

UK–ASEAN Trade: Strengthening the Supply Chain Linkages

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Executive Summary

Executive Summary

The United Kingdom (UK) shares rich historical, economic, and social relations with the Association of Southeast Asian Nations (ASEAN) and its Member States. The UK applied to become a Dialogue Partner of ASEAN and formally established a mission to ASEAN in 2020. The year 2020 was also witness to an extraordinary pandemic of the coronavirus disease (COVID-19) which, besides bringing untold misery and death, has resulted in restrictions or limitations on the movement of people and goods across borders. The resilience of trade mechanisms and the global and regional value chains are being tested for stress and shocks, as the pandemic continues in most parts of the world.

In this backdrop, both the UK and ASEAN have reinforced the will to work in partnership for rebuilding and recovery, and sustainable growth, in the post-COVID-19 phase. The UK is looking towards greater integration into Asia and playing a significant role in the emerging economic architecture in the Indo-Pacific in which ASEAN has a central role. Towards this, the UK initiated this study to

- understand the performance and resilience of supply chains in ASEAN during COVID-19
- implement the expansion and deepening of the UK–ASEAN trade and investment relationship, and
- deepen integration with the goods and services value chains in ASEAN and East Asia.

Through these, the UK will also support ASEAN's strategy for strengthening its economic resilience in the post-COVID-19 recovery and rebuilding.

The Economic Research Institute for ASEAN and East Asia (ERIA), Jakarta, has conducted this study for the UK, drawing data and evidence from its existing research and policy studies on trade and supply chains in the ASEAN region and East Asia. Evidence from ERIA's studies on COVID-19 and its effect on the regional economy has also been used.

ASEAN's Economic Resilience in Response to the Outbreak of COVID-19

ASEAN economies experienced overall growth of 4.6% in 2019. The COVID-19 pandemic in 2020 significantly affected trade and supply chains around the world, including ASEAN, resulting in the weakening of international trade. Except for China and the United States (US), ASEAN's trade with all the major trading partners declined during 2020.

According to ASEAN Secretariat publications, in 2020, the region's economy was projected to contract by 3.8% – the first contraction in 22 years. Fortunately, the quick restoration of supply chain activities after the first few months of negative supply shocks has ensured that the ASEAN region will regain positive growth in 2021. Before the pandemic, ASEAN's supply chains witnessed US–China trade tensions. However, the stable foundation of trade and investment links, and the absence of non-traditional trade policies from both the US and China to discriminate against international suppliers from the ASEAN region, have prevented the trade tensions from causing any significant alteration to supply chain linkages. Comparatively, the pandemic has brought about far more changes in firms' supplier and customer relations. These changes were made in response to the shocks encountered by the supply chains.

The ASEAN economies experienced three types of economic shocks caused by the COVID-19 pandemic. The first type is negative supply shocks experienced at the beginning of the COVID-19 pandemic in 2020 when the economies of the ASEAN Member States (AMS) experienced a shortage of intermediate inputs originating in China. The second type is negative demand shocks where lockdown measures brought about a demand shortage. The third type is positive demand shocks to the goods and services supplied in response to the demands arising from the COVID-19 pandemic, such as healthcare supplies, work-from-home requirements (e.g. information and communication technology (ICT) equipment), and internet-based services. These positive demand shocks are pressures on the current production network and service suppliers, but at the same time, are opportunities for firms to expand their business.

The AMS have seen that health policy, i.e. lockdown and social distancing, halts both supply and demand. ASEAN's production facilities and supply chains are still there – almost intact. After taming the disease, however, ASEAN must confront the negative demand shock because persistent low demand may decay its supply chains in the long term. Planning for a scenario in which the disease is brought largely under control will be important.

Policy Guidance for ASEAN's Economic Resilience and Rebuilding

Since the onset of the pandemic, the policy direction in ASEAN has shown unequivocal resolve to support ASEAN's core economic dynamism. The ASEAN Economic Ministers resolved to strengthen long-term supply chain resilience and sustainability, and to remain committed in keeping the ASEAN market open for trade and investment. They also recognised the importance of economic cooperation with external and development partners for strengthening regional supply chains.

The 'Hanoi Plan of Action on Strengthening ASEAN Economic Cooperation and Supply Chain Connectivity in Response to the COVID-19 Pandemic' stresses cooperation in enabling trade in important goods and the production of and access to COVID-19 medicines and vaccines through the strengthening of supply chain connectivity.

These policy measures provide a template to preserve the ASEAN supply chains' resilience and to enhance the trade and economic cooperation mechanisms within ASEAN and with its Dialogue Partners during and in the post-COVID-19 recovery phase.

For its collective and long-term socio-economic recovery, the ASEAN Comprehensive Recovery Framework (ACRF) was adopted at the 37th ASEAN Summit in Ha Noi, Viet Nam. It also serves as the consolidated exit strategy from the COVID-19 crisis.

The five broad strategies that are deemed most impactful to take the region through the recovery process and its aftermath are (i) enhancing health systems, (ii) strengthening human security, (iii) maximising the potential of the intra-ASEAN market and broader economic integration, (iv) accelerating inclusive digital transformation, and (v) advancing towards a more sustainable and resilient future.

The ACRF address both ASEAN's immediate needs during the **reopening** stage for a successful transition to the 'new normal', as well as its medium- and long-term needs through the stages of COVID-19 **recovery** and for longer-term **resilience**.

UK–ASEAN Partnership for Recovery and Building Back Better

Broad strategy 3 of the ACRF – maximising the potential of the intra-ASEAN market and broader economic integration – emphasises the importance of increased trade in ASEAN in the post-pandemic recovery. UK trade with ASEAN and enhanced trade relations with ASEAN’s major trading partners in the Indo-Pacific (Australia, China, India, Japan, the Republic of Korea, New Zealand, and the Pacific) will provide an important platform for supporting this critical strategy in the ACRF.

The UK upholds the policy for keeping markets open for trade and investment as it deepens its economic relations in ASEAN and the larger Indo-Pacific region. The ASEAN Economic Community is a natural partner for the UK in this exercise. Streamlining the investment facilitation process, eliminating non-tariff barriers, and creating regulatory coherence between the two economies (or at least with some AMS initially) are important next steps as they will create a conducive environment for deepening and expanding the UK–ASEAN supply chain, and support the post-COVID-19 rebuilding process. Infrastructural and institutional connectivity plans outlined in the Master Plan on ASEAN Connectivity 2025 should also attract new investments between the UK and ASEAN.

UK support to the priority areas of economic integration strategy of the ACRF must be based on the UK’s own core policy on post-COVID-19 recovery and rebuilding. The principle of ‘build back better’ should lead the UK’s economic engagement with ASEAN for recovery in the near term while enhancing the bilateral trade in goods and services on both sides.

The UK’s international policy to firmly establish itself as a global science and technology and responsible cyber power would be its signature contribution to partnership with ASEAN. This contribution would lie in investments and capacity building for greater participation of ASEAN in the supply chains of the digital economy, especially in manufacturing industries that utilise automation, robotics, and artificial intelligence. Creating capacities and markets for diversifying ASEAN’s trade in services into finance, ICT, and other services components of goods trade would be a strategic choice for both sides. Similarly, investments in the manufacturing of environmental products and green technology would forge a future-ready partnership. Bringing ASEAN’s core strength in manufacturing to the UK market would be a reciprocal step.

AMS, including the least developed countries, face the challenge of recovery from COVID-19 induced disruptions to the economy. AMS must rapidly undertake digital transformation and structural reforms to remain engaged in the value chain of a more digitalised global economy. COVID-19 instigated a beta test for ASEAN’s integration into the digital economy value chains and underlined the need for increased investment in digital connectivity and human capital. Concerted UK–ASEAN cooperation is required to cover a spectrum of needs, with infrastructure, regulatory frameworks, and data flow and security being the immediate challenges.

Demand for environmental and green products will continue to grow. The twin strengths of research and development and technology (UK), an established base in sectors such as electronics and motor vehicles (ASEAN), and the existence of an effective supplier network and integrated supply chains could be an important advantage for both partners in building back better supply chains for the future. The UK’s Ten Point Plan for policies and public investment in low-carbon technologies and services could be linked with ASEAN for supply chains and markets. This would ensure supply chain efficiency, trade integration, jobs, and growth on both sides.

ASEAN's trade in services relies greatly on the travel and tourism sector. Travel accounted for 33% of ASEAN's total services exports in 2019. The UK is a global player in the services sector, especially in finance, logistics, and ICT, which have important roles in the digital economy as well as being a component of goods trade. Investments and technical cooperation in these sectors would facilitate AMS diversifying into other sectors of services trade. On the UK's part, research and development (defined as 'other business services' in services trade) is a core strength of its economy. The future of work and employment growth in ASEAN requires greater expenditure and technical collaboration in education and innovative learning. Collaboration in higher education and research and development activities in medicine, agriculture, robotics, and low-carbon technologies would be the UK's quintessential role in the UK–ASEAN cooperation plan.

Bilateral Trade and Integration

Trade flows between the UK and ASEAN are modest at present, with the UK comprising about 1.26% of ASEAN's total trade. This is similar to other key European economies, even though the European Union (EU) is ASEAN's third largest trade partner from outside the region. The UK competes with the EU member countries for most export items – machinery and equipment, textiles, and chemicals and pharmaceuticals. A trade agreement with ASEAN (or with some key AMS) would put the UK at an advantage in the ASEAN markets.

Since 2010, China has emerged as ASEAN's top trading partner, replacing Japan, the EU, and finally the US. This reflects the intricate supply chains in ASEAN and East Asia, in which trade in parts and components is very high. This factor will resonate repeatedly in all bilateral trade plans and supply chain participation between the UK and ASEAN. From the UK perspective, the share of trade with ASEAN is higher and has increased on the export side, reaching around 3% of total UK trade in 2019. Still, the share of UK exports to ASEAN remains rather modest, particularly when compared with the size of ASEAN economies globally and, most importantly, their fast growth. The UK may note that the ASEAN region has also emerged as a market for finished goods. Machinery and equipment are the largest traded sector between the UK and ASEAN, followed by textiles. ASEAN's exports in the agriculture and food sector to the UK are important too, but are low compared with its agricultural exports to China, Japan, and the US.

On a bilateral basis, there are deviations in the sectoral composition of UK exports to ASEAN. The share of machinery and equipment is particularly large to Cambodia, the Lao PDR, Malaysia, and Singapore, while the share of metal products exported to Indonesia and Viet Nam and agricultural products to Myanmar is higher. The sectoral structure is more heterogeneous for UK imports across AMS partners, reflecting to a large extent the product specialisation of each ASEAN economy.

Apart from Singapore, UK trade in services with AMS is also low. At the country level, the UK has a trade surplus with Malaysia, Singapore (although sector-wise, Singapore has a favourable balance in business services, including professional activities), and Indonesia. Given the UK's large trade in services with other areas of the world, especially the US and the EU, ASEAN's growing markets provide an ideal opportunity for expanding trade with ASEAN. Japan is an existing competitor in financial services, so the UK must offer competitive and innovative products to ASEAN, especially to youth, start-ups, and new entrepreneurs.

Planning ahead, ASEAN offers an important opportunity for greater integration of the UK in the trade flows of Southeast and East Asia. The UK's decision to apply for accession to the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) is an important signal to the whole Asia-Pacific region, and will help the UK to participate in developing common standards and shaping the economic architecture of the region. Overcoming the gravitational forces that dictate value chain participation would be possible through deft and forward-looking policy arrangements with ASEAN. The Regional Comprehensive Economic Partnership (RCEP) will accelerate interconnectivity in ASEAN and East Asia, even though it is mostly concerned with trade in goods and tariffs. For greater trade integration, the UK must closely follow ASEAN's trading agreements, including ASEAN's own mechanisms such as the ASEAN Single Window (now open for Dialogue Partners) and the Guidelines for the Implementation of ASEAN Commitments on Non-Tariff Measures on Goods.

Trade integration is very important for ASEAN, especially participation in global value chains (GVCs). Significantly, ASEAN's trade integration has progressively shifted away from developed to developing economies. China-ASEAN and intra-ASEAN GVC integration is more prevalent, although a partial recovery with the EU has been noticeable since 2010. Structurally, GVC integration of ASEAN with other economies predominantly corresponds to backward participation, especially with the US and Japan. However, ASEAN's bilateral integration has changed over the years, positioning ASEAN more upstream with respect to the EU and downstream with respect to China – accounting for greater participation of Chinese inputs in ASEAN exports.

GVC integration between ASEAN and the UK is asymmetrical in both its characterisation and evolution. Backward participation accounts for the largest share for ASEAN, while forward participation contributes more for the UK – emphasising its input export specialisation. From a country perspective, the most significant bilateral integration is with Singapore.

Planning Ahead

Supply Chain Performance in ASEAN: Opportunities for the UK

An ERIA survey of domestic and international firms in ASEAN and India shows that the COVID-19 pandemic significantly impacted manufacturing and non-manufacturing firms in the AMS. While the impact was negative on average, most of the firms were able to quickly adjust trade with their customers and suppliers across countries and globally. Manufacturing firms showed better performance in 2020 than other industries, which suggests that international production networks in the region have been relatively robust to negative supply shocks. Additionally, ICT services firms experienced better business outcomes and are more likely to expand their businesses and to increase recruitment than other industries. Positive demand shocks have benefitted the ICT industry, and its growth will continue. Businesses that encountered increased sales have a positive outlook for 2021, with plans for expansion. However, firms expect greater support from the government in the form of tax rebates and restoration of the mobility of people across borders.

The better than average performance of the ASEAN markets – supported by policy measures such as the Hanoi Plan of Action to keep the market open to trade and investment – can help ASEAN's trading partners, including the UK, to plan and invest in the value chains of production in the region. The changing patterns of customer and supplier relationships amongst the firms in ASEAN present an opportunity for UK businesses to diversify their supply of goods and services as well as markets away

from the EU into the ASEAN region, and into the larger East Asia region with which ASEAN shares an intimate supply chain network and market. Increased mutuality between two economies will help to mitigate the negative supply shocks and negative demand shocks on both sides. Importantly, for the UK, the positive demand shocks create an opportunity to provide its goods and services in the ASEAN region.

The UK and ASEAN: Trade Policy Convergence for Enhanced Trade and Strong Partnership

The promise of building back better should be at the core of UK–ASEAN policy engagement in the months ahead, while the ASEAN Economic Community will be the UK’s most appropriate partner in the regional architecture. The ASEAN Economic Community Vision 2025, the Master Plan on ASEAN Connectivity 2025, and the ASEAN Outlook on the Indo-Pacific are important guides for implementing UK objectives of expanding and deepening its trade relations in ASEAN and the Indo-Pacific. Like all important economic partners of ASEAN, an ASEAN+1 process for the UK is the next step.

As ASEAN is already a manufacturing hub, closer trade relations with ASEAN would improve the UK’s integration in GVCs outside the EU, in particular those of Asia. GVCs are partial to efficiency, therefore product matching can be achieved only through supply chain efficiencies and market demand, as seen in the case of reduced trading in petroleum. Close evaluation of the future needs of the region will help grow the basket of traded goods between ASEAN and the UK. ASEAN is preparing to play a larger role in the value chains of the new digital economy. The UK’s competitiveness in the digital economy, services components of goods trade, research and development, financial services, and low-carbon and green products is an important channel for integrating the UK economy into both existing and pipeline supply chains in ASEAN and East Asia. Accession to the CPTPP would be helpful in this regard. More immediately, bilateral trade agreements concluded with Japan and Australia, and the forthcoming one with India, would also matter as these economies are closely networked with ASEAN’s economy. The economic and institutional diversity in ASEAN also point to the importance of bilateral trade agreements with individual AMS. Viet Nam’s free trade agreement (FTA) with the EU is a good example of mutual economic benefit and enhanced trade. The EU–Singapore FTA is similarly designed and complements the services economy on both sides.

The Road Ahead

The ASEAN region has shown, so far, that its supply chains have been fairly able to withstand the supply and demand shocks. The implications of the pandemic are principally macroeconomic, with some difference across sectors. So far, Southeast Asia has shown that it is particularly well placed to take advantage of improved global demand later in 2021, in particular from Europe and the US.

Trade and investment policies will assume more significance in the coming months as they determine the ability of firms to contest foreign markets or to source intermediate inputs from foreign suppliers. For the UK and ASEAN, trade and investment facilitation will be crucial as it can increase backward and forward linkages and deepen the trade integration. Nurturing the business environment would also play a role in structuring the trade relations.

A UK–ASEAN trade and economic cooperation plan must consider China – ASEAN’s largest trading partner. Closely integrated value chains between China and ASEAN have cast a shadow on some trade and investment partnerships of ASEAN, e.g. with the EU, and most noticeably with India. The emerging economic architecture in the Indo-Pacific, in which ASEAN has a central role, also faces the inescapability of supply chain integration between ASEAN and China. The Indo-Pacific is also working

towards diversified supply chains in the region. This underlines the recommendation that the UK plan for integration in the value chains of the digital economy in ASEAN, as there is both the scope and immediate need for efficient and trusted partners. Investments in infrastructure for the digital economy and cybersecurity are the two most pressing needs in the region for it to grow as a digital economy hub. The UK should be ready and able to fulfil both the capacity needs and trust issues required in this industry. Closer alignment with new supply chains emerging in the region – such as Australia–Japan–India, the Mekong Subregion, and India–Myanmar–Thailand – will be important for UK trade missions to keep the UK’s interest active in these emerging alignments.

The UK and ASEAN are some of the most open markets for both trade and investment. However, preferential trade and investment arrangements and regulatory connectivity focusing on identified core sectors will be better than wide-ranging FTAs. Concessions in the mobility of people and capital should be favourable in all plans, given that most regional trade arrangements have nearly by-passed these issues due to their emphasis on trade and tariffs, and less than meaningful services components.

Reviving the UK’s historical presence in the businesses of Southeast Asia through contemporary and future-ready trade facilitation and investment plans – and promoting ASEAN’s core competency in manufacturing in the UK – is the practical direction ahead for UK–ASEAN bilateral trade.

Chapter 1

Introduction

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Introduction

The relationship of the United Kingdom (UK) with the Association of Southeast Asian Nations (ASEAN) and its Member States has deep foundations and a long history. The UK shares rich historical, economic, and social relations with ASEAN, having been a Dialogue Partner of ASEAN through the European Union since 1977. The year 2020 was a landmark for UK–ASEAN relations, as the UK applied to become a Dialogue Partner of ASEAN and formally established a mission to ASEAN. The year 2020 was also witness to an extraordinary pandemic of the coronavirus disease (COVID-19) which, besides bringing untold misery and death, has resulted in restrictions or limitations on the movement of people and goods across borders. The resilience of trade mechanisms and the global and regional value chains was tested for stress and shocks. UK and ASEAN are nevertheless committed to increase the bilateral trade and support the post COVID-19 recovery plan in ASEAN.

The UK–ASEAN trade and economic partnership is on an upward trajectory. Over the last decade to 2019, bilateral trade increased by 68.5%, reaching £41.7 billion (\$52.1 billion) in 2019. The UK is the world's 6th largest economy, and has strong foundations in free trade, services, science and innovation, cybersecurity, green growth, and effective public health systems. The UK and ASEAN share common prospects for trade and technical cooperation; and significant potential for deeper economic collaboration, leading to shared prosperity.

The UK has given the highest priority to deepening trade and economic partnerships with ASEAN. The Asian economy, especially that of ASEAN and East Asia, has been the driver of the global economy in the recent past, and ASEAN continues to show strong resilience during the COVID-19 pandemic and is well positioned to emerge strongly from the economic crisis.

The global challenges have reinforced the UK's determination to work in partnership with Asia and the Indo-Pacific, and to make the prospects of deeper economic and trade collaboration between the UK and ASEAN even more timely and significant. The UK–ASEAN partnership is geared to enhance the East Asia region's economic dynamism and ensure supply chain connectivity for the smooth flow of trade between the UK and ASEAN. The UK–ASEAN partnership would also strengthen the UK's participation in the larger Indo-Pacific architecture, in which ASEAN has a central role. This partnership will fulfil the global role of the UK as an open economy and a maritime trading nation envisaged in the UK Government's Integrated Review of Security, Defence, Development and Foreign Policy.

Recognising the existing strengths and future scope of UK–ASEAN relations and the challenges emanating from the COVID-19 induced economic and health crisis, the UK has undertaken a study of UK–ASEAN supply chains that emanates from ASEAN's regional objectives and frameworks for strengthening and deepening ASEAN's economic resilience. The Economic Research Institute for ASEAN and East Asia (ERIA) has conducted this study, drawing data and evidence from its existing research and policy studies on trade and supply chains in the ASEAN region and in East Asia. Evidence has also been used from ERIA's studies conducted in the wake of COVID-19 and its effect on the regional economy. Trade statistics available in the public domain have also been processed to evaluate bilateral trade flows and trade integration between the UK and ASEAN, establish pathways for UK–

ASEAN trade in the post-COVID-19 recovery and rebuilding phase, and a prognosis for a longer-term roadmap of trade and economic cooperation. The guidance is placed in the context of the UK's blueprint for economic engagement with ASEAN and its participation in the emerging economic architecture of the Indo-Pacific.

ERIA is grateful to the UK government for being entrusted to carry out this important study and contribute to the economic integration of ASEAN and East Asia with UK.

The results of the study will be reported to the UK–ASEAN Economic Ministers' Dialogue/Meeting in September 2021.

Chapter 2

UK–ASEAN Trade: Strengthening the Supply Chain Linkages

Chapter 2

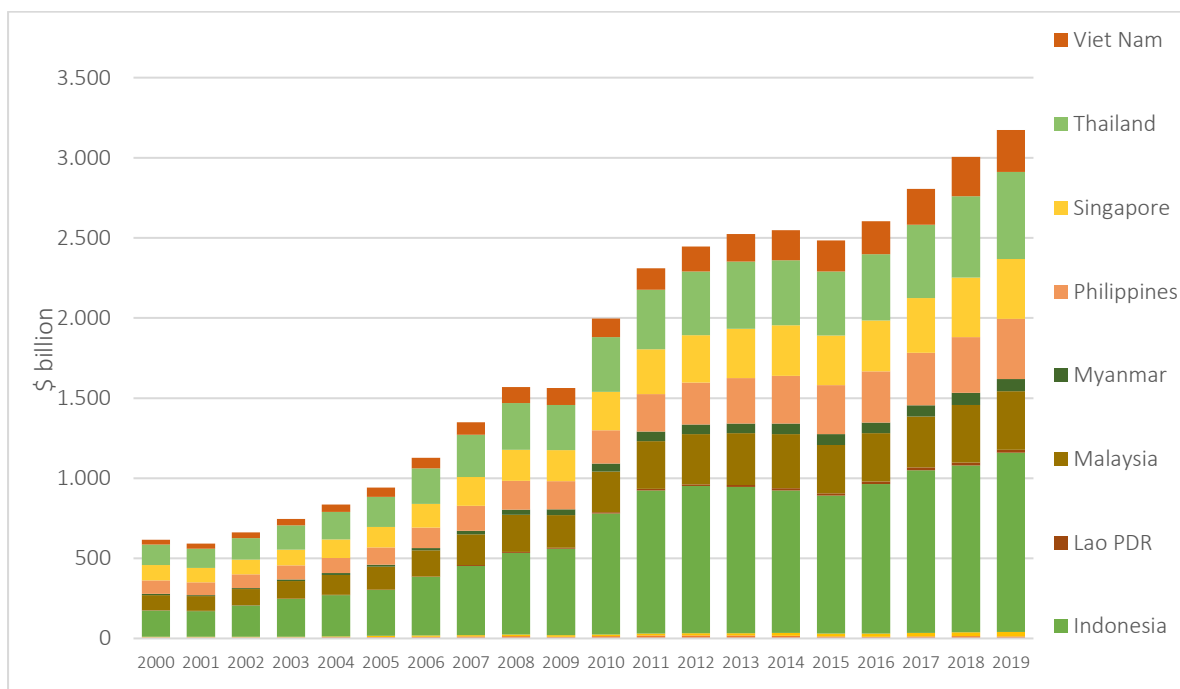
UK–ASEAN Trade: Strengthening the Supply Chain Linkages

This chapter sets the context for studying the supply chain linkages between the United Kingdom (UK) and the Association of Southeast Asian Nations (ASEAN). It covers the prevalence of supply chains in ASEAN, their performance and competitiveness, and institutional partnerships with major economies. It describes supply chain resilience and performance since the outbreak of the coronavirus disease (COVID-19), and policy directions for maintaining the supply chain dynamism in ASEAN – both at the government level and at the firm level. It describes the ASEAN Community framework for strengthening supply chains and rebuilding during and after COVID-19, and the likely support from the UK in specific areas. It outlines the policy convergence and pathways for UK–ASEAN supply chain linkages in goods and services, especially in the post-COVID-19 rebuilding phase.

ASEAN’s Economic Resilience in Response to the COVID-19 Outbreak

Before the outbreak of COVID-19, ASEAN economies experienced overall growth of 4.6% in 2019. Figure 2.1 indicates the diversity in economic size amongst ASEAN Member States (AMS) – with Indonesia as the largest, accounting for 35.4% of the region’s gross domestic product (GDP) in 2019, followed by Thailand (17.2%), the Philippines (11.9%), and Singapore (11.8%) (ASEAN, 2021).

Figure 2.1: Total GDP Growth in ASEAN Member States, 2000–2019 (\$ billion)



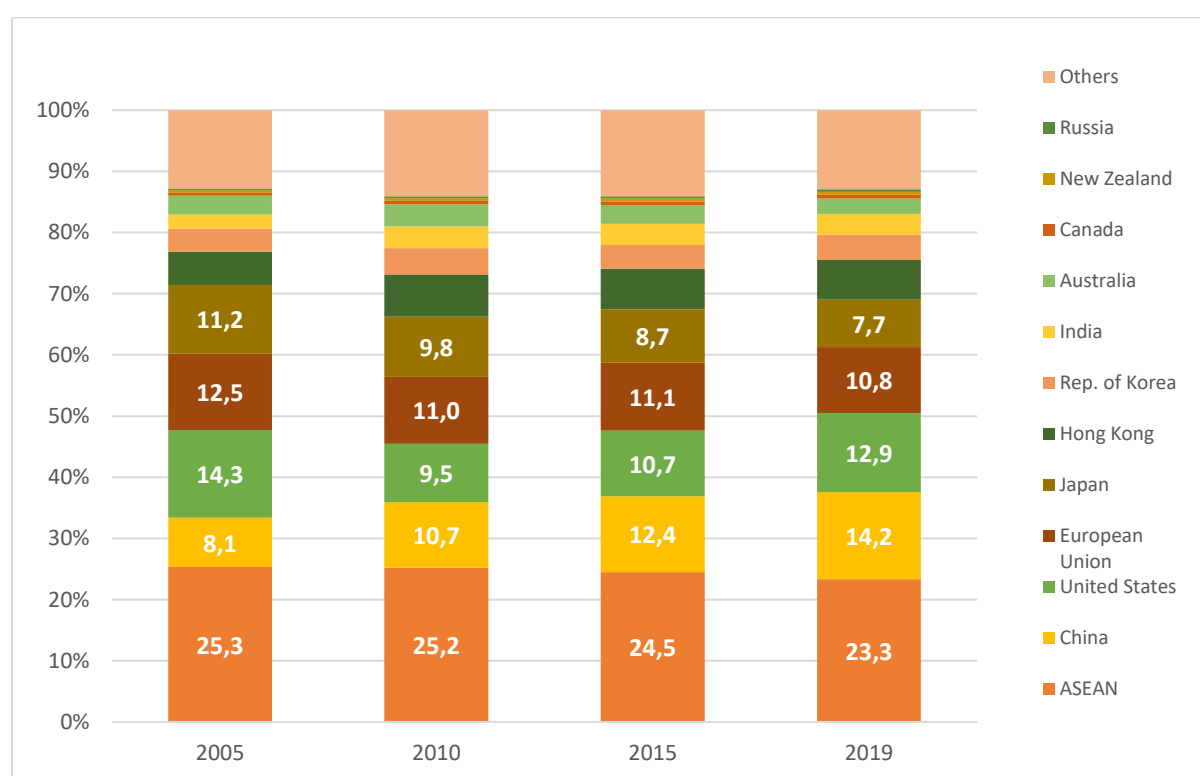
ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, Lao PDR = Lao People’s Democratic Republic.

Source: ASEANstats (ASEAN, 2021).

In terms of real GDP growth, Myanmar, the Lao People’s Democratic Republic (Lao PDR), and Cambodia were the best performers, with average annual growth of 13.2%, 7.7%, and 7.6%, respectively.

