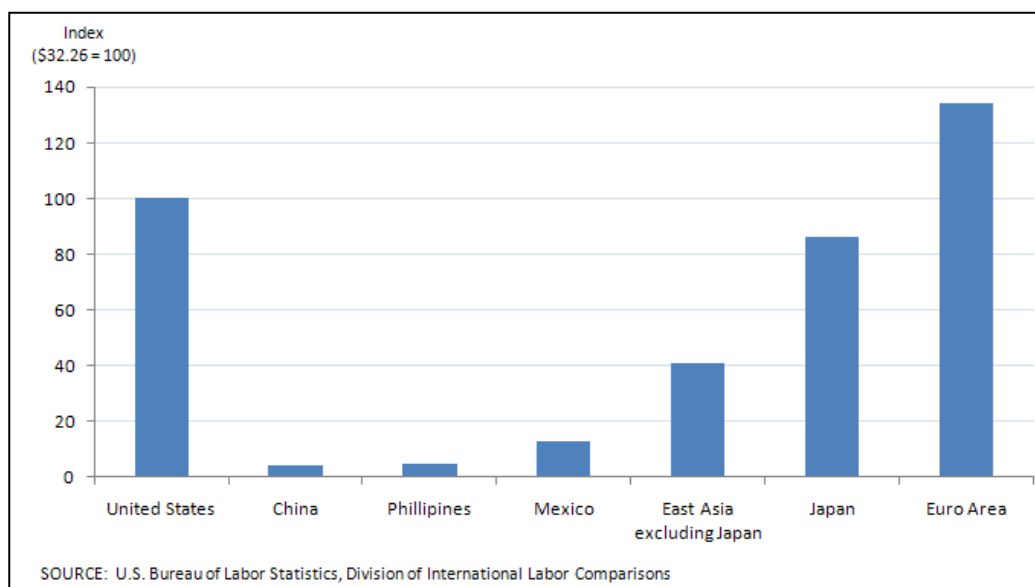


Figure 1.1 Labor Costs of Selected Economies and Countries

Note: “East Asia excluding Japan” refers to Korea, Philippines, Singapore and Taiwan.

“Euro Area” refers to the EU countries which use Euro as currencies at January 1, 2009.

From the perspective of input and output of labor cost, the productivity of China is still lower than other developed countries. For example, in 2010, the labor productivity of China was only \$11,612, comparing with the developed countries like U.S.A (\$102,903), France (\$81,977) and Japan (\$68,764) the labor productivity of China was very low (Japan Productivity Center, 2011). Whereby, the relative advantage of labor cost in international competition is not as obvious as the absolute advantage.

Secondly, the major part of labor cost of China is labor compensation which is composed of wage of employees and social insurance contributed by employers. According to the national sample investment on labor cost, labor compensation

accounts for around 80% of labor cost (Zhang, 2009). Due to the improvement of social security system and regulations on labor protection, social insurance cost is increasing rapidly in recent years. As shown in Figure 1.2, according to the report of U.S. Bureau of Labor Statistics (2012), average hourly compensation costs of manufacturing employees in China continued to increase from 2002 to 2009, of which social insurance cost has increased approximately 336%, higher than the increase of basic wage (146%).

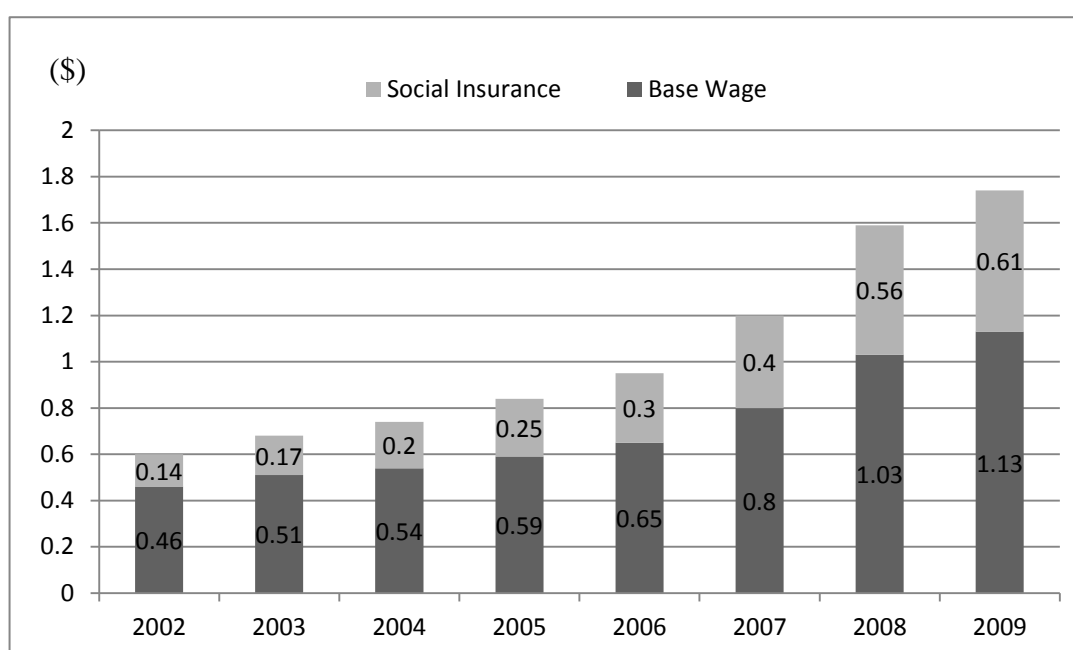


Figure 1.2 Average Hourly Compensation Costs of Manufacturing Employees in China by Components of Compensation, 2002-2009

Note: Data labels are rounded values.

Source: U.S. Bureau of Labor Statistics, International Labor Comparisons (2012).

Thirdly, there are great diversities among areas and industries. China has a vast territory, and the different economic situation of different places has resulted in a great diversity of labor cost in different areas and industries. Generally speaking, labor costs in eastern coastal areas, foreign invested enterprises, share-holding corporations and modern service industries are relatively higher. Judging by the

average wage of employed persons in urban units by region, in 2010, the average wage of Shanghai was, the highest, 66,115 RMB, Heilongjiang was the lowest of 27,735 RMB, and the average wage of Shanghai was 2.38 times of Heilongjiang. For the average wage by status of registration, in 2010, share-holding corporations Ltd. had the highest average wage, 44,118 RMB, followed by foreign funded units of 41,739 RMB, and urban collective-owned units and other domestic funded units (24,010 RMB and 25,253 RMB respectively) have the lowest wage. By industries, financial intermediation was 70,146 RMB, construction was 27,529 RMB, hotels and catering services was 23,382 RMB (National Bureau of Statistics of China, 2012).

