

The Reshoring Wave: It's Taking America by Storm

There's no doubt about it: The reshoring trend is rocking global business, with hundreds of companies working to bring their manufacturing operations back from China to North America. There are many factors fueling this move, including labor costs, transportation, quality issues and patriotism, among others. Hal Sirkin, a senior partner at Boston Consulting Group, has been examining this trend for years and admits that the recent surge in reshoring has shocked even experts and researchers. Knowledge@Wharton sat down with Sirkin to discuss the different elements contributing to the reshoring trend and how it affects global business dynamics, the labor market and even the U.S.-Mexico relationship.

An edited version of the conversation appears below.

Knowledge@Wharton: The last time we spoke in [February 2012](#), we discussed how it was widely believed that manufacturing in the U.S. was in long-term decline. But, in fact, manufacturing was actually starting to return to America. We also talked about some of the factors that were driving that change. Now, has that trend continued in the past two years? What has your research shown?

Hal Sirkin: In 2011 and 2012, we projected manufacturing wouldn't return to the U.S. in full force until 2015. I'm glad to say that we were wrong. Shortly thereafter we started seeing hundreds of companies bring back manufacturing to the U.S. We can identify 300 to 400 different companies that have done this, not for patriotic reasons but because it's just good business.

Knowledge@Wharton: Please explain this. Why does it make good business sense to bring manufacturing back?

Sirkin: In the late 1990s, labor costs in China were very low. When China entered the World Trade Organization in 2001, average labor costs were somewhere around 58 cents per hour. Companies saw that Chinese labor was cheap, and since the U.S. has a very fluid labor market where people can be hired and fired rather easily, employers opted for cheap Chinese labor instead of American labor. Manufactured goods were sent to China. Goods were made in China and then sent back to the U.S.

That caused hardship in this country, but since the U.S. is based on a truly free market, we made changes and adjustments. We adjusted, we adapted and we survived. Some companies went out of business. Other companies figured out how to stay in business in the U.S. Others out-sourced partially.

But over time, this demand for cheap Chinese labor became so strong that wages were pushed up. When Chinese labor costs rise from 58 cents an hour to \$1 an hour, you don't think about it. But over time, labor rates went up by 15% to 20% a year, and the cost differentials narrowed significantly. This prompted businesses to reconsider whether it was a good idea to keep their operations in China.

Knowledge@Wharton: China has always been a magnet for manufacturing. But in your recent research, Mexico seems to be emerging as a global manufacturing destination. What does this mean for China?

Sirkin: In 2012, my colleagues and I started to notice that it was becoming cheaper to manufacture certain goods in Mexico instead of China, not even counting the transportation costs. When you add in transportation, this makes a big difference from a cost perspective. We watched many manufacturers in the 1990s move from Mexico to China, but now they're coming back.

I often say, it's a four-day trip from Mexico to Chicago, but it's a four-month trip from China to Chicago. There are a lot of other costs that are added in when you transport such long distances. So we have watched Mexico become a very important manufacturing hub.

Here's an interesting fact: Mexican-made goods have four times more American content than Chinese-made goods. So when you start making goods in Mexico, your products have significantly more U.S. content.

Knowledge@Wharton: If Mexico is emerging as a global manufacturing destination, what does that mean for U.S. manufacturers? Is this something that benefits American

manufacturers? Or should U.S. manufacturers be worried about having another low-cost competitor?

Sirkin: This is beneficial for U.S. manufacturers because low-cost labor in Mexico helps lower the costs of their final products. This helps the U.S. be more competitive with China.

Knowledge@Wharton: People often worry about crime and safety issues in Mexico. How are American companies dealing with those risks?

Sirkin: Crime and safety are clearly issues that everybody needs to be aware of. It's probably one of the main reasons that the Mexican currency has not increased in value over time. But companies with Mexican operations are putting in security systems that allow them to produce in Mexico with reasonable safety levels. Some companies find ways to operate, but others don't think it's worthwhile. It depends on the product and how companies assess the manufacturing situation.

Knowledge@Wharton: In addition to the rise of Mexico, some of your research focuses on the price of American-made products. Do you find that American consumers are willing to pay a premium for products that are made in the U.S.?

Sirkin: When American consumers are shown two identical products, but one has a 'Made in China' label and the other has a 'Made in the USA' label, they will almost always choose the 'Made in the USA' product. There is a very strong preference for 'Made in America' versus 'Made in China', especially for health-related goods, baby care products and items you'd want to keep for a long time. Our research in China also shows 60% of Chinese people are looking for 'Made in America' products over 'Made in China' products.

