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CHAPTER 3 Economic Activity in a Changing World

Moving Up the Ladder: From Cheap Labor to Skilled Workers

by Mark L. Clifford in Hong Kong and Pete Engardio in Guadalajara, with Elisabeth Malkin in Ciudad Juarez, Dexter Roberts in Zhongshan, and William Echikson in Tab

Inside his cramped, two-bedroom house, in a subdivision of identical tan- and cream-colored dwellings, Jose Brigido Aguirre boasts of the changes in his life. Since he moved from his small hometown to booming Ciudad Juarez on the U.S.-Mexican border, he's found employment as a technician in a factory. Thanks to a mortgage he lined up through a program funded by the government and his employer, Delphi Automotive Systems Corp. in Troy, Mich., Aguirre, 25, now supports three generations—eight people in all—under one roof on $135 a week before taxes. After hours, Aguirre works on a manufacturing engineering degree at a local college in the hopes of further boosting his standard of living. And he wants to put his three younger siblings through school. ''I have plans for them to study so we can all make something of ourselves in life,'' Aguirre says.

RACE TO THE BOTTOM. Aguirre's story is one piece of evidence that globalization can lift up the poor. Yet in spite of thousands of stories like Aguirre's, not everyone will come away from Juarez impressed. The overcrowded city of 1.5 million is a ramshackle sprawl of cinder block houses and dirt roads. Each year it attracts as many as 80,000 new workers willing to work for less than $10 a day, plus benefits, at *maquiladoras*—factories that assemble goods for export, mainly to the U.S. To critics of globalization, these roaring plants, fueled by endless supplies of cheap labor, simply prove that free trade has triggered a desperate ''race to the bottom'' by the world's workers.

But that is a distorted picture—and one that in many developing nations is looking more and more at odds with reality. As U.S. companies continue to upgrade their Mexican operations to profit from the 1994 North American Free Trade Agreement, they are offering ambitious workers like Aguirre better careers, training, and benefits. Nations such as Hungary, Malaysia, and even China also have made the leap into high-end manufacturing—improving living standards and offering better careers for many workers.

What separates the countries whose workers thrive under globalization from those that seem perpetually stuck in the screwdriver assembly stage? More than anything, it is governments that are learning to make the best use of inflows of foreign investment and manufacturing know-how. Mexico, of course, is lucky enough to enjoy duty-free access to the enormous U.S. market. And Hungary, which has become a manufacturing haven and has attracted $23 billion in investment since the Iron Curtain collapsed, borders the European Union. the economic ladder. It requires a track record of business-friendly policies to lure multinationals and domestic tycoons alike to invest for the long term—training workers, investing in modern technology, and nurturing local suppliers and managers.

It also means paying more attention to basics such as solid macroeconomic management, good public education, a thriving private sector, a legal system that protects property rights, and a society where prosperity is widely shared. These are the kind of pro-growth policies that most of East Asia employed to develop from sweatshop havens in the 1960s and 1970s to industrial powers.

Countries that have failed to get these basics right often benefit the least from globalization. Whereas almost everyone in South Korea, Taiwan, Singapore, and Hong Kong received a high-school education when their countries' export drives began decades ago, in much of Central America half of the population never makes it to the fifth grade. The record is worse in sub-Saharan Africa. Since the 1960s, the gap between rich and poor has narrowed steadily in most East Asian countries, a sign that the benefits of growth were shared widely. In the rest of the developing world, however, income gaps have yawned. Such factors go a long way to explain why big increases in trade and foreign investment in countries such as Guatemala, Nigeria, and the Dominican Republic haven't translated into major reductions in poverty.

Weak government also partly explains the appalling working conditions still found in many developing nations. China, for example, has good labor laws. But they often are not enforced. Even in China, though, the issue of labor oppression is complex. Talk to the workers and they'll take issue with many Western stereotypes of exploitation.

You won't get Mao Genhe, 29, for example, to agree that his family would be better off if Nike Inc. had never come to China, as some U.S. activists assert. He and six of his brothers and sisters have left their poor village in Hunan province and taken jobs across the country. An elementary school graduate, Mao works at a Taiwanese-owned leather tannery in the southern city of Zhongshan that supplies makers of Nike and Adidas shoes. It's often nasty working inside the hot, dank factory, where pools of water and dye stain the concrete floors.

But Mao sends up to four-fifths of his $150 monthly earnings to his parents and a blind brother back in Hunan. He bought a new plow for his parents' rice fields. Two years ago, Mao spent $5,000 to tear down his parents' old house and build a new one, furnishing it with a 21-inch color television. In five years, Mao figures, he and his wife will have the $1,200 they need to open a small grocery or clothes store at home. As it is now, Mao rarely sees his wife: She works 64 kilometers away across the Pearl River Delta, at a Hong Kong-owned electronics plant. "Our goal is we don't want to be farmers," he says.