Intra-ASEAN trade has continuously accounted for the largest share of ASEAN total trade. In 2019, the year preceding the pandemic, intra-ASEAN trade accounted for 22.5% of total merchandise trade in the region – constituting 23.4% of ASEAN’s total merchandise exports and 21.5% of its imports. However, the share of intra-ASEAN trade in 2019 (22.5%) was lower than in 2018 (23.0%). The shares of ASEAN trading partners also indicated a slight decline in 2019 from the previous year, except for China (18.0% in 2019 from 17.1% in 2018) and the United States (US) (10.5% in 2019, from 9.3% in 2018). The largest external markets for ASEAN exports in 2019 were China (14.2%), the US (12.9%), the European Union (EU) 28 (members as of 2013–2019) (10.8%), and Japan (7.7%) (Figure 2.2).

Figure 2.2: Share of Merchandise Exports of the Top 5 Trading Partners, 2005–2019 (%)

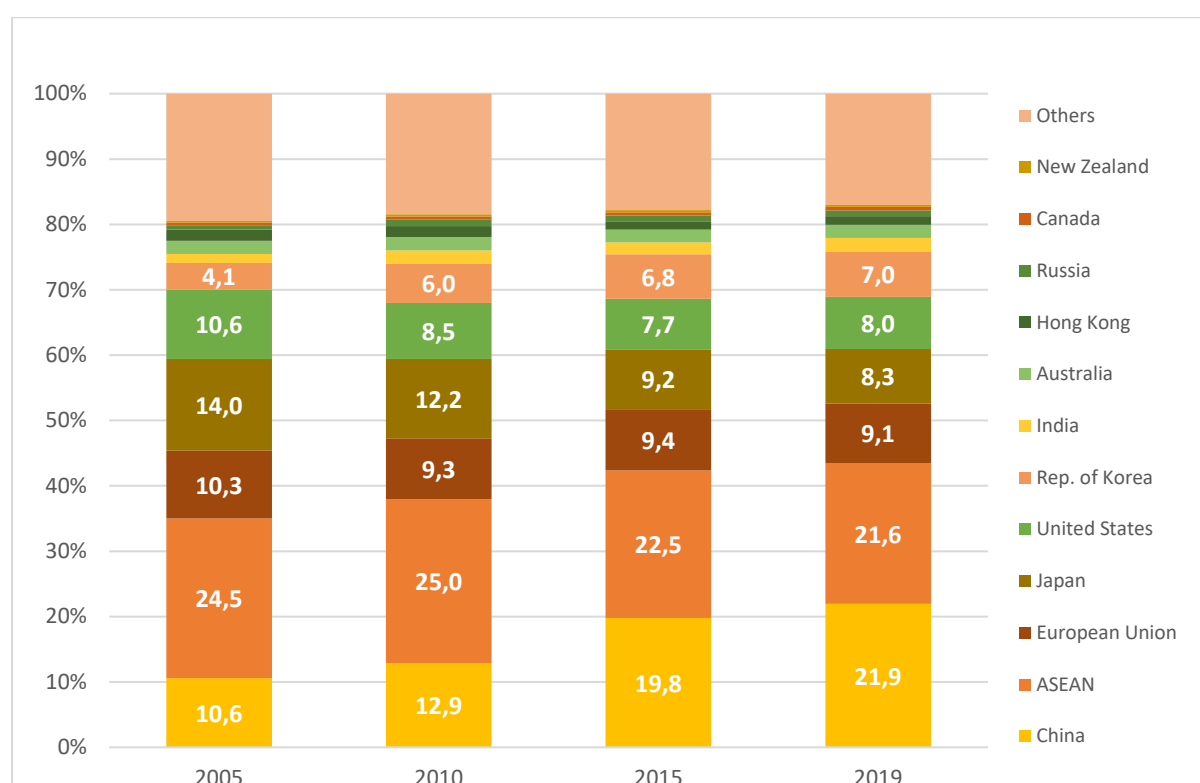


ASEAN = Association of Southeast Asian Nations.

Source: ASEANstats (ASEAN, 2021).

As for imports (Figure 2.3), China is the region’s largest external source of imports with a share of 21.9%, followed by the EU 28 (9.1%), Japan (8.3%), and the US (8.0%).

Figure 2.3: Share of Merchandise Imports of the Top 6 Trading Partners, 2005–2019 (%)



ASEAN = Association of Southeast Asian Nations.

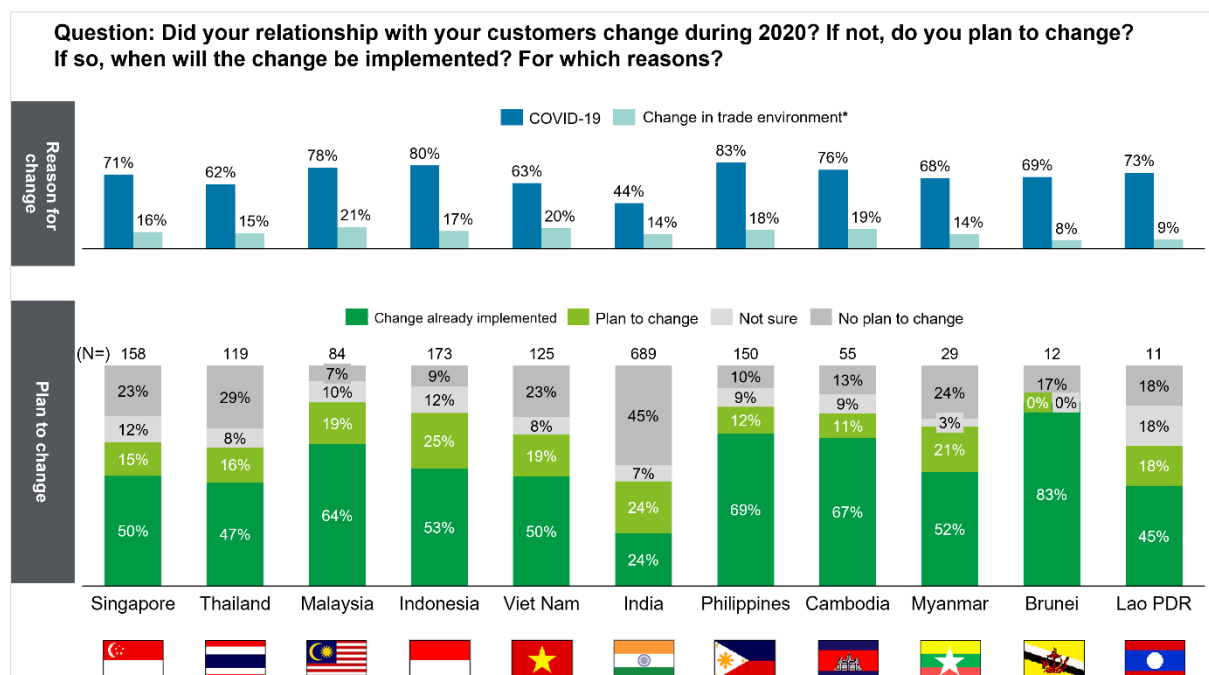
Source: ASEANstats (ASEAN, 2021).

Since it was declared a pandemic in March 2020, COVID-19 has disrupted livelihoods around the world. ASEAN has not been spared. In 2020, the region's economy was projected to contract by 3.8% – the first economic contraction in 22 years (ASEAN, 2020b). However, the quick restoration of supply chain activities after the first few months of negative supply shocks has ensured that the ASEAN region will regain positive growth in 2021.

ASEAN Supply Chains Are More Resilient to Trade Tensions than to COVID-19

Before the pandemic, US–China trade tensions were forecast to affect supply chains, investments, and production locations in the region. Supply chains in ASEAN rest on a stable foundation of trade and investment links. To the extent that there are risks, they are not primarily at a macro level. So far, neither the US nor China have used non-traditional trade policies to discriminate against international suppliers from the ASEAN region. The slowdown in ASEAN's supply chain integration with China is related in part to vertical integration of supply chains within China, and the fact that supply chain development in the region will not return to the rapid pace of integration seen in the early 2000s, at least in the short term. An Economic Research Institute for ASEAN and East Asia (ERIA) survey of domestic and international firms in ASEAN and India (Figure 2.4) showed that most firms have made changes in customer relationships due to COVID-19. US–China trade tensions and customs duties have a smaller effect on business decisions related to supply chains.

Figure 2.4: Changes Made by Firms in ASEAN due to COVID-19 and US–China Trade Tensions



ASEAN = Association of Southeast Asian Nations, COVID-19 = coronavirus disease, Lao PDR = Lao People's Democratic Republic, US = United States. * = e.g. imposition of additional customs duties, US–China trade discord.

Source: ERIA (2021).

ASEAN economies are generally very integrated into global movements of goods, services, ideas, people, and capital. As such, the reduction in consumer spending in most high-income countries has had an effect through the channel of reduced demand for exports, which has in turn put pressure on companies' cash reserves and led to some shedding of labour, with the attendant social costs from unemployment and lost income (Shepherd and Prakash, 2021). Think tanks and multilateral development banks have released positive forecasts for most ASEAN economies in 2021, but institutional information on the economic effects of the COVID-19 pandemic is still highly incomplete, as the situation is continuously evolving.

The ASEAN economies have experienced three types of economic shocks caused by the COVID-19 pandemic (Oikawa et al., 2021). The first type is negative supply shocks to international production networks (e.g. the Great East Japan Earthquake) where disruptions or damage in one place, including reduced production or closing of businesses, cause indirect damages to companies in other places through supply chains. If production is disrupted in company X in one country, the output production of customer company Y (that uses the parts produced by company X) in another country will also stop or decline. The negative supply shock is greater if the parts are difficult to replace. Moreover, supplier company Z's production will also suffer because of the reduced demand from company X. In January and February 2020, the AMS economies experienced and responded to a shortage of intermediate inputs originating from China (Kimura, 2020). Thus, at the beginning of the COVID-19 pandemic, the impact was in the form of negative supply shocks.

The second type is negative demand shocks to the macroeconomy (e.g. the global financial crisis in 2007–2009). The global financial crisis started in the US and spread to other advanced economies,

followed by its negative impact on emerging economies (Kose et al., 2012). The subprime mortgage problem affected the soundness of financial institutions. The financial sector's vulnerability impacted the real economy through negative wealth effects (sharp drops in housing and stock prices), low consumer confidence, and a credit crunch. Small open economies faced decreases in demand for exports. Together, these constituted negative demand shocks on the macroeconomy. In the case of COVID-19, negative supply shocks caused by lockdown measures brought about a demand shortage and created negative demand shocks. Economies that could contain COVID-19 still faced negative demand shocks for exports generated by economies struggling with the containment of the disease. COVID-19 spread globally in March 2020 and has continued to suppress economic activities throughout the world. As such, the AMS economies have experienced negative demand shocks since the global spread of COVID-19.

The third type is positive demand shocks to the goods and services supplied in response to the demands from the COVID-19 pandemic. The spread of COVID-19 significantly surged demand for critical supplies and personal protective equipment. The demand spikes created widespread shortages of these goods and stressed the health care supply chains. Social distancing and work-from-home requirements resulted in a rise in demand for information and communication technology (ICT) equipment and internet-based services (De et al., 2020). These positive demand shocks are pressures on the current production network and service suppliers but, at the same time, opportunities for firms to grow now and after the COVID-19 pandemic.

The AMS initially perceived COVID-19 as the source of a supply shock in January and February 2020, due to disruptions in the supply of certain intermediate products originating in China. Then the disease spread in March and a substantial share of production activities halted across the world. Production was stopped mainly to implement health policy, i.e. social distancing, which halts both supply and demand (Kimura, 2020). ASEAN's production facilities and networks are still there – almost intact. It may be useful to plan for a scenario when the disease is brought largely under control and production can be resumed if demand returns. After taming the disease, ASEAN must prepare to confront the demand shock as persistent low demand could decay its supply chains in the long term.

Policy Guidance on Recovery and Rebuilding

With COVID-19 declared a global pandemic, the ASEAN Economic Ministers (AEM) recognised 'the adverse impacts of the COVID-19 outbreak on the economy, particularly including but not limited to the travel and tourism, manufacturing, retail and other services sectors as well as the disruption of supply chains and the financial markets,' and agreed to resolve to 'strengthen a long-term supply chain resilience and sustainability, including through better transparency, agility, diversification and, in particular, the implementation of the Master Plan on ASEAN Connectivity (MPAC) 2025' (AEM, 2020: 1–2).

All ASEAN trade partners recognised the importance of the AEM statement. The AEM further resolved to 'remain committed in keeping the ASEAN market open for trade and investment ... and enhance economic cooperation with external and development partners to include initiatives aimed at strengthening regional supply chains to make them more resilient and less vulnerable to internal and external shocks' (AEM, 2020: 2).

Furthermore, the AEM adopted the 'Hanoi Plan of Action on Strengthening ASEAN Economic Cooperation and Supply Chain Connectivity in Response to the COVID-19 Pandemic' on 19 June 2020 (ASEAN, 2020c). The action plan includes cooperation in enabling the trade of important goods (food, medicines, medical equipment, and other related products), as well as assisting in the production of and improving access to COVID-19 medicines and vaccines through the strengthening of supply chain connectivity.

The AEM statement and the Hanoi action plan underline policy measures to keep the ASEAN supply chains resilient and provide a template to enhance the trade and economic cooperation mechanisms within ASEAN and with its Dialogue Partners during and in the post-COVID-19 recovery phase. In this regard, the study of UK–ASEAN trade and supply chains seeks to enhance bilateral trade with ASEAN through closer integration with supply chains in ASEAN. Trade and investment facilitation initiatives would be the assured pathway for both strengthening regional supply chains and increasing bilateral trade in goods and services, including the trade of important goods such as medicines, vaccines, and medical equipment. This economic integration would also fulfil the objectives of the regional plans for recovery and rebuilding of the economy in the post-COVID-19 phase.

ASEAN's Framework for Resilience and Rebuilding Measures of Supply Chains in the Post-COVID-19 Recovery

Given the scale and impact of the pandemic, ASEAN recognises that addressing the crisis requires coordinated actions within the region as well as cooperation with its partners. While the immediate priority for the region is to overcome the pandemic, ASEAN has concurrently planned its collective and long-term socio-economic recovery strategy. Thus, the ASEAN Comprehensive Recovery Framework (ACRF), adopted at the 37th ASEAN Summit in Ha Noi, Viet Nam, serves as the consolidated exit strategy from the COVID-19 crisis (ASEAN, 2020a).

ASEAN's recovery efforts will focus on five broad strategies that are deemed most impactful to take the region through the recovery process and its aftermath. The broad strategies will be pursued through several key priorities. The five broad strategies are:

1. Enhancing health systems
2. Strengthening human security
3. Maximising the potential of the intra-ASEAN market and broader economic integration
4. Accelerating inclusive digital transformation
5. Advancing towards a more sustainable and resilient future

Given the unprecedented nature of the current health and economic crisis, the ACRF and its implementation plan (ASEAN, 2020a) identified several cross-cutting enabling factors: (i) policy measures and responses, (ii) financing and resource mobilisation, (iii) institutions and governance mechanisms, (iv) stakeholder engagement and partnership, and (v) effective monitoring.

Optimal utilisation of resources and effective cooperation with partners will determine the progress on these fronts and the shape of the recovery. The UK–ASEAN partnership could be an important element of the international cooperation required for the implementation of the ACRF.

Supporting the ACRF for Broader UK–ASEAN Economic Integration

The ACRF and its implementation plan are intended to address both ASEAN’s immediate needs during the **reopening** stage for a successful transition to the ‘new normal’, as well as its medium- and long-term needs through the stages of the COVID-19 **recovery** and for longer-term **resilience**.

Broad strategy 3 – maximising the potential of the intra-ASEAN market and broader economic integration – focuses on priorities that intensify intra-ASEAN trade and investment and establish ASEAN as a competitive and contestable market. It is designed to normalise the movement of goods and people and to rebuild the disrupted goods and supply chains. From the UK perspective, supporting this strategy will feed equally and spontaneously into strategies 4 and 5: accelerating inclusive digital transformation in ASEAN, and supporting ASEAN’s advancement towards a more sustainable and resilient future.

Given the importance of trade in ASEAN, the post-pandemic recovery will require more, not less, trade. Intra-ASEAN trade is largest amongst the trading partners, followed by China, the US, the EU, and Japan. The UK partnership with ASEAN – along with a renewed trade engagement with ASEAN’s major trading partners in the Indo-Pacific (Australia, China, India, Japan, the Republic of Korea (henceforth, Korea), New Zealand, and the Pacific) – provides a useful policy platform for supporting critical economic elements in the implementation of the ACRF.

The UK is a global proponent of keeping markets open for trade and investment. This policy is important for the UK as it forges new economic relations and deepens existing ones in the Indo-Pacific region. The ASEAN Economic Community is a natural partner for the UK to forge freer movement of goods, services, labour, and capital between the two. Evaluating, streamlining, and expediting the investment process and facilitation will create a conducive environment for deepening and expanding the UK–ASEAN supply chain, and help in the rebuilding process after COVID-19. Eliminating non-tariff barriers and creating regulatory coherence between the two economies (or at least with some AMS initially) is an immediate and important step in this direction.

Supply chain connectivity, both infrastructural and institutional, will be at the core of new investments between the UK and ASEAN. This may well extend into plans outlined in the Master Plan on ASEAN Connectivity 2025.

However, UK support to the priority areas of economic integration strategy in the ACRF must be based on the UK’s own core thinking on the post-COVID-19 recovery and rebuilding. The principle of ‘build back better’ should lead UK economic engagement with ASEAN – for recovery in the near term and for resilient trade and investment in the longer term, besides enhancing bilateral trade.

Further, science and technology are an integral element of UK international policy to firmly establish itself as a global science and technology and responsible cyber power (HM Government, 2021). The UK has unique or significant strengths in areas of medical science, green technologies, and aspects of data and artificial intelligence, where it is well placed to support ASEAN in leading the advance towards the future.

Towards this, the UK’s signature contribution to partnership with ASEAN and for ACRF implementation would lie in

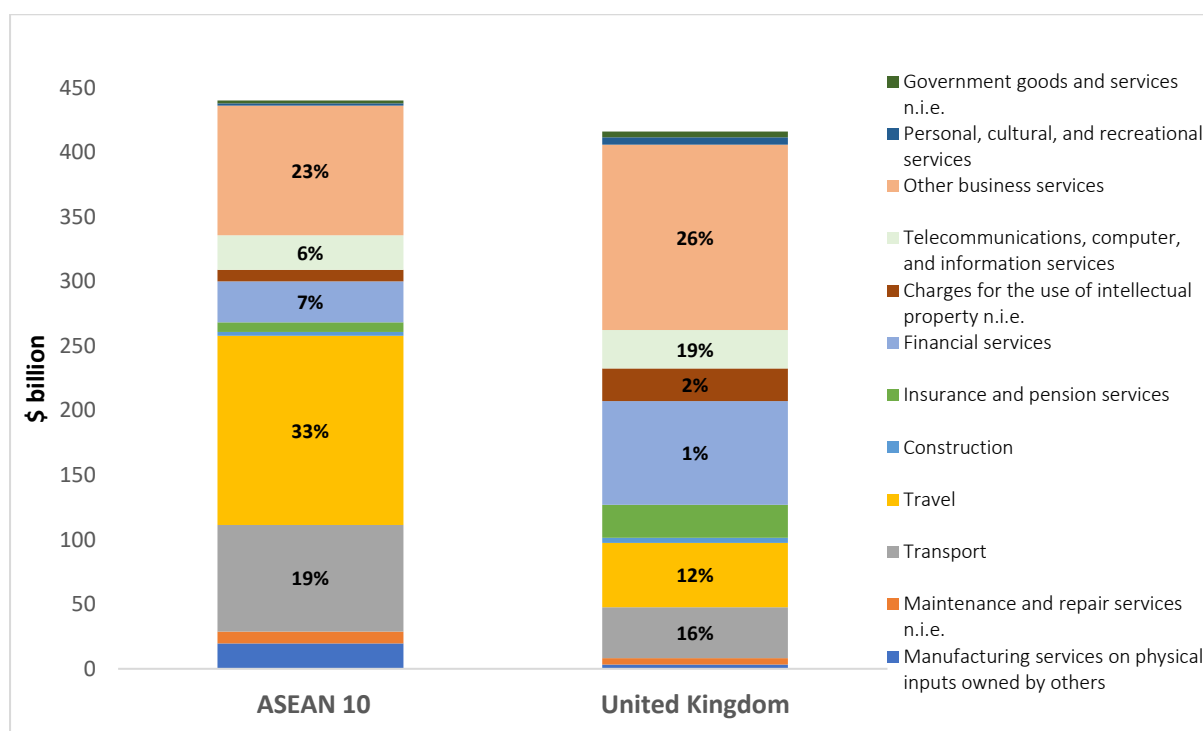
- (i) investments and capacity building for greater participation of ASEAN in the supply chains of the digital economy, especially in manufacturing industries that utilise automation, robotics, and artificial intelligence;
- (ii) investments in the manufacturing of environmental products; and
- (iii) diversifying ASEAN's trade in services into finance, ICT, and other services components of goods trade.

The major potential change in conditions facing supply chains is the rise in new sectors and modes of delivery (Shepherd and Prakash, 2021). The digital economy looms large in this regard, but so too do environmental products such as renewable power generation equipment (e.g. solar cells) and electric vehicles. AMS, including the least developed countries, have deepened their integration in regional value chains and embarked on trade-led growth. They now face the challenge of recovery from COVID-19 induced disruptions in the economy in general and in supply chains in particular. Concurrently, they must rapidly undertake digital transformation and structural reforms to remain engaged in the value chain of a more digitalised global economy, whose adoption of digital technology for production and supply chain management has accelerated due to the pandemic. This transformation cannot be delayed any longer. COVID-19 instigated a beta test for integration into the digital economy value chains and spotlighted a need for increased investment in digital connectivity and human capital for ASEAN's continued participation in production networks. Concerted UK–ASEAN cooperation is required to cover a spectrum of needs, with infrastructure, regulatory frameworks, data flow, and security being the immediate challenges.

Consumer tastes have been shifting towards environmental and green products for some time, and it is plausible that recovery programmes in high-income markets will favour this shift through incentives and other measures. If markets remain relatively open, ASEAN is well positioned to take advantage of these opportunities, given its established base in related sectors, such as electronics and motor vehicles. While retooling will be necessary, the existence of an effective supplier network and integrated supply chains could be an important advantage in building back better supply chains for the future. The UK has an ambitious target for net zero carbon emissions, and has adopted a Ten Point Plan (HM Government, 2020) that brings together ambitious policies and public investment in low-carbon technologies and services. Partnership with ASEAN for supply chains and markets will bring together supply chain efficiency, jobs, and growth on both sides.

ASEAN's trade in services relies greatly on the travel and tourism sector. In 2018, 12% of ASEAN's GDP came from this sector. Travel accounted for 33% of ASEAN's total services exports in 2019. Apart from Singapore, which is diversified into financial services and transport, most AMS require greater penetration in other sectors of services trade (Figure 2.5). The UK is a global player in the services sector, especially in finance, logistics, and ICT, which have important roles in the digital economy as well as being components of goods trade. Investment and technical cooperation in these sectors, especially in AMS where UK firms have significant presence, will forge a resilient and forward-looking partnership in which both partners build back better.

Figure 2.5: Services Exports (Sectoral) in ASEAN and the United Kingdom, 2019



ASEAN = Association of Southeast Asian Nations, n.i.e. = not included elsewhere.

Notes: Data for Brunei, the Lao People's Democratic Republic, and Myanmar are from 2018. The International Trade Centre defines 'other business services' as (i) research and development; (ii) professional and management consulting services; and (iii) technical, trade-related, and other business services.

Source: ITC (2021).

Research and development (defined as 'other business services' in services trade) is a sectoral link with significant potential for putting in place enhanced mechanisms for cooperation. The future of work and growth in ASEAN requires greater expenditure and technical collaboration in education and innovative learning. Collaboration in higher education and research and development activities in medicine, agriculture, robotics, and low-carbon technologies would be quintessentially the UK's role in an enhanced UK–ASEAN cooperation plan for building back better.

Structure of the Study

This chapter has made a broad assessment of the resilience of trade and the performance of supply chains in ASEAN before and during COVID-19, and underlines the pathways ahead for UK–ASEAN trade and economic cooperation, which are based on the UK's core principle for building back better even while utilising the existing core strengths of the two economies.

Chapter 3 covers bilateral trade flows between the UK and ASEAN; the evolution of gross bilateral exports and imports over the past decade, especially in key sectors (agriculture, food products, textiles, pharmaceuticals, parts & components, and machinery & equipment); and positions ASEAN–UK trade in the global context. It focuses on trade flows between ASEAN and the UK compared with EU member countries. It includes boxes on international trade in services and the RCEP and CPTPP

trade agreement in Asia, underlining the UK's policy directions for greater trade engagement with ASEAN and East Asia.

Chapter 4 assesses the degree and nature of ASEAN's trade integration with the UK and selected EU economies (Germany, France, the Netherlands, Italy, and Spain). It makes use of value chain analysis to describe the degree and nature of trade integration between ASEAN and the UK, and in the global context. It covers an overall characterisation, as well as sectoral disaggregation, of the main trading partners. It focuses on trade integration with the EU. Until recently, the UK was a member country of the EU; now it is a competitor of the EU in international trade and in trade with ASEAN. The EU is ASEAN's third largest trading partner and its fourth largest investor. The UK must forge new ground in bilateral trade and investment with ASEAN, and this chapter provides comparative data for the UK to establish its competitiveness in key goods and services sectors which have potential for further integration.

Chapter 5 maps the developments in international trade in ASEAN and the UK following the COVID-19 outbreak in 2020 and compares them with the EU and global performance during the same period. It covers an overall characterisation and, when possible, disaggregation by type of product for the main trading partners. It focuses on identifying the breaks in trade trends described in the previous two chapters.

Chapter 6 is a special addition to the study as it incorporates the results of an ERIA survey of supply chain mechanisms and trade performance amongst domestic and international firms in ASEAN during the COVID-19 pandemic in 2020. This chapter helps in understanding the types of shocks delivered to the ASEAN economy, and the subsequent performance and resilience of supply chains across major industries in the region. Data on changes made by firms in customer and supplier relations, their plans for business expansion, and government assistance to industries will help stakeholders in the UK and ASEAN to respond to and plan for trade and investment facilitation according to regional needs. The prognosis for the digitalisation of supply chains can also be sourced from these data.

The concluding chapter derives the policy directions emanating from the previous chapters and proposes a working strategy for expanding UK–ASEAN trade and deepen supply chain integration in the post-COVID-19 recovery and rebuilding months.

Faced with the twin economic and health crises, this study underlines the dynamism of businesses in the AMS. It is widely recognised that the trough of global economic performance is likely to be very deep and prolonged – causing a recession that will generate a serious demand shock which may decay the whole economy (Kimura, 2020). However, international cooperation and bilateral support is the way forward. The UK and ASEAN dialogue partnership comes at an opportune time, almost uniquely so, to contribute to economic resilience in the post-COVID-19 period, grow the bilateral economic linkages, and sustain the trade and investment plans of the future.

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Chapter 3

Trade Flows between ASEAN and the UK: A Comparative Study

Chapter 3

Trade Flows between ASEAN and the UK:

A Comparative Study

This chapter describes the evolution of bilateral trade between the United Kingdom (UK) and the Association of Southeast Asian Nations (ASEAN) over the past decade, especially in key sectors. Explained in the global context, it provides an overall characterisation as well as highlights of the main trading partners and sectoral disaggregation over the last 2 decades. It focuses on trade flows between ASEAN and the UK compared with European Union (EU) countries. It includes boxes on international trade in services and a recent trade agreement in Asia, underlining the UK's policy directions for greater trade engagement with ASEAN and East Asia.

Overview

ASEAN is one of the most open economic regions in the world, but the degree of openness is decreasing as domestic demands grow. Its economies are growing faster than the rest of the world and are converging in terms of production capacity as well as purchasing power. At the same time, a massive shift has taken place in the last 20 years, with China displacing the United States (US) as ASEAN's number one trading partner.

The UK and some key EU member countries have a smaller presence in trade with ASEAN, which has not improved in recent years. This is not surprising from an ASEAN perspective given the smaller size of the UK economy in the last few years. The same is true for the EU countries.

