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China starts to ship higher costs abroad

By Carter Dougherty International Herald Tribune

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FRANKFURT During 20 years in the toy business, Anthony Temple has reveled in the bounty of inexpensive stuffed animals, coffee mugs and resin figurines on sale in China. But a buying trip this year for his company, Rainbow Designs, based in London, was a rude awakening.

Traveling through the Pearl River Delta north of Hong Kong, Temple found that cost increases - for raw materials, but above all, for labor - dominated every discussion he had with suppliers.

Far from being eager to underbid each other, Chinese companies talked about marking up their prices from 5 percent to 10 percent so consistently that Temple, whose company owns the British distribution rights to such cuddly creatures as Paddington Bear and Jemima Puddle-Duck, became convinced that these were not simply negotiating gambits.

"When I went over there, I was under the belief that China is a bottomless pit of cheap product," Temple said. "When I left, I was not."

As the Chinese economy races forward, signs are multiplying through the global flow of goods from suppliers to manufacturers - and deep in some statistical tables - that the Asian giant is beginning to slow its exporting of something dear to the hearts of the world's central bankers: lower prices.

For at least a decade, China has provided a welcome tail wind for inflation fighters in Europe and the United States by supplying inexpensive goods that depressed overall price levels.

But more and more this year, China's role in global disinflation - as the phenomenon is known to economists - has toughened the agenda for central bankers. Striking anecdotes and evermore statistical evidence suggest that China's contribution to low prices may be ebbing.

And that, combined with more expensive raw materials like oil, means that central banks once again could be stuck with the painful dilemma that they faced in the early 1980s: to stop inflation by tightening credit, despite the potentially negative effects on economic growth and unemployment.

"Even in China, with its growing manufacturing base and large pool of labor, some indicators are showing upward pressures on export prices," Mervyn King, the governor of the Bank of England, said in a recent speech. "And in turn that is raising our import prices, over and above the increases resulting from higher energy costs."

After discussing the "China effect" this spring, the European Central Bank pledged to increase research into the phenomenon. Top officials of the U.S.

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