Thanks in large part to $328 billion in foreign investment, urban per capita incomes in China have grown more than tenfold, to $705, since reform began in 1978. Chinese industry pumped out $195 billion in exports last year. Much of the income from the thousands of shoe, toy, garment, and electronics factories on China's east coast has spread far into the poverty-ravaged interior.

But it takes more than geography and low wages to move up China also shows that, from humble beginnings, industry can advance rapidly, given the right conditions and a determined government. With two decades of experience with simple assembly plants under its belt, Chinese industry is now making great strides in electronics and machinery. Millions of engineers and scientists have helped the country become a big exporter of computer equipment, auto parts, and telecom gear. Homegrown manufacturers such as Legend Computers and appliance maker Haier Group not only dominate the local market but have begun exporting to the rest of Asia and the U.S.

Other countries are just now learning to imitate this pattern of public and private investment. Mexico isn't all the way there, either. While exports have soared five-fold since 1987, to $137 billion, 47 million people still live in poverty—about half the population. And only last year did real wages catch up with 1994 levels, when the peso crashed.

One problem is that half of exports come from assembly operations that have done little to create local industry because they import most parts and materials. Another: Only 50% of Mexicans have completed sixth grade—and just 20% enter high school.

Nevertheless, companies such as Delphi are now shifting more sophisticated work to Mexico to take advantage of its supply of well-qualified technicians. Delphi has opened a research-and-development center in Juarez that employs 700 engineers developing products Delphi sells worldwide. Travel to Guadalajara, and the trend is even more dramatic. Here, IBM, Hewlett-Packard Co., and other companies have long manufactured personal computers. But since NAFTA, there has been an influx of new computer and telecom-equipment plants that require modern production lines and lots of engineers. Big contract-manufacturing companies such as SCI Systems, Flextronics International, and NatSteel Electronics make everything from Ericsson cell phones to Cisco networking equipment and Palm Pilots. Moreover, these companies pay taxes, rely almost entirely on Mexican managers, often pay high school and college tuition for workers, and have helped spawn a parts-supply industry that includes plastic moldings, metal stamping, and printed circuit boards.

The boom in electronics, which has been surging 25% annually, has enabled Guadalajara's economy to come roaring back. Since 1995, joblessness has dropped sharply. And most factory workers, even in industries other than electronics, now earn at least twice the minimum wage of $3.72 a day.

To encourage high schools to churn out the right kind of workers needed, the government distributes pamphlets listing careers available at companies, along with their salaries. It also subsidizes job training for new hires. And to broaden its industrial base, Guadalajara promotes itself at international trade fairs and is working to woo multinationals that produce everything from medical equipment to liquid-crystal displays. "We're competing against China, Malaysia, Ireland, Hungary, and Brazil," says Sergio Garcia de Alba, economic-development director for Jalisco state.

One can see in the old Soviet bloc how that competition is dividing Eastern Europe into winners and losers. Hungary and Poland are thriving, while Romania, Bulgaria, and to some extent the Czech Republic are lagging. Different approaches to privatization help explain it. The Czech Republic and Russia issued vouchers to their populations to invest in privatizing factories which seemed like a fair way to benefit the public. But that approach got mired in corruption and left insiders in charge of their enterprises. Hungary, instead, sold factories to both local businessmen and multinationals such as General Electric, Ford Motor, and Flextronics. That accelerated restructuring of the formerly state-owned dinosaurs.

Take the story of Tab, a town of 5,500 in southwest Hungary whose economy collapsed when its main business, a components plant for Russian guided missiles, shut down after Moscow recalled its troops. ''We were desperate,'' recalls Mayor Istvan Farkas. At the end of 1992, the plant was sold to a British electronics entrepreneur, who in turn was bought out by Flextronics. The U.S. company reopened the factory and brought in state-of-the-art production machines from Western Europe. Now, after an $11-million expansion, it employs 1,500 workers—twice as many as under communism—making expensive recordable-CD players, facsimile machines, and stereos for Philips and other Western brands.

Employees say they work harder now than under the Soviets, and there's no union. But working conditions and pay have improved. ''When the communists were here, we paid for a union but they did nothing for us,'' recalls assembly worker Katalin Keng, 51, who earns $150 a month. Flextronics also funded the renovation of a local secondary school, and many of the most qualified employees now are solidly in the middle class. Laszlo Zoltai, a test engineer, earns about $900 a month, lives in a decent house and drives a small Suzuki car. ''I have to work harder now, but I am proud of what I am doing for the first time,'' he says.

The problem, of course, is that not all developing nations are run by leaders who pay attention to the basic conditions needed to sustain development. If a decade from now these countries are still stuck with low-end sweatshop work, they will have themselves—not just multinationals—to blame. As up-and-comers such as Mexico and Hungary are learning, the secrets of development don't belong exclusively to East Asia. The basic requirements are smart policies—and lots of hard work.