From the UK perspective, however, it is not easy to understand why its exports to such a dynamic region have increased so little as a share of the region's total imports. The trend is even worse for some key EU players, such as Germany, while France surprises on the positive side with ASEAN – gaining market share in its exports much faster than the UK and from a lower base.

The sectoral breakdown of UK bilateral trade with ASEAN is similar to that of the major EU countries, but with a greater presence of petroleum-related items. In other words, the UK competes with the EU for most export items – machinery and equipment, textiles, and chemicals and pharmaceuticals. This means that a trade agreement with ASEAN would put the UK at an advantage in these markets compared with the EU.

As for services, the situation is even more underwhelming as the share of ASEAN in the UK's trade in services is very small, in both directions. The exception is Singapore, mainly for business services. Japan dominates the ASEAN region in financial services, but still with a very low base compared with the UK's trade in services with other areas of the world, especially the US and the EU. UK imports of services from ASEAN are dominated by tourism, especially from Thailand, but with a much more limited scope than with other parts of the world, especially the EU.

Thinking ahead, ASEAN offers an important opportunity for the UK in terms of growing exchanges – whether trade in goods or trade in services. The UK's decision to apply to join the Comprehensive and

Progressive Agreement for Trans-Pacific Partnership (CPTPP) is an important signal regarding the increasing relevance of the Asia-Pacific region (ASEAN but also Australia and Japan as well as some Latin American economies, i.e. Chile and Mexico). While welcome, the UK will need to come to terms with the very strong gravitation of ASEAN towards China, given its huge economic size but also its central role in the global value chain (GVC). Such gravitation will probably accelerate thanks to the Regional Comprehensive Economic Partnership (RCEP) signed amongst ASEAN economies, Australia, Japan, the Republic of Korea (henceforth, Korea), and most importantly, China. However, the RCEP is a rather limited trade deal in terms of scope and mainly focuses on a slow but steady reduction in tariffs for goods. Still, the power of gravity is bound to push ASEAN's economic integration further towards China, which may make it difficult for the UK to reap the benefits within the CPTPP if it delays becoming part of it.

Box 3.1: Data Description and Definitions

Trade in goods

Annual gross goods trade flows analysed throughout this chapter are sourced from the United Nations International Trade Statistics Database (United Nations, n.d.), measured in nominal United States dollars. Sectoral data correspond to the aggregation of products from the Harmonized System (HS) classification at the two-digit level: agriculture and food industry (HS codes 1–24), petroleum (27), chemicals and pharmaceuticals (28–38), textiles (50–66), metals (72–83), machinery and equipment (84–89), and other activities (rest).

Trade in services

Annual gross services trade flows analysed in Box 3.2 are sourced from the United Kingdom's Office for National Statistics (2020) Geographical Breakdown of the Current Account in *The Pink Book*, measured in nominal pounds sterling. Types of services are based on the International Monetary Fund's *Balance of Payments and International Investment Position Manual* (IMF, 2009). Individual data for ASEAN Member States as trade partners are limited to Indonesia, Malaysia, the Philippines, Singapore, and Thailand.

Definitions

Trade openness corresponds to the sum of total exports and imports of a country over its gross domestic product (GDP).

Sectoral specialisation corresponds to a larger share of a sector in the total exports of a country compared with the world or a certain economic area.

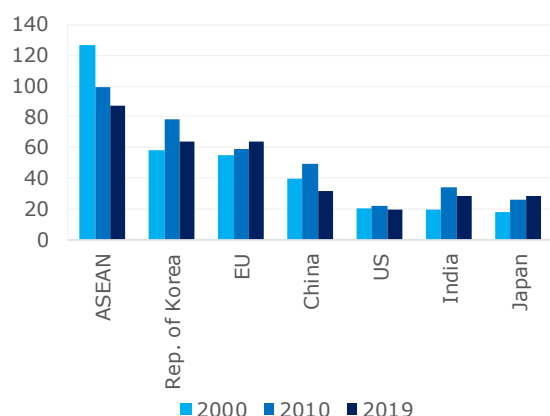
Source: Authors.

Trade flows in ASEAN

A comparison across the world's main economic areas shows that ASEAN trade openness is very high by global standards (Figure 3.1) – well above the levels in the US and even the highly integrated EU, as well as other economies in Asia, such as China, India, Japan, or Korea.

The picture holds for most of the ASEAN Member States (AMS), although there is still quite a lot of heterogeneity amongst countries, with Singapore the most open and Indonesia – the largest economy in the bloc – the least open (Figure 3.2).

Figure 3.1: Total Trade as a Share of GDP, by Economic Area (%)

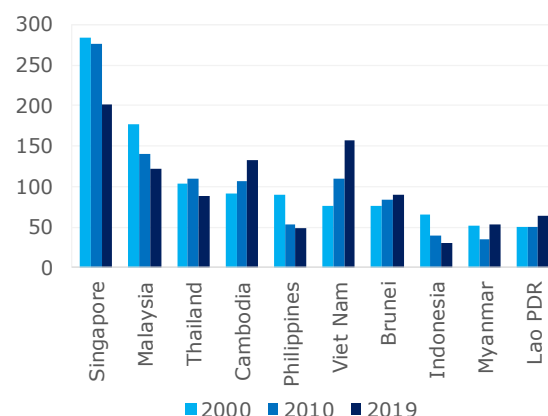


ASEAN = Association of Southeast Asian Nations, EU = European Union, GDP = gross domestic product, US = United States.

Note: Total trade is the sum of exports and imports.

Sources: UN Comtrade, UNCTAD, and WDI.

Figure 3.2: Total Trade as a Share of GDP, by ASEAN Member State (%)



ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product.

Note: Total trade is the sum of exports and imports.

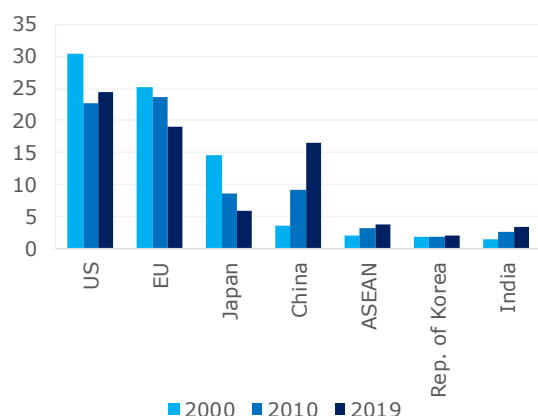
Sources: UN Comtrade, UNCTAD, and WDI.

In the last 2 decades, economic growth has been strong in developing and emerging Asia, increasing the share of China, India, and ASEAN in the world's gross domestic product (GDP) to the detriment of developed economies such as the US and, in particular, the EU and Japan (Figure 3.3).

Economic growth in developing and emerging Asia – China and ASEAN in particular – has been fuelled by the vast expansion of domestic demand resulting from gains in purchasing power and the rise of middle-income groups. This, and not lower participation in global trade, has been the key factor leading to a progressive and generalised reduction in the share of exports and imports over GDP (Figures 3.1 and 3.2) and the trade surplus with the rest of the world (Figure 3.4). This characterisation is opposed to that of most developed economies, where domestic demand has remained stagnant and external demand is an increasingly important growth engine.

Within ASEAN, two countries have become even more open since 2000 relative to GDP – Cambodia and Viet Nam – succeeding in both high economic growth and larger participation in global trade (Figure 3.2).

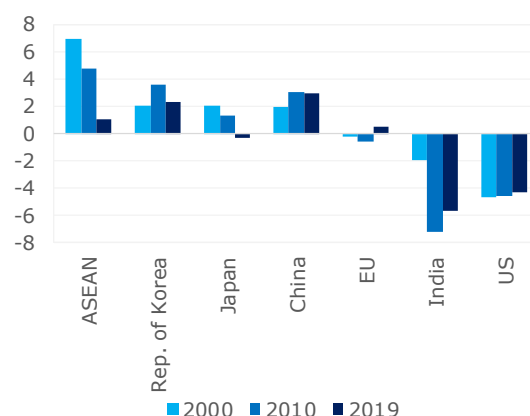
Figure 3.3: Share of World GDP, by Economic Area (%)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GDP = gross domestic product, US = United States.

Sources: UN Comtrade, UNCTAD, and WDI.

Figure 3.4: Trade Balance as a Share of Each Country's GDP, by Economic Area (%)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GDP = gross domestic product, US = United States.

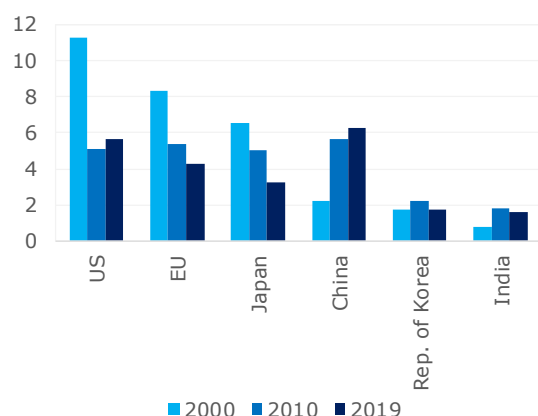
Note: Trade balance equals the value of exports minus imports.

Sources: UN Comtrade, UNCTAD, and WDI.

When looking into the geographical composition of trade, the main feature characterising ASEAN participation in global trade is the increasing relevance of China over the last two decades. The share of China as a destination for ASEAN exports rose from 2% in 2000 to more than 5% in recent years (Figure 3.5), while an even bigger increase was recorded on the import side during the same period, reaching a share of almost 15% (Figure 3.6). Accordingly, the increasing trade linkages between both economic areas are rather asymmetric, accumulating a sizeable trade deficit for ASEAN, which had run a surplus in the past.

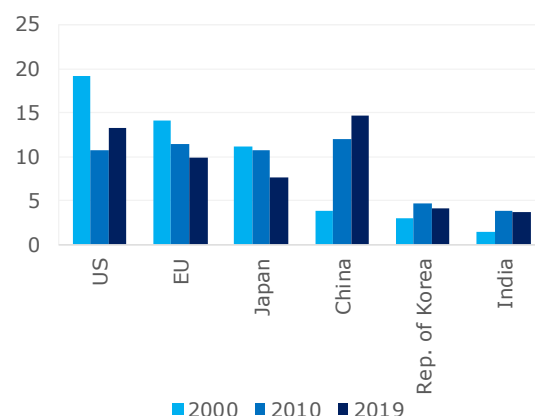
In sum, China has become the top trading partner of ASEAN to the detriment of the US, and, particularly, the EU and Japan – clearly diminishing the relative importance of developed economies in ASEAN's trade and establishing a stronger relation within Asian borders.

Figure 3.5: Exports from ASEAN as a Share of Total Exports, by Trading Partner (%)



ASEAN = Association of Southeast Asian Nations, EU = European Union, US = United States.
 Note: EU = member countries as of 1995–2003.
 Sources: UN Comtrade, UNCTAD, and WDI.

Figure 3.6: Imports of ASEAN as a Share of Total Imports, by Trading Partner (%)



ASEAN = Association of Southeast Asian Nations, EU = European Union, US = United States.
 Note: EU = member countries as of 1995–2003.
 Sources: UN Comtrade, UNCTAD, and WDI.

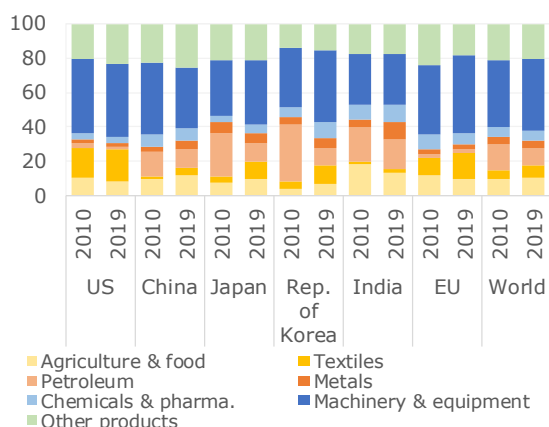
In terms of the sectoral composition of trade, the largest share of ASEAN exports to the world corresponds to machinery and equipment, followed by petroleum, and, in the commodity space, agriculture and food (Figure 3.7).

By trading partner, the most noticeable difference in the sectoral composition corresponds to a higher share of manufacturing goods in exports to Western developed economies (the US and the EU) and a higher share of commodities in exports to other Asian economies. In other words, ASEAN today is already a manufacturing platform, as it comes to the UK or the EU, so closer trade relations with ASEAN could improve the integration of the UK in the GVC and, in particular, that of Asia.

The overall sectoral composition is very similar from the import perspective, with a slightly higher share for metals (from other Asian economies) and petroleum and a lower one for textiles and agriculture and food (from developed economies in particular) (Figure 3.8).

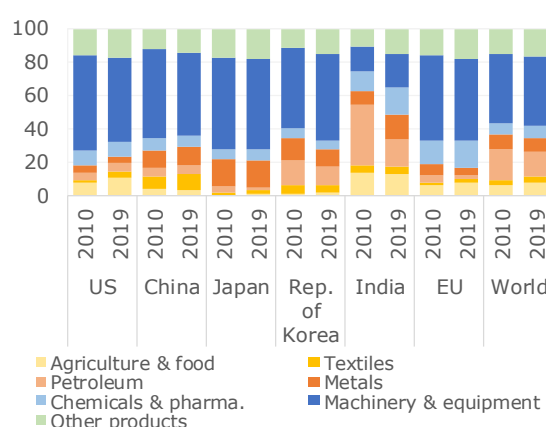
Sectoral specialisation is also changing over time, with the share of petroleum products having decreased overall in ASEAN trade during the last decade. On the export side, this reduction has been to the benefit of textiles in general, machinery and equipment to developed economies, and agriculture and food to China and Japan. On the import side, it has mirrored a generalised increase in the share of machinery and equipment (except for the US, for which imports of agriculture and food show the largest increase).

Figure 3.7: Sectoral Composition of Exports from ASEAN, by Trading Partner (%)



ASEAN = Association of Southeast Asian Nations,
EU = European Union, US = United States.
Note: See Box 3.1 for the definition of sectors.
Source: UN Comtrade.

Figure 3.8: Sectoral Composition of Imports of ASEAN, by Trading Partner (%)



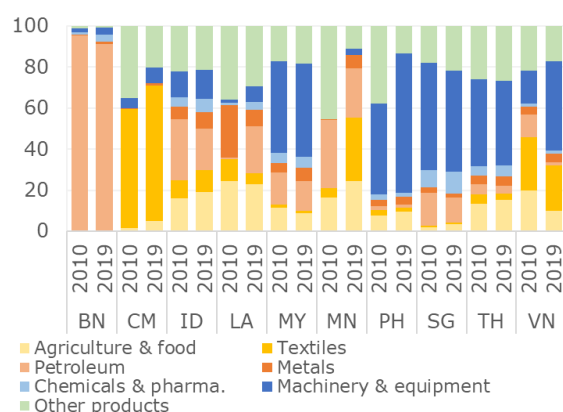
ASEAN = Association of Southeast Asian Nations,
EU = European Union, US = United States.
Note: See Box 3.1 for the definition of sectors.
Source: UN Comtrade.

At the country level, trade specialisation is very diverse across AMS, reflecting both the availability of natural resources and very different levels of economic development, which determine production capacities and demand patterns.

On the export side, the most pronounced specialisation is found for Brunei Darussalam (petroleum products) and Cambodia (textiles) (Figure 3.9). For machinery and equipment, which accounts for the largest share of ASEAN exports (as mentioned before), the Philippines, Singapore, Thailand, and Malaysia stand out, while Indonesia, the Lao People's Democratic Republic (Lao PDR), and Myanmar clearly fall behind the region's average. On the other hand, Viet Nam shows the most noticeable change in export specialisation during the last decade, increasing the share of machinery and equipment to the detriment of agriculture and food in particular.

In turn, the import structure by sector is much more similar across AMS than for exports (Figure 3.10). The largest deviations have been identified in the two countries with a more pronounced export specialisation – Brunei Darussalam and Cambodia – which both show the largest import share in the same product categories in which they are specialised, likely reflecting foreign intermediates processed for later exporting activities.

Figure 3.9: Sectoral Composition of Total Exports from ASEAN Member States (%)

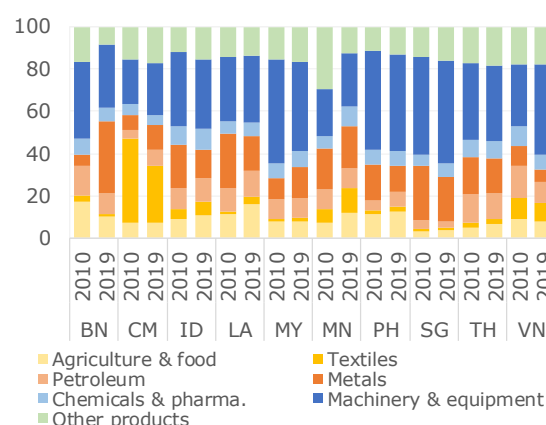


ASEAN = Association of Southeast Asian Nations, BN = Brunei Darussalam, CM = Cambodia, ID = Indonesia, LA = Lao PDR, MY = Malaysia, MN = Myanmar, PH = Philippines, SG = Singapore, TH = Thailand, VN = Viet Nam.

Note: See Box 3.1 for the definition of sectors.

Source: UN Comtrade.

Figure 3.10: Sectoral Composition of Total Imports of ASEAN Member States (%)



ASEAN = Association of Southeast Asian Nations, BN = Brunei Darussalam, CM = Cambodia, ID = Indonesia, LA = Lao PDR, MY = Malaysia, MN = Myanmar, PH = Philippines, SG = Singapore, TH = Thailand, VN = Viet Nam.

Note: See Box 3.1 for the definition of sectors.

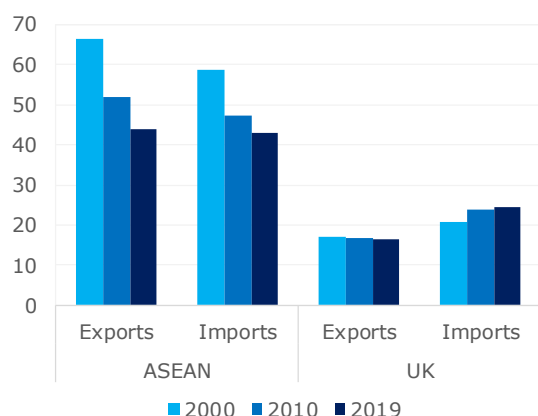
Source: UN Comtrade.

Trade flows between ASEAN and the UK

The UK has become more open, trade-wise, in the last two decades relative to its GDP, although its trade openness remains well below that of ASEAN (Figure 3.11) and most of the AMS (see Figure 3.2 for comparison). The larger increase on the import side has generated an increasing deficit in goods trade for the UK with the rest of the world, which is being only partially offset by the surplus in services trade (Box 3.2).

On a bilateral basis, and from the perspective of ASEAN, the share of trade with the UK has declined significantly in the last 2 decades, falling to less than 1% of ASEAN's total exports and imports in recent years from around 2%–3% in 2000 (Figure 3.12). This trend has been particularly intense for the UK as an export destination, and reflects the fact that the UK has become a smaller economy in the global context (its GDP share of the world total declined from 3.1% in 2000 to 2.2% today according to IMF (2021) figures).

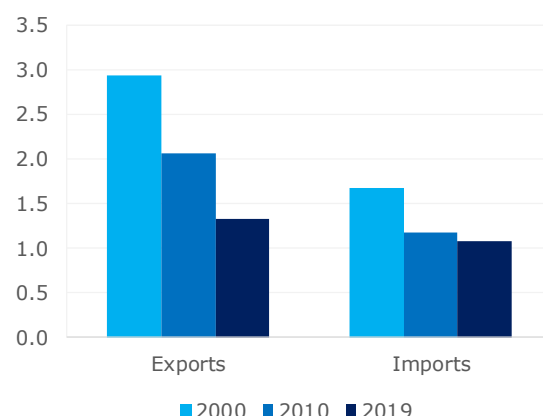
Figure 3.11: Total Exports and Imports of ASEAN and the UK as a Share of GDP (%)



ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, UK = United Kingdom.

Sources: UN Comtrade and UNCTAD.

Figure 3.12: Exports/Imports of ASEAN to/from the UK as a Share of Total ASEAN Exports/Imports (%)

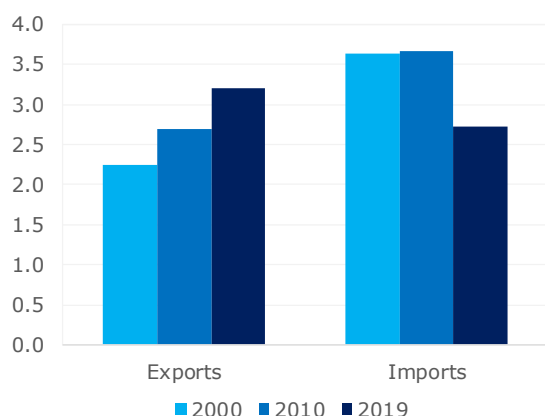


ASEAN = Association of Southeast Asian Nations, UK = United Kingdom.

Sources: Natixis, UN Comtrade, and UNCTAD.

From the UK perspective, the share of trade with ASEAN is higher and has increased on the export side in recent years due to faster growth in ASEAN demand, reaching around 3% of total UK trade in 2019 (Figure 3.13). Nevertheless, bilateral trade is still limited and the share of UK exports to ASEAN remains rather modest, particularly when compared with the size of ASEAN economies and, most importantly, their fast growth (Figure 3.14). Significantly, the UK's modest trade with ASEAN is also reflected in the UK's exports to other emerging economies, including China. On the other hand, trade with the EU, favoured by geographical proximity and past institutional ties, remains excessively large, at least when compared with the EU's economic size and growth performance (both past and expected).

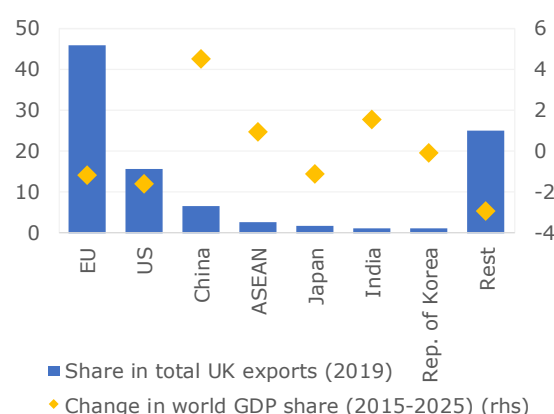
Figure 3.13: Exports/Imports of the UK to/from ASEAN as a Share of Total UK Exports/Imports (%)



ASEAN = Association of Southeast Asian Nations, UK = United Kingdom.

Sources: Natixis, UN Comtrade, and UNCTAD.

Figure 3.14: Share of UK Exports (%) and Expected Change in World GDP Share (% points), by Trading Partner



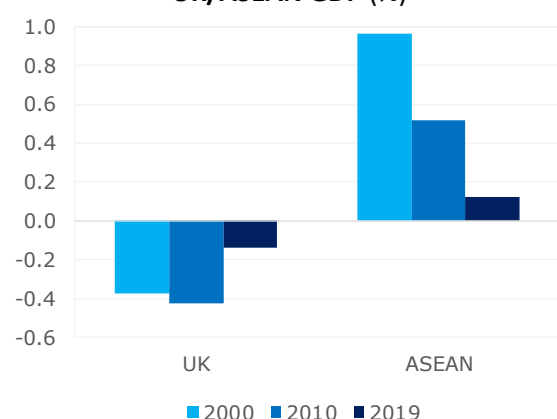
ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, UK = United Kingdom.

Sources: UN Comtrade and IMF.

The combination of the decreasing relative relevance of the UK for ASEAN and the increasing relevance of ASEAN for the UK, triggered by the positive growth differential in favour of ASEAN economies, has resulted in a narrower trade surplus for ASEAN and the reversion of the UK's structural deficit to virtually balanced trade (Figure 3.15).

At the ASEAN country level, a general decrease has been observed for the UK share of total exports during the last decade (Figure 3.16), which is particularly significant for Cambodia, the Lao PDR, Thailand, and Viet Nam.

Figure 3.15: Bilateral Trade Balance Between ASEAN and the UK as a Share of UK/ASEAN GDP (%)

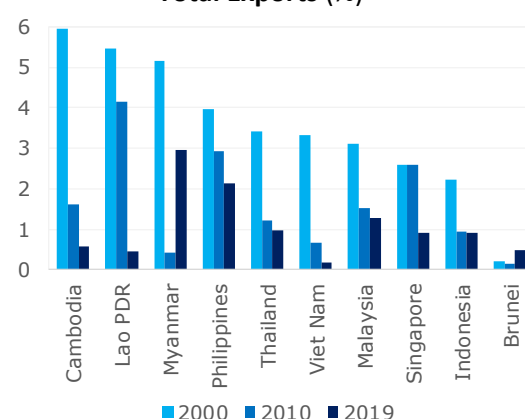


ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, UK = United Kingdom.

Note: Trade balance equals the value of exports minus imports.

Sources: Natixis, UN Comtrade, and UNCTAD.

Figure 3.16: Exports of ASEAN Member States to the UK as a Share of Total Exports (%)



ASEAN = Association of Southeast Asian Nations, UK = United Kingdom.

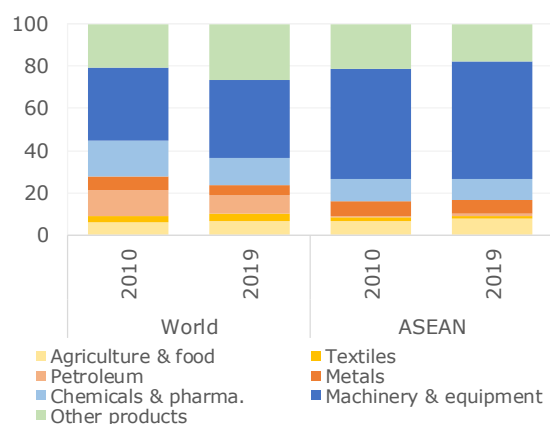
Sources: Natixis, UN Comtrade, and UNCTAD.

When looking into the geographical composition of trade, the largest product group in UK exports to the world corresponds to machinery and equipment, followed by chemicals and pharmaceuticals, and petroleum products (Figure 3.17). In contrast, the sectoral structure of UK exports to ASEAN is more concentrated, with a significantly higher share for machinery and equipment to the detriment of chemicals and pharmaceuticals as well as petroleum products.

On the import side, the sectoral composition for the UK is very similar to exports when considering total trade with the world (Figure 3.18). However, imports from ASEAN show a quite different structure, with a higher share for agriculture and food and textiles and a lower share for petroleum products and chemicals and pharmaceuticals.

The sectoral composition of trade flows between the UK and ASEAN has remained relatively stable in the last decade.

Figure 3.17: Sectoral Composition of Total UK Exports to the World and to ASEAN (%)

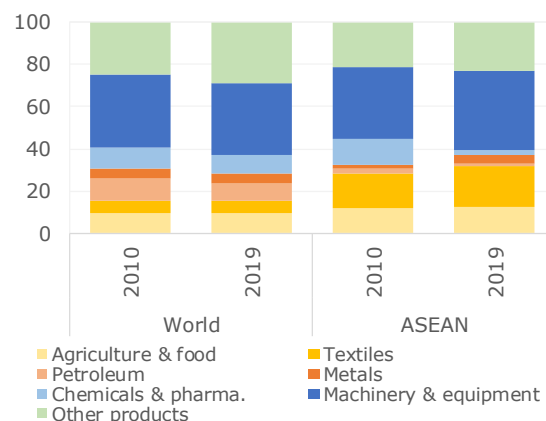


ASEAN = Association of Southeast Asian Nations, UK = United Kingdom.

Note: See Box 3.1 for the definition of sectors.

Source: UN Comtrade.

Figure 3.18: Sectoral Composition of Total UK Imports from the World and from ASEAN, by Trading Partner (%)



ASEAN = Association of Southeast Asian Nations, UK = United Kingdom.

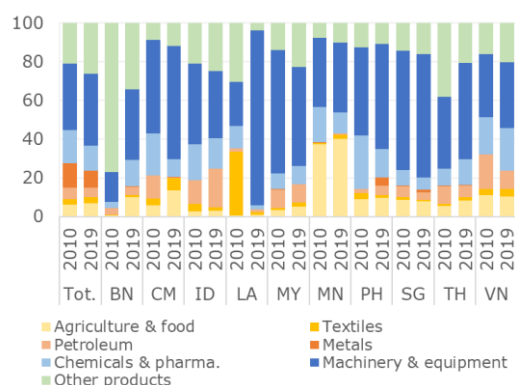
Note: See Box 3.1 for the definition of sectors.

