Benefitting from the Global Grid of Value Chains

by

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World trade and production is increasingly being structured around "global value chains" (GVCs). A value chain identifies the full range of activities that firms undertake to bring a product or a service from its conception to its end use by final consumers. Technological progress, cost, access to resources and markets and trade policy reforms have facilitated the geographical fragmentation of production processes across the globe according to the comparative advantage of the locations. This international fragmentation of production greatly increases efficiency and firm competitiveness. Currently, more than half of world-manufactured imports are intermediate goods (primary goods, parts and components, and semi-finished products), and more than 70 percent of world services imports are intermediate services.

The emergence of GVCs during the last two decades has implications for the impact of trade and investment barriers both on the country implementing the measures and on the global economy. There are a growing number of case studies on the globally integrated value chain at the product level. Likewise, more aggregate evidence has also been developed in order to get a more comprehensive picture of GVCs.

Capturing the Gains –making GVCs work for us

According to the World Investment Report (WIR) 2013, by United Nations Conference on Trade and Development (UNCTAD), it was noted that the Malaysian manufacturing sector is indeed making a transition from labor-intensive investments to high-technology investments. While other ASEAN countries had investments in the infrastructure, services and primary sectors, Malaysia's inbound FDI were largely in the manufacturing sector.

Are we moving from low value added economy with high participation to a high value added economy? Is Malaysia still a low cost manufacturing center and a parking space for capital & technology? Is our investment-driven growth strategy, sustainable & inclusive? Is there a trade-off between the environment and economic growth? Do we have a skill shortage that will impede us from becoming be a significant value enhancer?

It is no surprise that policy makers everywhere are looking for more and better policy evidence to examine the position of countries within international production networks. A number of indicators have been developed to help policy makers assess the role of their country in these GVCs. For example, trade policy instruments such as import tariffs, rules of origin and anti-dumping may directly hurt the competitiveness of domestic industries. A better understanding of whether countries are positioned upstream or downstream in the GVC will definitely help determine the actual costs of specific trade policies as well as assess the sensitivity of national economies to protectionist measures.

[1] The views and opinions expressed herein are those of the author and do not necessarily reflect the views of MIER.

Another issue is that of national competitiveness and growth, because of the growing interdependencies within GVCs, countries no longer rely exclusively on domestic resources to produce goods and services. National competitiveness not only reflect the technological capabilities and relative endowments that constitute a country's domestic production activities, but also the technological and factor endowments of countries from which the country in question imports intermediate goods. This would inevitably lead to moving up the value chain and innovation. Most of the value is thought to be created in activities upstream (examples include innovation, R&D, design) and downstream (examples include marketing, branding, logistics). On the other hand, it is hypothesized that only limited value is created in the pure manufacturing/assembly stages.

Interconnected Economies

It should be noted that with marked improvements in global interconnectedness, the effects of global systemic risks also become more pronounced. For example the earthquake/tsunami that hit Japan in March 2011 highlights the potential disruption/risks of value chains when key and upstream producers of inputs stop producing. As were with the flooding that occurred later in Thailand, which resulted in major disruptions in the automotive and electronics industries. Therefore mapping GVCs clearly illustrate the interconnectedness between economies and highlights the transmission of macro-economic shocks along global value chains. The vulnerability of individual countries to global shocks is directly determined by their participation and position in GVCs.

Jockeying for Economic Leadership in East Asia.

In the realm of international strategy and diplomacy, competition is usually a negative paradigm. Whether jostling over territory, contesting freedom of navigation or an arms race, strategic competition tends to be risky and counterproductive. In other domains, however, competition should be welcomed. For example, in a market economy, competition leads to innovation and efficiency. Therefore, what should be avoided between China and the United States is to be encouraged between Apple and Samsung.

Is the United States losing to China in the long-term geopolitical competition in East Asia? Are smaller states in Asia tilting towards China for economic benefits at the expense of US interests? Is the continuing uncertainty surrounding Trump’s external policies creating more room for China to expand its influence in Asia?

There is no reprieve for Malaysia, sooner or later would have to formulate our big power policy. Undoubtedly it will be driven by domestic political necessity, especially economic gains.