

# Global Value Chains: Restructuring and Challenges in the ASEAN+3 Region

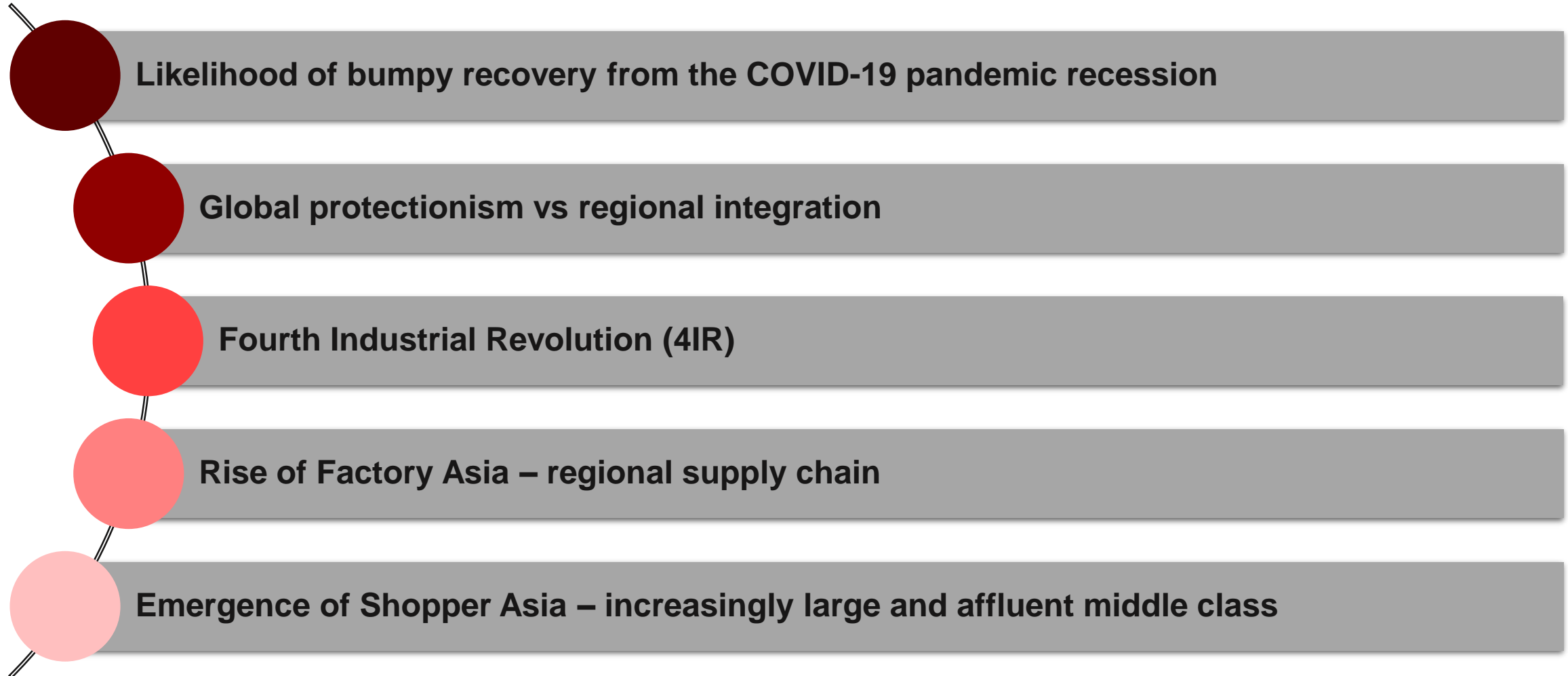
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Emerging Market Insight Webinar

September 25, 2020

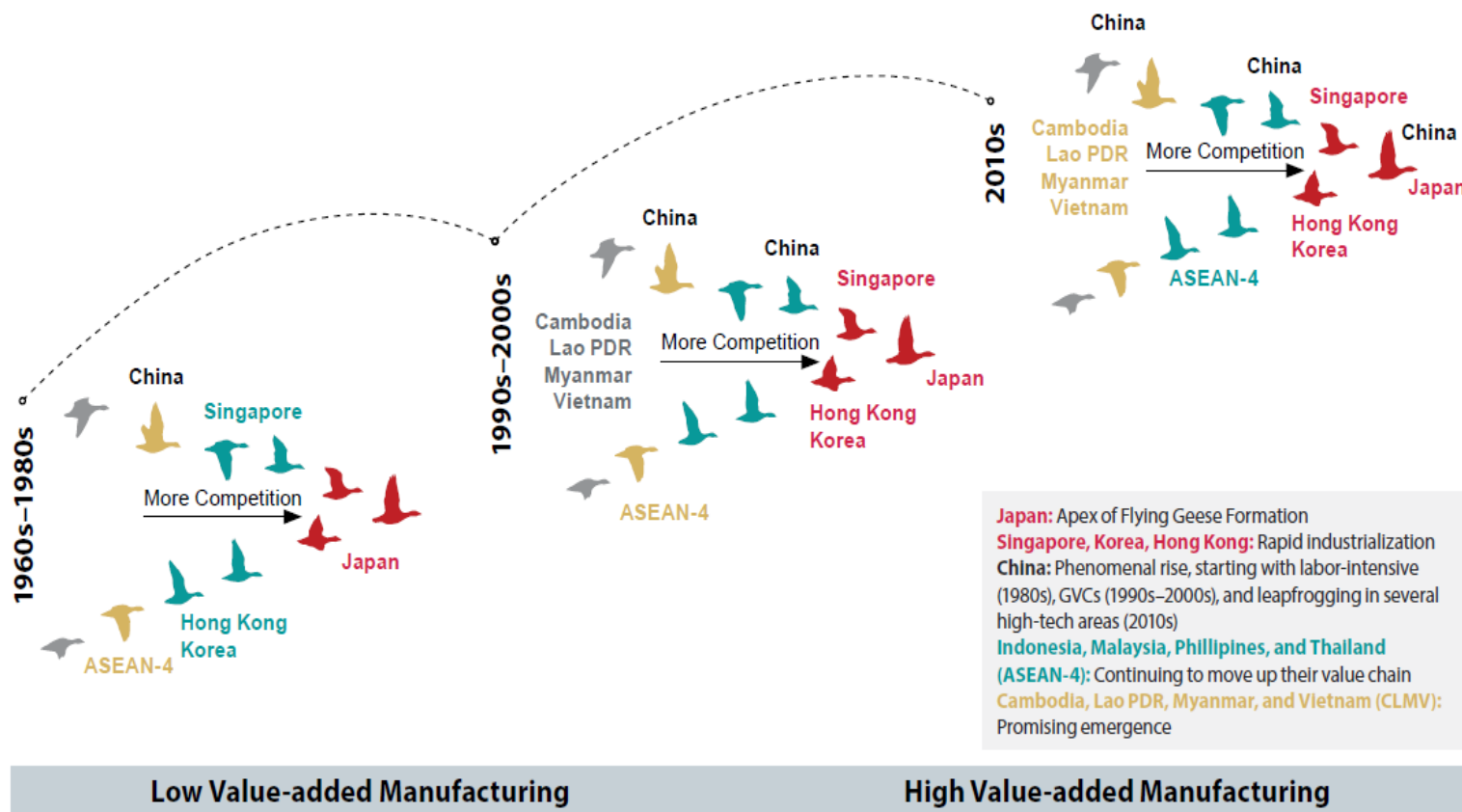


**As the region recovers from COVID-19, five key trends will shape the evolution of GVCs and determine what the region needs for strong medium-term growth.**



# The rise of Factory Asia is a development which has unfolded over decades, but has taken on a twist (or two) in recent years.

