

---

# Asian Rattan, Inc.

## CEBU CITY, THE PHILIPPINES

### Case Description

*Case Location:* Cebu City, Philippines

*Industry Focus:* Rattan furniture manufacturing and exporting

*Functional Emphases:* Business and Society, Organizational Behavior, Labor Relations, International Business, Business Ethics

### Issues Raised by the Case:

- The role and responsibilities of capitalist enterprises in the developing world—and elsewhere;
- The dynamics of labor-management relations in a developing country enterprise, responding to structural change in the economic/business environment, and coping with shifting comparative advantages in international business;
- The impacts of the modern global economy on traditional forms of worker-management relations.

As the Asian Rattan case unfolds, it exposes the student to a number of issues related to labor-management relations in the developing world. The overarching question that unifies all of these issues, however, is “What responsibilities do capitalist enterprises have toward their employees and society?” A discussion and analysis of the case will cause students to explore the role of capitalism in the development of the Third World and, by extension, their own society.

The central character in the case is the son of prosperous industrialist family, Jun-Jun Hernandez, whose once-caring and paternalistic relationship with the workers in his rattan furniture manufacturing business deteriorates into a bitter and rancorous strike over the issue of minimum wage. After 18 months of strike arbitration, Jun-Jun considers whether to reopen his furniture factory and endure the possibility of future labor problems, or to close the business permanently.

### Position in the Course

The case does not presuppose the mastery of technical material from any functional area within business, so it could conceivably be used anywhere within an individual course, and at any point within the MBA curriculum. Because the case is designed to provoke discussion on issues as fundamental as the role of capitalism in society, however, it may most appropriately be used at the beginning of a course. The issues that are raised by the case, and the conclusions reached by the students on these issues, could then be used as a philosophical framework for the rest of the course.

### Teaching Purpose and Objectives

This case will be a frustration for those students who want to walk out of the classroom with a set of definite conclusions or lessons learned, because it is designed to provoke thought and raise awareness, rather than teach a particular skill or lesson.

Asian Rattan presents students with a situation in which the supply and demand for labor match at a wage that is insufficient to provide workers with their basic needs (i.e., a nutritious diet, adequate clothing and shelter, rudimentary health care, etc.). It then asks them to consider the social and ethical basis for capitalist enterprise. The casewriter intends that the situation be provocative enough to evoke animated classroom discussion from a variety of viewpoints, ranging from socialist sentiments for a more egalitarian society, to hard-core capitalist viewpoints where market rationality is more important than the resulting human consequences. While an initial polarization in the classroom is perhaps inevitable (and desirable), the case presenter should try to steer students towards a consideration of the more positive aspects of capitalism, because (despite its attendant inequalities) it remains our only viable model for development. Ideally students should be led to consider whether there can be such a thing as an “enlightened capitalism,” where the risk and rewards of enterprise are shared more equally by the providers of capital and labor in society.

The underdeveloped economy of the Philippines provides an ideal setting for generating a discussion of the role of capitalist enterprises in society. Because the economic context of the Philippines is so dramatically different from that familiar to most American MBA students, these students should be freed to approach the issues presented by the case without their traditional biases. They should then be encouraged to apply whatever conclusions they reach about the roles and responsibilities of capitalist enterprise in the Philippines to the U.S. environment. The case presentation will be successful if these conclusions challenge and/or illuminate some of their traditional beliefs about the responsibilities of capitalist enterprise in their home environment.

## Study Questions and Discussion

### 1. What, if any, responsibilities did Jun-Jun have towards his workers before the strike? Should he have paid the minimum wage?

There are no right or wrong answers to this question, of course, only points that can be made in support or rebuttal of different ethical (or practical business) viewpoints.

It is easy to take the “side of the angels” and say that Jun-Jun should pay the minimum wage. It is the law of the land, and his workers obviously need that much and more to live even the most meager existence. Jun-Jun’s family is obviously wealthy, and the disparity between their lifestyle and those of their workers seems to be insupportable from a social equity standpoint.

From an economic and financial perspective, however, paying the minimum wage would present Jun-Jun with problems that could ultimately close the business altogether—which certainly is not in the worker’s best interest. The legislated minimum wage is above the market clearing wage for labor in Cebu, as is demonstrated by the fact that most companies in Cebu do not pay the minimum, and yet they still have several applicants for every job they need to fill. Because most of Jun-Jun’s competitors are not forced to pay the minimum wage (either their small size or their owner’s political clout puts them beyond the reach of DOLE), they actually pay considerably less. AR’s competitors in Indonesia, Vietnam, and China are also paying lower wages. If Jun-Jun is forced to pay the minimum and he does not have any compensating gains in productivity, Asian Rattan may be forced out of business by lower-priced competitors.

Obtaining those gains could prove difficult. Jun-Jun could try to increase the value of AR’s production by going for the higher-end furniture markets, but this would require investments in better finishing equipment and materials, worker training, and improving their in-house design capabilities. This route would also require substantial time to implement. Alternatively, AR could continue to produce medium-end furniture but try to increase the volume of the factory’s output. This too would require further investments, in this case for improved capital equipment and physical facilities. Both alternatives to increase productivity would require higher capital investments, and it is unlikely that AR’s provider of capital (Jun-Jun’s father) would be willing to invest more in AR in light of his other alternatives (as an example, Philippine T-Bills were paying between 13–16% over this period). Like the manager of any American corporation, Jun-Jun has an obligation to earn a risk-adjusted rate of return to those who provide his capital. If he pays the minimum wage, he runs the risk that his father will force him to close the

business, and then all of his workers will be thrown out of their jobs.

