Global Environment: Four Key Trends

- Protectionism and regional integration
- 4th Industrial Revolution

- Rise of Factory Asia – regional supply chain
- Shopper Asia – rising middle class

Asia’s Growth Catch-up Through Globalization: Navigating Complex Challenges

- **Trade tensions, protectionist policies globally**
  - undermine export strategy?

- **Disruptive technology**
  - leapfrogging, not incremental upgrading
  - first mover advantage, network scale economies
  - evolution of comparative advantage: no longer orderly

- **New economy**
  - shift from manufacturing to services

- **Emergence of China**
  - huge consumer market
  - huge (low cost) labor force
  - disrupting the status quo...
  - a more insecure US, Europe

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

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

Source: AMRO staff.
Sectoral shifts: not the end of manufacturing/exports

- Advanced ASEAN+3 countries and then the upper-middle income ones gained much from the conventional manufacturing-for-exports growth model.
- Manufacturing’s contribution to growth and jobs will peak earlier and lower.

Thailand’s automobile industry also involves increasing integration between manufacturing and services. Domestic VA 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 along the Automotive Value Chain

#### Factory Stage
- Quality Assurance
- Production Management Service
- Warehousing Services for intermediate goods
- Sewage water treatment services
- Repair and maintenance services of machines and equipment

#### Delivery and sale stage
- Design of packages
- Packaging Services
- Freight transportation services
- Storage and warehousing services for finished goods

#### Post-sale Stage
- Customer Services
- Repair and Maintenance

#### Pre-production stage
- Industrial design
- Custom-related services for imported raw materials
- Storage of raw materials
- Freight transportation services of raw materials

Source: Asia-Pacific Economic Cooperation (2015); and AMRO staff.
- Factory Asia increasingly resembles a services hub, and is much more involved in value creation through R&D, product designs, and customizing service experiences.
- China becoming a key node in GVNs for services is a prime example.

**China’s integration into GVNs for service exports**

**2000**

**2018**

Sources: Asian Development Bank; and AMRO staff calculations.
As a large EM region, and the fastest-growing in the world, our region has a responsibility to be a key counterweight to the rise of protectionist tendencies in some parts of the world in recent times.

Elements of protectionism need to be addressed, and those trends reversed.

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

Sources: The World Bank; United Nations Conference on Trade and Development; and AMRO staff calculations.
At the aggregate level, domestic demand has become a much stronger driver of growth, especially in ASEAN-4, China, and Vietnam.

Global Financial Crisis and European Sovereign Debt Crisis led to a collapse in external demand and major growth rebalancing towards domestic demand.

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

<table>
<thead>
<tr>
<th>Year</th>
<th>Private consumption (net of imports)</th>
<th>Public consumption (net of imports)</th>
<th>Investment (net of imports)</th>
<th>Real GDP growth</th>
</tr>
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<tbody>
<tr>
<td>2006</td>
<td>10.5</td>
<td>11.9</td>
<td>8.3</td>
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<td>2007</td>
<td>9.6</td>
<td>8.3</td>
<td>7.5</td>
<td>6.4</td>
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<td>7.5</td>
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<td>7.1</td>
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<tr>
<td>2009</td>
<td>6.4</td>
<td>6.3</td>
<td>6.7</td>
<td>6.4</td>
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<tr>
<td>2010</td>
<td>6.3</td>
<td>6.4</td>
<td>6.3</td>
<td>5.8</td>
</tr>
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</table>

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

<table>
<thead>
<tr>
<th></th>
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<tbody>
<tr>
<td>2005</td>
<td>34.2</td>
<td>11.8</td>
<td>27.4</td>
<td>31.5</td>
<td>22.8</td>
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<td>2011</td>
<td>31.8</td>
<td>11.8</td>
<td>27.4</td>
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<td>2015</td>
<td>33.7</td>
<td>13.0</td>
<td>27.4</td>
<td>31.5</td>
<td>19.4</td>
</tr>
</tbody>
</table>

Sources: Organization for Economic Co-operation and Development; and AMRO staff calculations.
But the rise of Factory Asia has been very much a broad region-wide phenomenon, not limited to China and ASEAN.

Furthermore, 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**

<table>
<thead>
<tr>
<th>Year</th>
<th>Domestic Consumption</th>
<th>Investment</th>
<th>Exports</th>
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<tr>
<td>2005</td>
<td>28</td>
<td>35</td>
<td>32</td>
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<tr>
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<tr>
<td>2015</td>
<td>32</td>
<td>34</td>
<td>33</td>
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</table>

**ASEAN: Share of Value-Added Exports**

<table>
<thead>
<tr>
<th>Year</th>
<th>EU</th>
<th>US</th>
<th>ASEAN+3</th>
<th>RoW</th>
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<tbody>
<tr>
<td>2005</td>
<td>17</td>
<td>20</td>
<td>14</td>
<td>15</td>
</tr>
<tr>
<td>2006</td>
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<tr>
<td>2015</td>
<td>13</td>
<td>13</td>
<td>14</td>
<td>14</td>
</tr>
</tbody>
</table>

Sources: Organization for Economic Co-operation and Development; and AMRO staff calculations.
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 the income ladder.