## Evolving comparative advantage (H-O-R) flying geese model

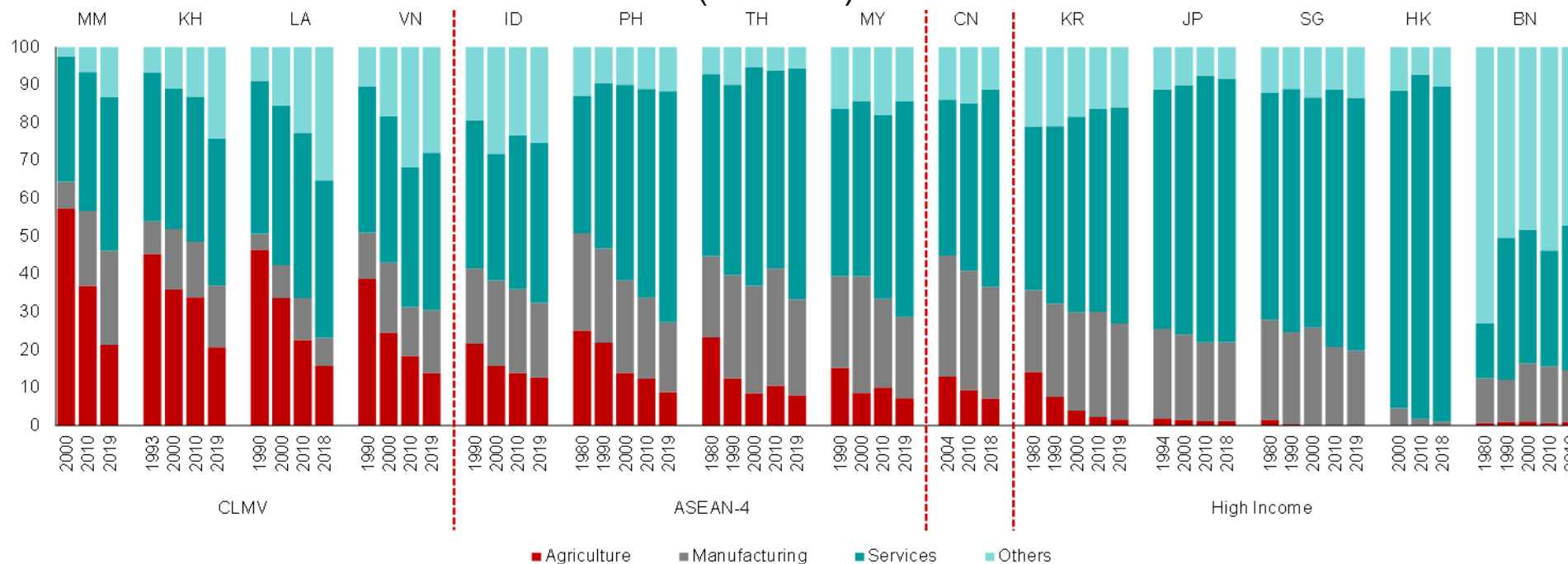


- ✓ *Maximizing gains from comparative advantage: Heckscher-Ohlin (H-O)*
- ✓ *Developing new competitive advantage: Ricardian elements*
- ✓ *Development of the Regional Supply Chain*

## Sectoral shifts do not spell the end of the manufacture-for-exports strategy for growth catch-up. Far from it. GVC disruptions matter massively for the region.

- *Advanced ASEAN+3 countries and then upper-middle income ones have gained much from manufacturing-for-exports growth model.*
- *Manufacturing's contributions to growth and jobs are peaking earlier and lower.*
- *But several countries can still extract a lot more from manufacturing, and need to do well in GVCs.*

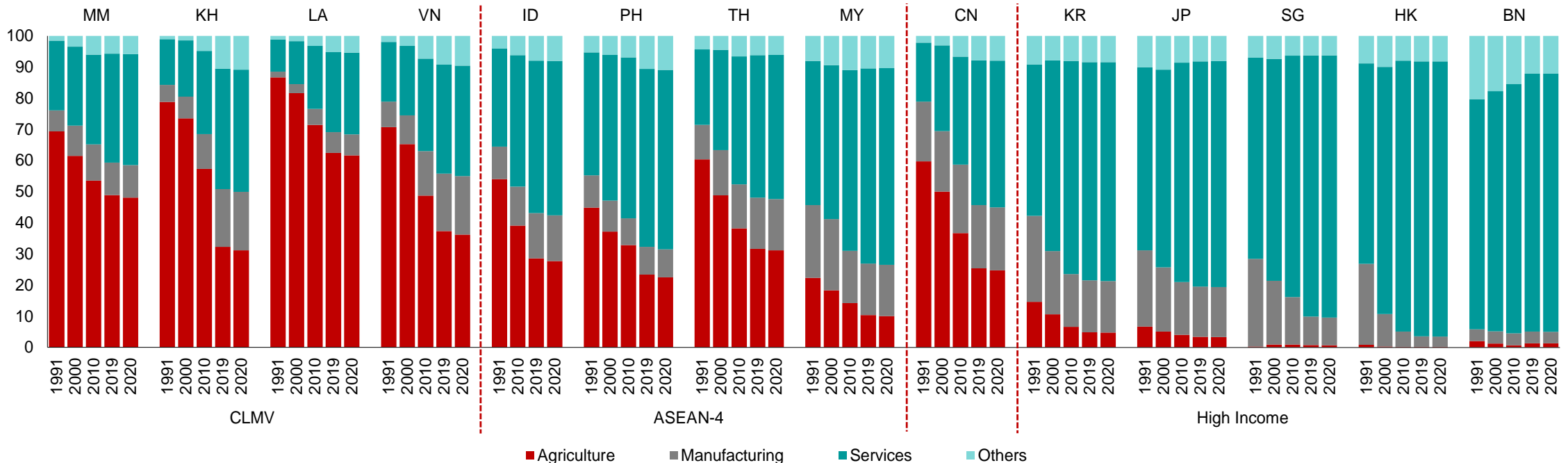
**ASEAN+3 Economies: Shares of GDP by Sector**  
(Percent)



# Labor has shifted from agriculture to manufacturing and services across economies; many services are now geared towards supporting manufacturing.