Fourth, the increasing trend of labor cost is basically in accordance with the economic development in China. Figure 1.3 shows the relationship between the average wage increase rate of employed persons in urban units and the per capita GDP growth rate.

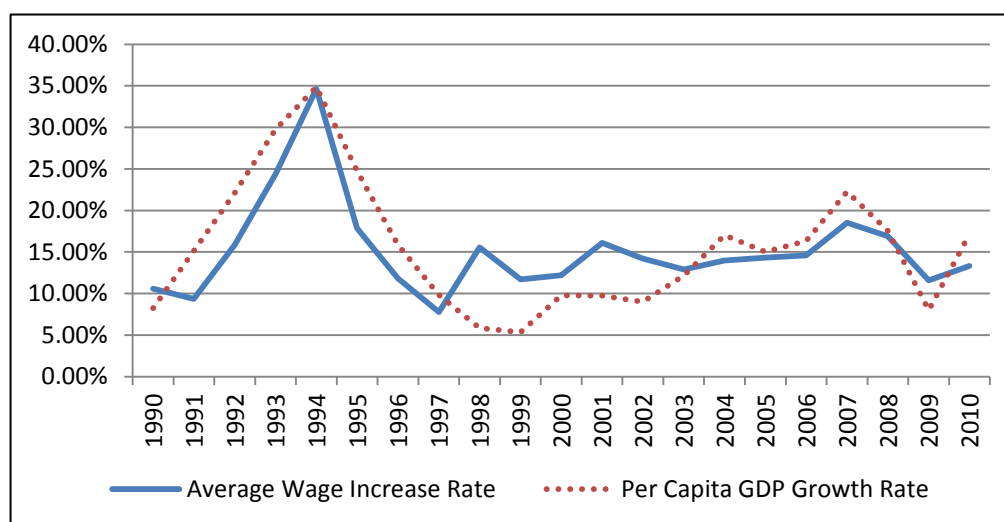


Figure 1.3 The Average Wage Increase Rate of Employed Persons in Urban Units and the Per Capita GDP Growth Rate.

Source: National Bureau of Statistics of China (2012)

As shown in Figure 1.3, in the period of 1997 to 2003 and the year of 2009, the increase rate of average wage were beyond the growth rate of per capita GDP, but for the rest of years were lower than growth rate of per capita GDP. From 2000 to 2010, the average increase rate for wage reached 14.42%.

Finally, the major contributors for the rising labor costs in manufacturing industries of China, especially in urban area, can be briefly summarized in the following aspects:

a) The income of employees continues to rise. In recent years, the rising of commodity prices and inflation are very distinct. In 2006, China's Consumer Price Index (CPI) is 101.5 (previous year is 100), and reached to 104.8, 105.9 in the following 2 years, but decreased to 99.3 as the global economic crisis of 2008 has impacted the general price level in China. However after 2009, CPI continued to rise and reached to 103.3 and 105.4 separately for 2010 and 2011 (National Bureau of Statistics of China, 2006-2011). Thus, people need more money to maintain their usual living standards. In the meantime, housing in urban areas has become a major social as well as economic issue, whereby employers have to increase salaries to allow workers to pay higher rents or mortgages (Balchin, Isaac and Chen, 2000). Additionally, education and medical service costs continue to rise, which also become a major driving force for the increase of labor costs. b) In China, social insurance accounts for approximately 20% of labor costs, and 60% of the non-wage (or indirect) labor costs (Zhang, 2009). The Chinese government has concentrated on the completion of social security system since the 1980s, and with the implementation of social insurance, China has established a formal social insurance system including Basic Pension Insurance, Basic Medical Insurance, Unemployment Insurance, Work Injury Insurance and Maternity Insurance. With the improvement and legislation of the social insurance system, number of contributors has increased continually, implying for a growing social insurance contribution burden for the

employers (in China, the contribution of the social insurance is shared by the government, the employer and the employee).

1.1.2 Urbanization Process of China

With the high speed of economic growth of China, urbanization has accelerated by the increase of urban population and the number of cities and towns (Li and Piachaud, 2006; Wang, Zhou, Sun and Zhu, 2009). Unlike the “parallel-urbanization” (an urbanization process developed synchronously with the economic growth in developed countries) or the “over-urbanization” (which outpaced economic development and industrialization process of some developing countries), the urbanization process in China is known for its unique feature – whereby most of the researchers believe that the urbanization process in China lags behind economic growth (Konrad and Szelenyi, 1974; Ofer, 1980; Lin, Cai and Li, 1994; Dong and Putterman, 2000). From a historical perspective, as shown in Figure 1.4, since the establishment of People’s Republic of China in 1949, urbanization in China has demonstrated positive trends. From 1949 to 2011, the urbanization rate has increased by 40.53 %, from 10.64% to 51.27%.

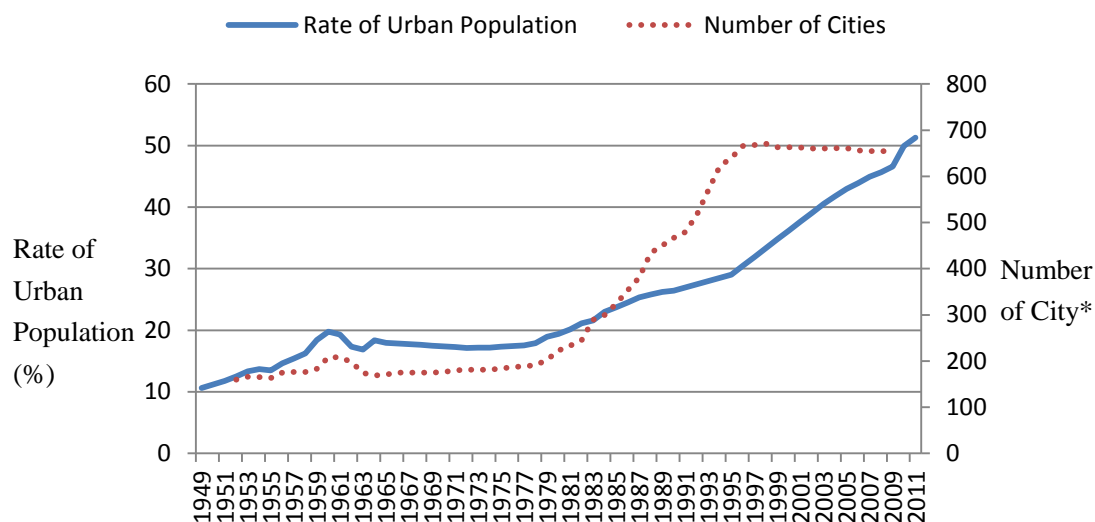


Figure 1.4 Urbanization Process in China, 1949-2011

* According to City Planning Law of the State Council of P. R. China (1989), CITY refers to a municipality directly under the central government, a city or a town based on the administrative division of the state.

