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Apple's Exceptionalism, China's Mean Trade, and America's Media Mediocrity

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In 1981 I was the long haired, 18-year-old co-founder of a video game startup exhibiting our wares at the West Coast Computer Faire in San Francisco. The geek crowd's big social objective for the weekend was to impress "Woz", the legendary designer of the Apple II computer that made our industry possible. We respected engineering above all else and viewed the "other Steve" as a business guy with a reputation for being a jerk. However, when both Steves stopped by our booth, Jobs left a more lasting impression. There was no doubt that this fellow was far smarter than your average bear.

Following Job's departure as Apple CEO, the press has been falling over itself to extol his unique virtues. The creative genius and superb execution that he consistently delivered must never be confused with the mean talents steering Apple's unworthy competition. Steve Jobs and the firm he drove from a suburban garage to the pinnacle of corporate success are the very definition of exceptional.

Unfortunately, this exceptionalism has been lost on the business scholars who study Chinese off-shoring and the pundits who channel them. It has become a real fad for management academics (particularly at my own school) to analyze in minute detail the cost break down of the iPod, iPhone, and iPad with studies that inspire our talking heads to conclude that "nearly all the product's value accrues to America." As a good student of Goebbels, [Wen Jaibao repeats this tripe and Fareed Zakaria](#) kindly provides him with an unblinking venue to do so.

The authors of a recent San Francisco Federal Reserve Board Economic Note ([The U.S. Content of "Made in China"](#)) used one of these studies ([Xing and Detert, 2010](#)) to back their assertion that off-shoring to China has little impact on America. Galin and Hobjin confidently wrote that of the \$179 in input costs for this technical miracle, "only \$6.50 was actually due to assembly costs in China." The context implies that Apple products are like commodities and this sort of ratio might be extrapolated to the aggregate.

Making the same assertion, the Cato Institute's, Daniel Ikenson went so far as to proclaim "[the world should rejoice in China's becoming the world's largest exporter](#)." Let us all take a moment out and join Mr. Ikenson in a big, happy, "Hurrah!" for the victory of jack

booted dictators and factories with suicide nets! Then, after a fast run to the privy, let us claw our way back to reality.

Honestly, we all know that \$500 products are NOT leaving China for \$6.50 and building untold wealth in America. I've seen how those who profit off the backs of China's labor are living it up in Shanghai, and I experience California's unemployment and fiscal disaster all too personally. Trust me that would NOT be the outcome of Silicon Valley firms taking advantage of China's poor little manufacturers. Besides plain-old common sense, there are several ways to dispel this muddle headed fantasy. We have space for a couple.

Firstly, despite the pundit's claim to the contrary a lot of the iPhone's sub-sub-components and their raw material inputs are Chinese despite being branded differently. For instance, you can bet your bottom Yuan that the Japanese compass and battery and the Korean LCD are made with over-priced Chinese rare earth elements. Many of them might even come out of a Joint Venture Chinese factory that says "Toshiba" or "Samsung" on the marque. There just aren't any good input/output tables available online (never, ever leave your office, PhDs) to account for that sort of thing, so good academic economists take the high road and, well, they sweep it under their statistical rug.

Secondly, Apple's contract assembler, Hon Hai Precision (FoxConn) is a lot more than that. You can't make a great product without great production engineering and that requires being close to the manufacturing process. I was kindly hosted by the folks at Foxconn city in Shenzhen last December and they were effusive about the amount of value they add in design and testing (though they will never officially acknowledge who they work for). I believe they may contribute as much as 15% to a finished product's design, and tell me it ain't going out the door for free. That work is being done by their expensive high-end, American, Taiwanese, and Japanese trained engineers who have moved to where all the jobs are these days. In fact, finding a production engineer in America is getting to be hard. Do you really believe that they are all doing charity work over there in Guangzhou so the value can continue to "enrich America"?

All that said, Apple is still an exception, because what they don't do is invest their money into China or get hauled into an involuntary joint venture with a Chinese majority "partner" who captures 60-80% of the revenue and seizes their valuable intellectual property -- either via forced transfer rules or outright theft. While Jobs is far too savvy to fall into that trap that is precisely what is happening to your average American firm trying to make it in Communist China. The opportunity cost of all that lost U.S. capital and stolen technology is never accounted for in the academic studies and is never, ever mentioned by your "free trade" pundit.

The real bottom line is that only a nut would ever hold Apple up as average though clearly our business press is chock full of them.

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