- *High-income economies in the region have been deindustrializing and have moved into services.*
- *In less developed economies, employment in agriculture has been shrinking due to structural transformation.*
- *Apart from services for end-consumption, many services are now geared towards supporting manufacturing.*

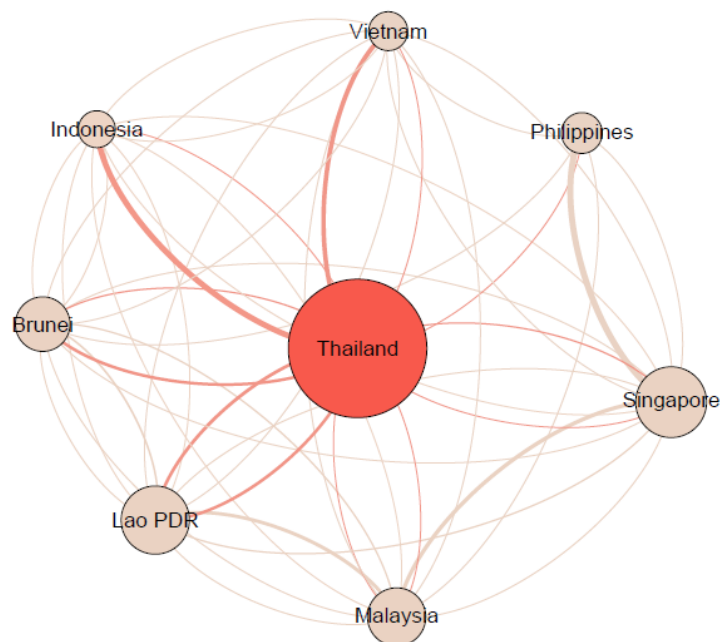
**ASEAN+3 Economies: Shares of Employment by Sector**  
(Percent of total employment)



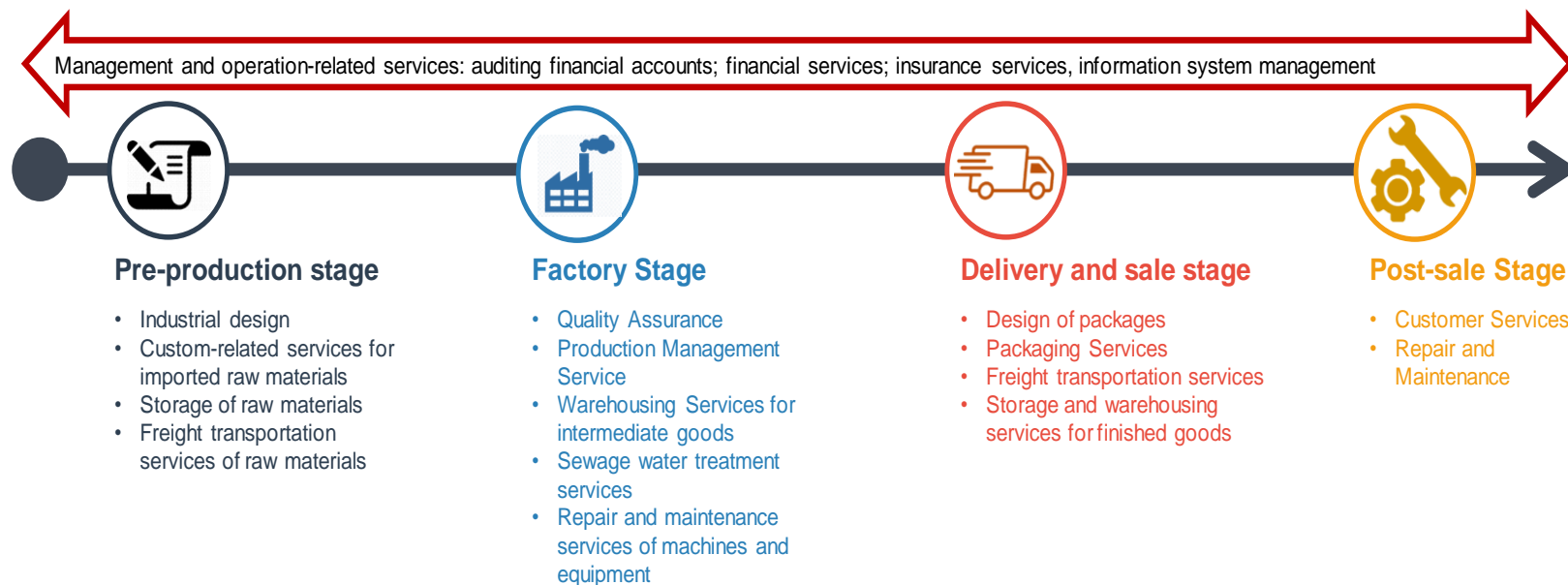
## Example of services' importance for manufacturing: Thailand's automobile sector.

- Domestic value-add of Thai automotive services exports in 2018 was nearly double that of other ASEAN countries combined. Its production network is most connected with that of Indonesia and Vietnam.
- Services intertwining into manufacturing improves efficiency but also increases vulnerability to GVC disruptions.

### Thailand's Automobile Value Chain



### Services along the Automotive Value Chain



Sources: Asian Development Bank; and AMRO staff calculations.

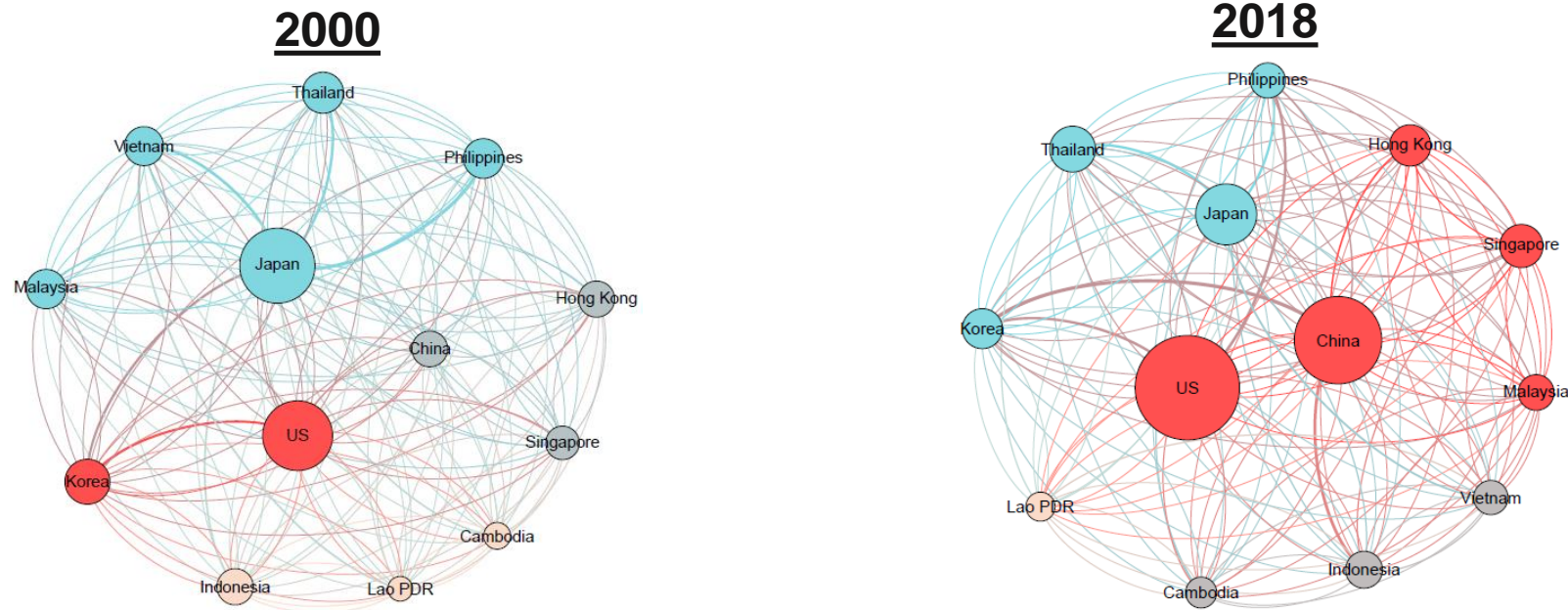
Note: The node size represents the weighted degree of the economy in the network. The arrow thickness is scaled according to the volume of trade in value-added terms. The trade in value-added of "Sale, Maintenance, and Repair of Motor Vehicles and Motorcycles Services" (C19) from ADB Multi-Regional Input-Output Tables is used as a proxy for Service Automotive Exports. Our focus is on Thailand within the ASEAN region. Therefore, Japan, Korea, and China are not included here, although Japan and Korea are important automotive hubs in Asia.