Source: National Bureau of Statistics of China (2012)

The most significant turning point of the urbanization process since 1949 is the implementation of the Reform and Open Policy in 1978, which divided the Planned Economy and Market Economy, and greatly influenced every field of economic and social development of China, including the urbanization process. Therefore, the urbanization development of China is usually divided into two parts: before and after the Reform and Open Policy of 1978, or “pre-reform era” and “post-reform era” for short (Mou, 2006; Guang, 2008).

1) Urbanization in Pre-Reform Era

Before the implementation of Reform and Open policy (1978), China was under a highly centralized planned economy system. Urbanization development of this period was greatly influenced by a series of policies and historical events, such as policies to control urban population, first Five Year Plan, the “Great Leap Forward”

campaign and Cultural Revolution. Figure 1.5 shows the timeline of the major historical events and the urbanization development during 1948 to 1977, which will be elaborated in the following sections.

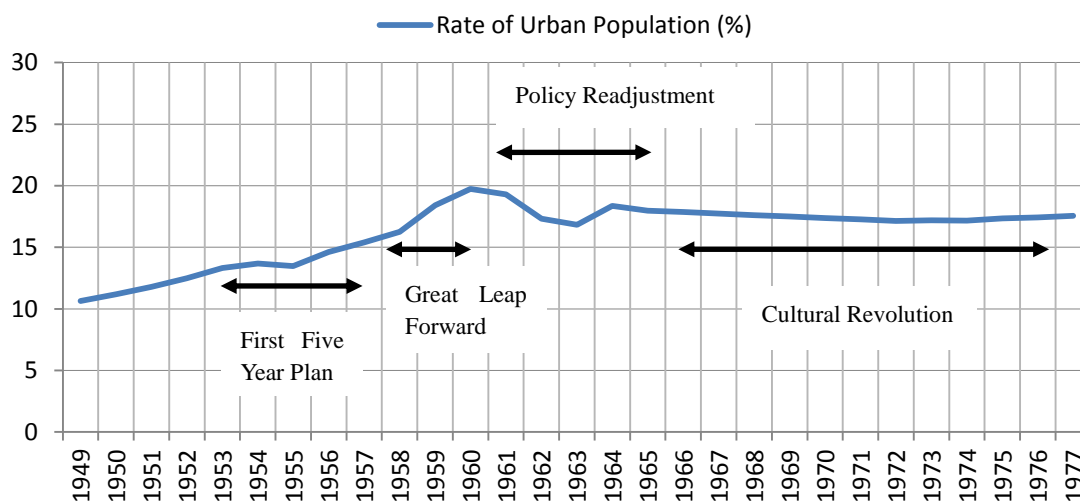


Figure 1.5 Urbanization Process and Major Historical Events in China, 1949-1977

From 1949 to 1952, the socialist country of China was just established, the major task of Communist Party of China (CPC) and the government was to recover the national economy and reorganize the political system. A series of measures were taken, including redistributing of rural land among peasants, confiscating bureaucratic capital, stabilizing price of commodities, and adjusting industrial and commercial policies. Urbanization development of this period (1949-1952) was smooth and synchronized with the economic recovery. After a brief “rehabilitation”, the first Five Year Plan was proposed in 1953, aiming at realizing socialist industrialization. In order to imitate the socialism mode of the Soviet Union, the development of heavy industries was given priority. A large number of mining and industrial processing cities were built coinciding with the redevelopment of selected old industrial cities (Kamal-Chaoui, Leman and Zhang, 2009). When the first Five Year Plan was accomplished in 1957, a city industrial system with highly-developed division of labor was set up (Sachs, Hu and Yang, 2003). As more and more rural

labors were absorbed into urban industrial sectors, it had resulted in a heavy burden on agricultural production. The Chinese government subsequently set up a resident registration system, and a temp regulation (*About Setting up Regular Hukou Registration System*) was issued in 1955, requiring all the residents (both rural and urban) to obtain the official approval before changing places of residence, which explained the slight decrease of urbanization rate in 1955. On the whole, the urbanization development of the period from 1949 to 1957 was smooth, and the overall rate of urbanization increased from 10.6% to 15.39%.

In the second Five-Year Plan period (1958-1962), aimed at rapidly transforming China from an agrarian economy into a communist society through rapid industrialization and collectivization, Mao Zedong started an economic and social reform campaign, known as the Great Leap Forward. Massive rural-urban migration was encouraged by the government to supply labors for the heavy industry development. And this situation was deteriorated by a widespread famine in the countryside which resulted in a rapid increase of urban population (McGee *et al.*, 2007). From 1956 to 1960, the urban population increased to 388.8 million, of which 26.6% (103.4 million) was natural increase, while the rest 73.4% was caused of other reasons, such as rural-urban migration and the increase in the number of cities (Li, 1999). On the contrary, the economy sagged because of the natural calamity and the deterioration of the relationship between China and Soviet Union. Facing this situation, the central government issued *Nine Measures to Reduce Urban Population and Compress Urban Provisions* (The State Council of P. R. China, 1961) to control the increase of urban population. In addition, a readjustment on the Chinese economy was started after the Great Leap Forward campaign to cool off the enthusiasm of rapid industrialization (Sun, 1994). With the shutting down of most heavy industries, rural labors that migrated to the cities during the Great Leap Forward campaign were sent back to the rural areas. Therefore, the urbanization process of the period from 1958 to 1965 was artificially fluctuated which was visually shown in Figure 1.4.