Even if we can agree that Jun-Jun has a moral obligation to look after the economic welfare of his workers, it is still not clear how that welfare might best be served. Is it by paying minimum wage, and perhaps jeopardizing the long-term financial viability of the company? Or is it by paying something closer to the true market-clearing wage so that he can earn a rate of return acceptable to his father? We would hope that Jun-Jun and his workers could be successful in a mutual effort to raise the value of the company's output, so that higher wages could be paid while the company continues to earn an acceptable return.

**2. What, if any, responsibilities does the Philippine government have to the country's unskilled laborers? Should they impose and enforce a minimum wage?**

No doubt this debate is as contentious in the Philippine setting as it is in our own society. The motivation for the implementation of a minimum wage is straightforward—the government would like to ensure that those who work will be afforded their basic needs, so they set a minimum wage that will allow a worker to obtain adequate clothing and shelter, nutrition, etc. The question this raises is whether the minimum wage really serves the best interests of a society that is desperately short of opportunities for productive work.

In the Cebu setting of the case, the minimum wage is above what would be the market-clearing wage for labor. If the wage is enforced, then demand for labor will be reduced and many people who want to work will be unable to find jobs. Depending on the elasticity of demand for labor, the implementation of the minimum wage might even reduce the total wages paid to unskilled workers (i.e., if the elasticity of labor demand is greater than one, then the number of workers employed after the minimum wage is enforced will decrease by a greater percentage than wages are increased, so total wages paid will decrease.) Another way to look at the issue is that the minimum wage increases the return to labor but decreases the return to capital. Capital suppliers will therefore provide less new investment after minimum wages are enforced, decreasing the opportunities for work.

It is not clear, therefore, that a minimum wage is the best way for the government to look after the economic welfare of its citizens. There may be other—and more effective—means for the government to influence the welfare of its country's working citizens. By providing better educational and training opportunities, the government could increase workers' productivity and therefore the wages they could command in the marketplace. Community-level health care and housing assistance programs have proven to be a cost-effective means to help meet two of workers' greatest basic needs. Government efforts such as these would help to insure the welfare of the working poor without the distortions in the labor market that accompany minimum wage legislation.

**3. What, if any, responsibilities does an American buyer have to the workers in the factories from which they buy?**

Many large American corporations have recently been wrestling with this issue. After a "60 Minutes" report on the use of child labor by foreign firms from which U.S. companies source their products, many American firms are going through the difficult process of developing sourcing policies that try to do economic and ethical justice to everyone involved.

Certainly U.S. companies should avoid dealing with foreign firms that are engaged in unfair and exploitative labor practices, but as this case illustrates, it is not always easy to translate U.S. concepts of fairness and exploitation to a developing-country context. Rather than insisting that their developing country suppliers adhere to an arbitrary set of wage standards, it might be more constructive for U.S. buyers to offer assistance in raising the productivity of their suppliers' operations. In the AR case, U.S. buyers could offer AR assistance in building up its in-house furniture design and construction capabilities, so that they could move their production towards the higher end. It is also important that AR keep up with the trends in the world's furniture markets, and its U.S. buyers would be in a position to help Jun-Jun access various international resources and market information on world design trends. By helping to build up AR's capabilities as an organization, its U.S. buyers would ultimately be contributing more to the welfare of AR's workers than if they forced Jun-Jun to comply with an arbitrary set of labor standards.

**4. What should Jun-Jun do? Should he reopen the factory? If yes, should he rehire any of the previous workers? What should he do differently to avoid repeating his labor problems in the future?**

If Jun-Jun reopens the factory, it is unlikely that he will rehire any of the previous workers. The accusations and recriminations associated with the strike were a direct affront to his public "face," making it difficult or impossible for him to hire them back.

He will face many obstacles if he tries to reopen the business. AR's old customers will have to be convinced that AR will be a viable and stable supplier in the future. Jun-Jun's father will have to be convinced that the business will earn an acceptable rate of return on the family's investment. The organization will have to be restaffed from the ground up. If he is successful, then the unions would be particularly anxious to target his business again.

Because of the pressures of international competition and potential unionization, his focus on the reopened business will have to be on increasing productivity. This will mean investing in improved design capabilities, better finishing equipment and materials, more efficient production facilities and improved worker training.

### **Subsequent Events**

Jun-Jun reopened the Asian Traders business, but he chose not to reopen the entire factory. Rather than manufacturing his products in-house, Jun-Jun concentrated on marketing and design while subcontracting actual production to several of the hundreds of small furniture subcontractors in the Cebu area. The only production activity he continued to keep in-house was the finishing, which was performed in the old factory building.

By using subcontractors, Jun-Jun has largely avoided the labor issue altogether. These small contractors are beneath the notice of DOLE or the unions, so they pay something closer to the equilibrium wage for labor than the legislated minimum. As a result, they can offer prices to AR that are lower than if AR manufactured themselves. The biggest problem with using the subcontractors is maintaining quality control, so Jun-Jun employs several "QC checkers" who spend their days traveling from subcontractor to subcontractor, checking their production against customer specifications and offering technical advice.

In addition to the QC checkers, Jun-Jun employs a staff of professional designers, several administrative clerks, and a small finishing department. He is trying to develop core skills in design and finishing and hopes to bring all manufacturing activities in-house eventually.