Sources: Asia-Pacific Economic Cooperation (2015); and AMRO staff.

## More broadly, services are becoming a more critical part of global integration: China, a manufacturing powerhouse, is now a key node in GVCs for services.

- *Factory Asia – deeply plugged into GVCs – now increasingly resembles a services hub.*
- *It is much more involved in value creation through R&D, product designs, and customizing service experiences.*
- *China becoming a key node in GVCs for services is a prime example.*
- *Both business and personal services have become more tradable than before.*

### China's integration into GVCs for service exports



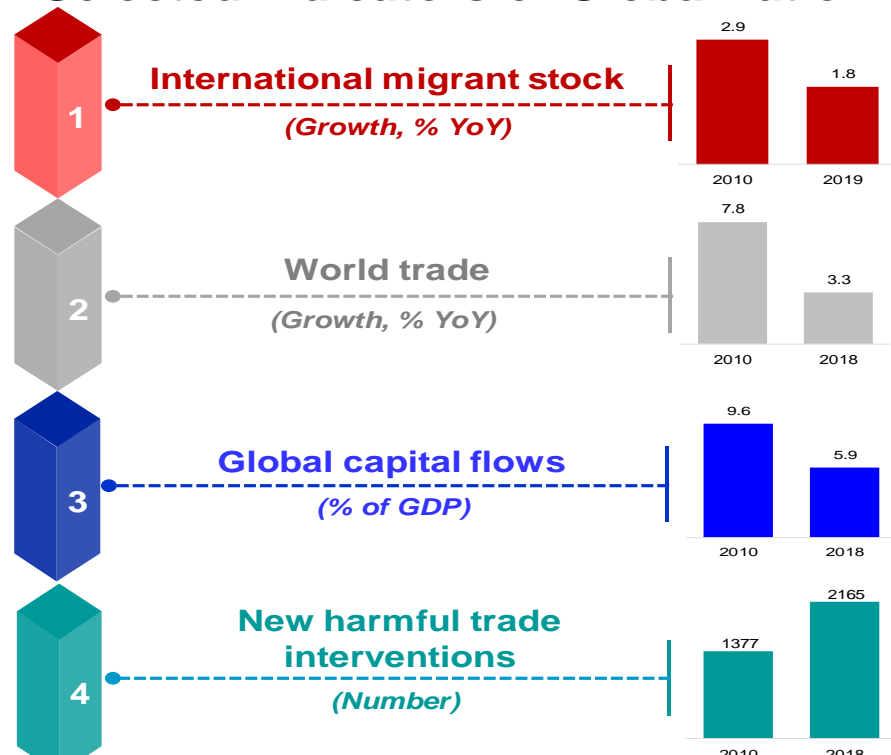
Sources: Asian Development Bank; and AMRO staff calculations.

Note: The node size represents the weighted degree of the economy in the value chain. The node color represents the “community” to which the economy belongs. “Community” is detected using methodology outlined by Blondel and others (2008). The arrow thickness is scaled according to the volume of trade in value-added of service export. Services include all business and personal services.

# Regional integration in ASEAN+3 has continued: an important counterweight against more pronounced protectionist tendencies following COVID-19.

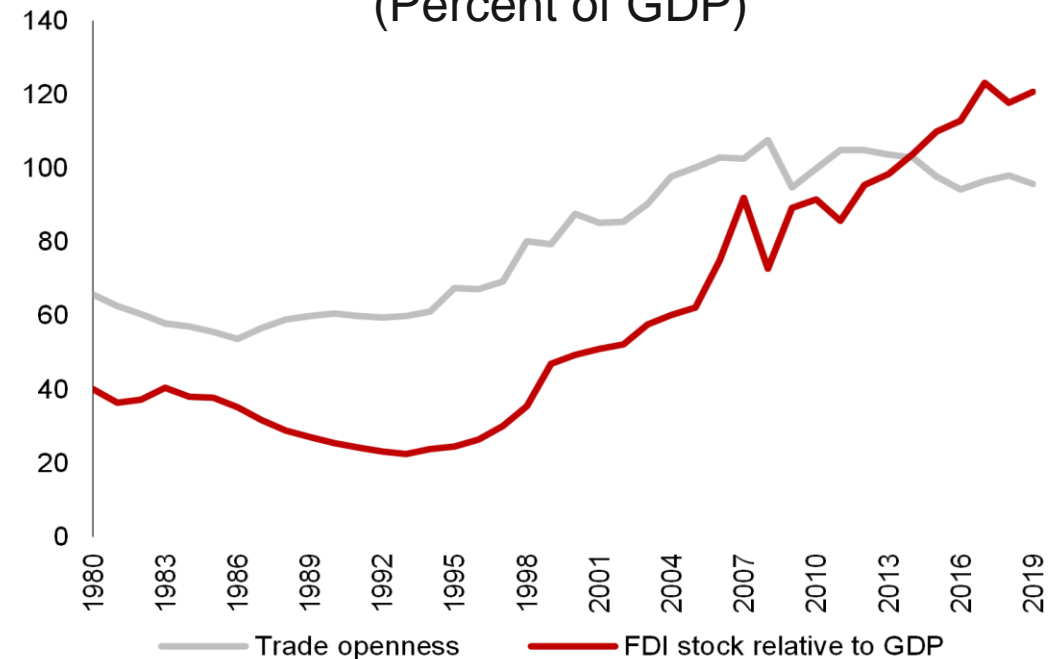
- *Some signs of deglobalization: interpret carefully: impact of economic downturns and growth rebalancing.*
- *ASEAN+3 region has a responsibility to be a key counterweight to protectionist tendencies.*

## Selected Indicators of Globalization



Sources: World Trade Organization; United Nations Conference on Trade and Development; Global Trade Alert; and AMRO staff calculations.

## EMEs: Trade and FDI Relative to GDP (Percent of GDP)



Sources: The Bank for International Settlements; The World Bank; United Nations Conference on Trade and Development; and AMRO staff calculations.