In 1966, Mao launched the Cultural Revolution to unsettle the “ruling class” and keep China in a state of “perpetual revolution” that served the interests of the majority, rather than tiny elite (Feigon, 2002). The Cultural Revolution (1966-1976) caused chaos across the country, and millions were persecuted because of the extreme ideas of eliminating class stratification and old ideologies. Schools were closed and the young intellectuals living in cities were forced to perform hard labor work in the countryside to be "re-educated" by the peasants. 14-18 million urban youth, 10-12% of China's total urban Hukou population, were deprived of their urban Hukou and sent to rural areas during this period (Kamal-Chaoui *et al.*, 2009). The increase of urban population slowed down, and urbanization rate was nearly stagnant. With the deterioration of the relationship with Soviet Union and the threaten of U.S.A, the Chinese government transferred the construction of national defense, science and technology, industry and transport facilities to middle and western areas to prepare for the possible war. As the government invested most of manpower and material resources into remote mountain areas, the urbanization development and constructions of this period were hardly proceed (Guang, 2008). In 1966, urban population accounted for 17.9% of the total population, and it remained the same in 1978.

In general, in the Mao era from 1949-1978, the urbanization pace of China increased slightly in the first 8 year till 1957, but increased sharply during the Great Leap Forward period (1958-1962), and almost remained unchanged during the Cultural Revolution period (Li, 1999; Mou, 2006; Guang, 2008; Wang *et al.*, 2009).

2) Urbanization in Post-Reform Era

After the implementation of Reform and Open policy in 1978, there was a great improvement on economy level, social development and comprehensive national power, the development of urbanization also increased steadily, urbanization

rate increased from 17.92% of 1978 to 46.49% of 2009, and the average year increase rate reached 0.92%, while number of city also rise sharply from 191 to 665. However, since 1978 when the Reform and Open policy was implemented, China was in the stage of transforming from planned economy to market economy, recessive urbanization (although some rural migrants live in cities, they are not formal registered permanent residences, so they cannot join urban social endowment insurance and other social welfare for urban residents) and quasi-urbanization (the public infrastructures in some urbanized small cities and towns are very poor, and although some urban residents have been registered in urban Hukou system, they still need work in agricultural industries.) were the main features of China urbanization process (Guang, 2008).

In 1978 the Chinese government began the reform on the rural economic system and carried out “household contract responsibility system” which aroused the enthusiasm of farmers. In the meantime of rising productivity in rural areas it has brought about large surplus labors which have offered a possibility for the quick urbanization of China. In 1984, a city-centered national economic system reform was issued, the industrial development, infrastructure construction, management level of cities were further improved. After the opening of four Economic Zones (Shenzhen, Zhuhai, Xiamen, Shantou) the government developed another 14 coastal port cities (Dalian, Qin Huangdao, Tianjin, Yantai, and Ningbo etc.), the open policy propelled the economic growth of coastal areas and also accelerated the urbanization development in these areas. During this period, rural township and village enterprises (TVE’s) were blooming because markets for land and labor really emerged only in the 1990’s and financial institutions were still in the midst of a gradual process of adaptation to market forces (Oi, 1993; Naughton, 1994; Pei, 1999; Sachs *et al.*, 2003). From 1978 to 1991, city number increased by 288, the number of towns rose from 2173 to 12455, and urbanization rate increased by 9.02%.

Since 1992, the socialist market economy of Chinese characteristics was being improved, and urbanization process accelerated because of the motivation of economic growth. The Central Committee of the CPC adopted active financial policies, constructed infrastructures (for example, highways, electric railways, ecological environmental protection projects) and by issuing national debt through banks to make full use of surplus productivity (Gu, Wu and Cook, 2012). The government also carried out policies to encourage the economic development in coastal areas which attracted large number of rural surplus labors, manufacturing industries in coastal cities began to prosper during this time. Meanwhile, the distribution of towns and township enterprises was gradually centralized, and it has had positive influences on the economic development and urbanization process around it. Moreover, the nation became more proactive in international business affairs and policies of relaxing or eliminating restrictions for foreign investment have boosted the development of foreign invested enterprises. This Open Door policy then gradually expanded to inland areas (such as provincial level capitals) and promoted the nationwide urbanization development greatly (Guang, 2008; Meng and Wang, 2011). By the end of 2011, the urbanization rate had reached 51.27%.

At least four driving forces are considered as the factors that facilitate Chinese urbanization in the post-1978 era. First, the implementation of “household responsibility system” in the countryside has greatly increased the agricultural productivity and led to a large amount of surplus labors in the countryside. Second, relaxed state control over population mobility has allowed people to move freely among cities and places. Third, the implementation of open-door policy has encouraged local government to attract foreign investments by establishing “development zones”. Most of these zones were located in the economically advanced coastal regions, particularly in the suburb of large cities, such as Shenzhen, Zhuhai, Shantou, Xiamen, and Hainan, creating constant demand for labor (Liang and Ma, 2004; McGee *et al.*, 2007; Logan, 2008). Fourth, the ever growing income

gaps between urban and rural areas have stimulated rural people to move to cities for better lives.

To conclude, the researcher believes that urbanization development process of China before the implementation of Reform and Open Policy of 1978 was mainly artificially controlled by the government, and natural growth of urban population was twisted by a series of historical events. After the implementation of Reform and Open Policy in 1978, which symbolized the beginning of market economy, urbanization development of China is market and economy oriented with government macro control.

1.2 Statement of the Problem

China, as a developing country, is experiencing an unprecedented economic and social development. Urbanization is a natural part of this ongoing development of China, and having profound impacts on promoting economic growth, improving people's living conditions, and integrating social network (Tellnes, 2005; McGranahan and Tocoli, 2006). Although the rapid urbanization have caused a series of problems, such as excessive consumption of land for industrial growth, extended urban-rural income gap, rising living cost in cities, and "urban diseases" like traffic congestion, shortfall in resources and infrastructure capacity as well as environment pollution (Song and Ding, 2007; Wagner, 2008; Ning, 2012), urbanization is "the road that China must take in its modernization drive, and it serves as a strong engine for sustainable and healthy economic growth" according to The National New-type Urbanization Plan (2014-2020) (The State Council of P. R. China, 2014).

