Regional Economic Integration and Internationalization for Overseas Manufacturing Plants

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Abstract

Multinational Corporations (MNCs) often set up manufacturing plants in overseas locations to save costs through inexpensive land and labor opportunities. Deciding where to invest involves many factors beyond low-cost land and labor. Free Trade Agreements (FTAs) and Regional Economic Agreements (REAs) often provide tax free exports and friendly government relations; wanting to be housed in or near a country where they do business; and opening up a plant in a sector of the world to open up opportunities in surrounding countries are all common motivations for MNCs. This paper examined factors impacting two MNCs who recently invested in manufacturing plants on foreign soil: Haier is a Chinese appliance manufacturer who signed a contract to largely expand their plant in Pune, Maharashtra, India in 2015. Honda, the infamous Japanese car makers, opened their manufacturing plant in Celaya, Mexico in 2014. Findings revealed that although REAs have benefited the two corporations, country laws and labor standards have costed them more possibly more than the agreements have benefited them. It is recommended that outside factors be considered and weighed before setting up a manufacturing plant in a country that offers free tariffs through FTAs.

Keywords: Manufacturing, Regional Economic Agreements, Multinational Corporations, Motivation

Introduction

Manufacturers face a variety of unique challenges such as having to face continuous regulatory compliance demands, keeping up with product innovation, keeping equipment updated and functioning, and considering environmental concerns (Iera, 2014). These challenges can be time consuming and costly, but can be curbed when two countries are connected through trade, industry, and regional economic agreements. The following is an examination of two multinational corporations (MNCs) who have recently invested in manufacturing plants on foreign soil. The first, Chinese MNC Haier, is an appliance manufacturer who signed a contract with the Indian government in 2015 to largely expand their plant in Pune, Maharashtra. Honda, the infamous Japanese car makers, opened their manufacturing plant in Celaya, Mexico in 2014. For each MNC, a brief description of the company's expansion is given followed by an evaluation of the laws and labor standards, regional economic agreements, and competitive advantages related to each endeavor.

Haier Manufacturing Plant in Pune, India

After acquiring a local refrigerator manufacturing company in Qingdao, China in 1984, Haier, a Chinese home appliance company, was founded. In 1992, the company achieved the goal of attaining global quality control by passing the ISO9001, the gold standard of international quality management systems (Psomas & Antony, 2015). This led Haier to initiate a global brand strategy in 1994 with the opening of a 132 acre Haier Industrial Park in Qingdao. In 1996, the home appliance manufacturers set up their first overseas plant in the Philippines, followed by Malaysia in 1997, and the US in 2000. The company has since expanded to Africa, Europe, the Middle East, and India (About Haier, n.d.). In 2015, Hair announced their plan to expand their manufacturing plant in Pune, Maharashtra, India. The company signed a contract with the Maharashtra government promising to invest $4.9 billion dollars into the expansion in support of the country's Central Government "Make in India" initiative (Haier Expands, 2016).

Regardless of how good the relationship has been, there are always challenges that come when opening or expanding a manufacturing plant in a foreign country. The following is an examination of how India's labor standards, laws, and regional economic agreements have impacted Haier's manufacturing plant. In addition, we will examine the factors that give Haier the competitive advantage in the region.

Laws and Labor Standards

After India won their independence in 1947, the government focuses on building their economy through industrialization and foreign direct investment (FDI). The country struggled in the beginning due to their strict industrial and trade regulations, but opened up flexibility in the 1980's by allowing open general licensing among imports, particularly in the areas of technology. This foundation has aided India's technological advancement, but has stifled domestic industrial advancement, creating an environment of inefficiency among workers (Kanda, 2015). The primary manufacturing law in India is the Industrial Disputes Act (IDA). This act covers dispute resolution, hiring and firing of workers, closing establishments, and strikes (Chaurey, 2015). Recently, the Wage Code Bill was passed by the Indian government. This will require all workers, regardless of prior pay, to received Rs 18,000 ($280) per month (Cabinet, 2017).

The structure of the Indian economy has benefited Haier in the past because there were no minimum wage requirements and FDI was highly encouraged by the government. However, with the passing of the Wage Code Bill, Haier may suffer large financial losses with their recent expansion because they promised the Indian government that they would increase their workforce from 1,100 to 2,900 and open a Research and Development Center (Haier Expands, 2016).

Regional Economic Agreements

China and India are the two largest countries in Southeast Asia in terms of land mass and population. They are currently connected through two regional partnerships. The first is the Asia Pacific Trade Agreement (APTA). This agreement was formerly known as the Bangkok Agreement and was initially signed in 1975. Several Asian countries benefit from the agreement through tariff concessions and preferential treatment. China was added to the membership in 2001. This was the first favorable partnership in which China had ever participated (The 4th Ministerial, 2017).

The second agreement is the Regional Comprehensive Economic Partnership (RCEP) founded by the Association of Southeast Asian Nations (ASEAN) and is still in its development stage. The goal of the RCEP is to expand Asia's regional connections. The agreement joins ASEAN's 10 countries with the six countries in the region that have free trade agreements (FTAs) with ASEAN members. This agreement adds more benefits to the China-India economic relationship (Das, 2014).