Note: EMEs are Algeria, Argentina, Brazil, Chile, China, Colombia, Czech Republic, Hong Kong, Hungary, India, Indonesia, Israel, Korea, Malaysia, Mexico, Peru, the Philippines, Poland, Russia, Saudi Arabia, Singapore, South Africa, Thailand, Turkey, and United Arab Emirates.



## **COVID-19 will not “undo” GVCs: These have become so intertwined and efficient that pulling out is nonviable. Business models will drive new and high-VA GVCs.**



Based on comparative advantage, even as countries develop new strengths and move up value chains.

No country can be self-sufficient. Not the US or China. Smaller countries have no chance.

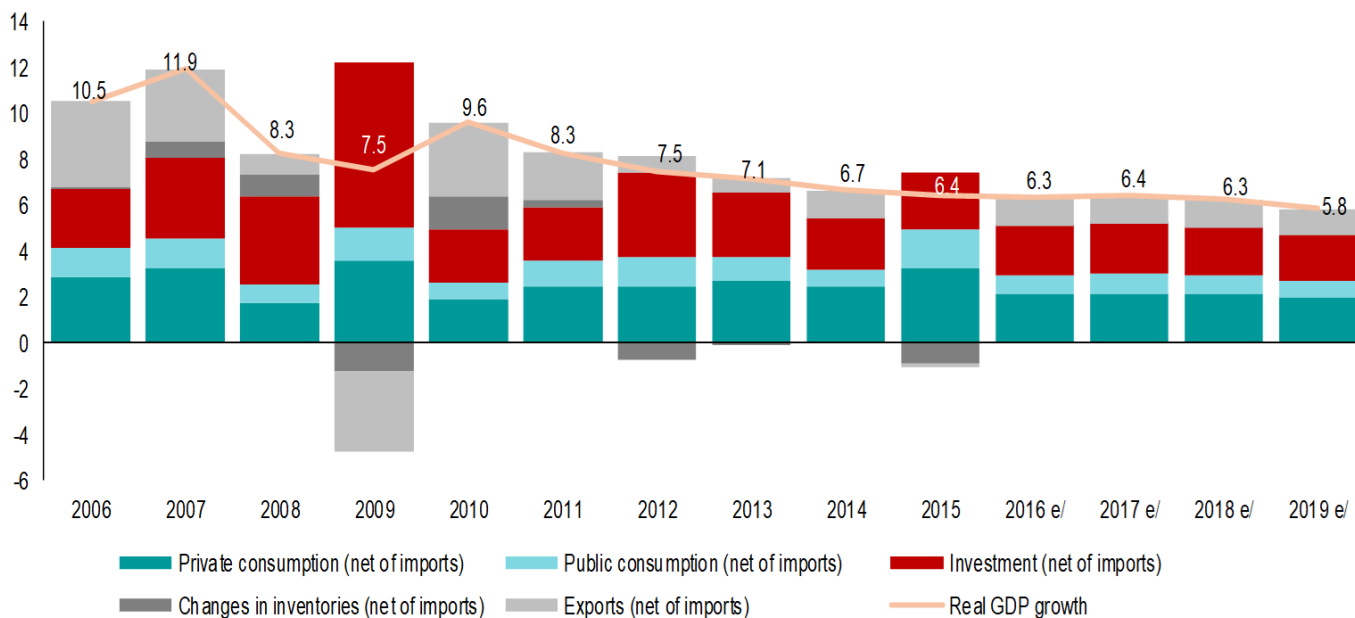
Regional groupings may be (seen as) an alternative “solution. But efficiency would be compromised.

More likely, further pursuit of competitiveness will lead to formation of newer and higher-VA GVCs.

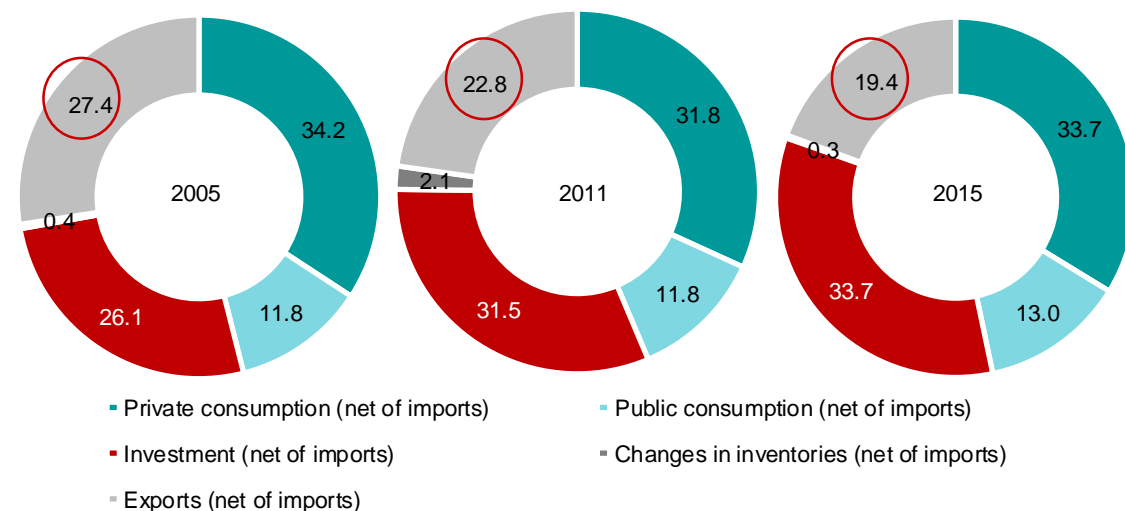
# The region confronts this challenge from a position of strength. Growth catch-up and rebalancing most pronounced among a sub-group: ASEAN-4, China, Vietnam.

- *GFC and European debt crisis led to collapse in external demand and major growth rebalancing.*
- *Domestic demand has become a much stronger driver of growth, especially in ASEAN-4, China, and Vietnam.*