The rising labor cost is another inevitable phenomenon of the ever-growing industrialization and modernization of China. Fast-rising wages, worker activism, and intermittent labor shortages that caused by the declining of working age (15-64) population are implying that China is running out of its cheap labors (Minami and Ma, 2009; Das and N'Diaye, 2013). Besides analyzing the consequences of the rising labor cost to the Chinese economy, researchers and scholars also have had a hot discussion on the reasons or the impact factors of the rising labor cost. However, the researcher believes that urbanization and the change of labor cost in China are closely related. Because there is a direct connection between urbanization and labor cost change – rural migrant worker. On one hand, the large number of rural migrant workers has provided cheap labors to the urban labor market; on the other hand, it has accelerated the urbanization process and city development in China. Urbanization is an important phenomenon of social development, it always accompanied with market economy, competition, division of labor, industrialization, and changes in urban life as well. With the economic growth and the quick urbanizing process, the living costs in urban areas, including education fee of children, rent or purchase housing, medical care and other costs, have risen greatly. Thus, people need higher income to maintain a standard life in cities. In addition, knowledge accumulation in urban environments will lead to improved worker productivity, and the productivity growth will stimulate wages (Mincer, 1974; Willis, 1999), meaning urbanization has positive effect on the income of employees by increasing the population education levels. Meanwhile, due to the intense competition, employers will provide job training programs to improve the employees' working proficiency and efficiency and offer more welfare benefits to attract and retain talented people. All of the aforementioned changes are caused by urbanization and will possibly impact labor cost of enterprises. No researcher has done this assessment theoretically or empirically in China. Therefore, this study is designed to test the possible relationship between urbanization and labor cost, and give a rational explanation on the impact of urbanization on labor cost in China.

1.3 Objective of the Study

To examine the impact of urbanization on labor cost, this research has the following objectives:

1) To identify the major components of labor cost in manufacturing industries of China, and investigate which component is rising.

2) To empirically identify the rising situations of labor cost in manufacturing industries of China, and the possible differences based on the size and ownership of the enterprises.

3) To identify the factors those have influenced the change of labor cost under the urbanization process.

4) To discuss how the factors of urbanization impact labor cost in manufacturing industries of China and recommend policies for the government and enterprises.

1.4 Research Questions

1) What are the major components of labor cost in manufacturing industries of China? And which components of labor cost are rising?

2) How do these components of labor cost change in manufacturing industries of China? And are there differences based on the size and ownership of the enterprises?

3) What are the impact factors for the change of labor costs under the urbanization process in China?

4) How do these factors impact labor costs in manufacturing industries of China?

1.5 Significance of Study

The rising labor cost has drawn lots of scholars and researchers' attention (Cai, 2007; Ceglowski and Golub, 2007; Cai and Wang, 2008; Ang, 2010), and there are also many studies on urbanization (Li, 1999; Madlener and Sunak, 2011; Guang, 2008). But there is still not a systematic analysis on the relationship between labor cost and urbanization, both of which are significantly affected by the economic and social development of current China. Therefore, this study attempts to examine the relationship between urbanization and labor cost, namely how urbanization impact the change of labor cost in China. The study is significant in the following aspects:

First, this study gives a relatively integrated description of labor cost on its components and changing trends in China. And the labor cost in manufacturing industries will be elaborated based on the comparative study on enterprises of different size and ownership. This will offer references for the scholars, researchers and whoever is interested in labor costs study.

Second, urbanization is an important token of social development, studying on the relationship between urbanization and labor cost will expand the theories of urbanization, and be beneficial for the government in making the city developing policies.

Third, research on labor cost, analyzing its changing trends will provide information for the enterprise that are planning or experiencing the transition from labor intensive industries to technic intensive industries. As the rising of labor cost is inevitable in China, manufacturing industries need to maintain market competitiveness through technique innovation and cost reduction. Analysis on the impact factors of the change of labor cost from the perspective of urbanization will

diversify the suggestions and measures on minimizing the negative effect of the rising labor cost for the enterprises.

Fourth, modeling labor cost with urbanization is a fresh combination of the two different concepts. Multiple research methods and data collection techniques are used in the study, and these may be helpful for the other researchers.

1.6 Scope and Limitation

Urbanization is a comprehensive concept of multidiscipline (Wu, 2006). It can be defined and studied from different fields of economics, demography, sociology, and environment science. In this study, theories and literatures on urbanization study mainly focused on the process of urbanization in China and its influence on economy and society from the perspective of demography and sociology. Additionally, urbanization is an abstract expression, while in the research of this study it will use concrete data of population, i.e. urban population's proportion on the total population, to describe the urbanization level of certain area. Furthermore, there are disputes on the urbanization level of China, where some scholars have revised the official data on urbanization level (Zhang and Zhao, 1998; Zhou and Ma, 2003), but a common revising standard is still needed; on the other hand, the official data are more authoritative and comparable, and, more importantly, official data is the major reference for the government making relevant policies. Therefore, data used in this study are official data from China Statistical Yearbook or other official publications.

Labor cost has an international generally accepted concept, to be specific, it includes basic wages, cost-of-living allowances, and other guaranteed and regularly paid allowances, bonuses and remuneration, employer contribution to social insurance, unfunded employee social benefits, cost of training and taxes regarded as

labor costs (International Labor Organization, 1999). Because of the complex contents of labor costs, usually people use compensation or even wage which account for the major part of labor cost to measure the value of labor cost. Unlike compensation measurement way of Bureau of Labor Statistics (U.S.A), industry earnings data from Chinese publications refer only to urban manufacturing units and do not include required employer social insurance payments or other nonwage labor costs (Zamora and Kirchmer, 2010). Therefore, in this study, when using the value of compensation to estimate or analyze the changing trend of labor cost, data are calculated by the researcher based on data on wage and social insurance contributions.

The sample of the study is limited to the manufacturing industries in Hebei province. However, there are two limitations. Firstly, China is a vast country spanning thousands of miles from western deserts to eastern ocean, each province, and even each city has unique economic and social situations, thus a single case cannot stand for other provinces real condition. Finally, as the interpretations of the research findings are inevitable subjective, therefore there are discrepancies between the research results and reality.