**Source:** The World Bank.
Shopper Asia: intra-regional vs global demand

- China is at the core of this: Its demand for luxury goods is anticipated to double within the next five years, from about RMB 770 billion to RMB 1.23 trillion – accounting for some 40 percent of the global market.

- This is about manufacturing. And global demand remains highly important.

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

The new growth paradigm of Factory Asia serving Shopper Asia also involves the rapid development of certain sectors that enables the production capacity of the former to meet the pent-up demands of the latter.

Need to put in place or strengthen public infrastructure, including that for financial safety nets and social safety nets.

### Traditional manufacturing for exports
- Comparative advantage based on production costs
  - Global value chains (GVCs)
  - Physical goods
  - Specialization for cost efficiency; penalty for product differentiation (less scale economies)
- External demand, export-driven growth
- Growth: orderly, upward progression
  - Primary to manufacturing to services
- Capacity & connectivity
  - Labor upgrading, technology adoption
  - Physical infrastructure

### New growth paradigm
- Competitive advantage driven by (cost efficiency and) demand drivers
  - Global value networks (GVNs)
  - New Economy: services and experiences, gig economy
  - Customization to demand; product differentiation by bundling goods with (different) services
- Rebalancing: domestic & final demand in ASEAN+3
- Eclectic growth: lateral & upward progression
  - Leapfrogging, potentially disruptive
- Capacity & connectivity
  - Innovation, data analytics, new services
  - Physical, soft, digital, financial infrastructure
Case study: tourism: Customizing new economy services to Shopper Asia (e.g. medical tourism)

Studies highlight that apart from its growing role in ASEAN countries’ growth, tourism exhibits extensive linkages with other sectors of economies.

Sources: National authorities; and AMRO staff calculations.
### New growth paradigm: Logistics

- E-Commerce will give a boost to the logistics industry
- The conventional logistics value chain is not highly automated, but new technologies are creating potential for automation and productivity gains.

#### Logistics Value Chain

<table>
<thead>
<tr>
<th>Step</th>
<th>Activity</th>
<th>Degree of Automation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Shipper/origin</td>
<td>Low</td>
</tr>
<tr>
<td>2</td>
<td>First-mile transport</td>
<td>Low</td>
</tr>
<tr>
<td>3</td>
<td>Port/hub storage/loading</td>
<td>Medium</td>
</tr>
<tr>
<td>4</td>
<td>Customs/border</td>
<td>High</td>
</tr>
<tr>
<td>5</td>
<td>Ocean/long-distance transport</td>
<td>High</td>
</tr>
<tr>
<td>6</td>
<td>Customs border</td>
<td>High</td>
</tr>
<tr>
<td>7</td>
<td>Port/hub storage/loading</td>
<td>Low</td>
</tr>
<tr>
<td>8</td>
<td>Inland transport</td>
<td>Low</td>
</tr>
<tr>
<td>9</td>
<td>Warehouse, contract hub &amp; fulfillment</td>
<td>Medium</td>
</tr>
<tr>
<td>10</td>
<td>Delivery</td>
<td>High</td>
</tr>
<tr>
<td>11</td>
<td>Customer</td>
<td>High</td>
</tr>
</tbody>
</table>

New growth paradigm: Sustainability is key

- Factory Asia – Shopper Asia in the new growth paradigm will shape sustainable growth for ASEAN+3 region

  - Jumpstart (post-covid19) growth; address middle-income stagnation, flying geese "congestion"

- Disquiet about inclusiveness of technology-driven growth

  - Distributional concerns; economic and social disruptions

### Job Creation and Job Destruction in ASEAN-6

<table>
<thead>
<tr>
<th>Sector</th>
<th>Displacement effect</th>
<th>Income effect</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture &amp; mining</td>
<td>-10.1</td>
<td>4.3</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>-4.3</td>
<td>4.9</td>
</tr>
<tr>
<td>Utilities</td>
<td>-0.1</td>
<td>0.2</td>
</tr>
<tr>
<td>Construction</td>
<td>-2.0</td>
<td>2.9</td>
</tr>
<tr>
<td>Wholesale &amp; retail</td>
<td>-4.4</td>
<td>6.1</td>
</tr>
<tr>
<td>Transport &amp; tourism</td>
<td>-2.9</td>
<td>3.9</td>
</tr>
<tr>
<td>Business services</td>
<td>-1.2</td>
<td>1.9</td>
</tr>
<tr>
<td>Government &amp; community services</td>
<td>-3.0</td>
<td>3.9</td>
</tr>
</tbody>
</table>

Number of workers (million)

Source: Oxford Economics, Cisco.
Key takeaways: global production base and marketplace

- Tech-driven GVCs: nowhere to hide
- Services: supply and demand story
- Manufacturing still key: esp. for CLMV
- Integration, disruption, and protection

Challenges and Policy Implications

- Pervasive transition to tech-driven growth
  capacity to apply if not originate

- Supply side
  enhance sector-specific efforts alongside broad enablers

- Development strategy
  manufacture-for-exports
  still relevant, especially CLMV

- Openness
  hard/soft infrastructure, connectivity, regulatory frameworks

- Demand side
  maximize global demand for newer goods and services

- Human capital
  new economy skillsets – innovation, creativity, soft skills

Source: AMRO staff.
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