### ASEAN-4, China, Vietnam: Contribution to GDP Growth, Import-Adjusted Method (Percentage point)



### ASEAN-4, China, Vietnam: Share of GDP Components, Import-Adjusted Method (Percent)



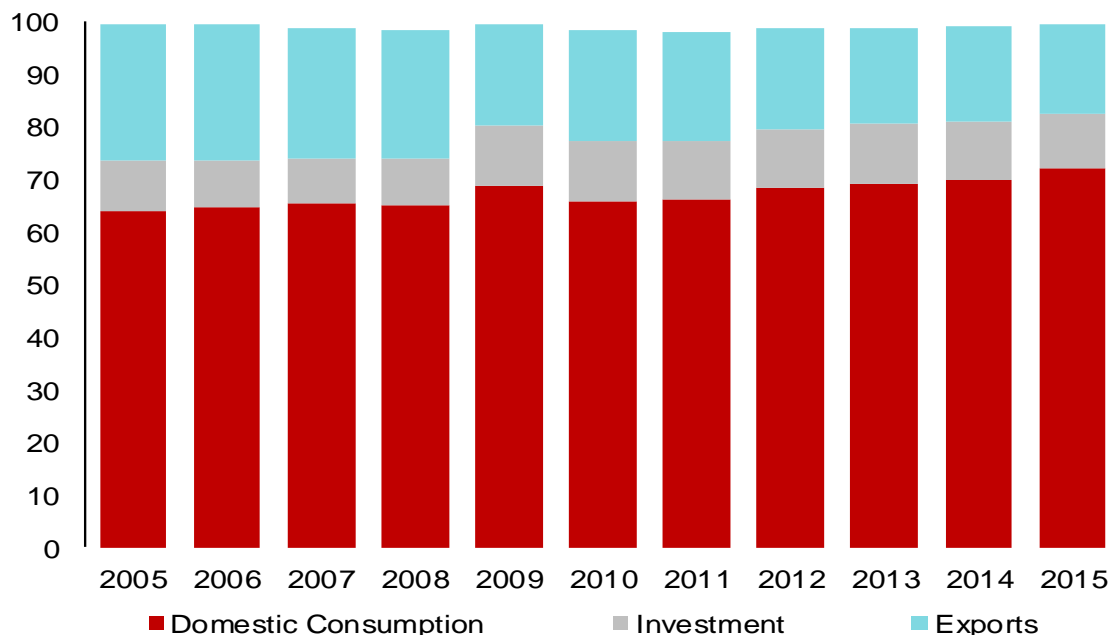
Sources: Organization for Economic Co-operation and Development; and AMRO staff calculations.  
 Note: OECD Input Output tables are only available from 2005 to 2015. Therefore, 2016-2019 estimates of each component are based on 2015 share. Real GDP growth is actual data.

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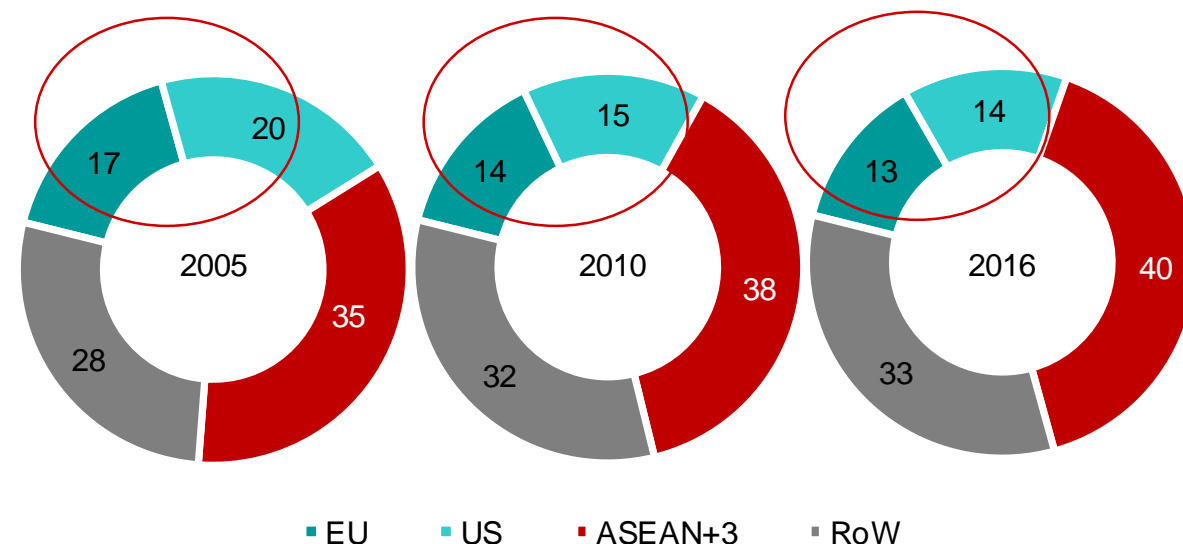
## While COVID-19 can prove to be a defining crisis, it is important not to lose sight of structural elements: Factory Asia has come a long way.

- *Factory Asia has been very much a broad region-wide phenomenon, not limited to China and ASEAN.*
- *Besides domestic demand, intra-regional demand has also strengthened markedly within a decade.*

**ASEAN-4, China, and Vietnam: Shares of Domestically Manufactured Goods for Domestic Demand and Exports**  
(Percent of total output)



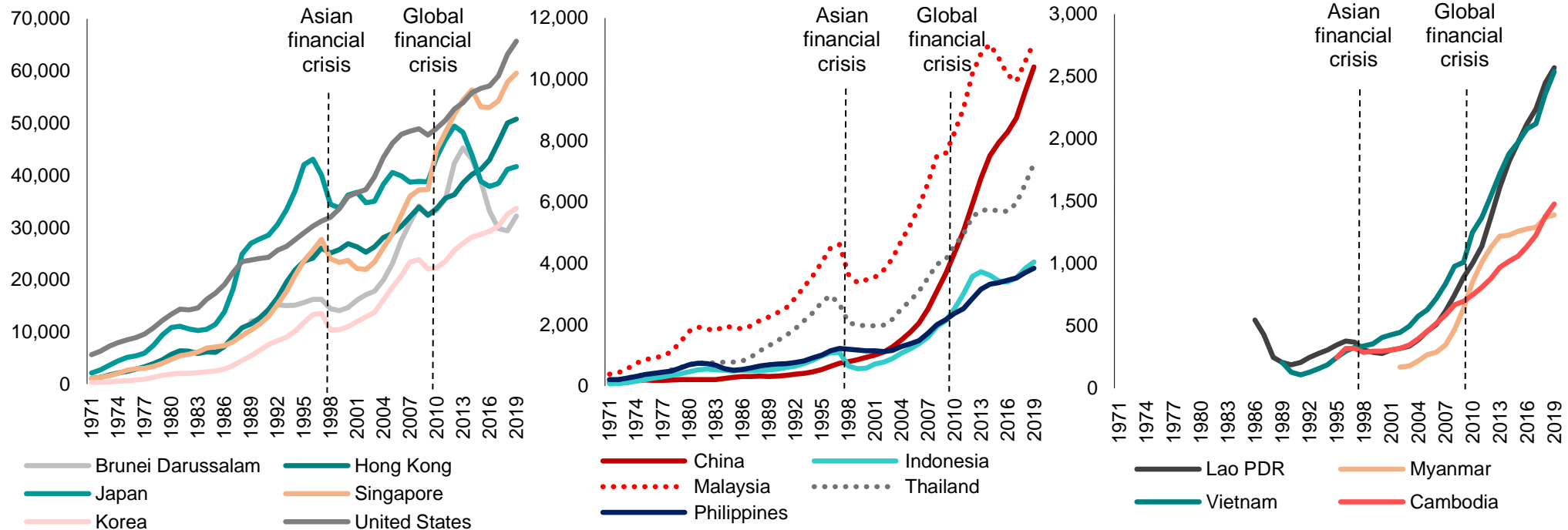
**ASEAN: Share of Value-Added Exports**  
(Percent)



# Shopper Asia came later, but is now also an important part of the story of the region's growth catch-up – as well as its prospects for post-COVID recovery.