Source: UN Comtrade.

On a bilateral basis with AMS, a number of deviations are observed with respect to the sectoral composition of total UK trade. For instance, on the export side, the share of machinery and equipment is particularly large for UK exports to Cambodia, the Lao PDR, Malaysia, and Singapore, while the same happens to the share of metal products exported to Indonesia and Viet Nam or agricultural products to Myanmar (Figure 3.19).

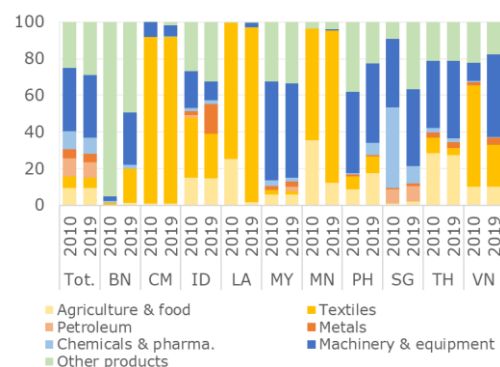
The sectoral structure is more heterogeneous for UK imports across AMS partners, reflecting to a large extent the product specialisation of each ASEAN economy (Figure 3.20). This is particularly the case for Cambodia, the Lao PDR, and Myanmar, with an underwhelming importance of textiles in their export basket to the UK, as well as Thailand in the case of agricultural products.

Figure 3.19: Sectoral Composition of Total UK Exports and UK Exports to AMS (%)



AMS = ASEAN Member States, ASEAN = Association of Southeast Asian Nations, BN = Brunei Darussalam, CM = Cambodia, ID = Indonesia, LA = Lao PDR, MY = Malaysia, MN = Myanmar, PH = Philippines, SG = Singapore, TH = Thailand, UK = United Kingdom, VN = Viet Nam.
Note: See Box 3.1 for the definition of sectors.
Source: UN Comtrade.

Figure 3.20: Sectoral Composition of Total UK Imports and UK Imports from AMS (%)



AMS = ASEAN Member States, ASEAN = Association of Southeast Asian Nations, BN = Brunei Darussalam, CM = Cambodia, ID = Indonesia, LA = Lao PDR, MY = Malaysia, MN = Myanmar, PH = Philippines, SG = Singapore, TH = Thailand, UK = United Kingdom, VN = Viet Nam.
Note: See Box 3.1 for definition of sectors.
Source: UN Comtrade.

Box 3.2: Trade in Services: UK's Competitive Advantage in ASEAN and East Asia

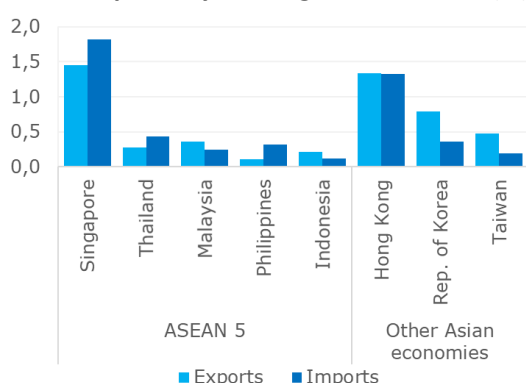
Geographical composition

UK's trade in services with the European Union (EU), as in the case of goods, remains excessively large, representing around 45% of exports and imports (Figure A). The second partner of the United Kingdom (UK) is the United States (US), with 20%–25% of total services trade – above the share in goods trade (around 15% as shown in Figure 3.14).

On the other hand, compared with overall economic size, services trade with Asia is rather modest, not exceeding a 3% share for Japan, China, or India. Figures are particularly low for China when compared with goods trade, while the ASEAN 5 (Indonesia, Malaysia, the Philippines, Singapore, and Thailand) appear higher in the ranking although still modest given the fast economic growth in the region.

At a country level, Singapore is the UK's main ASEAN partner for services (Figure B), representing around 1.5% of total UK trade in services, while the bilateral relation with other ASEAN Member States is very limited (0.0%–0.5%). Beyond Singapore, relations with other Asian economies appear to be more relevant for the UK, such as the case of Hong Kong or the Republic of Korea (Figure B).

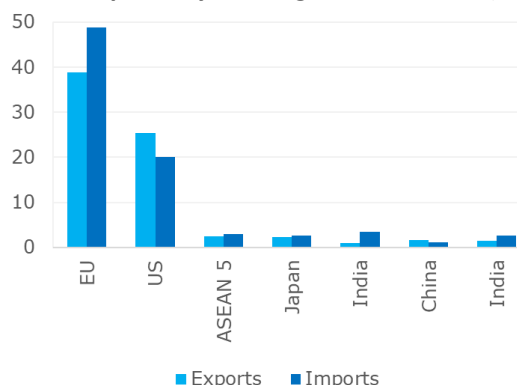
Figure A: Share of Total UK Services Exports and Imports by Trading Partner, 2019 (%)



ASEAN 5 = Indonesia, Malaysia, the Philippines, Singapore, and Thailand; ASEAN = Association of Southeast Asian Nations; EU = European Union; UK = United Kingdom; US = United States.

Source: Office for National Statistics (2020).

Figure B: Share of Total UK Services Exports and Imports by Trading Partner, 2019 (%)



ASEAN 5 = Indonesia, Malaysia, the Philippines, Singapore, and Thailand; ASEAN = Association of Southeast Asian Nations; EU = European Union; UK = United Kingdom; US = United States.

Source: Office for National Statistics (2020).

Composition by type of service

By type of service, the largest share of UK trade with the rest of the world is concentrated in three categories: travel, financial services, and business services.

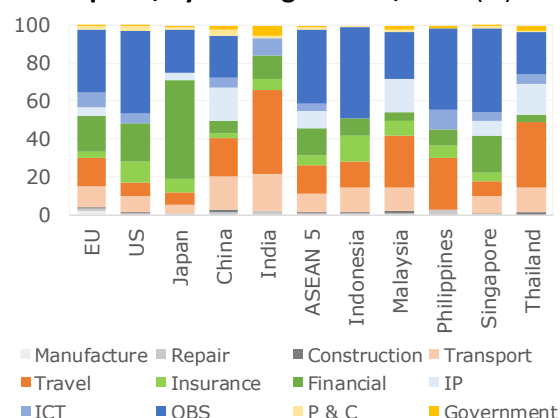
On the export side (Figure C), the largest category of aggregate services trade with the ASEAN 5 corresponds to business services including professional activities (close to 40% in value terms), followed by travel and financial services (almost 15% in each case), transportation and intellectual property (near 10% each), and insurance and information and communication technology (ICT) services (5% each).

At the country level, and compared with the ASEAN 5 benchmark, business and financial services represent a significantly larger share of exports to Singapore, as well as travel and intellectual property in the case of Malaysia and Thailand.

On the import side (Figure D), the structure of the bilateral relation with the ASEAN 5 mainly differs from exports in the larger share of travel services (25%) and the minimal role of insurance and intellectual property import flows (less than 1% in each case).

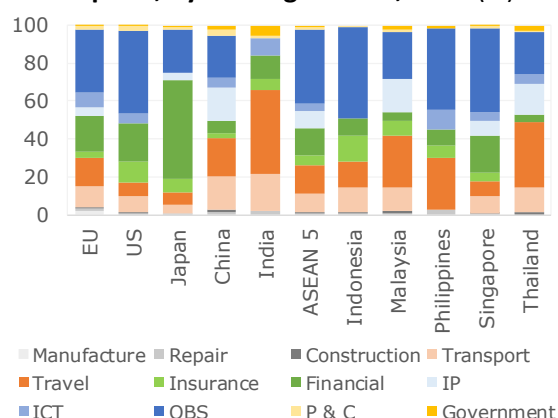
This picture is much starker when considering individual countries beyond the case of Singapore. UK imports of travel services represent more than 40% for the rest of the ASEAN Member States, reaching almost 80% in the case of Thailand.

Figure C: Sectoral Composition of UK Services Exports, by Trading Partner, 2019 (%)



ASEAN 5 = Indonesia, Malaysia, the Philippines, Singapore, and Thailand; ASEAN = Association of Southeast Asian Nations; EU = European Union; IP = intellectual property; ICT = information and communication technology; OBS = other business services; P & C = personal and cultural services UK = United Kingdom; US = United States. Source: Office for National Statistics (2020).

Figure D: Sectoral Composition of UK Services Imports, by Trading Partner, 2019 (%)



ASEAN 5 = Indonesia, Malaysia, the Philippines, Singapore, and Thailand; ASEAN = Association of Southeast Asian Nations; EU = European Union; IP = intellectual property; ICT = information and communication technology; OBS = other business services; P & C = personal and cultural services UK = United Kingdom; US = United States. Source: Office for National Statistics (2020).

Services trade balance

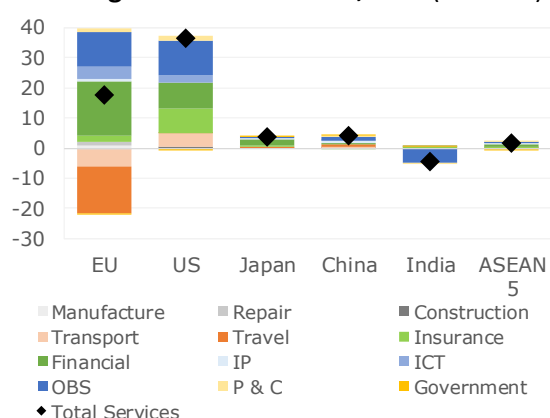
The UK is a global leader in providing services to the rest of the world, recording a significant trade surplus (around £100 billion in 2019) (Figure E). On a bilateral basis, this surplus is higher with the US (\$36 billion) than with the UK's main partner, the EU (\$18 billion). This situation is the result of a trade deficit in both transportation and, particularly, travel services.

The balance with Asian economies is also positive against Japan, China, and the ASEAN 5, while it is negative in the case of India due to ICT services imports by the UK.

At the country level (Figure F), the UK has a trade surplus with Malaysia, Singapore, and Indonesia, while the balance is slightly negative with the Philippines and Thailand due to a bilateral deficit in travel services.

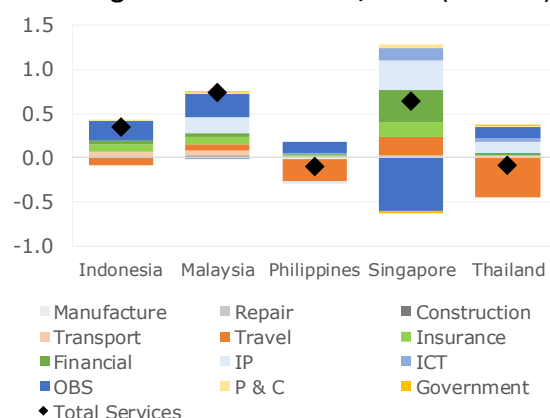
In the case of Singapore, the UK's main service trade partner in ASEAN, the UK is specialised in providing financial services and intellectual property, while the same happens for Singapore in the category of 'other business services', which includes professional and technical activities.

Figure E: UK Services Trade Balance by Trading Partner and Sector, 2019 (£ billion)



ASEAN 5 = Indonesia, Malaysia, the Philippines, Singapore, and Thailand; ASEAN = Association of Southeast Asian Nations; EU = European Union; ICT = information and communication technology; UK = United Kingdom; US = United States.
Source: Office for National Statistics (2020).

Figure F: UK Services Trade Balance by Trading Partner and Sector, 2019 (£ billion)



ASEAN 5 = Indonesia, Malaysia, the Philippines, Singapore, and Thailand; ASEAN = Association of Southeast Asian Nations; EU = European Union; ICT = information and communication technology; UK = United Kingdom; US = United States.
Source: Office for National Statistics (2020).

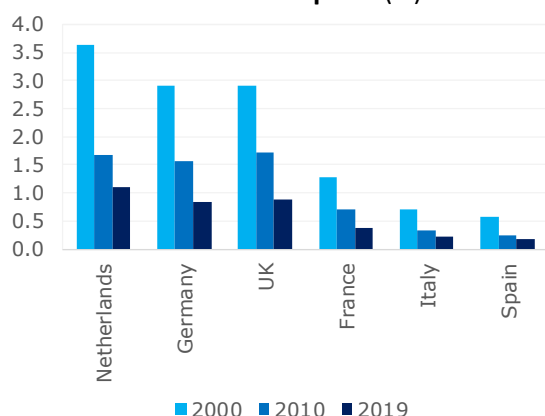
Box source: Authors.

Trade flows between ASEAN and the EU compared with the UK

EU economies, as we observed in the previous section for the case of the UK, have lost their relevance as a destination for ASEAN exports, reflecting stagnant economic growth compared with that of other ASEAN trading partners, especially China and the rest of Asia. This is true for all major EU countries (as measured by GDP size), and particularly for Germany and the Netherlands, showing in all cases a share below 1% as an export destination for ASEAN products in 2019 (Figure 3.21).

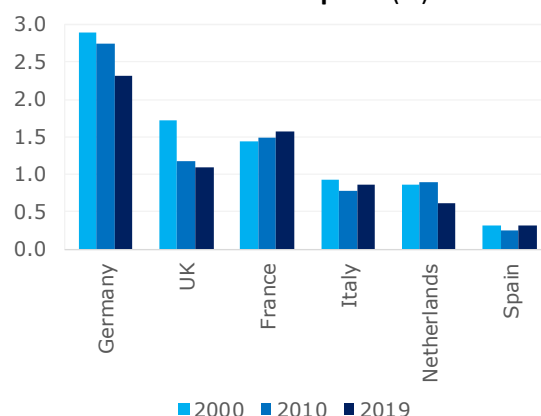
On the import side, a more heterogeneous picture is observed, with imports from Germany and the Netherlands becoming less relevant in relative terms for ASEAN (Figure 3.22) – similar to the trend described above for the UK. In contrast, the share of total ASEAN imports has remained relatively stable for Italy and Spain, and even increased for France.

Figure 3.21: ASEAN Exports to the UK and the Largest EU Countries in Total ASEAN Exports (%)



ASEAN = Association of Southeast Asian Nations, EU = European Union, UK = United Kingdom.
Sources: Natixis, UN Comtrade, and UNCTAD.

Figure 3.22: ASEAN Imports from the UK and the Largest EU Countries in Total ASEAN Imports (%)

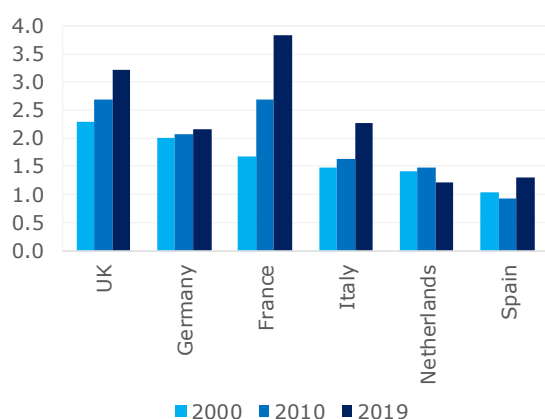


ASEAN = Association of Southeast Asian Nations, EU = European Union, UK = United Kingdom.
Sources: Natixis, UN Comtrade, and UNCTAD.

When looking from the EU perspective, the relative share of ASEAN in total exports has increased – as for the UK in the previous section – for most large EU economies (Figure 3.23). That is particularly the case of France, which has experienced a doubling of the share of exports to ASEAN since 2000.

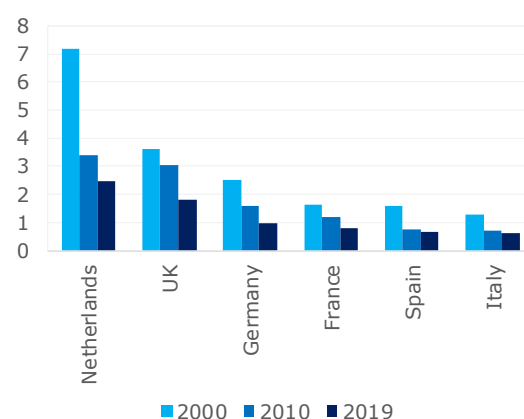
On the import side, the share of ASEAN has come down – as observed before for the UK – in all EU countries and particularly for the Netherlands, which seems to contradict ASEAN’s increasing economic weight and might reflect a fast-rising dependence on China’s products (Figure 3.24).

Figure 3.23: Exports to ASEAN in Total Exports, by Country (%)



ASEAN = Association of Southeast Asian Nations, EU = European Union, UK = United Kingdom.
Sources: Natixis, UN Comtrade, and UNCTAD.

Figure 3.24: Imports from ASEAN in Total Imports, by Country (%)



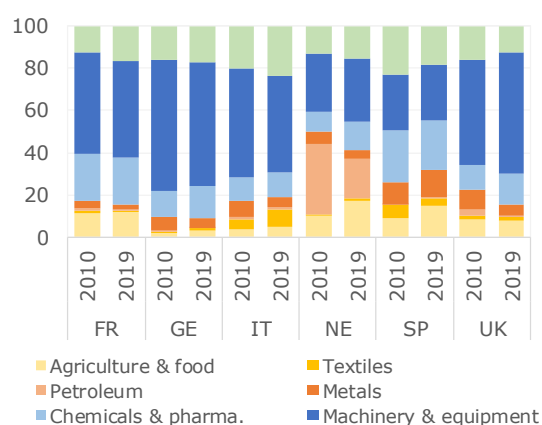
ASEAN = Association of Southeast Asian Nations, EU = European Union, UK = United Kingdom.
Sources: Natixis, UN Comtrade, and UNCTAD.

Moving to the sectoral composition of ASEAN trade with the largest EU economies, some differences can be identified. While similar for Germany, France, Italy, and the UK, the relative share of Dutch and

Spanish exports of machinery and equipment to ASEAN is much smaller compared with other export destinations (Figure 3.25). In turn, the Netherlands exports more petroleum products to ASEAN and Spain exports more chemicals and pharmaceuticals to ASEAN.

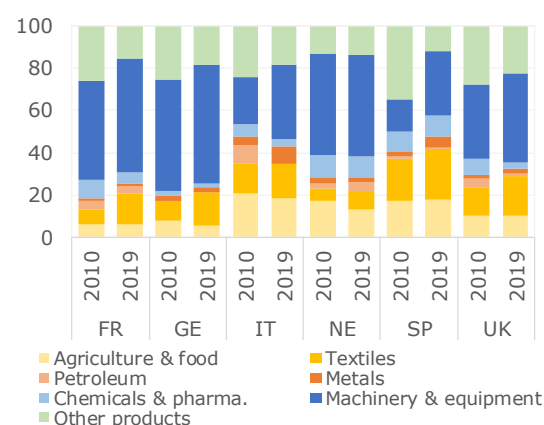
The sectoral structure of imports from ASEAN is again similar for Germany, France, and the UK (Figure 3.26), with machinery and equipment as the largest product group followed by textiles. In this case, agricultural and food products are more relevant for Italy and Spain.

Figure 3.25: Sectoral Composition of ASEAN Imports, by Trading Partner (%)



ASEAN = Association of Southeast Asian Nations, FR = France, GE = Germany, IT = Italy, NE = Netherlands, SP = Spain, UK = United Kingdom. Note: See Box 3.1 for the definition of sectors. Source: UN Comtrade.

Figure 3.26: Sectoral Composition of ASEAN Exports, by Trading Partner (%)



ASEAN = Association of Southeast Asian Nations, FR = France, GE = Germany, IT = Italy, NE = Netherlands, SP = Spain, UK = United Kingdom. Note: See Box 3.1 for the definition of sectors. Source: UN Comtrade.

Box 3.3: RCEP – A Regional Trade Agreement with Asian Linkage Only

After 8 years of negotiations, the Regional Comprehensive Economic Partnership (RCEP) comprising 15 Asian countries was announced in November 2020. The trade deal is expected to tighten ties amongst Asian countries in terms of key liberalisation measures and the value chain in Asia.

As the largest trade agreement so far, the RCEP links 15 Asia-Pacific economies in trade liberalisation – the 10 Association of Southeast Asian Nations (ASEAN) Member States, Australia, China, Japan, New Zealand, and the Republic of Korea (henceforth, Korea). The signatories to the agreement make up nearly one-third of the world's total population and nearly 29% of global gross domestic product (GDP).

The aim of the RCEP was even bigger when the negotiations started in 2012. Not only was the geographical coverage larger – with India, the third largest economy in Asia – but the scope in terms of liberalisation was also greater. India withdrew from the negotiations because of the potential negative impact on its local industry development from Chinese imports. Furthermore, when the RCEP started as a response to the then Trans-Pacific Partnership (TPP), the strategic competition between the United States (US) and China was just starting; now, it is pulling RCEP members in different directions. The best example is the ongoing trade friction between China and Australia, which started almost immediately after the RCEP was concluded in the last quarter of 2020. Although the US is not

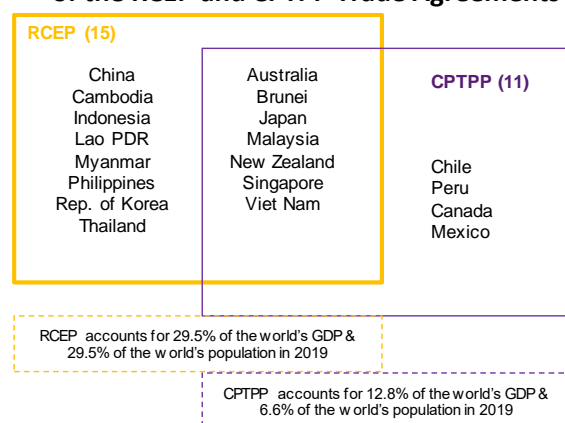
a member of the RCEP, increasingly pervasive US sanctions against China targets will affect the RCEP's performance.

The importance of the RCEP is apparent on both economic and political fronts. The RCEP is expected to reduce tariffs over a 20-year period, streamline customs procedures, and replace a number of bilateral trade agreements in the region with one set of rules. The unique value of the RCEP is in simplifying and minimising different rules of origins, thus equating the requirements for all players. The RCEP is not as broad an agreement as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) because it focuses only on trade in goods, excludes services, and does not mitigate the influence of state-owned enterprises in the economy (Figure A). Still, it is a valuable regional structure as it links the major economies in the Asia-Pacific region and tightens the bond between Asian countries, particularly in a time of de-globalisation and post-pandemic recovery, without the involvement of the US or Europe.

The impact from the RCEP is believed to be incremental, as the existing trade agreements have already pushed the tariffs low. In fact, the current average tariff is 4.4% amongst the members of the RCEP and only 2.7% amongst the members of the CPTPP, yet the GDP per capita of CPTPP members is 1.5 times higher than that of the RCEP members (Figure B). For the RCEP to enter into force, at least six ASEAN Member States and three non-ASEAN countries need to ratify the agreement. By the end of April 2021, China, Singapore, and Thailand had completed the procedures for ratification, while Japan is in the process of completion.

Beyond the economic benefits, which may not be obvious in the short term as tariffs are already low, the high point of the RCEP may be simplifying different rules into a single set of rules of origin – equating the requirements for all players.

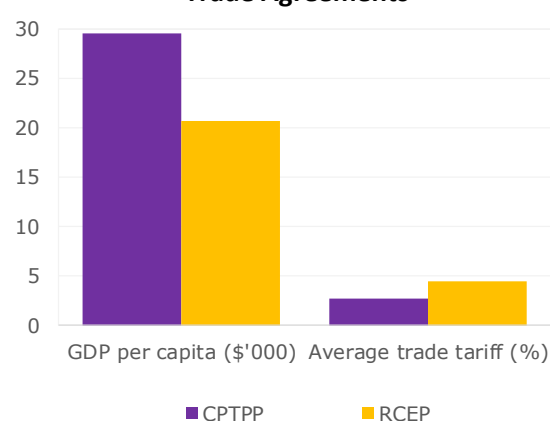
Figure A: Membership and Characterisation of the RCEP and CPTPP Trade Agreements



CPTPP = Comprehensive and Progressive Agreement for Trans-Pacific Partnership, GDP = gross domestic product, RCEP = Regional Comprehensive Economic Partnership.

Sources: Natixis and WDI.

Figure B: Characterisation of the RCEP and CPTPP Trade Agreements



CPTPP = Comprehensive and Progressive Agreement for Trans-Pacific Partnership, GDP = gross domestic product, RCEP = Regional Comprehensive Economic Partnership.

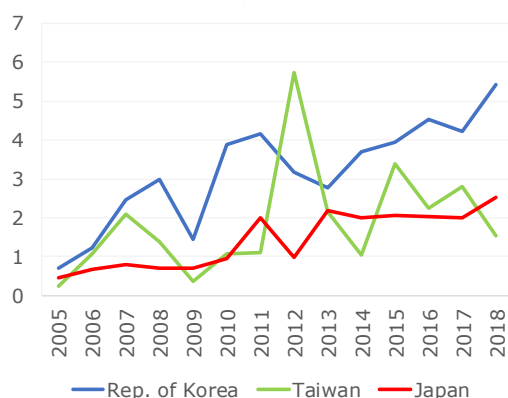
Sources: Natixis and WDI.

ASEAN will lead the reshuffle in value chains

ASEAN has been receiving increasing manufacturing foreign direct investment (FDI) from Korea, Taiwan, and Japan (Figure C), and the amount has already been larger than to China (Figure D). This is

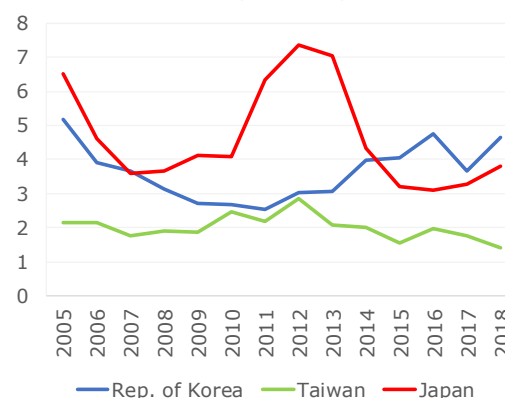
in response to the increasingly high labour costs in China compared with the rest of ASEAN, and the need to diversify the risks from a value chain that remains overly concentrated in China. With the increasing amount of FDI, and the ease of the RCEP rules, ASEAN will be able to grow its manufacturing capacity to serve the massive market of North Asia. China's ageing population makes this trend even more meaningful.

Figure C: FDI in ASEAN
(\$ billion)



ASEAN = Association of Southeast Asian Nations,
FDI = foreign direct investment.
Sources: Natixis and CEIC.

Figure D: FDI in China
(\$ billion)



FDI = foreign direct investment.
Sources: Natixis and CEIC.

Potential impact on the US and the EU

The RCEP and the CPTPP will shape the regional economic architecture, but the RCEP poses challenges for the CPTPP, and to the influence of the US and the European Union (EU) in the Indo-Pacific region. With the US perhaps re-joining the CPTPP, participating in the CPTPP requires a higher level of commitment than the RCEP as it covers more areas of trade and investment well beyond tariff reduction. In addition, the existing members have potential veto power – offering less negotiation room for newcomers to alter existing rules. As such, the CPTPP is poised to receive attention from several countries, especially after the closure of the RCEP negotiations, but the actual expansion of its membership might not be as fast.

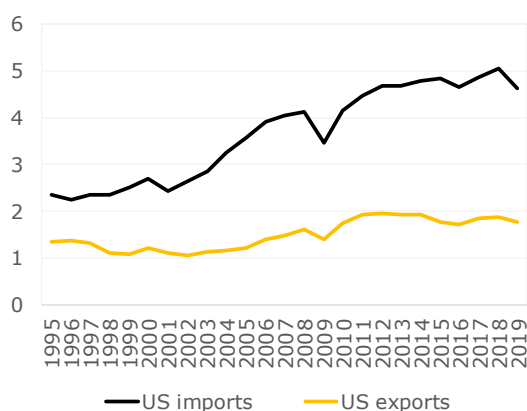
Multiregional trade between the US and the EU with Asian countries has been evolving, with increases in both imports and exports. Both the US and the EU have incorporated heavy trade relations with Asian countries beyond the RCEP (Figures E and F), particularly with China, Japan, and Korea.

Since the US and the EU are not yet part of either trade deal, the RCEP may tilt economic reliance towards China – reducing Asian dependence on the US market. The RCEP covers all East Asia, which is a hub for the supply chain networks of major manufacturing companies. The gradual shift of manufacturing from China to more cost-efficient Southeast Asia could enable China to accumulate more cost-competitive exporting power to the US. On the other hand, the RCEP includes key US allies – Korea, Japan, Australia, and New Zealand. Tighter economic ties with these countries could provide leverage for any aspiring member of the RCEP.