1.7 Why Hebei Province

China is a country with vast land, and there are 34 provincial level regions, including 23 provinces (Liaoning, Jilin, Heilongjiang, Hebei, Shanxi, Shaanxi, Shandong, Anhui, Jiangsu, Zhejiang, Henan, Hubei, Hunan, Jiangxi, Taiwan, Fujian, Yunnan, Hainan, Sichuan, Guizhou, Guangdong, Gansu, and Qianghai), 4 municipalities directly under the control of Central Government (Beijing, Tianjing, Shanghai, and Chongqing), 5 Autonomous Regions (Guangxi, Inner Mongolia,

Ningxia, Xinjiang, Tibet), and 2 special administrative regions (Hong Kong and Macao). Because of complicated reasons, such as natural resources, geographical environments and population, there are distinct regional differences in social and economic development. Therefore, choosing a right province to study the impact of urbanization on labor cost and hopefully to reflect the conditions in the whole nation is a difficult and challenging work. Synthesizing complex factors, Hebei province is chosen as the research objective in the end.

Hebei province is located in north of China with an area of 187.7 thousand square kilometers. The topography of Hebei slopes from the northwest to the southeast with complicated and varied landforms. Hebei is the sole province with seashore, plains, lakes, hills and plateaus and has a large quantity and variety of natural resources. Hebei province surrounds Beijing and Tianjin, the Beijing-Tianjin-Hebei economic zone is the economic center of northern China and becomes one of the most powerful regions in overall strength. With a population of 72 million, Hebei province has abundant labor forces, which makes it a labor-exporting province. There are 11 prefecture-level cities in Hebei province, and subdivided into 172 county-level divisions. Figure 1.6 presents the location of Hebei province in the map of China and Table 1.1 gives an overview data of Hebei province in 2011.



Figure 1.6 Location of Hebei Province

Table 1.1: Overview of Hebei Province in 2011

	Hebei Province	Whole Nation*	Rank in Whole Nation*
GDP (100 million RMB)	24,515	472,881	6
Per Capita GDP (RMB)	33,858	35,097	14
Number of Industrial Enterprises above Designated Size**	11,570	325,609	11
Gross Output Value of Industrial Enterprises above Designated Size** (100 million RMB)	39,699	844,268	7
Population	72,405,100	1,347,350,000	6
Household Consumption Expenditure (RMB)	9,551	12,272	21
Average Wage of Manufacturing Industry (RMB)	22,159	24,138	15
Urbanization Rate (%)	45.6	51.27	21

Source: National Bureau of Statistics of China, 2012

* Data of Mainland (31 provinces), not including Hong Kong, Macao and Taiwan.

** Industrial enterprises include mining, manufacturing and production and supply of electricity, gas and water. Designated Size refers to enterprises with an annual sales over 20 million RMB.

With reference to Table 1.1, in 2011, GDP of Hebei province was about 2.451 trillion RMB (US\$379 billion), an increase of 11.3% over the previous year and ranked 6th in the whole nation. The primary, secondary, and tertiary sectors of industry contributed 11.9%, 53.5% and 34.6% respectively (Hebei Economic Statistic Yearbook, 2012), which means secondary industries (including mining, manufacturing, production and supply of electricity, gas and water, and construction) are the major driven forces for the economic growth in Hebei province. And it also can be proved by the number of industrial enterprises and gross output value of industrial enterprises, both of which were higher than the national average level, ranked 11 and 7 separately.

According to the sixth National Census, Hebei province has a population of 71.9 million in the year-end of 2010, and increased to 72.4 million in the year-end of 2011 and 45.6% are urban residents. The large population is a two-edged sword, it provides abundant cheap labor forces, and on the other hand, problems such as fast aging speed and the brain drain become obstacles for the economic growth and society development in Hebei province. Table 1.1 shows that household consumption expenditure and urbanization rate of Hebei province are below the national average level and only ranked 21, which indicates that social development of Hebei province is lagged behind by economic development.

Therefore, the reasons to choose Hebei province can be summarized as: first, Hebei province can represent the average economic and social development condition of China, because no matter economic development or the social development, Hebei province is in the medium position of 31 provincial regions and close to the national average level. Second, the large number of secondary industries could provide sufficient data for the studies on the changing labor cost in manufacturing industries. Third, the urbanization process in Hebei province is found slightly lagging behind economic growth which shares the same condition with the

urbanization development on the national level (Chen, Lu and Liu, 2010). So findings on the impact of urbanization on labor cost changes in Hebei province can be representative of China, and be applied to other provinces for future study. While choosing Hebei province as the research objective may not completely reflect or explain what China is experiencing, it is a good option for this exploratory study.

1.8 Research Process

The thesis of urbanization and labor cost is an exploratory study, rarely research can be found for this topic, thus several questions are proposed in different research phases to make sure the study is a valuable work, such as “is my topic interesting”, “is my research doable”, and “is my survey is a valid survey”? The research process is shown in Figure 1.7.

The initial works of the research are topic selection, background reading and develop the research strategy. When the topic is deemed as interesting, literature review can be proceeded followed by the development of theoretical framework and conceptual model. As a sequential mixed method is used in this study, qualitative data collection and analysis will be conducted firstly to build to the survey questionnaire. The following work is quantitative data collection and analysis, and the research process will be end after the report is prepared.