Both of these agreements have benefited Haier and have played a large role in Haier's decision to expand their manufacturing plant in India and increase their workforce from 1,100 to 2,900 over the next few years. This is primarily because Haier is largely owned by the Chinese government. These agreements have aided both the Chinese and Indian governments in establishing a mutually beneficial relationship (Haier Expands, 2016).

Competitive Advantage

The largest competitive advantage that Haier has in India is the government involvement on both ends. The Chinese government owns a majority of Haier's holdings and has worked hard to expand the company on a global level. India's government has launched a "Make in India" initiative and is working with Haier (the Chinese government) to build that vision (Haier Expands, 2016). In addition, Haier India launched a green initiative in 2011 as a global rebranding effort. Both China and India have been pressured over the past decade to improve air quality and increase sustainability efforts. Haier's Eco-Life series answers the call on behalf of both countries. Eco-Life products are advertised as being energy efficient and safe to the environment (Mohanty & Nayak, 2017).

Honda Manufacturing Plant in Mexico

Honda Motor Company was incorporated in 1948 in the small village of Hamamatsu, Japan. The small bicycle auxiliary engine manufacturer would grow to be one of the largest and most respected MNCs in the automotive industry (Honda Corporate, n.d.). In 2014, the conglomerate opened a manufacturing plant in Celaya, Mexico. The location is close to Mexico City and cost Honda Motors $800 million to build. The manufacturing focus was their redesigned 2015 Fit subcompact.

Since its inception, the Mexico plant has brought numerous problems to the company. The following will evaluate the labor standards, laws, and regional economic agreements that may have influenced these problems. In addition, a look at Honda's competitive advantage will be discussed and compared with the numerous car manufacturers that have also recently built plants in Mexico.

Laws and Labor Standards

Mexico has a strong focus on environmental laws, and has many policies in place to protect the health of its citizens by maintaining clean air and water. Part of this is due to their partnership with the North American Free Trade Agreement (NAFTA), which requires the country to adhere to the environmental standards laid out in the agreement. However, Mexico has gone above and beyond the agreement requirements. The country's most predominant environmental law is the General Law on Ecological Equilibrium and Environmental Protection (Mexico's Envrionmental Laws, 2015).

The heavy focus on ecology has left other areas unprotected that are normally handled by the government such as efficient rail systems and crime, both which slow down Honda's production and incur financial losses (Boudette, 2014). In addition, Donald Trump's recent threat to add a 20% tariff tax to all cars coming into the United States (U.S.) via Mexico could cause significant setbacks to the Honda plant because a majority of their cars sold in the U.S. are manufactured in Mexico (Campbell & Webber, 2017).

Another area where Mexico has been sorely lacking is their implementation of labor laws. Until 2012, the government had made no reforms to the informal, yet restrictive system for over 40 years. The reforms in 2012 included easing restraints on a company's ability to hire and fire, include a probationary period, and allow for the hiring of part-time employment (Agren, 2012). These laws are beneficial to Honda in that they have more flexibility in hiring choices, but these laws have increased the expectation for legal hiring practices, which may have increased costs to the Honda plant. The company has suffered in part due to its young, inexperienced labor force and language barriers – both factors that slow down production (Boudette, 2014).

Regional Economic Agreements

After 14 rounds of negotiations, the governments of Mexico and Japan signed the Economic Partnership Agreement between Mexico and Japan (EPA) in 2004. This agreement linked Japan to all of Mexico's regional economic partners, specifically NAFTA, opening up opportunities for Japan to do business with the U.S. It also lifted tariff restrictions for Honda, which allows them to export to the U.S. at much lower costs than those not connected to NAFTA (Sánchez, Regalado, Bravo, & Guzman-Anaya, 2016). The recent threats of President Trump to raise import tariffs on Mexico by 20% and remove the U.S. from NAFTA have been strains to Honda's Mexico plant.

Competitive Advantage

Honda's greatest competitive advantage has been the Mexico-Japan EPA, which has allowed the company to produce in a low-cost location with low-cost labor and export their products to the U.S. with low travel costs and minimum tariffs. However, language barriers, inexperienced workers, slow railways, and hijacked cars have outweighed the benefits from its recent decision to spend $800 million on a manufacturing plant in Mexico.

Conclusion

MNCs set up manufacturing plants in offshore locations for two reasons. They either want a low-cost landscape or they want to manufacture in the country where they are expanding. Regardless of motive, it is important for MNCs to find out about the country's Free Trade Agreements (both Regional and non-regional), as well as laws and labor practices that might impact their business. In the cases of Haier and Honda, the regional economic agreements that connect each MNC to their country of choice have been the greatest benefit and most likely a primary driver in their decision-making strategies. However, country laws and labor standards have been costly to both MNCs for varying reasons. Haier may suffer from a new minimum wage law that will be implemented in India due to their agreement to increase labor from 1,100 to 2,900 employees. Honda suffers from Mexico's high crime rate, slow rail system, and barriers related to language and an inexperienced employee pool. It is recommended that these outside factors be considered and weighed before setting up a manufacturing plant in a country that offers free tariffs through FTAs.

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