The EU has concluded the Comprehensive Agreement on Investment with China and free trade agreements with Korea, Japan, Singapore, and Viet Nam. Amongst the existing economic relations, the RCEP could benefit the EU through a reduction in costs under rules of origin as European companies participate in intra-Asian supply chains or subsidiaries. On the other hand, the cost-competitive manufactured products from Asian countries could threaten EU manufactured goods with

more intense competition. That said, the impact of the RCEP on EU–Asia economic relations will be seen incrementally in the long term.

Figure E: US Trade with RCEP Countries as a Share of GDP (%)

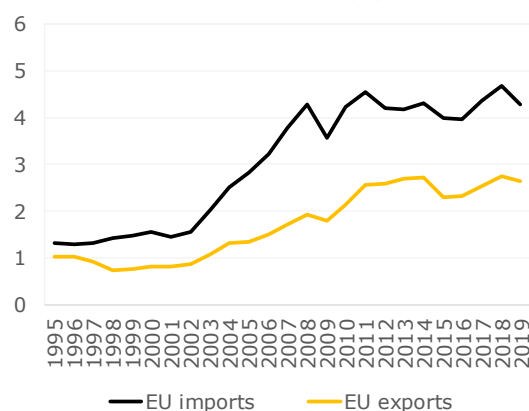


GDP = gross domestic product, RCEP = Regional Comprehensive Economic Partnership, US = United States.

Note: In 2015 constant prices.

Sources: Natixis and UNCTAD.

Figure F: EU Trade with RCEP Countries as a Share of GDP (%)



EU = European Union, GDP = gross domestic product, RCEP = Regional Comprehensive Economic Partnership.

Note: In 2015 constant prices.

Sources: Natixis and UNCTAD.

UK–ASEAN partnership in the Indo-Pacific and the RCEP

The United Kingdom (UK) Government’s Integrated Review of Security, Defence, Development and Foreign Policy (HM Government, 2021) provides a current assessment of the major trends that will shape the national security and international environment to 2030. Timely and strategic participation of the UK in global and regional initiatives is the key to realising the Prime Minister’s Vision for the UK to 2030 (HM Government, 2021: 6–7).

The Integrated Review spells out the global role of the UK as an open economy and a maritime trading nation with a large diaspora. It identifies the Indo-Pacific as one of the dynamic regions of the world, and deepening of connections with the economic architecture of this region will enhance the UK’s future prosperity. ASEAN is at the centre of the Indo-Pacific, and UK cooperation with ASEAN will be crucial to any prospective participation in the RCEP and the CPTPP. The UK has important trade linkages with the 10 ASEAN Member States of the RCEP, as well as the other five – Australia, China, Japan, Korea, and New Zealand. The RCEP and the CPTPP will also provide pathways for the UK to adapt to the intricate regional value chains in the Indo-Pacific and the balance of power, while working with existing structures.

To attain the objectives under the strategic framework, stronger diplomatic and trading ties are envisaged with several countries in the region such as China, India, and Japan; and extend to others including Korea, Viet Nam, Indonesia, Malaysia, Thailand, Singapore, and the Philippines. Although closer relations through existing institutions such as ASEAN and the CPTPP (the UK has applied for accession to the CPTPP) are clearly spelled out in the strategic framework, UK–ASEAN relations may also find a unique synergy through the RCEP.

Chapter 20 (Final Provisions) of the RCEP sets out the relationship between the RCEP agreement and other international agreements, a general review mechanism, procedures to amend the agreement, and an accession provision. The RCEP agreement is open for accession by any state or separate customs territory 18 months after its entry into force.* The Depositary¹ for the RCEP will be

responsible for receiving and disseminating documents to the acceding state or customs territory, including any notifications, requests for accession, and instruments of ratification acceptance, approval, or accession. The provision on entry into force provides that the RCEP agreement would need signatory states, including at least six ASEAN and three non-ASEAN signatory states, to deposit their instruments of ratification, acceptance, or approval for the RCEP agreement to enter into force. The UK still has time to consider its accession plans to the RCEP.

* This agreement is open for accession by India, as an original negotiating state, from the date of its entry into force, without waiting 18 months.

¹ The RCEP Agreement has designated the Secretary-General of ASEAN as the Depositary for this Agreement and any amendment thereto. The Depositary will accept the instruments of ratification and notice for withdrawal and accession, amongst other functions.

Source: Authors.

Main takeaways for UK opportunities in ASEAN

UK trade with ASEAN is modest, given the increasing relevance of ASEAN in the global economy. This is true for trade in goods and services. Changing this trend will not be easy, as the rule of gravity has pushed China to the centre of ASEAN exchanges. This is particularly true for trade in parts of components, given ASEAN's large integration in the global supply chain.

For the UK to increase its share of trade in goods and services, it is important to accelerate the UK's accession to the CPTPP while reaching bilateral deals with some AMS to further support economic exchanges with this region. The recent trade deal between the UK and Australia is a good case in point, given Australia's close relations with ASEAN.

More importantly, the UK needs to target its efforts towards its comparative advantage – services and, most importantly, digital services. Achieving strategic autonomy in the increasingly harsh competition between the US and China can only help the UK achieve this goal.

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Chapter 4

Trade Integration between ASEAN and the UK

Chapter 4

Trade Integration between ASEAN and the UK

This chapter makes use of value chain analysis to describe the degree and nature of trade integration between the Association of Southeast Asian Nations (ASEAN) and the United Kingdom (UK), and in the global context. It provides an overall characterisation as well as sectoral disaggregation of the UK's main trading partners, focusing on trade integration with the European Union (EU). It provides comparative data for the UK to establish its competitiveness in key goods and services sectors which have potential for further integration. It also includes a box on definitions and data related to value chain analysis.

Overview

Trade integration is very important for ASEAN, especially participation in global supply chains. This is particularly the case of electronics and other parts and components. However, supply chains are increasingly less global and more dominated by Asian players, especially China.

The participation of ASEAN in the value chain is mostly downstream. In other words, ASEAN economies import a large share of intermediate goods, with which they produce goods for re-export. Hence, they are very dependent on the rest of the world to re-export, and the value added produced domestically is rather limited. This is no longer the case for China. In fact, a good part of the intermediate goods imported by ASEAN economies come from China, as the latter has moved up the production ladder in the past couple of decades.

ASEAN does not import as many intermediate products from the EU for re-export as it does from China (or Japan or the Republic of Korea (henceforth, Korea)) or even the United States (US). Furthermore, the relative importance of the EU as a provider of intermediate goods for ASEAN to re-export is waning. This is even more true for the UK.

In sectoral terms, electronics are critical in the participation of ASEAN economies in the global supply chain, but with a very important characteristic: ASEAN imports most intermediate goods from China to re-export, but most of ASEAN's exports of intermediate – or final – goods go to the West. In other words, Asia's value chain is increasingly asymmetrical in China's favour. This makes it hard for the UK to benefit as much as could have been the case in the past before China acquired such a central role in the production of parts and components.

The mirror of China's centrality in the global supply chain is that the share of the UK – or even the EU – in key areas of the supply chain has been shrinking, especially in electronics. Trade in business services, however, has increased significantly. This trend is shared to a lesser extent by EU economies. The question is how far the UK can go without a trade deal which includes further liberalisation in trade in services.

Against such a backdrop, the UK should look at ASEAN as an area of great potential, not only for its current size – but most importantly, potential – given its population dynamics. However, the law of gravity makes it very difficult for the UK to carve out a space in a region increasingly dominated by China. This is not only the case of trade in goods, which has been fostered by China's rapidly increasing role in the global supply chain and its fast move up the production ladder, but also beyond trade issues. China is very engaged in building hard and digital infrastructure in ASEAN as well as developing

common standards. The longer the UK waits to become a full member of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), the harder it will be to carve out market share even in services, especially digital services.

Our findings call for a swift move towards speedy accession to the CPTPP as well as any other form of bilateral deals. The recently announced free trade agreement between the UK and Australia is a good example, given Australia's close integration with ASEAN – both economically and politically.

Box 4.1: Data Description and Definitions

Value chain framework

Products that are traded internationally are composed of inputs from different countries and sectors around the world, creating global production chains. Conventional measures of international trade (e.g. gross exports and imports) used throughout chapter 3 do not capture these complex relations.

Studying the global macroeconomy with its country and cross-sectoral linkages, by using global input–output data, has become a widely used approach since the pioneering work of Hummels, Ishii, and Yi (2001). Broadly speaking, the input–output accounting structure comprises all economic transactions between the possible combinations of producing sectors and countries, differentiating between production used for further processing (intermediate demand) and production used for final consumption or investment (final demand).

Global value chain (GVC) analysis refers to the study of how value added is generated and distributed through global production chains (from *upstream* to *downstream* activities), making use of the relations defined in the input–output framework.

Definitions

The degree to which a country is integrated in GVCs is usually captured by a metric called *GVC participation*, which is the sum of two components: foreign value added in exports (FVA or *backward participation*) and domestic value added in foreign exports (DVX or *forward participation*). In other words, GVC participation accounts for value added generated in a country that crosses at least two borders in international trade relative to gross exports. In terms of specialisation, a country that is backwardly integrated in a GVC corresponds to an economy that relies on foreign inputs for its exports to the rest of the world and is positioned downstream within value chains, while a country that is forwardly integrated in GVC supplies inputs to other economies for their exporting activities and is positioned upstream within value chains.

Participation or integration in value chains could also be applied to narrower economic areas or bilateral relations between countries. For instance, a regional value chain corresponds to transactions between members of a common economic area. The forward and backward participation of each country within the regional value chain could be evaluated with the aforementioned metrics.

Alternatively, if a regional bloc is considered as a single economy, the *regional participation in a GVC* accounts for both the use of inputs sourced out of the regional bloc that are later exported out of the common area (backward participation) and the supply of inputs to a non-member for its exports to a third country (forward participation).

Sectoral approach

A global production chain encompasses a number of participating activities from different sectors. Accordingly, the sectoral characterisation of GVC participation can be defined in many ways. The criterion used throughout this chapter is centrality, and takes as a reference the sector of the exporting activity located midstream of the value chain, i.e. the sector that uses foreign supplies for

exports when analysing backward participation and the sector to which supplies are sold for re-export in the case of forward participation.

Alternatively, the sectoral composition of GVC participation could be analysed considering the sector where the value added being traded across borders was originally generated, i.e. the sector selling supplies used for exports in a different country, both in terms of backward and forward participation. However, this approach looks very similar to the standard analysis of sectoral specialisation in bilateral gross trade as the one used in chapter 3.

Database

Annual data in nominal United States (US) dollars are sourced from the 2018 release of the Organisation for Economic Co-operation and Development (OECD) Trade in Value Added database ([TiVA](#)), which covers 2000–2015 (OECD, 2018).^{*} Country coverage includes, amongst others, all 27 European Union (EU) member countries, the United Kingdom (UK), the US, China, Japan, India, the Republic of Korea, and eight of the 10 Association of Southeast Asian Nations (ASEAN) Member States (Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam).

Sectoral data correspond to codes from the International Standard Industrial Classification of All Economic Activities ([ISIC](#)) at the two-digit level (United Nations, 2008). Sectors are first defined broadly and divided into three categories: manufacturing activities (ISIC codes 10–33); business services (45–82); and other activities (including agriculture, mining, utilities, construction, and public services). Manufacturing activities are then disaggregated into food products (ISIC codes 10–12), textiles (13–15), petroleum products (19), chemicals and pharmaceuticals (20–21), metals (24–25), electronics (26), machinery and equipment (27–28 & 30), motor vehicles (29), and other activities (*other manufacturing*). In turn, business services are disaggregated into trade activities (ISIC codes 45–47), transportation (49–53), information and communication technology (ICT) services (58–63), and other activities (*other business services*).

* An update with data until 2018 is expected during 2021.

** No data were available for the Lao People's Democratic Republic and Myanmar.

Source: Authors.

ASEAN trade integration

Countries' participation in global value chains (GVCs), as measured by the value added generated in a country that crosses at least two borders in international trade relative to gross exports (see Box 4.1 for detailed definitions of GVC concepts used throughout this chapter) reached a peak at the global level in 2008 and progressively declined afterwards.¹ This feature also included Asian economies and the ASEAN region (Figure 4.1).

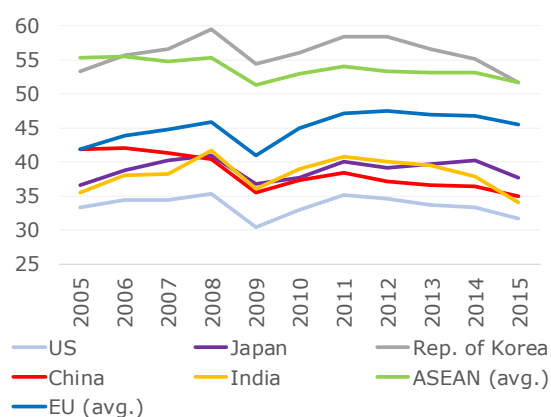
From a more structural perspective, the degree of GVC participation for ASEAN is high by global standards (Figure 4.2), both when considering the average for its Member States and in terms of regional participation in GVCs. This reflects the global orientation of ASEAN regional value chains – in contrast with the internal market orientation of EU trade networks.

By type of participation, the share of foreign value added in gross exports (FVA) – or backward integration – accounts for almost two-thirds of ASEAN participation in GVCs, stressing its global

¹ The database used in this chapter covers 2000–2015, as indicated in Box 4.1. Unfortunately, data for GVC analysis are published with a substantial delay and the available sample does not allow a thorough analysis of recent trends – particularly the effect of the coronavirus disease (COVID-19) outbreak. For the latter, higher-frequency but indirect and partial metrics are used in chapter 5 to provide insights on potential GVC reshuffling originated by the pandemic.

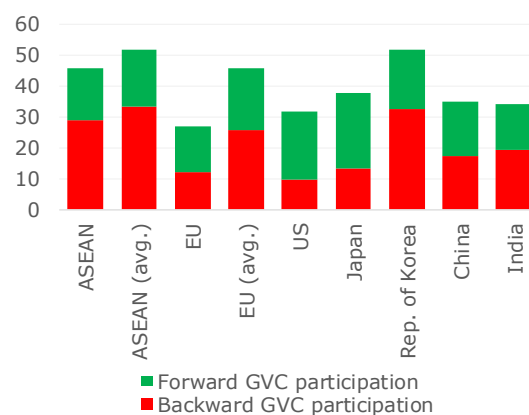
upstream position as final exporter (Figure 4.2). This contrasts with the predominant role of the share of domestic value added in foreign exports (DVX) – or forward integration – in the US and Japan, both specialised in intermediate exports.

Figure 4.1: GVC Participation by Economic Area (% of gross exports)



ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States. Notes: See Box 4.1 for the definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019. Source: OECD (2018).

Figure 4.2: GVC Participation by Economic Area and Type, 2015 (% of gross exports)



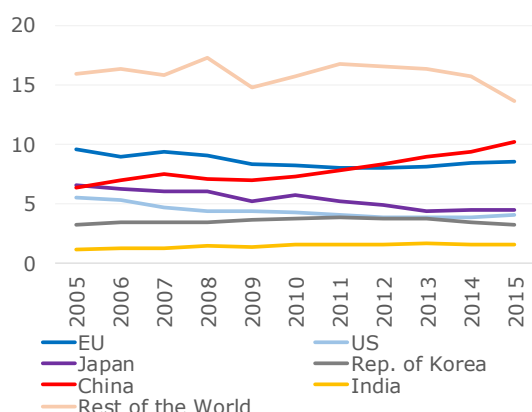
ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States. Notes: See Box 4.1 for the definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019. Source: OECD (2018).

ASEAN integration with the main developed economies has declined since its peak in the late 2000s, keeping a steady negative trend vis-à-vis the US and Japan, while we observe a partial recovery with respect to the EU. On the other hand, ASEAN has become increasingly integrated with the two largest Asian economies, particularly with China, which has become the main individual partner in GVCs.

ASEAN integration has progressively shifted away from developed to developing economies, particularly reflecting what is known as ‘China centrality’ in GVCs (Figure 4.3). Within developed economies, a steady negative trend has been observed for ASEAN integration with the US and Japan since its peak in the late 2000s. In contrast, a partial recovery took place in recent years with respect to the EU, which remains the main integration partner for ASEAN amongst developed economies.

On a structural basis, the GVC integration of ASEAN with other economies predominantly corresponds to backward participation, i.e. importing foreign products that are incorporated into ASEAN exports (Figure 4.4). This is particularly strong vis-à-vis the US and Japan, while it is more balanced with the rest of the world. Interestingly, the nature of bilateral integration has changed over time, positioning ASEAN more upstream with respect to the EU and downstream with respect to China, accounting for a larger participation of Chinese inputs in ASEAN exports.

Figure 4.3: GVC Participation of ASEAN, by Partner (% of gross exports)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain, US = United States.

Notes: See Box 4.1 for the definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019.

Source: OECD (2018).

Figure 4.4: GVC Participation of ASEAN, by Partner and Type (% of gross exports)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain, RoW = rest of the world, US = United States.

Notes: See Box 4.1 for the definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019.

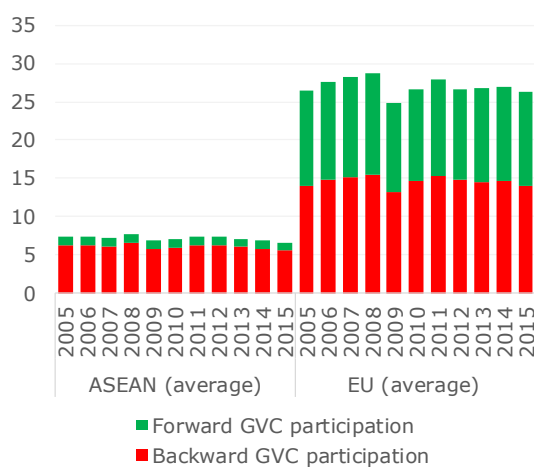
Source: OECD (2018).

The degree of integration within an economic bloc can be measured by the size of its regional value chain, which corresponds to the sum of foreign supplies imported from non-members and used in exports to other member countries (backward participation) and inputs exported by a member state that are re-exported within the regional borders to a third country (forward participation).

According to this definition, the integration of the ASEAN regional trade network has remained very low (Figure 4.5), particularly when compared with the extensive multi-country production network of the EU, as well as with the aforementioned high GVC participation of ASEAN. These contrasts highlight the external orientation of ASEAN regional trade as opposed to the more internal-oriented single market in the EU.

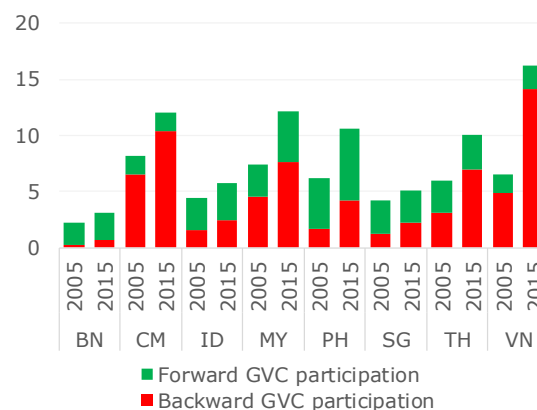
From a country perspective, the main partners of ASEAN Member States (AMS) in GVC participation correspond either to other ASEAN economies, the EU, or China. Integration with China has increased in recent years in all cases, particularly for Cambodia, Malaysia, the Philippines, Thailand, and Viet Nam (Figure 4.6). As mentioned before for ASEAN as a region, increasing backward participation has been the main contributor to this push towards further integration with China, with Chinese inputs having reached close to 15% of the gross value of Vietnamese exports in 2015.

Figure 4.5: RVC Participation in ASEAN and the EU, by Type (% of gross exports)



ASEAN = Association of Southeast Asian Nations, EU = European Union, RVC = regional value chain. Notes: See Box 4.1 for the definition of RVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019. Source: OECD (2018).

Figure 4.6: GVC Integration of ASEAN Member States with China, by Type (% of gross exports)

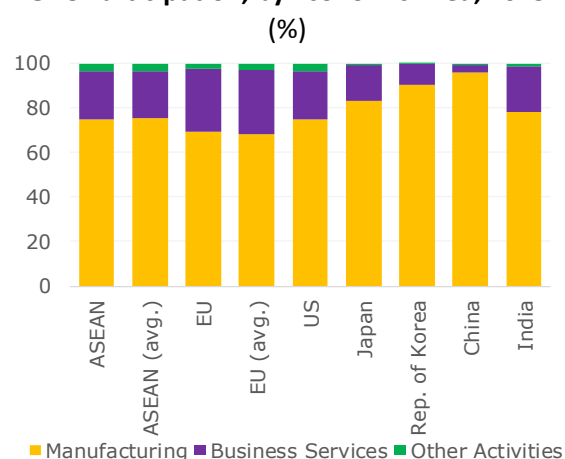


ASEAN = Association of Southeast Asian Nations, BN = Brunei Darussalam, CM = Cambodia, GVC = global value chain, ID = Indonesia, MY = Malaysia, PH = Philippines, SG = Singapore, TH = Thailand, VN = Viet Nam. Notes: See Box 4.1 for the definition of GVC participation. No data were available for the Lao PDR and Myanmar. Source: OECD (2018).

Moving to the sectoral composition of trade integration (see Box 4.1 for details), manufacturing exports concentrate the vast majority of GVC participation across all main global economies, reflecting both a higher degree of tradability and a more internationally fragmented value chain (Figures 4.7 and 4.8).

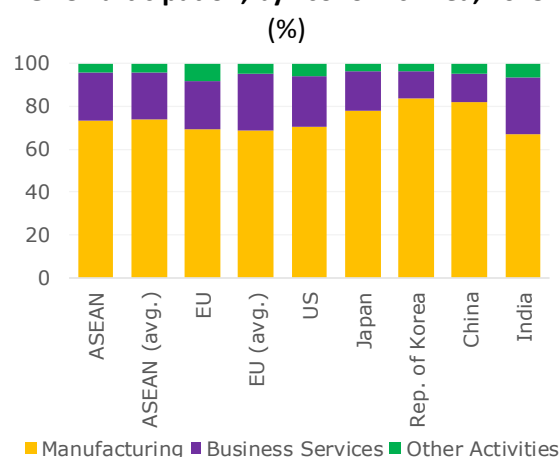
Having said that, certain specialisation is observed across different economic areas. For instance, China, Japan, and Korea show a higher share in manufacturing GVC participation by exporting sector, particularly as purchasers of foreign inputs (backward participation). On the opposite side, the EU and India are relatively specialised in GVC participation for business services exports, while the US and ASEAN show a mixed picture.

Figure 4.7: Sectoral Composition of Backward GVC Participation, by Economic Area, 2015



ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States. Notes: See Box 4.1 for the definition of backward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019. Source: OECD (2018).

Figure 4.8: Sectoral Composition of Forward GVC Participation, by Economic Area, 2015

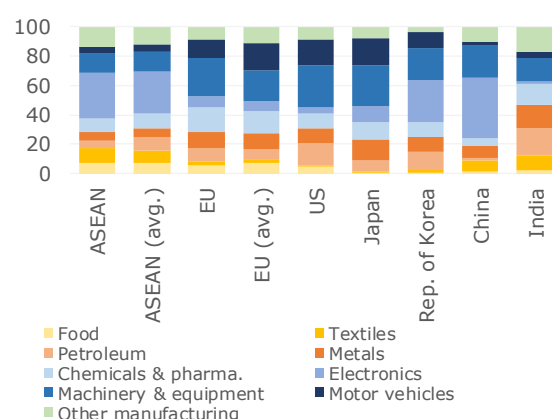


ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain, US = United States, avg. = country weighted average. Notes: See Box 4.1 for the definition of forward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019. Source: OECD (2018).

Heterogeneity is larger at a more disaggregated level. For instance, when looking into GVC participation in manufacturing exports, the EU, the US, and Japan are relatively specialised in backward integration for motor vehicles and machinery and equipment exports, while China and ASEAN are specialised in backward integration for electronics, food, and textiles (Figure 4.9).

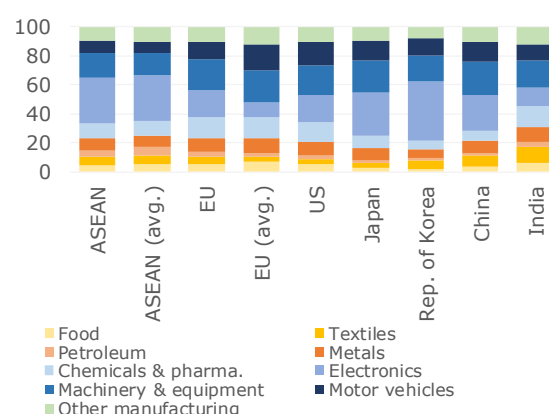
Specialisation patterns are less intense in terms of forward GVC participation (Figure 4.10), although still significant for some manufacturing exports: motor vehicles and chemicals and pharmaceuticals for the EU and the US, textiles for China and India, and electronics for Korea and ASEAN.

Figure 4.9: Sectoral Composition of Backward GVC Participation in Manufacturing Exports, by Economic Area, 2015 (%)



ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States. Notes: See Box 4.1 for the definition of backward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019. Source: OECD (2018).

Figure 4.10: Sectoral Composition of Forward GVC Participation in Manufacturing Exports, by Economic Area, 2015 (%)



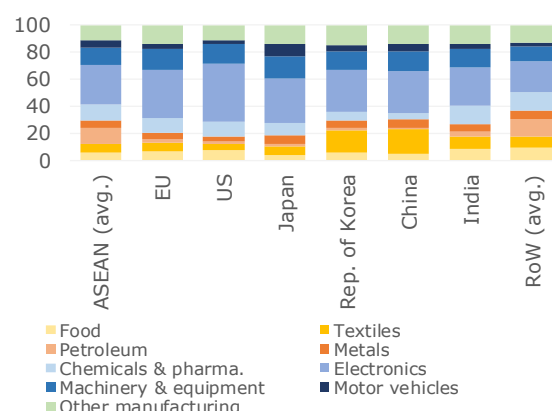
ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States. Notes: See Box 4.1 for the definition of forward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019. Source: OECD (2018).

When looking into the bilateral integration of ASEAN with other economic areas, the sectoral composition would in principle reflect ASEAN export specialisation for backward GVC participation and partners' specialisation for forward GVC participation.

For instance, ASEAN GVC integration in manufacturing exports is characterised by the pivotal role of electronics. In terms of backward integration, electronics accounts for the largest share vis-à-vis all partners, being slightly higher relative to developed countries (Figure 4.11), while the picture is rather heterogeneous for forward participation manufacturing, observing the largest sectoral shares in bilateral integration with China and Korea (Figure 4.12).

A similar characterisation could be drawn for the second largest sectoral category in ASEAN GVC participation – machinery and equipment – which shows a relatively homogeneous share in backward integration and a significantly higher weight with developed economies in forward integration.

Figure 4.11: Sectoral Composition of ASEAN's Backward GVC Participation in Manufacturing, by Partner and Exporting Sector, 2015 (%)

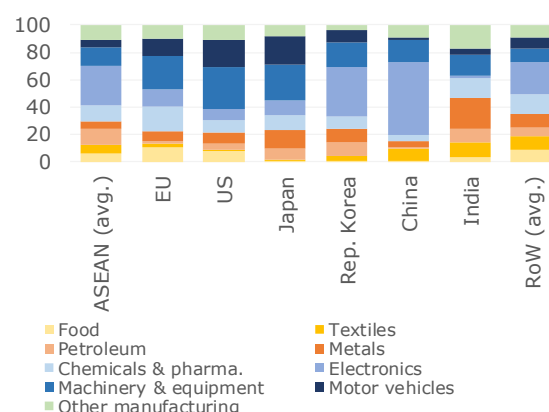


ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States, RoW = Rest of the world.

Notes: See Box 4.1 for the definition of backward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019.

Source: OECD (2018).

Figure 4.12: Sectoral Composition of ASEAN's Forward GVC Participation in Manufacturing, by Partner and Exporting Sector, 2015 (%)



ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States, RoW = rest of the world.

Notes: See Box 4.1 for the definition of forward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019.