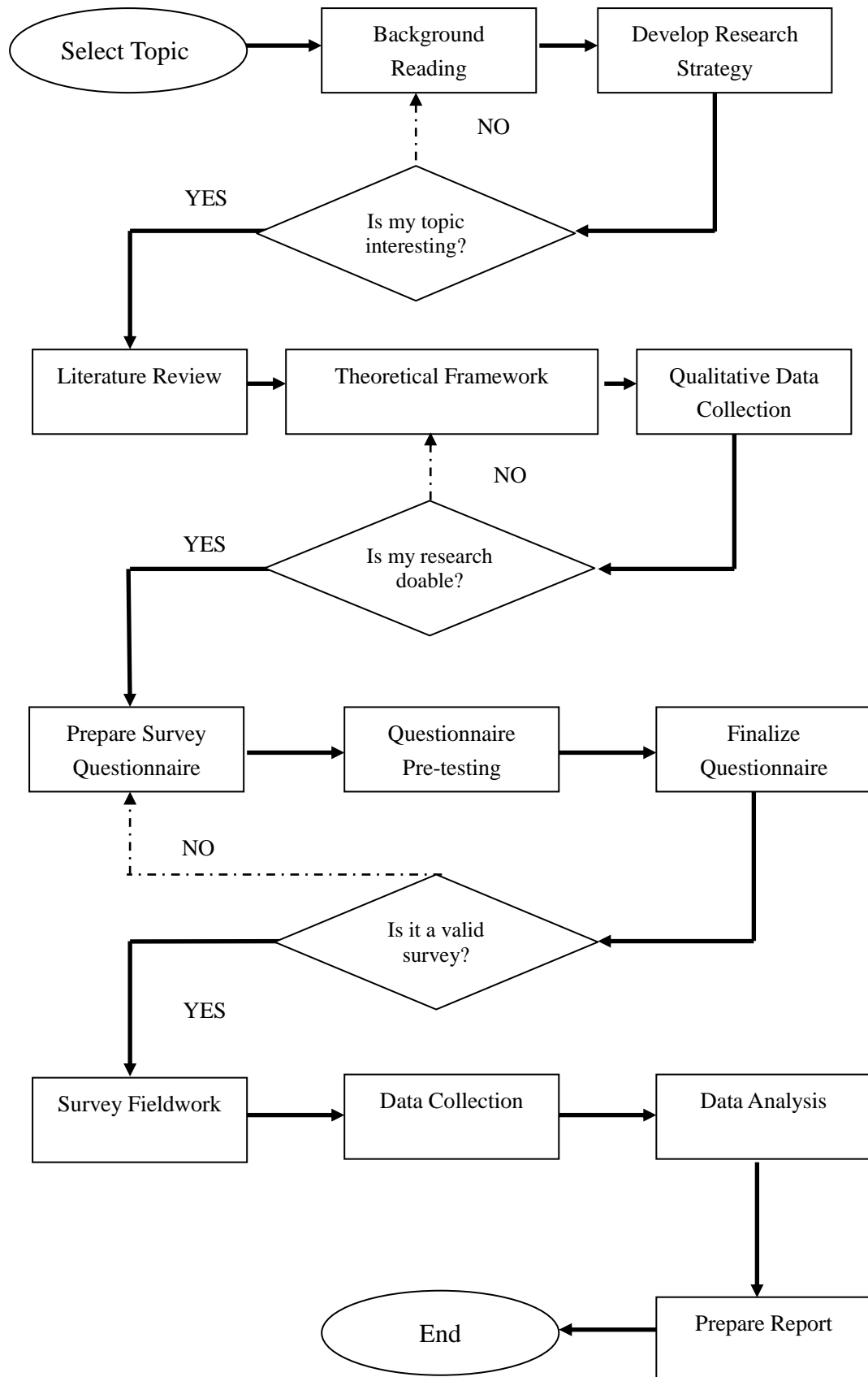


Figure 1.7 Research Strategy

1.9 Definition of Terms

1) Urbanization

Urbanization is a natural part of development (Henderson, 2002), whereby people keep agglomerating in cities, making the scale and numbers of cities to increase accordingly. There are many different definitions of urbanization given by the scholars from multi-perspectives, such as Morikawa (1989) defined urbanization as the transformation process experienced by rural population toward an urban life style, showing as the increase of urban population, the expansion of urban built-up area, the creation of landscape and urban environment with social and life style changes. Werner (1990) defined urbanization as the transformation of economy from rural economics which is labor intensive, sparsely populated and evenly distributed to urban economics which has the basically opposite figures. While the Japanese economist Yamada (1991) believed that the content of urbanization can be divided into two parts: one is the urbanization phenomenon of economic bases; the other is the urbanization phenomenon of social culture (superstructure). From the perspective of the Chinese researchers, Xie and Deng (1996) argued that urbanization is a changing process of human producing modes, living patterns and inhabiting ways which is led by the reform of social productivity; whereas Qi (2004) stated that urbanization ultimately is a form of social evolution of industrialization and economic structure in one country or an area.

For the study of this thesis, the researcher defined that urbanization is a process of the continuous increase of urban population and transforming of industrial structure, and it will gradually integrate urban and rural society through disseminating city civilization to rural areas. Besides, the researcher needs to highlight that the urbanization rate or urban population addressed in this thesis was calculated or refers to the people who are permanent urban residents (with or without

urban *Hukou* – household registration system).

2) Labor Cost

Labor cost means the employer's cost of hiring an incremental unit of labor, all costs of employment are included, not just direct wage payments (Triplett, 1983; International Labor Organization, 1999). To better understand the concepts of labor cost, a comparison among the definitions of Wage, Earning, Labor Compensation and labor cost was presented in Figure 1.8.

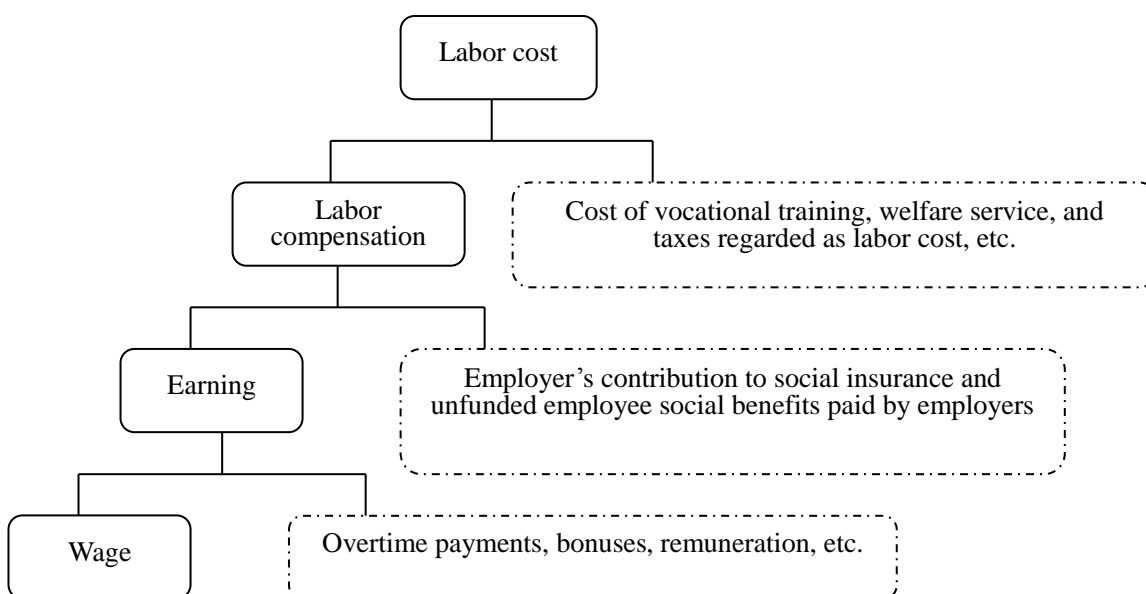


Figure 1.8 Concepts and Relationships of Wage, Income, Labor Compensation and Labor cost

Source: Summarized according to the terminologies of International Conference of Labor Statisticians (ICLS), International Labor Organization (ILO), 1999

In Figure 1.8, higher layer means more contents for the item. Wage refers to the basic payment, cost-of-living allowances, and other guaranteed and regularly paid allowances; earning is wage plus overtime payments, bonuses and remuneration; labor compensation includes earning and social insurance cost of the employers; labor cost, on the top layer of Figure 1.4, has the broadest concepts or contents –

including labor compensation and other labor-related cost.

