

## Why “Made in China” Costs More in China

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While Americans are faced with continuing economic hardship and complain about cheap ‘made in China’ products undermining local manufacturing. The Chinese would likely respond that Americans are actually getting a better deal! A recent survey shows, that the [cost of living in Beijing and Shanghai](#) has already surpassed New York, even though China’s [gross income per capita 2010](#), measured by purchase power parity is only a sixth of United States.

In China, a pair of Nike shoes on sale price is almost 100 dollars. Levis jeans 799 yuan (\$122), Tommy Hilfiger T-shirts 799 Yuan (\$245). A grande sized cup of Starbuck’s coffee costs \$5.23(34 yuan); and one scoop of Haagen-Dazs ice cream costs \$4.3 (28 yuan ). Any western fashion brand from GAP to Versace, even clothings made in China, are priced 30% to several times more than the same product in the US. An Armani suit sold in US for \$ 1000, has an asking price above \$4500 (30,000 yuan) in China.

While China is the world’s factory, making most consumer eletronics, domestic consumers always have to pay more for the products made in their backyards. A 16 GB iPad is sold the in U.S for \$499, but Chinese customers have to pay an amount equal to \$757. Even the Chinese native brand Lenovo is selling at a price 10% higher than it is in U.S. An irony most Americans are unfamiliar with is that most “Made in China” products are actually more expensive in China than they are in U.S.

Considering that the average Chinese person is still making significantly less than their American counterparts, such a large pricing disparity does not make much sense. It is easy for an American to conclude that it is all due to ‘artificially under-valued yuan by Chinese government’. A charge Americans often hear from the media regarding the

trade imbalance. While such an assertion has some validity, it is only one stroke of the Chinese character.

### **Tax Exemption Is the Key**

In China, exported goods are exempted from domestic consumption related taxes. To the Chinese government, export-led manufacturing was an employment solution to absorb the massive surplus of rural labor. Tax exemption on export-led manufacturing was an accommodating strategy to encourage the growth of the manufacturing base. There are two major models of export entrepreneurship: processing on order and direct export. Processing on order plants are often set up in tax free economic zones, where foreign entrepreneurs bring in raw materials, tools, technology, etc., China supplies hard working, disciplined labor, and all finished products are shipped overseas.

The other model is direct exporting entrepreneurship which receive the same tax treatment as any other business, but they can get a full tax rebate when transaction documentation proves exportation occurred. Tax exemption is the single most important factor separating prices in China and the US.

In China the government is heavily reliant on tax collections from the logistic chains of goods flowing to domestic consumers. Almost [seventy percent of tax revenues](#) are collected from consumption related taxes (i.e. value-added, consumption, business tax, tariff, and related taxes) while the remaining 30% is from personal income, corporate income, and other taxes.

Among the consumption taxes collected, [value-added tax](#) is the most significant. Each turnover of goods going through the supply chain is subjected to a standard VAT of 17%. Food and household fuel is taxed at 13% and small businesses are taxed at 5%. This tax alone accounts for almost [60% of the](#) government's annual revenue.

[Consumption tax](#) rates range from 5% to 45%, and is imposed to 14 main categories. Goods which are deemed as luxury, harmful to your health, or depleting of rare natural resources are taxed at the highest rates. Some examples are tobacco, alcohol, jewelry, forest products etc. Business tax is imposed on service rendered transactions usually at 5%.

Since tax reform began in 1994, the annual tax revenue has grown almost twice as fast as the GDP rate. It is debated in China, that the current tax structure almost holds domestic consumption hostage. As outspoken economist [Lang XianPing](#) asserted, consumption related tax is an obstacle for China to move toward a consumption economy.

Take cosmetic products as an example, it was reported that for every 100 yuan worth of cosmetics sold, 14.53 yuan is value-added tax, 25.64 yuan is consumption tax, and 4.02 goes to urban construction tax. These three tax items alone, total 44.19% of the sale price.

Imported goods are also subjected to tariff. To sell an iPad made in China's tax free zone, Apple has to ship it out of mainland China, then ship it back through customs and pay tariffs which latest rate is 10% of it's cost.

Value-added tax is not used in the U.S. Wholesale and sales of raw materials or unfinished goods are not taxed. Only sales to end customers are subjected to sales tax with a rate generally less than 10%.

### **Inflation Eats Away the Value of Yuan**

Inflation is the other primary reason pushing price up in China. Even though China is being pressured internationally to appreciate its currency, the persistent inflation has been eating away the purchasing power of yuan in domestic market. In 1980, 1 Jin (1.1023 lb) of pork costs [0.96 Yuan](#), today the same amount costs [16 Yuan](#) (\$2.42), price increasing of 16 times in 30 years. The latest report of CPI ended in June has surged [6.4%](#) from a year ago. Empirically, many food and household item prices have gone up much more than that rate. Pork price has gone up for 70% in ten months.

Some Chinese economists believe that the current surge of inflation was caused by over supply of yuan in the past two years. To levy the effect of global financial meltdown, China issued a [4 trillion yuan](#) stimulus package, which was mainly funded as loans by the banking system. The balloon of credit rapidly increases the M2 supply; and meanwhile, China still maintains pegging to dollar even with massive surplus in current

account from export and capital inflow. In order to keep the pegging, China's central bank has to issue proportional amount of yuan into circulation for every dollar coming in, further popping up the supply of M2, and intensifying the domestic inflation pressure.

### **Logistics Still an Obstacle**

Logistical deficiency in distribution of goods apposing as one of the biggest problem for China to boost consumption. The transportation expenditure significantly adds up to the cost of goods sold.

In the past 20 years, China has built the world's second most extensive highway system, but since government funding was limited, most highways were built as investment opportunities, and are for profit.

[It was reported](#), that among the 140,000 km of toll roads in the world, 100,000 km is in China. The Chinese government tries to limit the number of tolls to one station every 50 km, but in some areas, drivers have to dig into their pocket after traveling less than 20 km. In addition to toll, random charges of fees levied by local governments along the highway also significantly add up the cost of transportation.

[Reported news](#) indicates that a kilogram of cargo shipped from Shanghai to New York costs ¥1.50 while the same weight shipped from Shanghai to Guizhou (the capital city of an inner province that is 2000km away) costs between ¥6- ¥8. This makes the total cost of shipping from Shanghai to Guizhou 4-5 times as expensive as shipping to New York, which is 11862 km away. Transportation cost added to storage, and distribution management costs, lead to logistics costs [18% of GDP](#), that's more than twice as much as the U.S

### **Yuan Pegging to Dollar Benefits U.S**

Today, China is a top exporter of the world, and 'Made in China' has become an inescapable presence in American life. But the irony is that often Chinese exports are not Chinese products. Rarely have Chinese brands made it into the consciousness of American consumers. Among the 61 Chinese companies that made into the global 500, only Lenovo is somewhat recognizable.

In reality, often 'Made in China' is only a component of the global manufacturing supply chain sitting on the lower end of the earning scale. It was reported that for an iPad produced in China, selling for \$499 in the US market, only [\\$11.2](#) goes to China.

Chinese migrant workers work long and hard on assembly lines, producing goods that are bought in dollars by U.S consumers. The Chinese central bank takes in dollars which is used to buy U.S treasury notes, increasingly on the risk of default. The Chinese workers receive yuan as compensation, while high inflation is eating away at it's purchasing power.

Chinese get the jobs, while Americans get the consumer products; Chinese government gets the dollar, but the U.S government gets to spend the dollar! Chinese like to say: the Americans get a better deal!

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