- *The rise of Factory Asia has enabled the emergence of Shopper Asia.*
- *ASEAN+3 economies have been highly successful in using the manufacturing-for-exports strategy to industrialize and move up the production value chain – and just as importantly, climb up the income ladder.*

### Gross National Income Per Capita (US dollars)

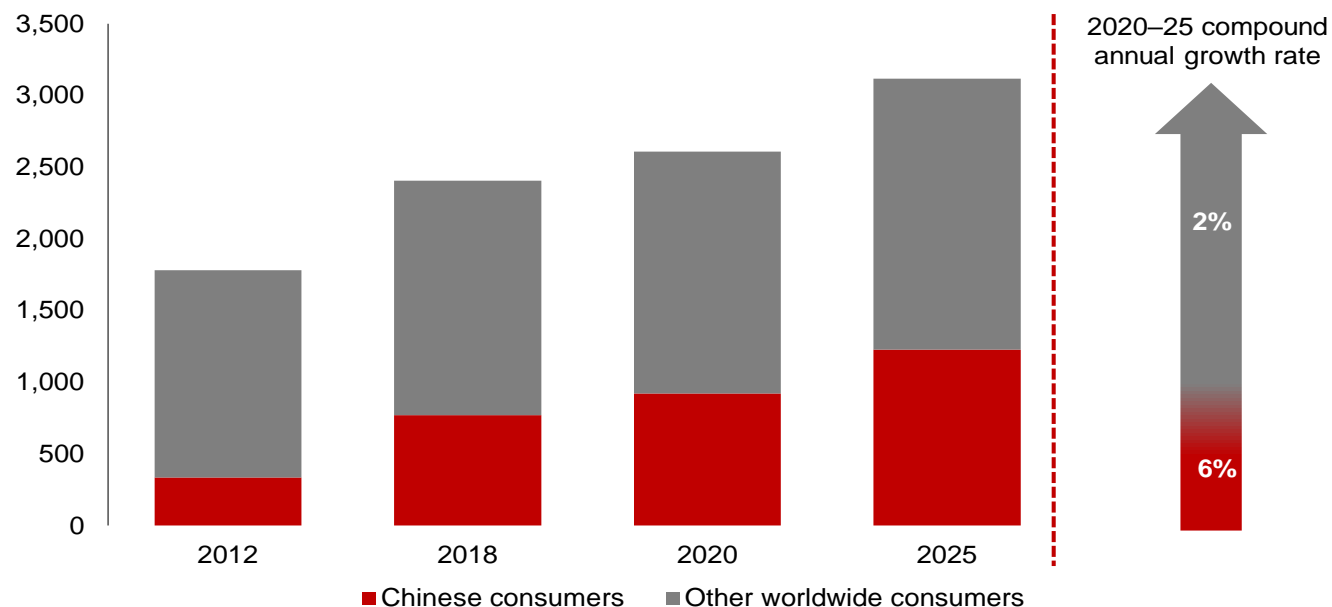


Source: The World Bank.

# A significant part of the Shopper Asia story continues to be about manufacturing, with both regional and global demand being important.

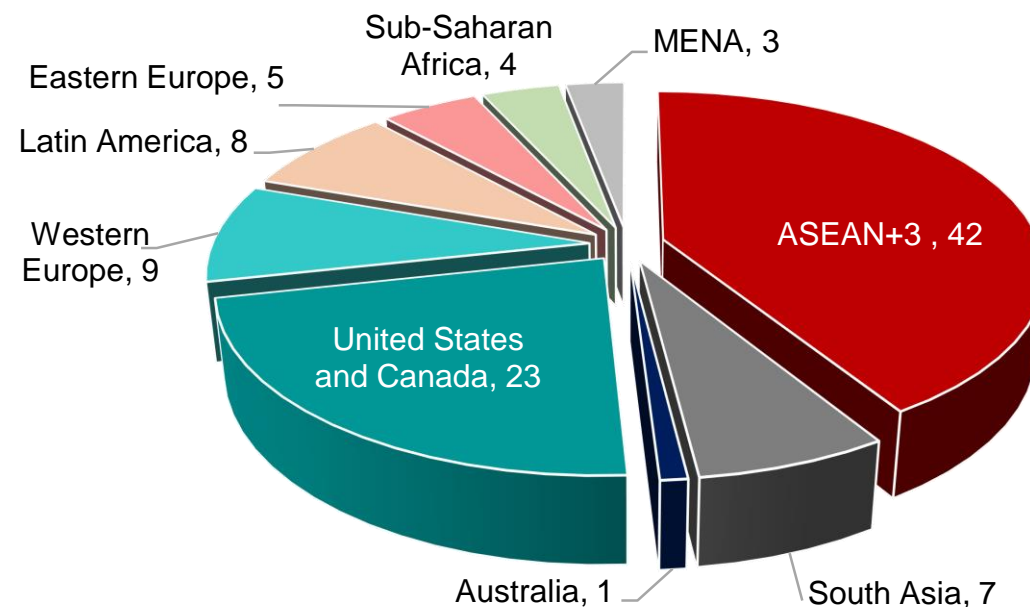
- *China is at the core: Its demand for luxury goods could double in next five years, from RMB 770 billion to RMB 1.23 trillion – some 40 percent of global market.*
- *ASEAN+3 region could drive 42 percent of global urban consumption growth by 2030.*

### China and the Rest of the World: Spending on Luxury Goods (RMB Billions)



Source: McKinsey & Company.

### Share of Urban Consumption Growth, 2015-30 (Percent)

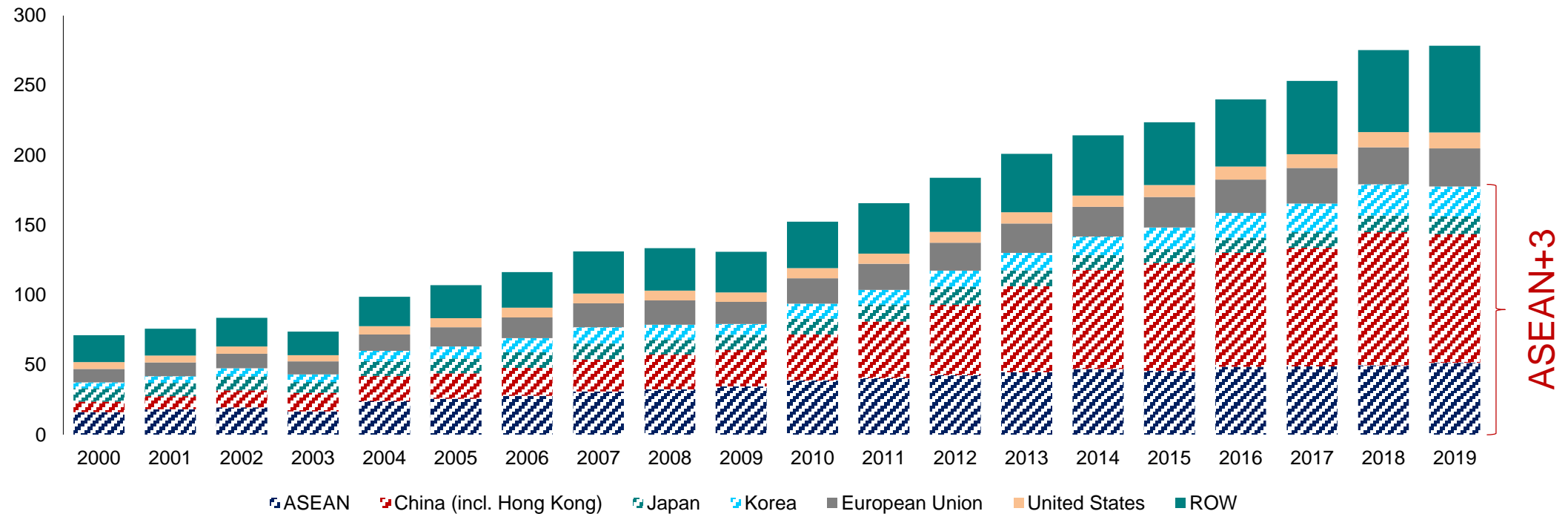


Source: McKinsey; AMRO staff calculations.