3) Perceived Change of Labor Cost

Perception is the organization, identification, and interpretation of sensory information in order to represent and understand the environment (Schacter, Gilbert and Wegner, 2008). In this thesis, perceptions on the change of labor cost or perceived change of labor cost are defined as the change of labor cost that is measured by observation, insight and experience.

4) Manufacturing Industry

Manufacturing industry includes the physical or chemical transformation of materials, substances, or components into new products. The raw materials are products of agriculture, forestry, fishing, mining or quarrying as well as products of other manufacturing activities (United Nations, 2008). China follows the same definition and classification of manufacturing industry. There are 30 sub-categories of manufacturing industries in China (refers to Appendix A), and based on which the manufacturing enterprises that studied in this thesis are selected.

1.10 Plan of Thesis

There are five chapters in the thesis. Chapter one gives an overview to the thesis and proposes the problem. Chapter two reviews the literatures of urbanization and changing labor cost in China, and discuss the theoretical framework and conceptual models for the study. Chapter three is methodology. In this chapter,

research methods of the study are introduced in details, including data collection methods, data analysis tools, population and sample, and research variables and hypothesis. Chapter four presents the results of the qualitative and quantitative data analyses. And in the end, Chapter five makes a conclusion for each research question, provides implication of model development and implications for the government and the enterprises, and suggests the future studies. Figure 1.9 gives a visual description of the plan of the thesis.

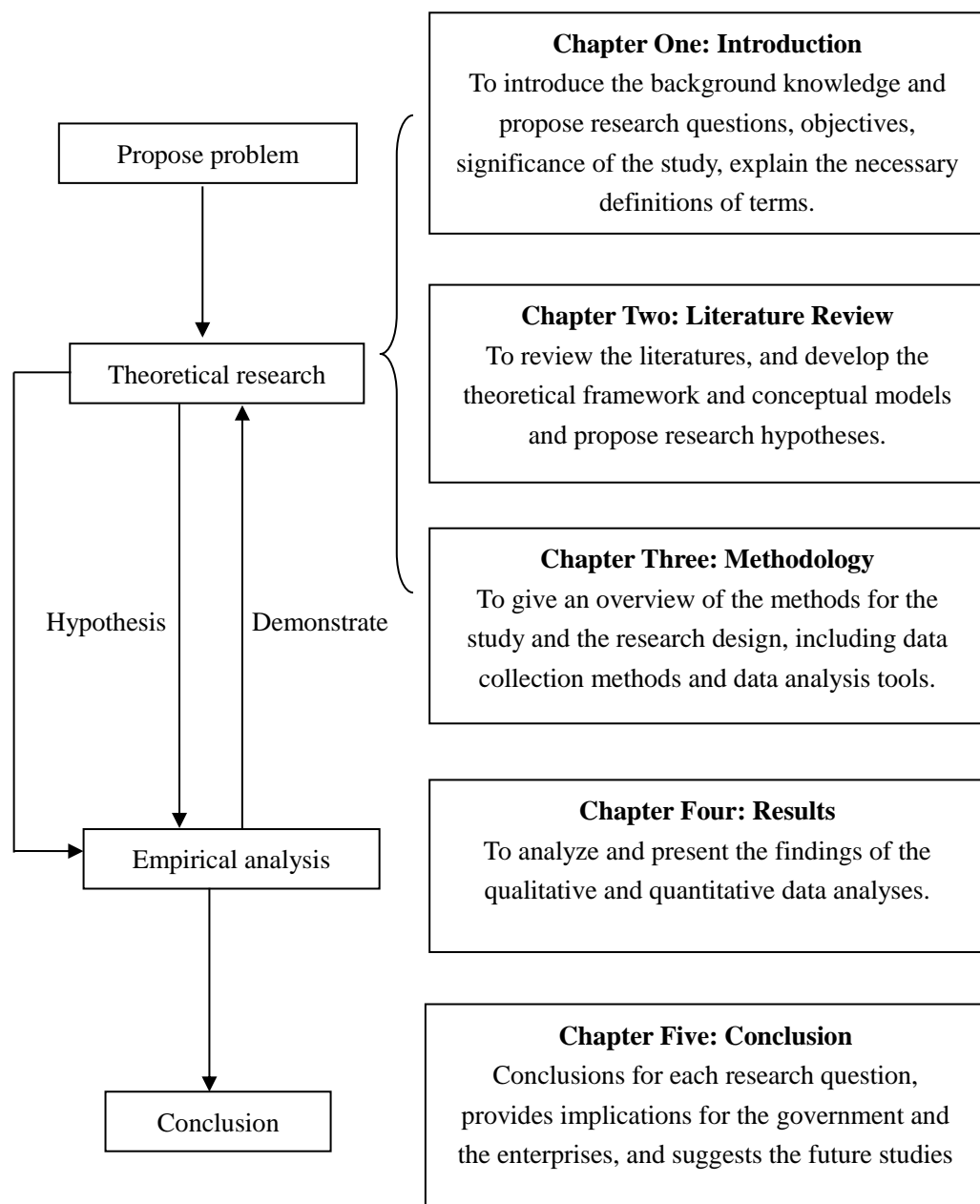


Figure 1.9 Plan of Thesis

In this study, the research on the relationship of urbanization and change of labor cost is based on a series of expert opinion assessments and survey questionnaires which are more micro, and the change of labor cost is evaluated through respondents' perceived change. Therefore, future study may be conducted from the macro perspective, developing a mathematical model and using official statistical data.

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