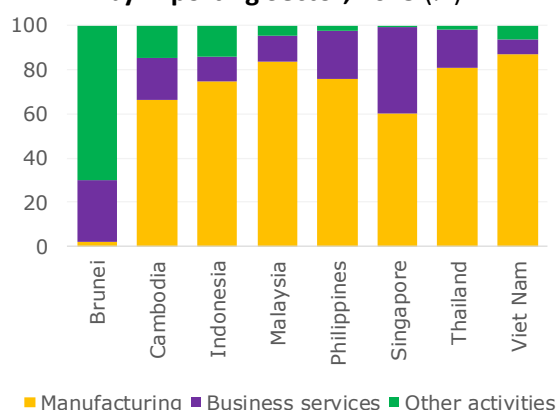
Source: OECD (2018).

At the country level, sectoral specialisation in GVC participation across AMS is rather heterogeneous, reflecting overall production resources and capabilities, as well as competitive advantages within regional and global trade networks.

Heterogeneity is already observed when using broad sectors and is particularly acute in terms of backward participation (Figure 4.13). For instance, while 70% of GVC-related foreign value added is used for mining exports in Brunei Darussalam, the rest of the AMS concentrate backward integration in manufacturing and business services exports, with manufacturing more dominant in Viet Nam and business services more dominant in Singapore.

The composition of forward GVC participation is more homogeneous at this level of analysis, reflecting similarities in the export composition of ASEAN partners (Figure 4.14). Again, Singapore is the exception – showing a marked specialisation in providing inputs for business services exports.

Figure 4.13: Sectoral Composition of ASEAN Member States' Backward GVC Participation, by Exporting Sector, 2015 (%)

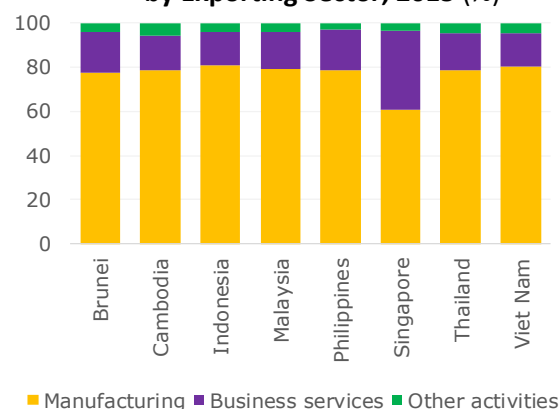


ASEAN = Association of Southeast Asian Nations, GVC = global value chain.

Notes: See Box 4.1 for the definition of backward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).

Source: OECD (2018).

Figure 4.14: Sectoral Composition of ASEAN Member States' Forward GVC Participation, by Exporting Sector, 2015 (%)



ASEAN = Association of Southeast Asian Nations, GVC = global value chain.

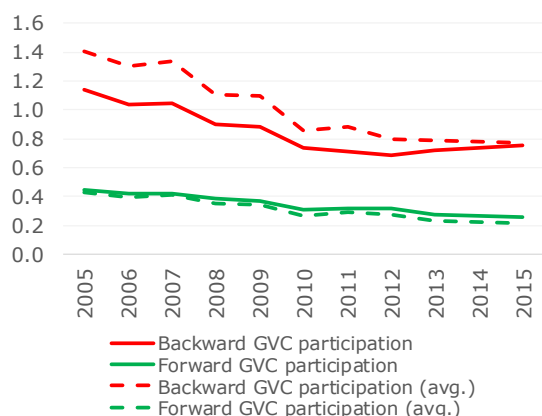
Note: See Box 4.1 for the definition of forward GVC participation and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).

Source: OECD (2018).

Trade integration between ASEAN and the UK

GVC integration between ASEAN and the UK is asymmetrical in both its characterisation and evolution. Backward participation accounts for the largest share from the ASEAN perspective (Figure 4.15) and forward participation is the main contributor from the UK's side (Figure 4.16), showing its input exporter specialisation. As for gross trade flows covered in chapter 3, bilateral integration has become less important for ASEAN, particularly in terms of backward participation, while it has remained relatively stable from the UK perspective.

Figure 4.15: GVC Integration of ASEAN with the UK by Participation Type
(% of ASEAN gross exports)

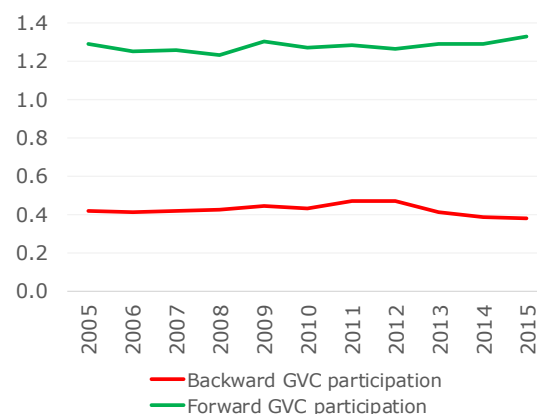


ASEAN = Association of Southeast Asian Nations, GVC = global value chain, UK = United Kingdom.

Notes: See Box 4.1 for the definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).

Source: OECD (2018).

Figure 4.16: GVC Integration of the UK with ASEAN by Participation Type
(% of UK gross exports)



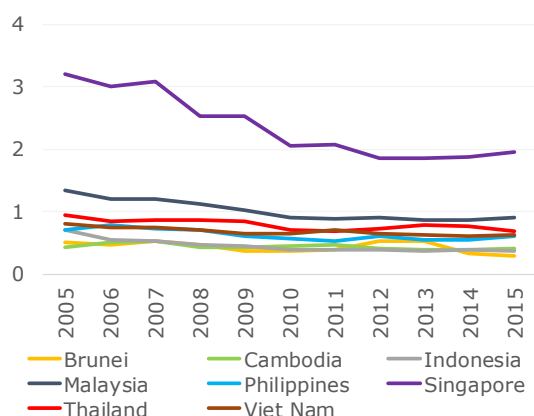
ASEAN = Association of Southeast Asian Nations, GVC = global value chain, UK = United Kingdom.

Notes: See Box 4.1 for definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).

Source: OECD (2018).

From a country perspective, the most significant bilateral integration is observed between Singapore and the UK (Figures 4.17 and 4.18), reflecting the offshore nature of Singapore and holding from the perspective of both partners. For the rest of the AMS, it has remained relatively limited, particularly for commodity exporting countries such as Brunei Darussalam, Cambodia, and Indonesia.

Figure 4.17: GVC Integration of AMS with the UK (% of AMS gross exports)

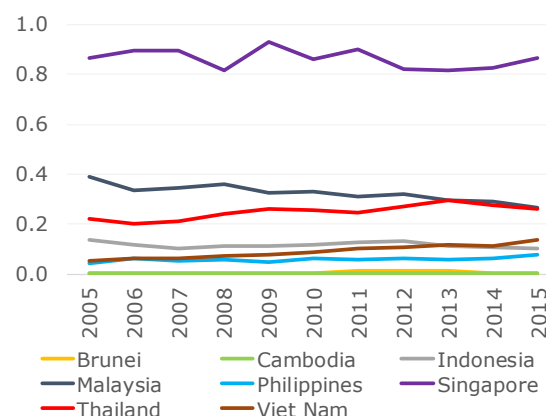


AMS = ASEAN Member States, ASEAN = Association of Southeast Asian Nations, GVC = global value chain, UK = United Kingdom.

Notes: See Box 4.1 for the definition of GVC integration. No data were available for the Lao PDR and Myanmar.

Source: OECD (2018).

Figure 4.18: GVC Integration of the UK with AMS (% of UK gross exports)



AMS = ASEAN Member States, ASEAN = Association of Southeast Asian Nations, GVC = global value chain, UK = United Kingdom.

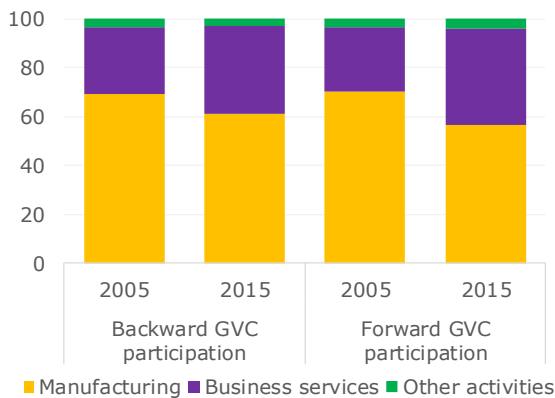
Notes: See Box 4.1 for the definition of GVC integration. No data were available for the Lao PDR and Myanmar.

Source: OECD (2018).

When looking into the sectoral composition of integration between the UK and ASEAN (Figure 4.19), the first noticeable feature is the relatively high share of business services when compared with the overall structure of ASEAN GVC participation (Figures 4.7 and 4.8), reflecting the UK's specialisation in service activities. Furthermore, the share of bilateral integration in business services has been rising over time in both directions (Figure 4.15). More disaggregated data show that this increase has been mainly driven by financial and professional services.

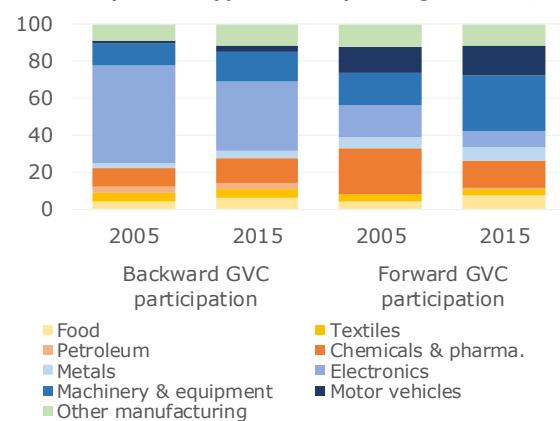
Nevertheless, as in the global perspective, most of the bilateral integration between ASEAN and the UK is in manufacturing exports (Figure 4.19). Within this sector, UK inputs for ASEAN electronics exports (backward participation) account for the largest share, although it has declined over time (Figure 4.20). On the other hand, machinery and equipment is the main category in ASEAN inputs for UK manufacturing exports, followed by motor vehicles. In both cases, the share has increased in recent years.

Figure 4.19: Sectoral Composition of GVC Integration of ASEAN with the UK, by Participation Type and Exporting Sector (%)



ASEAN = Association of Southeast Asian Nations, GVC = global value chain, UK = United Kingdom.
 Notes: See Box 4.1 for the definition of GVC participation types and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).
 Source: OECD (2018).

Figure 4.20: Sectoral Composition of GVC Integration of ASEAN with the UK in Manufacturing, by Participation Type and Exporting Sector (%)



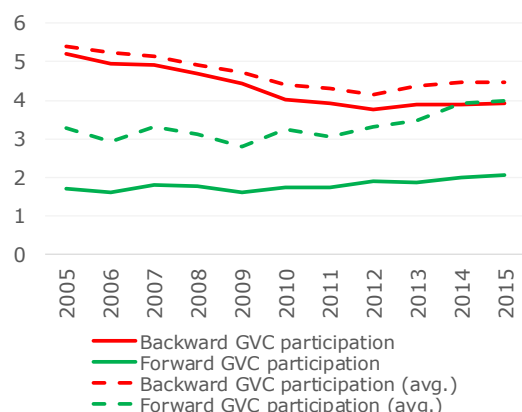
ASEAN = Association of Southeast Asian Nations, GVC = global value chain, UK = United Kingdom.
 Notes: See Box 4.1 for the definition of GVC participation types and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).
 Source: OECD (2018).

Trade integration between ASEAN and the EU compared with the UK

GVC integration between ASEAN and the EU is much more significant from the perspective of ASEAN, which can be explained by both the EU's larger economic size and the internal orientation of its regional production network (Figures 4.21 and 4.22). In recent years, the picture has slightly changed, with the EU becoming less relevant for ASEAN and ASEAN becoming more relevant for the EU as an input provider.

When compared with the UK, GVC integration between ASEAN and the EU is not as asymmetrical as in the previous section (Figures 4.15 and 4.16), although it still confirms the ASEAN downstream GVC specialisation.

Figure 4.21: GVC Integration of ASEAN with the EU by Participation Type
(% of ASEAN gross exports)

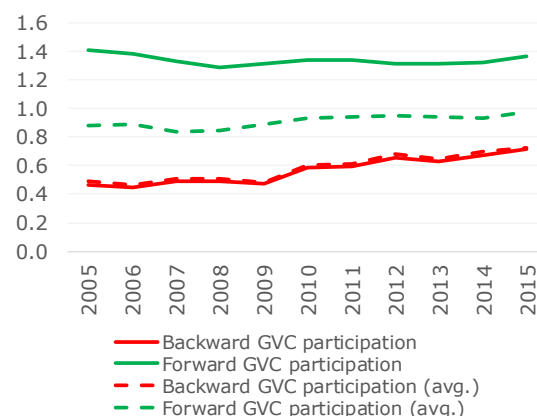


ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain.

Notes: See Box 4.1 for the definition of GVC participation types. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 1995–2003.

Source: OECD (2018).

Figure 4.22: GVC Integration of the EU with ASEAN by Participation Type
(% of EU gross exports)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain.

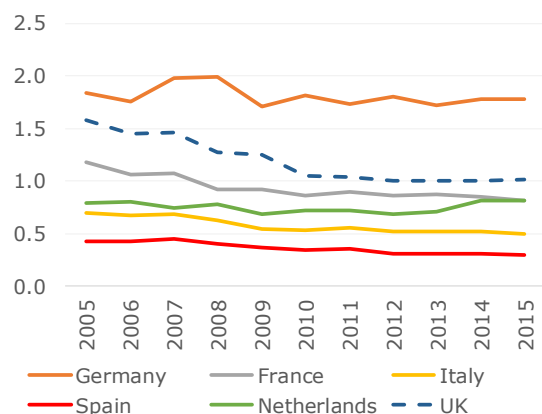
Notes: See Box 4.1 for the definition of GVC participation types. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 1995–2003.

Source: OECD (2018).

By partner, and from the ASEAN perspective, Germany has consolidated its position as the most relevant integration EU counterpart, maintaining relatively stable GVC participation in its exports (Figure 4.23). This contrasts with the declining relevance of other EU countries, such as France, Italy, and Spain – a similar trend to the one described for the UK in the previous section.

On the other hand, the relevance of integration with ASEAN has increased for a number of EU countries since the Great Recession in 2008 (Figure 4.24) – for the Netherlands in particular – while it has remained stable over the whole period for Spain (similar to what was previously noted for the UK). Still, given ASEAN’s economic size and growth perspective, bilateral integration with ASEAN remains generally low.

Figure 4.23: GVC Integration of ASEAN with the UK and the Largest EU Countries
(% of ASEAN gross exports)

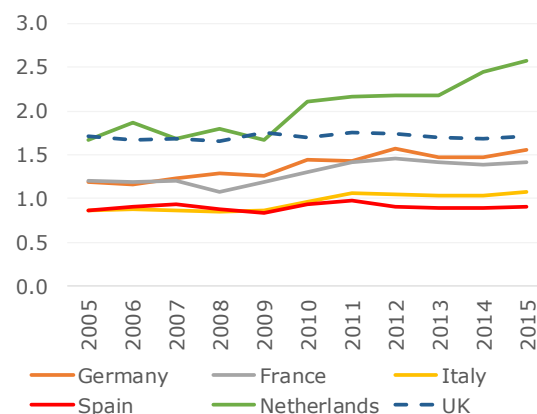


ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain, UK = United Kingdom.

Notes: See Box 4.1 for the definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).

Source: OECD (2018).

Figure 4.24: GVC Integration of the UK and the Largest EU Countries with ASEAN
(% of EU countries/UK gross exports)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain, UK = United Kingdom.

Notes: See Box 4.1 for the definition of GVC participation. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar).

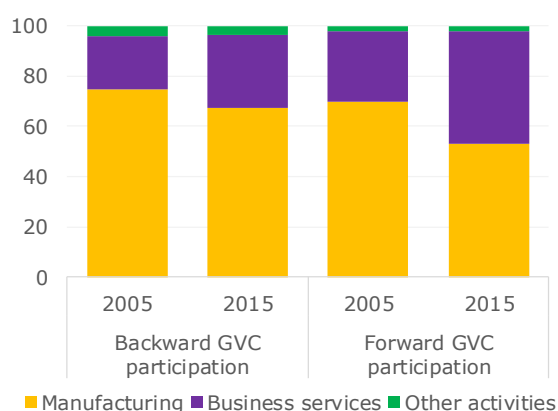
Source: OECD (2018).

In sectoral terms, the bilateral integration of ASEAN with the EU, as concluded in the previous section for the UK, shows both a differentiated nature relative to overall sectoral specialisation patterns, as well as significant changes over time.

At a broad sectoral level (Figure 4.25), in line with global patterns, most of the bilateral integration between ASEAN and the EU is for manufacturing exports. However, the share in both the backward and forward GVC participation of business services has increased over time, and it is not only particularly high when compared to ASEAN specialisation patterns, as was the case for the UK, but also in the opposite direction (i.e. ASEAN inputs used in EU business services exports). ASEAN–EU integration in business services has been driven by information and communication technology (ICT) services in contrast to the leading role of financial and professional services observed for the UK.

Within manufacturing exports, changes over time have been very similar to those of ASEAN–UK integration, with the significant decline in bilateral GVC participation for electronics exports being the most distinctive feature (Figure 4.26), while an opposite trend was observed for machinery and equipment, particularly for the participation of ASEAN supplies in EU exports (ASEAN forward integration).

Figure 4.25: Sectoral Composition of GVC Integration of ASEAN with the EU, by Participation Type and Exporting Sector (%)

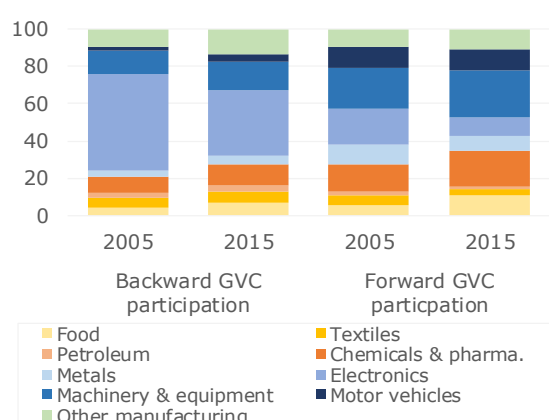


ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain.

Notes: See Box 4.1 for the definition of GVC participation types and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 1995–2003.

Source: OECD (2018).

Figure 4.26: Sectoral Composition of GVC Integration of ASEAN with the EU in Manufacturing, by Participation Type and Exporting Sector (%)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain.

Note: See Box 4.1 for the definition of GVC participation types and sectors. ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 1995–2003.

Source: OECD (2018).

Main takeaways for UK opportunities in ASEAN

The UK, in line with the trend for the EU, but possibly even more so, has so far missed ASEAN as an export market. This is true for final goods but, possibly, to a larger extent for intermediate goods. The latter is particularly important since ASEAN region is becoming increasingly integrated in the global supply chain and in which China is playing an increasingly central role. It may seem difficult for the UK to make great strides on this front for a number of reasons. First, China's positive growth differential with the UK is here to stay, even if China's growth is expected to slow down in the following decade and even more sharply after 2035. Second, China's growing market size and the push to remain relevant in the industrial space with stepped up innovation will make it very hard for ASEAN to turn towards suppliers of intermediate goods other than China. Third, China has stepped up efforts to reduce trade barriers with ASEAN, the best example of which is the Regional Comprehensive Economic Partnership, signed in November 2020. Both the size and improved market access make China hard to beat as regards intermediate goods. Still, the UK has a comparative advantage in services, especially finance and education, which is rather untapped.

Furthermore, in the UK Government's overarching international policy objectives to 2025, an important objective is to establish an open and innovative digital economy, where the UK would strive to remain a global services, digital, and data hub and continue to be one of the world's most open economies. ASEAN, on the other hand, is working towards greater participation in the GVCs of the

new digital economy and increasing its trade in services. The UK could be an important and reliable partner for ASEAN to engage in the value chain of a more digitalised global economy through a spectrum of cooperation in infrastructure, regulatory frameworks, data flow, and security related to services trade.

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Hummels, D., J. Ishii, and K.-M. Yi (2001), 'The Nature and Growth of Vertical Specialization in World Trade', *Journal of International Economics*, 54(1), pp.75–96.

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Chapter 5

Trade Developments following the COVID-19 Outbreak

Chapter 5

Trade Developments following the COVID-19 Outbreak

This chapter maps the developments in international trade in the Association of Southeast Asian Nations (ASEAN) and the United Kingdom (UK) following the coronavirus disease (COVID-19) outbreak in 2020 and compares it with the performance of the European Union (EU) and the global economy during the same period. It provides an overall characterisation and, when possible, disaggregation by type of product for the main trading partners. It focuses on identifying the breaks in trade trends described in the previous two chapters.

Overview

While COVID-19 led to a sharp reduction in global trade, a rebound has been taking place in ASEAN – especially for its exports – driven by China’s fast economic recovery.

As demand from China is the main reason for the resilience of ASEAN exports, the relevance of the UK (and also the EU) as a trading partner may have decreased further, even if only temporarily. In other words, COVID-19 has made the UK’s efforts to increase integration with ASEAN even more difficult – both for goods and services. In fact, lockdowns and quarantine rules have severely affected a good part of the UK’s exports of services, including to ASEAN (from business services to education or tourism). The same is true for ASEAN’s exports of services, in particular tourism.

The UK’s bilateral deficit with ASEAN has been shrinking, which is also the general trend for the EU. On the other hand, the deficit with China has increased even more in 2020 – both for the UK and the EU.

In this context, the UK needs to move fast in taking UK services to ASEAN, especially digital services, at a time of increasing strategic competition between the United States (US) and China. In fact, such competition may offer an advantage for middle – and autonomous – powers, such as the UK, especially as regards digital infrastructure and standards.

Box 5.1: Data Description and Definitions

Trade flows in volume terms are sourced from the CPB Netherlands Bureau for Economic Analysis (2021) World Trade Monitor, which provides seasonally adjusted export and import flows at a monthly frequency for the world; country aggregations (advanced and emerging economies, as well as regions within these groups); and the main global economies considered individually (euro area, the United States (US), Japan, and China).

Data for the Association of Southeast Asian Nations (ASEAN) as an aggregate in volume terms and by individual Member States in nominal US dollars are based on data from the World Trade Organization (2021).

The product and geographical composition of trade flows at a monthly frequency for European Union (EU) member countries correspond to data collected by Eurostat (2021), and the equivalent for the UK is sourced from the Office for National Statistics (2021). Sectoral data for EU countries correspond to the Broad Economic Categories (BEC) classification and for the UK to the Standard International Trade Classification (SITC).

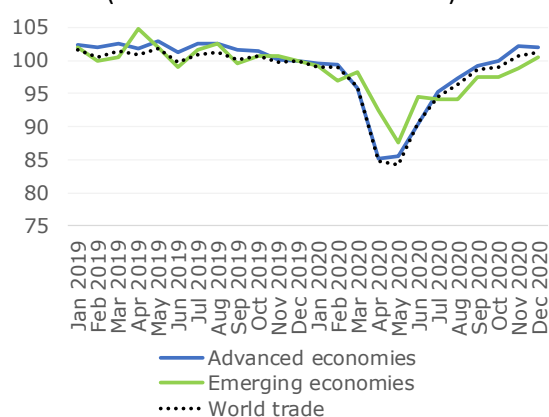
Source: Authors.

Global characterisation

Driven by value chain disruptions, supply shortages, mobility restrictions, and population lockdowns (Baldwin and Freeman, 2020), world trade collapsed by 15% in volume terms between February and April 2020 following the COVID-19 outbreak, and previous levels were only recovered in the last quarter of 2020 (Figures 5.1 and 5.2).

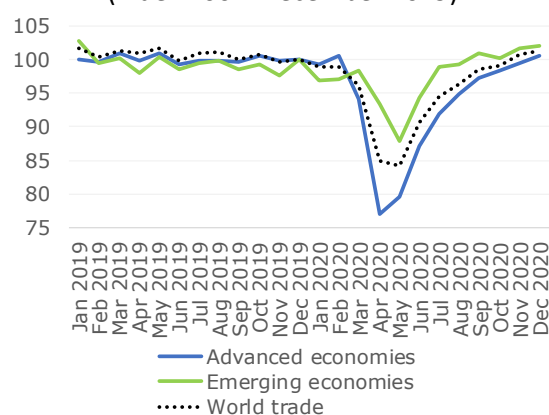
The fall in trade flows was more intense for advanced economies than for emerging economies, reflecting the overall largest impact of the aforementioned driving factors. Value chain disruptions seem to have played a more relevant role for advanced economies, given the much more negative developments on their export side (Figure 5.2).

Figure 5.1: World Trade and Imports by Economic Area
(index 100 = December 2019)



Note: Based on seasonally adjusted volume.
Source: CPB Netherlands Bureau for Economic Policy Analysis (2021).

Figure 5.2: World Trade and Exports by Economic Area
(index 100 = December 2019)



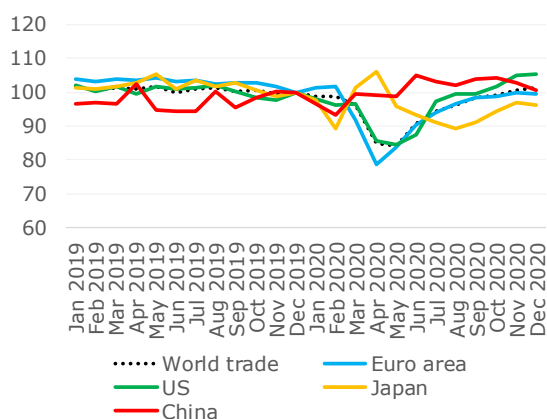
Note: Based on seasonally adjusted volume.
Source: CPB Netherlands Bureau for Economic Policy Analysis (2021).

Within the group of advanced economies, the impact of the COVID-19 outbreak was larger and followed a similar bust–recovery pattern in the euro area and the US (Figures 5.3 and 5.4).

In contrast, imports by Japan jumped in March and April 2020, likely because of supply security reasons, while remaining below pre-outbreak levels during the rest of the year due to weak domestic demand. Exports had a quicker recovery, benefiting from Asian growth.

Finally, trade flows in China declined early in 2020 as a result of factory shutdowns but did not experience a severe downturn afterwards. Exports recovered more strongly, and in December 2020 were almost 10% above the same period of the previous year.

Figure 5.3: World Trade and Imports by Country (index 100 = December 2019)

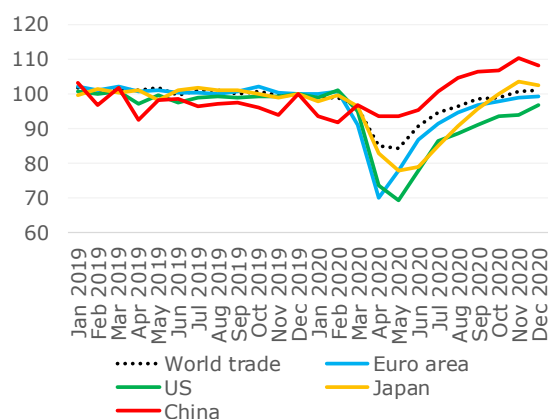


US = United States.

Note: Based on seasonally adjusted volume.

Source: CPB Netherlands Bureau for Economic Policy Analysis (2021).

Figure 5.4: World Trade and Exports by Country (index 100 = December 2019)



US = United States.

Note: Based on seasonally adjusted volume.

Source: CPB Netherlands Bureau for Economic Policy Analysis (2021).

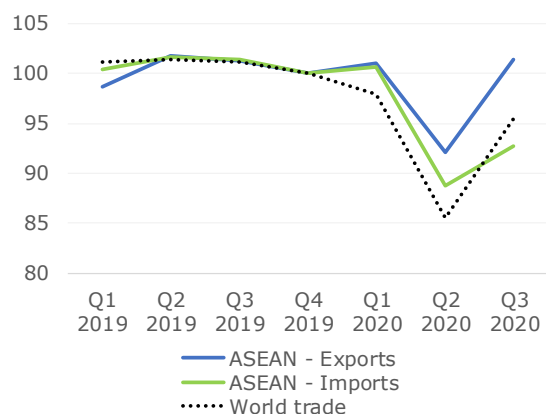
Developments in ASEAN

ASEAN trade flows declined less than in the rest of the world following the COVID-19 outbreak (Figure 5.5), benefiting from stronger integration with China, which, as mentioned in the previous section, was more resilient to the pandemic crisis than advanced economies.

The softer fall in ASEAN trade was particularly visible in the case for exports, which already reached pre-outbreak levels in the third quarter of 2020, while imports had a milder recovery from a more pronounced decline.