## But demand for services is growing rapidly, an intriguing case study for the new growth paradigm being tourism.

- *Tourism involves customizing “new economy” services for Shopper Asia.*
- *Studies highlight that tourism exhibits extensive linkages with other sectors of economies.*
- *How long will tourism activities take to recover to pre-COVID levels? Will GVCs remain intact?*

### ASEAN+3: Composition of Tourist Arrivals (Millions of People)

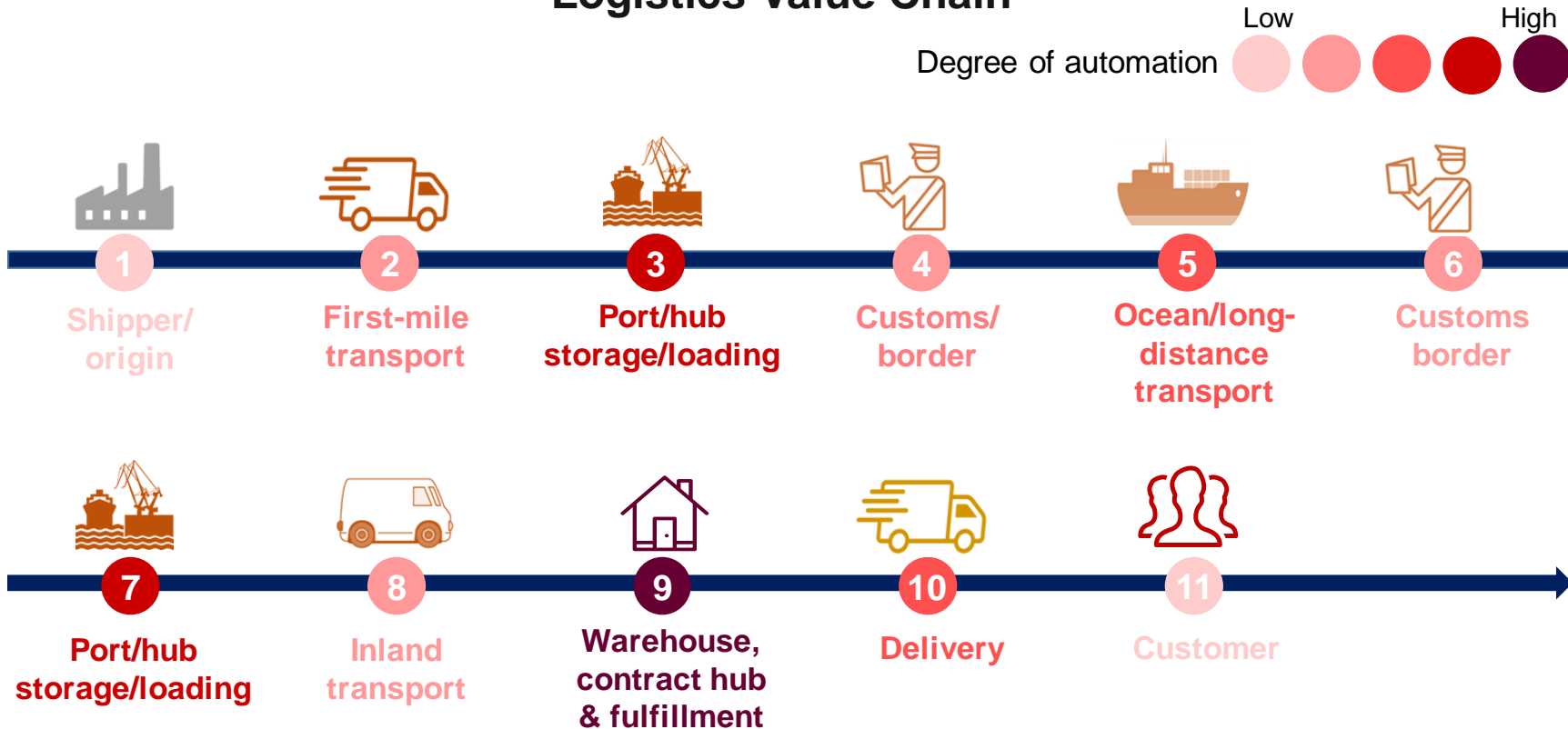


Note: 2019 China's and Lao PDR's tourist arrivals by country are estimated given data unavailability.  
Sources: National authorities; and AMRO staff calculations.

# Another case study for GVC upgrading is logistics: the sector will be lifted by growth of e-commerce; increased automation will focus on resilience and safety.

- *E-commerce was growing rapidly even before the pandemic; has picked up pace since.*
- *Logistics sector value chain was in the early stages of becoming more automated and efficient.*
- *Improvements henceforth will focus on resilience and safety, alongside efficiency and speed.*

## Logistics Value Chain



- *Use robots and drones to execute “contactless” tasks along entire value chain*
- *Further develop cross-border connectivity to widen options for moving goods*
- *Speed up adoption of digital tech to deliver services at different nodes of value chain*
- *What types of human capital will be needed to do all this?*

# The new economy is therefore about bringing Factory Asia and Shopper Asia together, leveraging on new digital technologies and developing “soft” factors.

## Traditional manufacturing for exports

- **Comparative advantage / cost-driven**

- GVCs
- Physical goods
- Specialization for cost efficiency

- **External demand growth**

- **Growth catch-up: “orderly” progression**

- Primary to manufacturing to services

- **Capacity and connectivity**

- Labor, capital, technology
- Physical infrastructure

## New growth paradigm

- **Competitive advantage and demand drivers**

- Production and trade networks
- New Economy: customized goods, services, experiences

- **Rebalancing:** domestic and final demand in ASEAN+3

- **Eclectic growth:** Leapfrogging, “disruptions”

- **Capacity and connectivity**

- Innovation, data analytics, new services
- Greater emphasis on soft infrastructure

- *Factory Asia serving Shopper Asia: several sectors will grow briskly*

- *GVCs are here to stay: need to extract even more gains and boost resilience to shocks*

- *Physical infrastructure is key*

- *Soft infrastructure becoming more critical*

- *Safety nets: financial, social*



## **Sum-up: GVCs will remain an integral part of the post-COVID global economy: the region must plug deeply into the global production base and marketplace.**



**Challenging external environment: covid-19 scar(e)s, protectionism, disruptive technology**

**GVC will be reconfigured and evolve because of protectionism and digital technology**

**ASEAN+3 region will do well - highly competitive and has a rapidly growing middle class**

**Region will be more integrated, but will continue to plug more deeply into the GVC.**

Thank you.



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