The demand is clearly there because we know about the melamine issues and the planes from Australia flying over with baby formula and diapers because of concerns about Chinese products. But over time, China will work through these problems, as economies do. But for the time being, consumers in China and the U.S. have real concerns. Another factor that encourages 'Buy America' sentiment relates to Americans wanting to support their neighbors and communities. And, of

course, there's also patriotism. We are a strong country and we have strong patriotic views.

Knowledge@Wharton: Are there some product categories that benefit from a 'Made in America' premium and others that don't?

Sirkin: Categories that involve children benefit: consumers want to make sure that teething blocks and teething plastics do not have any issues, so people look for the 'Made in America' label on these items. When it comes to durable items such as hammers and tools, consumers tend to pay more for the 'Made in America' products, although the cost differential is now getting a lot lower between the American-made and foreign-made products.

Knowledge@Wharton: Your research also found that Chinese consumers are willing to pay more for these products, but Europeans are not. What are the reasons behind this?

Sirkin: Europeans have a high set of safety standards for products; the standards are very similar to American standards. So there's not a real reason for them to demand American-made products. Plus, if you are German or French, then you'd be patriotic and more likely to buy products from your home country. Plus, if it's made in Europe, it could be cheaper because there wouldn't be extra transportation costs.

Knowledge@Wharton: What about other Asian consumers?

Sirkin: It depends. Asia is a big continent and it depends on where you are. If you're in some of the lower wage countries then there are some real issues with some products. The population that can afford American-made goods will buy the American-made goods or the German-made goods or the French-made goods. But for those who cannot afford these products, they end up buying the cheaper cell phones and the cheaper baby products because that's all they can afford.

Knowledge@Wharton: As manufacturing returns to the US, there's a concern that our population has lost manufacturing-related job skills. Do you think that problem has been overstated?

Sirkin: Right now we don't really have a major 'skills gap'. But we do have shortages for some types of workers: people in the natural gas fields, welders and plumbers. We've been able to fix these shortages by bringing in people from other countries. But there's a big concern when it comes to welders, for example -- the average welder age is 58 years old right now. It was roughly 57 years last year, and it was 56 years two years ago. So we have a fundamental problem approaching.

There are two ways we can solve this problem. The first solution: get better vocational schools and better training, either from schools or employers. For example, the skills shortage for welders is only going to get worse and employers must figure out how to address this. The other thing to do: import skilled people. We're doing some of that now. America is a great place and people want to come to this country.

The educational system, particularly for the trade schools, is very important. We need to start thinking about education in a very different way. For example, as you know, I went to the Wharton Business School and, in many ways, that was a trade school where I learned a trade and that trade was business. But at the same time, I went to the University of Pennsylvania and I got a liberal arts degree simultaneously. This helped me become a more well-rounded person. I don't see why our welders, plumbers and tradesmen shouldn't get a two-year degree, in essence, in liberal arts, and a two-year degree in their trade. I think that would give them better job skills and a more satisfying career. Unfortunately our current educational system doesn't cater to this.

Knowledge@Wharton: Are there parts of the country where this problem is more acute than others? What can be done about this?

Sirkin: The oil and natural gas sector is seeing acute problems. In North Dakota, housing prices are higher than apartments in New York City. It's cold up there and it's hard work, but people can make a lot of money. We're seeing problems there. The problems will get worse if we don't do something. The natural solution would be to start importing people to do this kind of work.

Knowledge@Wharton: How do you think companies can be more proactive about future skills gaps?

Sirkin: I think it's all about training. I think it's simple. U.S. workers are becoming more efficient and, therefore, we need to hire fewer people for the same level of output. In the last 40 years we've boosted our manufacturing output with 30% less labor. That's the skills of the U.S. worker, automation and lean manufacturing all taking effect. It's all making the U.S. more productive.

Knowledge@Wharton: You've done research over the years focusing on the American manufacturing renaissance. What would you say has surprised you the most?

Sirkin: The speed at which it's taking place. We were thinking the changes wouldn't be noticeable until 2015. But we underestimated America's resilience and the business community. Managers started to look at what they were doing in China, and many said, "The economics don't work." They decided to start bringing manufacturing back.

For a long time, China was the default location for manufacturing because it was cheap. But now, we need to look at the whole package. If a product doesn't have the same quality or if the product has different, non-durable characteristics, you're probably paying more money than you should be paying for a potentially inferior product.

Knowledge@Wharton: What are some areas that you plan to research in the future?

Sirkin: We're releasing new research on global competitiveness. We're looking at the competitiveness of 25 leading countries. This will give people a perspective on how competitive each one of those countries is, taking into account key factors such as labor productivity, worker pay, electricity costs and exchange rates. We're also working on research related to automation, which is very interesting, but could be controversial.

Knowledge@Wharton: We look forward to discussing competitiveness and automation with you in the future. Thanks so much for joining us at Knowledge@Wharton.

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