By trading partner (Figure 5.6), ASEAN flows with China continued to increase significantly, in contrast with the decline observed for both exports and imports with the EU and the UK (both developed economies), showing stronger integration within the Asian region.

Figure 5.5: World Trade and ASEAN Exports/Imports
(index 100 = December 2019)

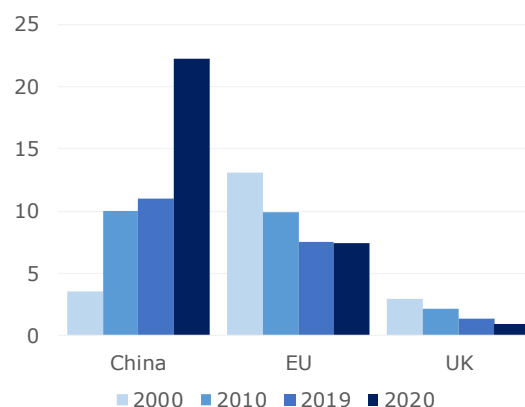


ASEAN = Association of Southeast Asian Nations,
Q = quarter.

Note: Based on seasonally adjusted volume.

Source: World Trade Organization (2021).

Figure 5.6: Share of ASEAN Exports by Trading Partner (%)



ASEAN = Association of Southeast Asian Nations,
EU = European Union, UK = United Kingdom.

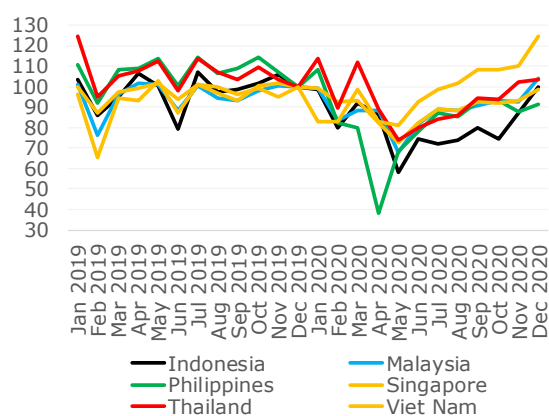
Note: 2020 data for ASEAN exclude Brunei Darussalam, Cambodia, the Lao PDR, and Myanmar.

Sources: China's Ministry of Commerce, Eurostat (2021), and Office for National Statistics (2021).

At the country level within ASEAN, the largest decline in trade from February to April 2020 was observed for the Philippines – a fall of around 50% on both the import and export sides (Figures 5.7 and 5.8). In contrast, the most resilient performance took place in Viet Nam, where disruption from February to April 2020 was milder and the recovery was much stronger, as both export and import flows were 25% above pre-outbreak levels in December 2020.

The rest of the ASEAN Member States for which data are available (Indonesia, Malaysia, Singapore, and Thailand) show a similar pattern, recording an initial fall of around 25% and recovering previous levels by the end of 2020.

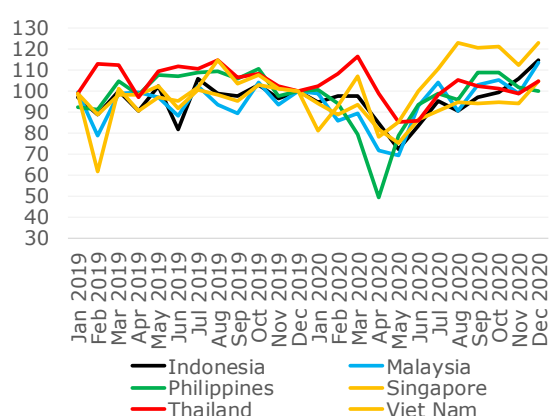
Figure 5.7: Imports by ASEAN Member State
(index 100 = December 2019)



Note: Based on the seasonally adjusted value (\$).

Source: World Trade Organization (2021).

Figure 5.8: Exports by ASEAN Member State
(index 100 = December 2019)



Note: Based on the seasonally adjusted value (\$).

Source: World Trade Organization (2021).

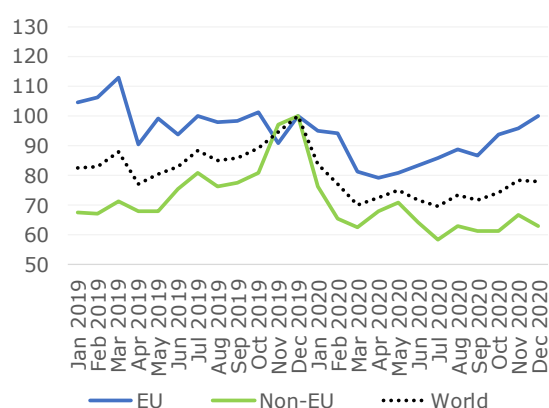
Developments in the UK compared with the EU

UK exports started to decline in January 2020, when Brexit entered into force. This was exacerbated by the COVID-19 outbreak, bringing the decline to 30% in the first quarter of 2020 (Figure 5.9).

By trading partner, the decline in exports to the EU extended the negative trend observed in 2019, although the collapse due to COVID-19 was larger for exports to the aggregate of non-EU countries (almost 40% vs. 20%). More interestingly, in the second half of 2020, exports to the EU recovered strongly while remaining well below pre-outbreak levels during 2020 for exports to non-EU markets.

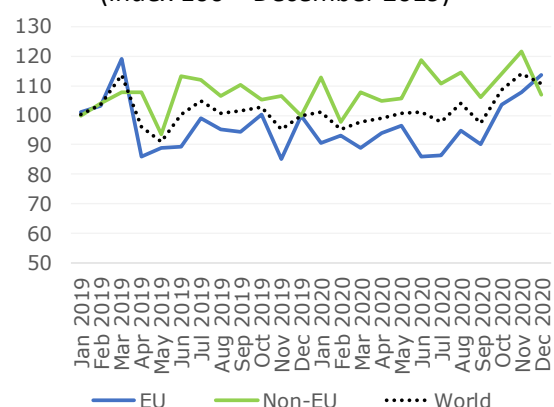
When looking into types of products, exports of semi-manufactures (chemicals, metals, and other intermediate goods) were more resilient than other products to these shocks, and even showed a higher volume in December 2020 than 1 year before (Figure 5.10). In addition, exports of semi-manufactures show a similar evolution by trading partner in contrast with total exports.

Figure 5.9: UK Total Exports by Destination
(index 100 = December 2019)



EU = European Union, UK = United Kingdom.
Notes: Based on seasonally adjusted volume. World is the sum of EU and non-EU countries.
Source: Office for National Statistics (2021).

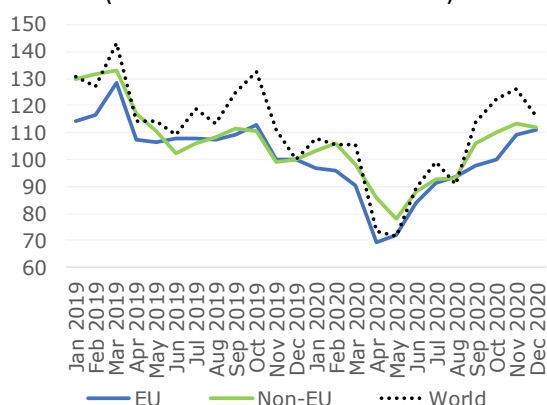
Figure 5.10: UK Exports of Semi-Manufactured Goods by Destination
(index 100 = December 2019)



EU = European Union, UK = United Kingdom.
Notes: Based on seasonally adjusted volume. World is the sum of EU and non-EU countries.
Source: Office for National Statistics (2021).

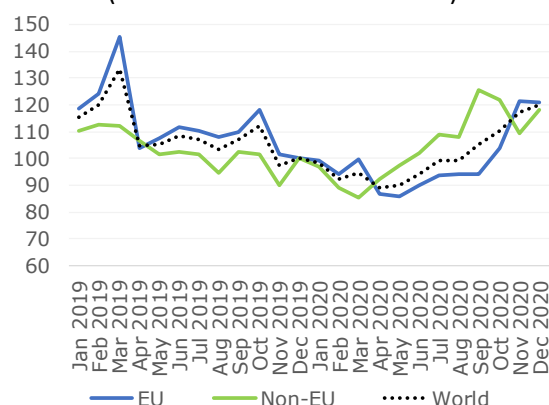
Some relevant features are found when comparing the performance of exports and imports. On the one hand, total imports, for which the COVID-19 outbreak deepened the negative trend shown in 2019, strongly increased in the second half of 2020 along with the progressive recovery of UK domestic demand. On the other hand, the pattern for imports seems more homogeneous both by origin and type of product (Figures 5.11 and 5.12).

Figure 5.11: UK Total Imports by Origin
(index 100 = December 2019)



EU = European Union, UK = United Kingdom.
Notes: Based on seasonally adjusted volume. World is the sum of EU and non-EU countries.
Source: Office for National Statistics (2021).

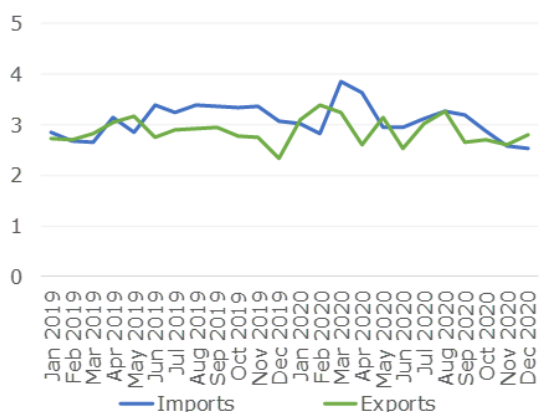
Figure 5.12: UK imports of Semi-Manufactured Goods by Origin
(index 100 = December 2019)



EU = European Union, UK = United Kingdom.
Notes: Based on seasonally adjusted volume. World is the sum of EU and non-EU countries.
Source: Office for National Statistics (2021).

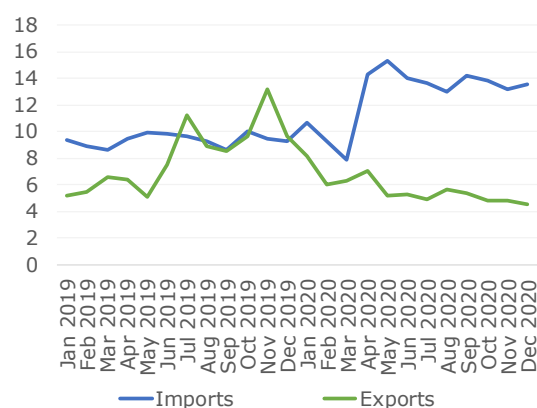
On a bilateral basis, the share of UK trade with ASEAN has remained relatively stable over the last 2 years (Figure 5.13), at around 3% of both total UK exports and imports. On the other hand, the weight of China as an export destination declined considerably in 2020 (to the benefit of the EU share – Figure 5.14 compared with Figure 5.9). In contrast, the opposite happened with imports just after the COVID-19 outbreak, jumping to 12%–15% of total UK imports and increasing the bilateral import dependence.

Figure 5.13: UK Exports/Imports to/from ASEAN as a Share of Total UK Exports/Imports (%)



ASEAN = Association of Southeast Asian Nations, UK = United Kingdom.
Note: Based on seasonally adjusted value terms (\$).
Source: Office for National Statistics (2021).

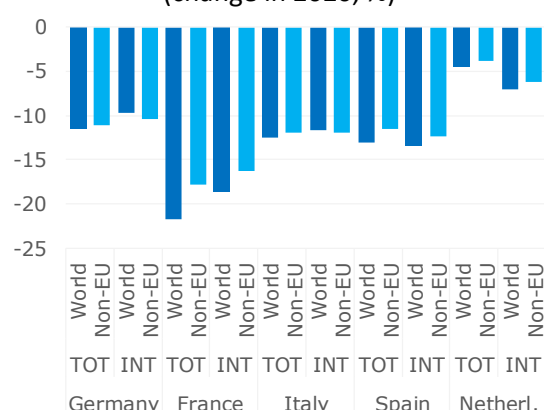
Figure 5.14: UK Exports/Imports to/from China as a Share of Total UK Exports/Imports (%)



UK = United Kingdom.
Note: Based on seasonally adjusted value terms (\$).
Source: Office for National Statistics (2021).

When comparing the trade developments of the UK with those in the EU during the COVID-19 outbreak, trade also declined significantly in 2020 for the largest EU economies (Figures 5.15 and 5.16). That was particularly the case of France (15%–20%), followed by Italy and Spain (10%) and Germany (5%–10%), while the softest contraction was observed for the Netherlands in both exports and imports. The geographical composition of trading partners seems to have played a role in this heterogeneous picture.

Figure 5.15: Exports of EU Countries, by Type of Product and Destination
(change in 2020, %)

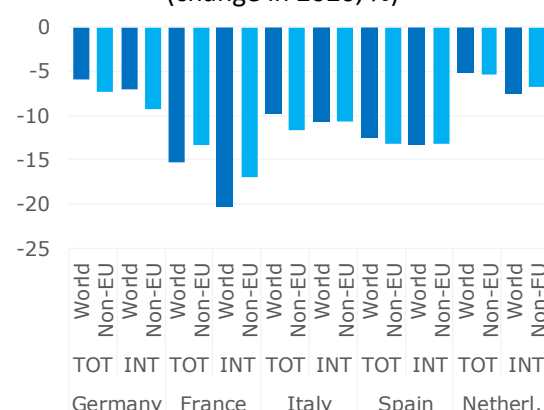


EU = European Union, TOT = total exports, INT = exports of intermediate goods, non-EU = exports to non-EU countries.

Note: Based on seasonally adjusted volume terms.

Source: Eurostat (2021).

Figure 5.16: Imports of EU Countries, by Type of Product and Origin
(change in 2020, %)



EU = European Union, TOT = total exports, INT = exports of intermediate goods, non-EU = exports to non-EU countries.

Note: Based on seasonally adjusted volume terms.

Source: Eurostat (2021).

Strikingly, but in line with the observation for the UK, the decline in exports was larger than for imports. In addition, we observe that while the contraction in exports was larger for total products than intermediates, the fall in intermediate imports was larger than for the aggregate. These developments, although still unclear, could have an interpretation from the value chain perspective.

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Chapter 6

ERIA Survey of Supply Chain Resiliency in ASEAN during COVID-19

Chapter 6

ERIA Survey of Supply Chain Resiliency in ASEAN during COVID-19: Opportunities and Challenges for ASEAN and Trade Partners

This chapter explains the findings of a survey conducted by the Economic Research Institute for ASEAN and East Asia (ERIA) of supply chain mechanisms and trade performance amongst national and international firms in the Association of Southeast Asian Nations (ASEAN) during the coronavirus disease (COVID-19) pandemic in 2020. The survey results and their explanation help in understanding the types of shocks delivered to the ASEAN economy in general, and the subsequent performance and resilience of supply chains across major industries in the region. Data on changes made by firms in customer and supplier relations, their plans for business expansion, and government assistance to the industries will help stakeholders in the United Kingdom (UK) and ASEAN respond to the undergoing changes in business activities and plan for trade and investment facilitation according to regional needs. The prognosis for digitalisation of supply chains can also be sourced from these data.

Overview

ERIA conducted a questionnaire survey in the last quarter (October 2020–January 2021) of 2020 amongst local and foreign companies in ASEAN and India to understand the impact of COVID-19 on corporate activities and supply chains, with the objective of utilising the results for policy recommendations to national governments and international organisations. Some features of the survey results from firms in Singapore, Thailand, and Malaysia are explained in greater detail as these ASEAN economies are most integrated into the international production networks (IPNs). These survey results help improve understanding of the shocks to the supply chains, and general resilience and adaptation of firms' customer- and supplier-side features. The findings are important for ASEAN's trading partners for planning and investing in the post-COVID-19 supply chain structures and markets in the region. They are especially meaningful for the UK as it sets up trade and investment relations independent of the European Union (EU), and looks for new partnerships and markets in Asia.

The initial results of the survey have revealed important insights into firms' business activities, production and supply chain movements, and the likely course of action in 2021 and beyond – particularly for the post-COVID-19 recovery phase. The survey has highlighted the effect of COVID-19 on the participation of micro, small, and medium-sized enterprises in the overall economic activities; and revealed the conditions necessary for their continued participation in the regional supply chains and production networks in the recovery years.

While the results of the survey depict the supply chain activities of national and international firms, including many UK firms located in ASEAN, the findings have an important bearing on the post-COVID-19 economic recovery. Both ASEAN and its partner countries with extensive production networks can draw out the focus areas for policy support to bilateral trade and investment, for deepening the production networks and improving the overall business environment. For new partners such as the UK, the survey findings will supplement their overall plans for deepening bilateral trade and investment with ASEAN, especially for sectoral competitiveness.

Regaining positive growth in 2021

The ERIA survey has also drawn on data from other institutions to forecast that most countries will have negative gross domestic product (GDP) growth in 2020 but will largely regain growth in 2021.

COVID-19 has impacted the surveyed economies differently. Singapore and India are the most affected by COVID-19, followed by Thailand and the Philippines. Since the end of the survey period, India has suffered a second wave of the pandemic – leading to a high number of deaths per million population, which has negatively impacted its economy and infrastructure growth. At the time of finalising this study, many ASEAN Member States (AMS) are also facing a second wave of COVID-19, resulting in further negative impacts on the economy. Malaysia, which introduced severe lockdown measures in 2020, has also witnessed a high number of deaths in the second wave in 2021. Cambodia, the Lao People's Democratic Republic (Lao PDR), and Myanmar fared better in managing the pandemic in 2020, but are now facing the second wave of COVID-19 and are likely to face lower GDP growth in 2021.

The growth matrix (Figure 6.1) was developed from the GDP forecast in GDP Growth in Asia and the Pacific of *Asian Development Outlook* (ADB, 2021) and the COVID-19 data from John Hopkins University (as on 8 June 2021). Since all the surveyed countries will be reporting GDP growth in 2021 from a lower base (due to slow or negative growth in GDP in 2020), India and Singapore have reported high forecasts for 2021 despite their economies being severely affected by COVID-19. High death rates in India, Singapore, and Malaysia (JHU, 2021) may have set back their economic activities but the forecast for growth remains encouraging. Malaysia will be growing from a lower base in 2020, so its forecast is higher than that of other bigger economies in ASEAN such as Indonesia and the Philippines. The smaller economies of Cambodia, the Lao PDR, and Brunei will have medium growth, but Myanmar's growth figure is expected to decrease considerably. The negative growth forecast has been revised further downwards since the military coup in January 2021. Viet Nam is an exception which has managed to both prevent the COVID-19 spread in 2020 and retain high growth in 2021. In sum, the matrix supports the findings of the ERIA survey that economic activities in this region faced initial shocks in 2020 but regained momentum towards growth in 2021.

Figure 6.1: Impact of COVID-19 on GDP Growth in Surveyed Countries (%)

Annual GDP growth rate	High growth (> 5%)	Viet Nam (6.7)		India (11) Singapore (6.0) Malaysia (6.0)
	Medium growth (0% to 5%)	Cambodia (4.0) Lao PDR (4.0) Brunei (2.5)	Thailand (3.0)	Philippines (4.5) Indonesia (4.5)
	Low growth (0% or less)		Myanmar (-9.8)	
		Low no. of cases (0–999)	Medium no. of cases (1,000–4,999)	High no. of cases (5,000+)
Number of COVID-19 cases per million population (as of 8 June 2021)				

COVID-19 = coronavirus disease, GDP = gross domestic product, Lao PDR = Lao People's Democratic Republic.
Sources: COVID-19 cases: JHU (2021), GDP growth: ADB (2021).

Key findings of the survey:

- The COVID-19 impact is likely to promote changes in the supply chain, although the supply chains have shown greater resilience to shocks. In the short term, the resultant effects on supply chains will be somewhat greater than those caused by trade frictions between China and the US.
- Many of the surveyed firms have already implemented customer-side changes. Less changes have been made on the supplier side and in the production location. All changes are likely to be permanent.
- Cost reduction/optimisation is the preferred supply chain measure in response to COVID-19, but not many firms have adopted digitisation.
- About 40% of the **manufacturing** respondents have already implemented or planned to change the production location, but this is mainly due to COVID-19 supply and demand shocks. The US–China trade tensions have a very meagre effect on production location change plans.

Survey design

The survey findings are grouped into three important aspects of firms' operations during COVID-19 in 2020 and the early part of 2021. The firms answered key questions under each of the three sections.

1. Business activity: This section covers firms' responses to the impact of COVID-19 on sales and operating profits, and their business outlook for the next few years. Sales performance and changes in operating profits were found to be a strong indicator of supply chain resilience. Firms reporting negative or reduced business activity in 2020 still maintained a positive or no-change outlook for 2021. Their responses on measures taken to recover from COVID-19 – in terms of customers, suppliers, production location, etc. – are not very different from the firms reporting positive sales and operating profits.

2. Supply chain activity: This section measures the impact of COVID-19 on the demand, supply, and production activities of firms in five important sectors – manufacturing, wholesale and retail, communications and software, transportation, and others. It also analyses changes in customer and supplier relations, and production location, to maintain or expand trade. Key measures undertaken by firms for sustaining and optimising the supply chain during the pandemic are also illustrated in this section.

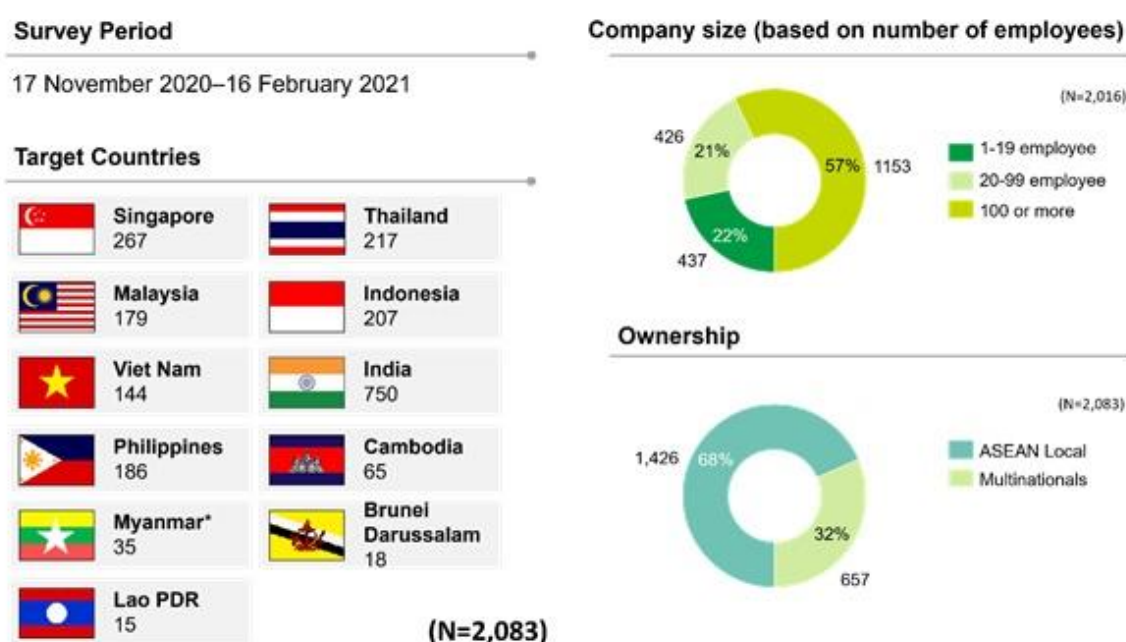
3. Impact of the COVID-19 pandemic: This section covers the status of funding and payment amongst firms during the pandemic. Firms’ expected policy support from the government – in terms of tax benefits, assistance packages, and policies supporting the mobility of goods and people – is reported in this section.

Four categories of questions on the impact of COVID-19 on business activities and supply chains were answered by manufacturing and non-manufacturing companies in ASEAN and India. The first is how significantly COVID-19 affected business performance in the region. This category of questions asks respondents about the effect of COVID-19 on sales and operating profits, and firms’ business outlook in the next few years. The second is how the COVID-19 shocks impacted and are expected to change the regions’ supply chain networks. Third, companies were asked about measures taken to recover from the COVID-19 impact. The fourth category is about the status of government assistance to companies and the support expected from the government.

Company profile and attributes

A total of 2,083 companies in the 10 AMS and India responded to the survey questions (Figures 6.2 and 6.3). Some 57% of the firms (1,153) can be categorised as large firms employing more than 100 persons. Small and medium-sized firms were also evenly represented, at 21% and 22%, respectively.

Figure 6.2: Profile of Surveyed Companies

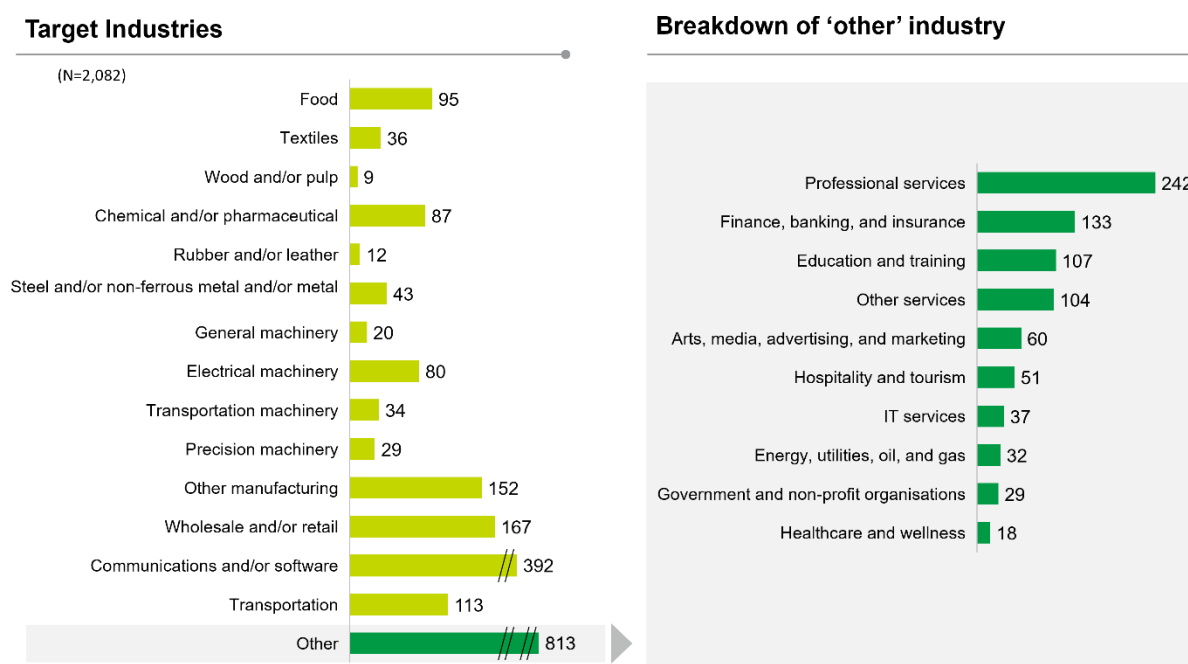


ASEAN = Association of Southeast Asian Nations, Lao PDR = Lao People’s Democratic Republic.

* = Almost all (32 out of 35) the Myanmar respondents answered the questionnaire before the military takeover in February 2021.

Source: ERIA (2021).

Figure 6.3: Profile of Companies by Industry



IT = information technology.

Source: ERIA (2021).

Survey coverage of economic shocks to supply chains

The ASEAN and Indian economies experienced three types of economic shocks caused by the COVID-19 pandemic, as explained in the introductory chapter of this study. The first – negative supply shocks to IPNs or supply chains – was experienced in the early months of the COVID-19 pandemic. The AMS economies experienced and responded to a shortage of intermediate inputs originating in China.

The second – negative demand shocks to the macroeconomy – was caused by the demand shortage brought about by lockdown measures and suppressed economic activities, both in the domestic economy and in the major markets.

The third – positive demand shocks to the goods and services supplied in response to the demands arising from the COVID-19 pandemic – has two aspects. The surge in demand for critical healthcare items led to stressed healthcare supply chains. Social distancing, working from home, and restricted movement of people across borders resulted in a rise in demand for information and communication technology (ICT) equipment and internet-based services. These positive demand shocks are also opportunities for firms to grow now and after the COVID-19 pandemic.

These three types of shocks to the supply chains, and the firms' adaptive features, are captured in the three sections of the survey.

Business activity: Sales, performance, and business outlook

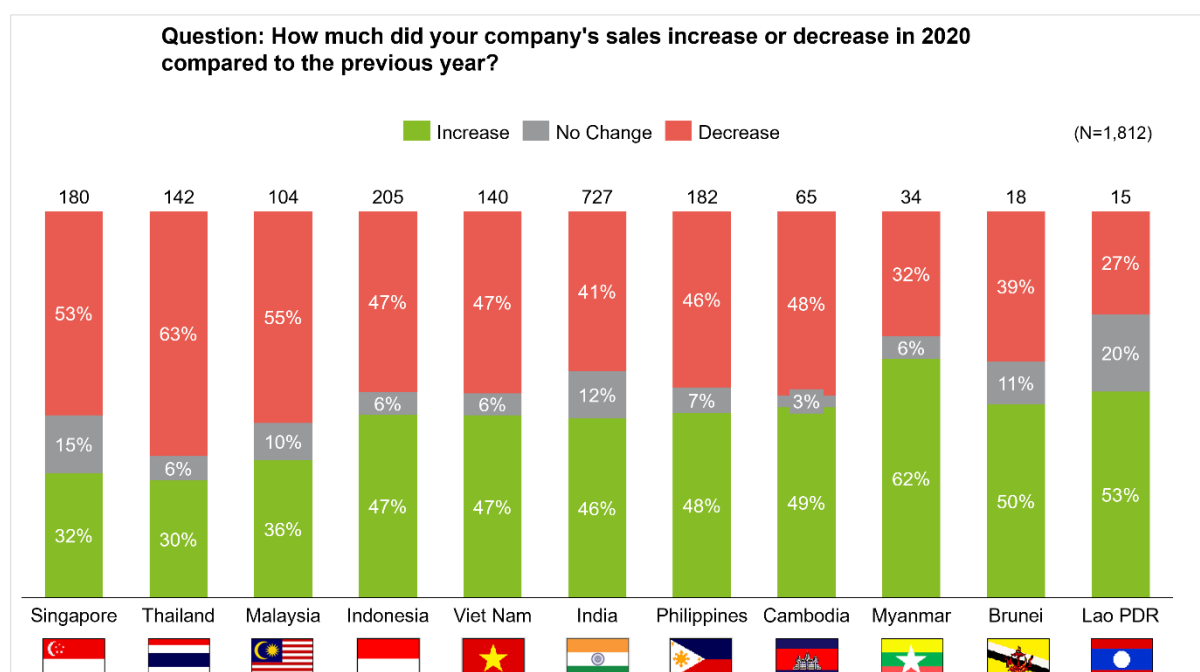
Firms' business activities were surveyed under the broad question head: How significantly did COVID-19 affect business performance in the region? Specific questions asked were: How were the firms' sales, exports, and operating profits growth rates in the first year of the COVID-19 pandemic distributed? How do the firms envisage their business outlook? What attributes of firms affect their

business performance and outlook? Did any specific pattern of the firms' supply chains influence them? A collation of the replies shows that firms' business performance during the pandemic was distributed widely from positive to negative, and the firms that were adaptive to the COVID-19 shock in terms of quickly re-arranging their supply chains were more likely to perform well and have a better outlook for 2021. Moreover, manufacturing and ICT firms tended to show better performance in 2020 than other industries, which suggests that IPNs in the region have been relatively robust to negative supply shocks while positive demand shocks have benefitted ICT services and industries.

Even though most of the surveyed firms were affected by COVID-19, the business outlook remains positive. More than half the companies expect increases in profits and plan to hire more employees in the next few years.

Firms in smaller countries (e.g. Brunei, Myanmar, and the Lao PDR) experienced better sales in 2020 than those in larger economies (e.g. Singapore, Malaysia, and Thailand) (Figure 6.4). Singapore, Malaysia, and Thailand are more mature economies with greater IPN linkages and higher GDP per capita. Their mix of firm type, size, and backward and forward supply chain linkages is more varied than that of the smaller ASEAN economies. The larger economies also faced greater negative supply and negative demand shocks to their supply chains than the smaller AMS. Amongst industry types, manufacturing, ICT, and business services firms showed better performance than the 'other' industry category (Figure 6.5). This is due to the positive demand shocks generated for goods and services unique to COVID-19 measures and needs. Negative demand shocks are seen in the decrease in the sales performance of the retail and wholesale sector.

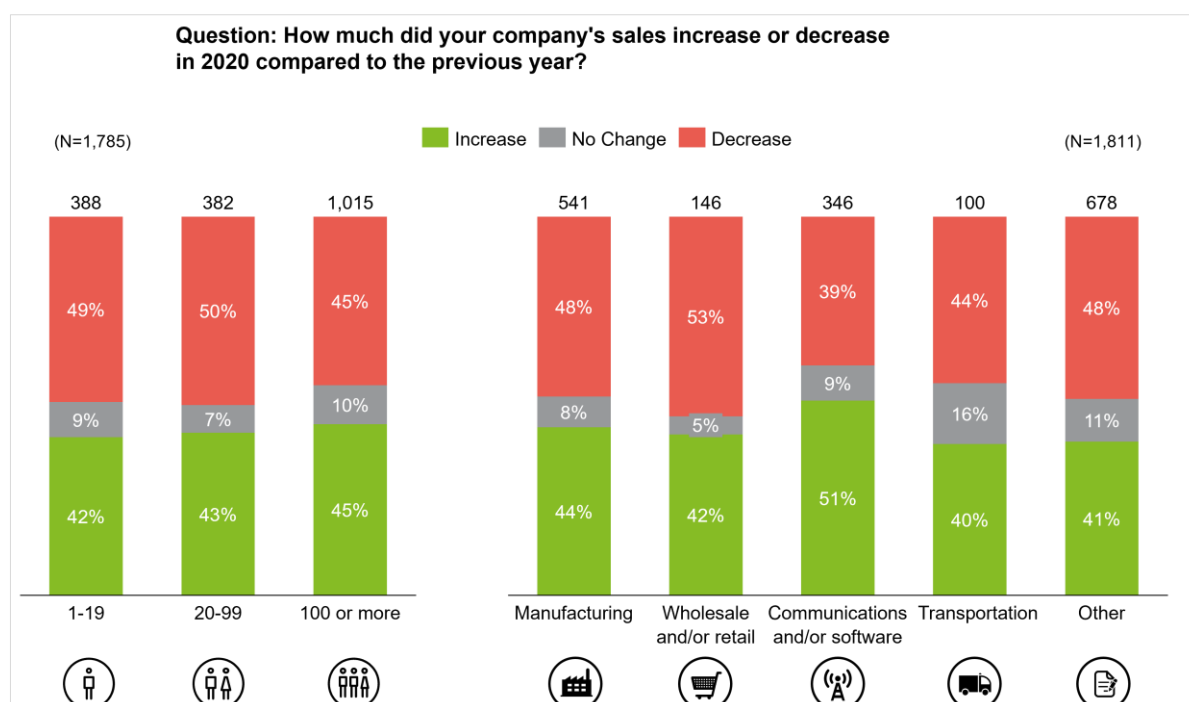
Figure 6.4: Sales Performance of Firms in ASEAN



ASEAN = Association of Southeast Asian Nations, Lao PDR = Lao People's Democratic Republic.

Source: ERIA (2021).

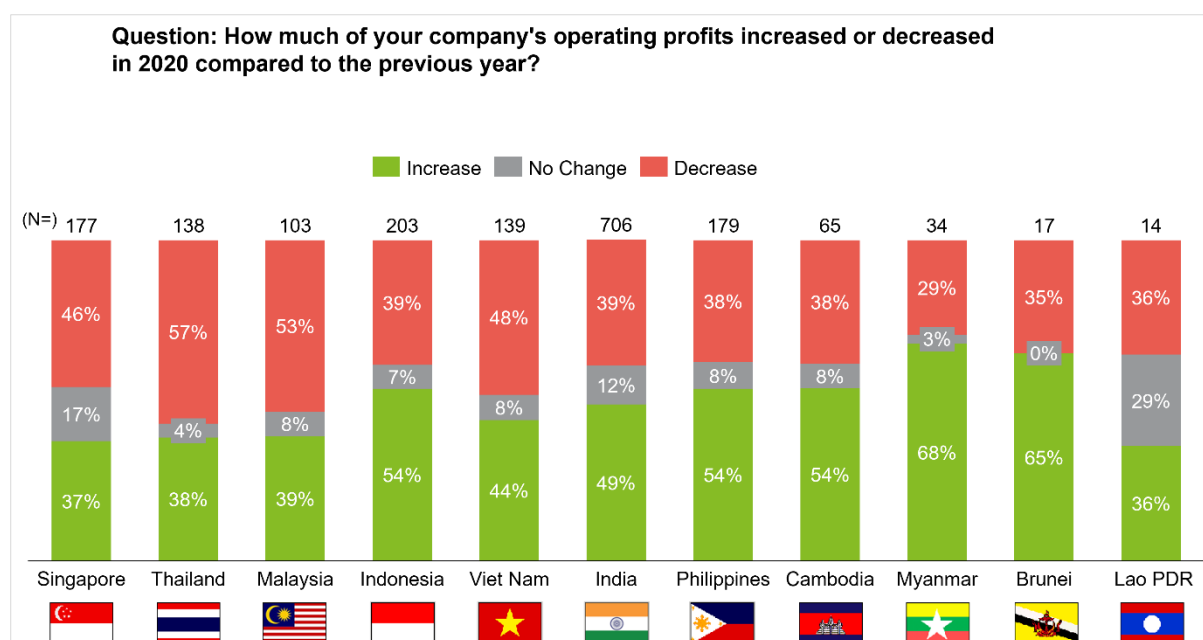
Figure 6.5: Sales Performance, by Company Size and Industry Type



Source: ERIA (2021).

A noteworthy feature of firms in smaller economies in 2020 is the increase in operating profits, when compared with larger ASEAN economies. More than 60% of the respondents in Myanmar and Brunei experienced an increase in operating profits in 2020, while slightly less than 40% of the respondents in Singapore, Thailand, and Malaysia did so (Figure 6.6). Most of the firms reported (except in the Lao PDR) that decreases in profits were due to COVID-19. There is a direct link between improved operating profits and increased sales, as in the case of smaller economies. However, this suggests that when compared with counterparts in larger ASEAN economies, firms in smaller economies were able to manage the overall costs of production better.

Figure 6.6: Change in Operating Profits of Firms in ASEAN, 2020



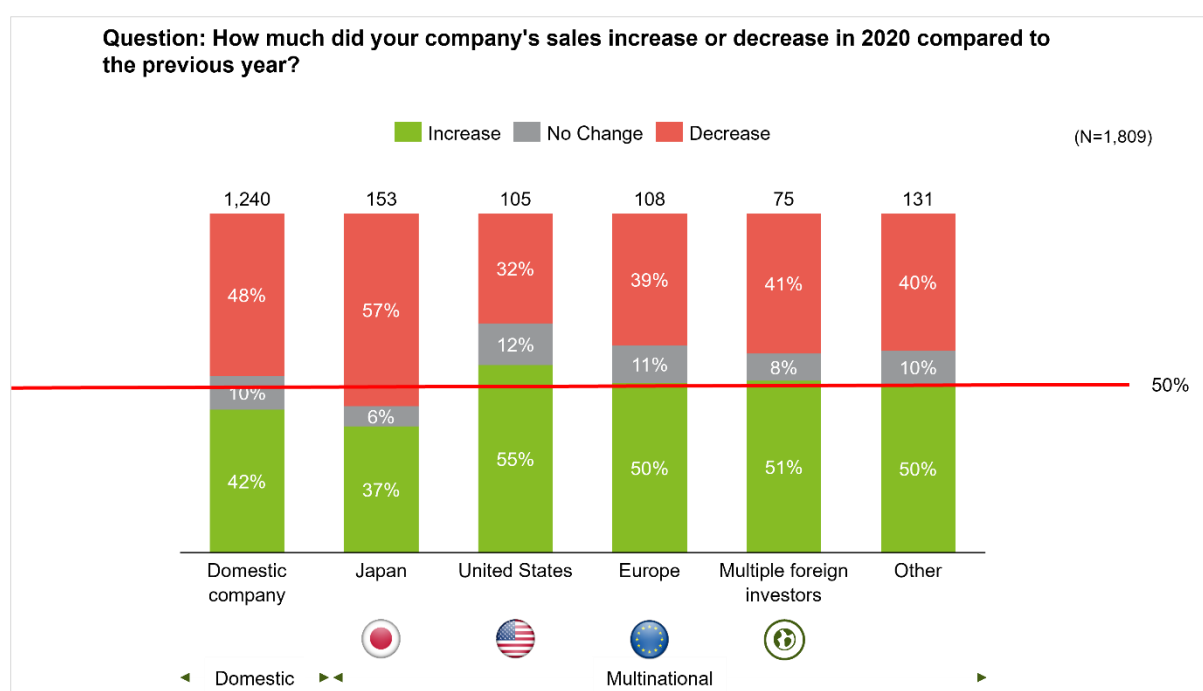
ASEAN = Association of Southeast Asian Nations, Lao PDR = Lao People's Democratic Republic.

Source: ERIA (2021).

The survey results also show that more than half of the foreign-affiliated firms (except for Japan) experienced increased sales in exports in 2020. Comparatively, domestic firms experienced lower sales from exports than foreign-affiliated firms (Figure 6.7).

These results show that COVID-19 has negatively impacted on business performance in the ASEAN region. However, there were significant differences amongst the firms in terms of the vectors of COVID-19 impacts, and the majority of firms have been able to withstand the demand and supply shocks with optimism for business plans in 2021 (Oikawa et al., 2021).

Figure 6.7: Profits Amongst Foreign-Affiliated Firms

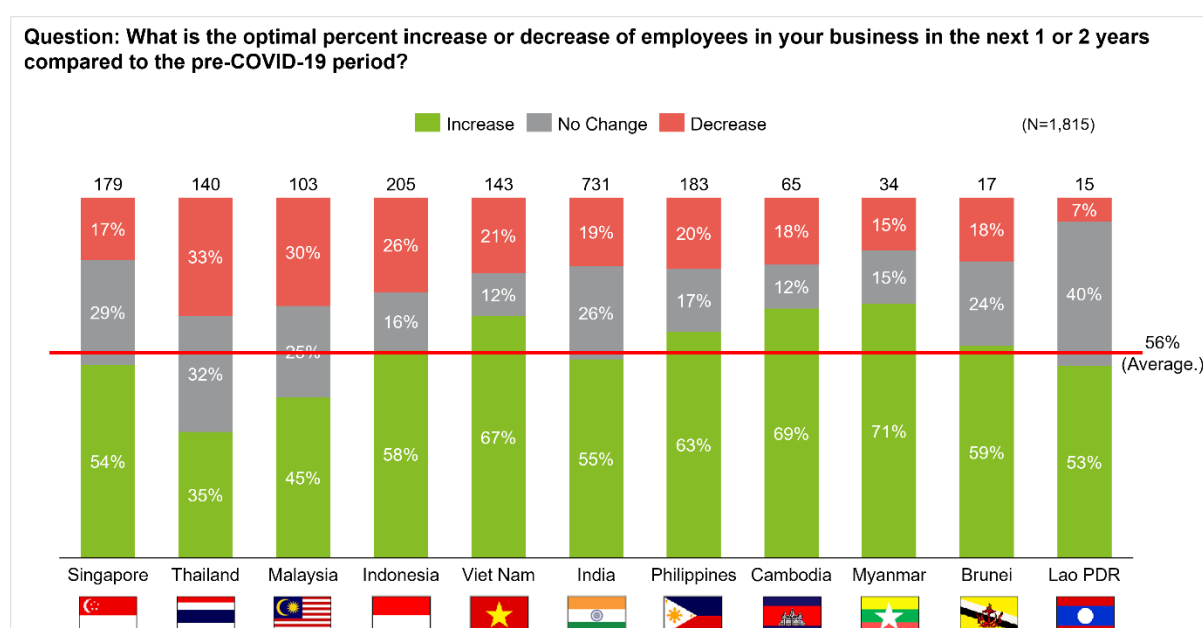


Source: ERIA (2021).

Business plans for 2021 and ahead

As testimony to their performance and resilient outlook, 56% of ASEAN firms reported plans for hiring additional labour in 2021 (Figure 6.8). Some 71% of companies in Myanmar, 69% in Cambodia, 67% in Viet Nam, and 58% in Indonesia plan to increase employment, while only 35% of Thai and 45% of Malaysian companies plan to increase hiring. In keeping with their performance, firms in smaller economies presented a better business outlook for 2021. Firms that broadened supplier arrangements across countries during 2020 are less likely to downsize business and more likely to hire more workers in the next few years. This may, however, still be subject to change due to continued negative demand shocks coming from important markets in the US and the EU. Intra-ASEAN demand for goods and services will be equally important for business plans in the next 2 years.

Figure 6.8: Business Plans of Companies in 2021 and Ahead



COVID-19 = coronavirus disease, Lao PDR = Lao People's Democratic Republic.

Source: ERIA (2021).

Supply chain performance

This section of the survey covers the changes in firms' supply chain activities and measures the respondents' plans (or lack thereof) to change their customer, supplier, or production relationship due to COVID-19. The survey also maps measures such as cost reduction/optimisation and digitisation as a supply chain measure during COVID-19. The broad question for mapping changes in the supply chain activities is: Did the firm's relationship with its customers and suppliers change during 2020? For which reasons? Firms were asked further sub-questions: How did (or would) the firms reconstruct their customer and supplier relationships and production locations in the year of the COVID-19 outbreak? To what degree? Are the changes temporary or in a medium- or long-term perspective? Did the pre-COVID-19 transaction links between customers and suppliers increase, remain the same, or shrink during 2020? For what reason? What elements of transaction links affected the firm's vulnerability to the COVID-19 shocks?

To map the measures related to the supply chains undertaken, the firms were asked to respond to these questions: What kind of measures related to the supply chains did firms take in response to the COVID-19 pandemic? Were there any combinations of different measures against COVID-19 that firms preferred to implement? Were there any differences in the attributes of firms that took different measures against COVID-19?

The survey reveals that many firms restructured their supply chains to a certain extent in response to the COVID-19 shock. Furthermore, most of the supply chain reforms are unlikely to be reversed. Cost reduction is the most common supply chain measure adopted by the firms. It is noteworthy that the least common adopted measure was supply chain digitalisation. Remote operations were not a preferred measure. The firms that implemented supply chain digitalisation tend to have implemented

both supply chain optimisation and remote operations. Large or young firms, or firms with diversified customers across countries, were more likely to implement supply chain digitalisation.

Most companies in all countries experienced changes in supplier relationships due to COVID-19 (Table 1). The majority of the firms changed or planned to change customer or supplier relationships in response to the COVID-19 shock. About 70% of firms have reviewed their customer relationships, and about 60% have already undertaken and/or plan to undertake changes in supplier relationships. The number of surveyed firms that had no plan to change their supplier relationships is somewhat larger, but changes in supplier relationships were identified by firms as a major step in meeting the negative supply shocks as well as meeting production demand. Supplier relationship changes also helped in meeting positive demand shocks in the manufacturing, ICT, and transport sectors.

Table 6.1: When (Row) and to What Degree (Column) Supplier Change Is Made

When?	To What Degree?					Total
	No plan	1%–9%	10%–29%	30%–99%	100%	
No plan	39.0	0.0	0.0	0.0	0.0	39.0
By 2020	0.0	13.8	17.1	9.3	3.8	44.0
2021, 1st half	0.0	4.0	5.5	1.6	0.7	11.8
2021, 2nd half	0.0	0.8	1.5	1.5	0.4	4.1
2022 or beyond	0.0	0.2	0.4	0.4	0.1	1.1
Total	39.0	18.8	24.4	12.9	4.9	100.0

Notes: Survey size – 1,305 firms. Each cell's value stands for the ratio of the number of respondents that reported the corresponding row and column category choices to the grand total. Percentages may not sum 100% due to rounding.

Source: Oikawa et al. (2021).

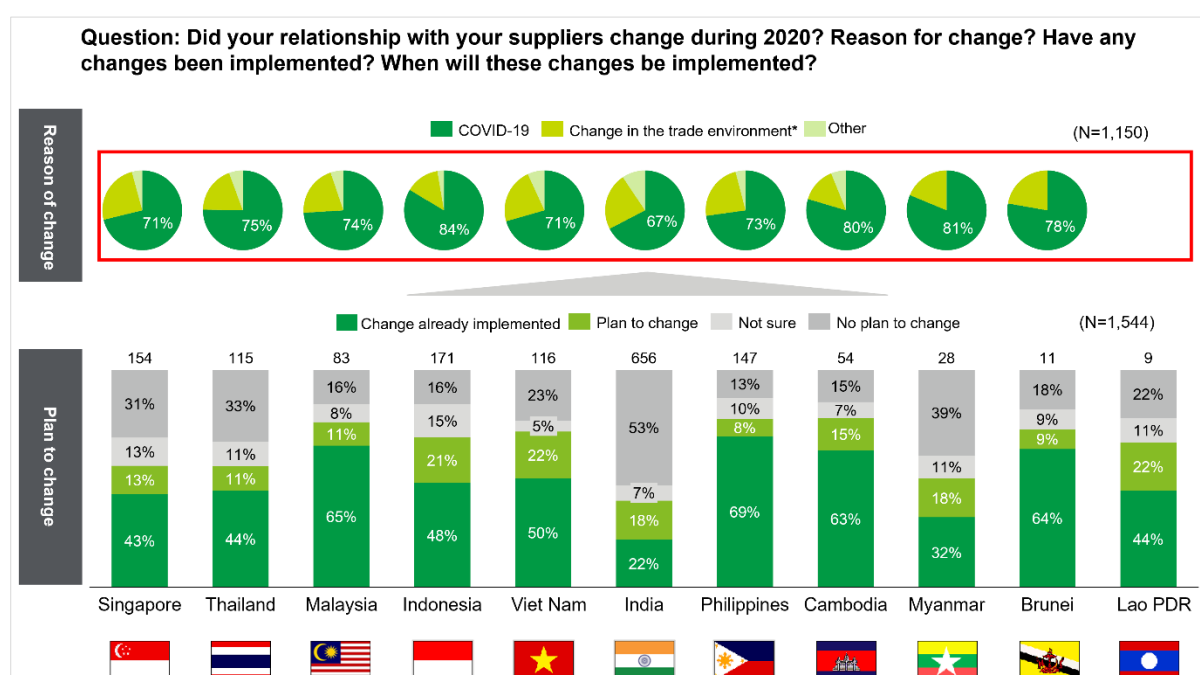
More than half of the firms surveyed in Cambodia, Brunei, and Viet Nam, which are smaller economies, have made changes in their supplier relationships (Figure 6.9). Malaysia and the Philippines stand out as important examples of larger economies where more than 60% of the surveyed firms had to carry out changes in supplier relationships to remedy the negative supply and demand shocks. Malaysia and the Philippines have a large component of domestic suppliers. The survey reveals that the greater the component of domestic suppliers (as in the case of Malaysia, at 70%), the less confidence in sustained supplies in 2021 and afterwards. The top suppliers of most firms in Singapore (77%), Thailand (88%), and Malaysia (95%) are from Asia. However, unlike Singapore and Thailand, which reported positive or stable sentiments about suppliers, the surveyed firms in Malaysia reported a further drop in or suspension of supplies from domestic suppliers (49%) and overseas suppliers (36%) in 2021 and afterwards.

While the surveyed firms in Singapore, Thailand, and Malaysia have indicated general confidence in their top suppliers in ASEAN and East Asia, 44% of Malaysian firms anticipate a suspension of supplies from suppliers located in ASEAN in 2021 and afterwards. Malaysia has largest component of domestic suppliers (70%) amongst all ASEAN economies. In 2020, Malaysia had the most severe restrictions for manufacturing industries amongst AMS. The Malaysian government imposed a movement control order, limiting Malaysian firms' activities except for food and medical equipment firms. A Japan External Trade Organization study (JETRO, 2020) pointed out that Japanese, European, and US firms have reduced their supplies in Malaysia because of the stringent local lockdown measures. The same study also reported that Thailand's delayed customs procedures (due to the work-from-home

requirement for customs officials) have affected international supply chains and would also lead to Thailand's prospective decrease in trade with customers.

Manufacturing firms have remained relatively stable, and only about 40% of them reconstructed or planned to reconstruct their supply chains. Most supply chain rearrangements by firms were implemented during the first year of the pandemic. Most firms have changed or are expected to change their supply chains by 10% or more, but less than 30% in terms of trade or production value. The majority of the firms that rearranged their supply chains, or plan to change, have done this in a medium- or long-term perspective. These findings imply that firms in the ASEAN region responded quickly to the COVID-19 shock and reconstructed their supply chains to a certain degree. Furthermore, many of the changes implemented in supply chains are unlikely to return to the pre-COVID-19 status.

Figure 6.9: Changes Implemented or Planned in Supplier Relationships



COVID-19 = coronavirus disease, Lao PDR = Lao People's Democratic Republic.

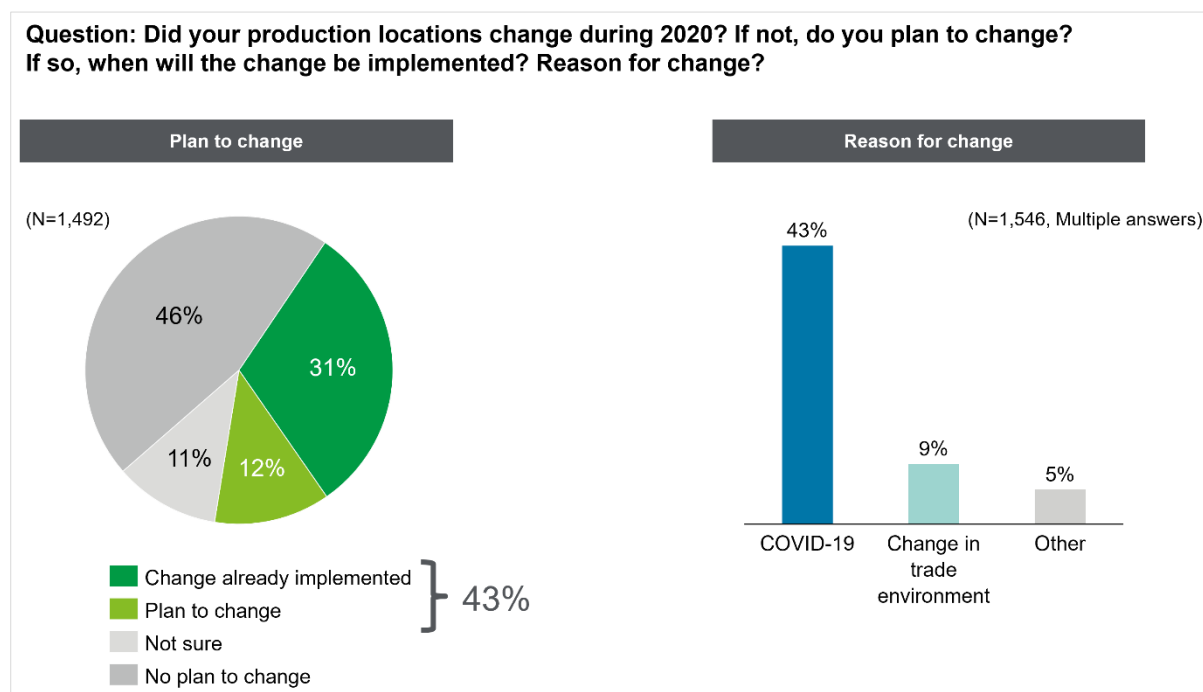
* = e.g. imposition of additional customs duties, US–China trade discord

Source: ERIA (2021).

Changes in production locations were considered by just 43% of surveyed firms that responded to the question on location change (Figure 6.10). The retail and wholesale sector has witnessed more changes in production locations. However, about 40% of the manufacturing companies also responded that they have either already implemented or plan to change production location. Most companies that experienced production location changes answered that the reason was due to the impact of COVID-19. An average of 65% of firms in Malaysia and the Philippines reported changes in production location. Negative supply shocks are the main reason for changes in production location, but fulfilling the positive demand shocks may also be an important reason behind the plans for changes in location, especially for ICT and transportation companies that must meet a surge in demand. So far, the surveyed firms have not accounted for US–China trade frictions and tariff and non-tariff measures as a significant reason for location change. Clearly, businesses are focused on preserving and expanding markets/clients amidst the negative and positive COVID-19 shocks. Changes

in production location only supplement the measures undertaken to keep the supply chains resilient to shocks. It is also noted that firms with less workers are more inclined to change location than larger firms (Figure 6.11).

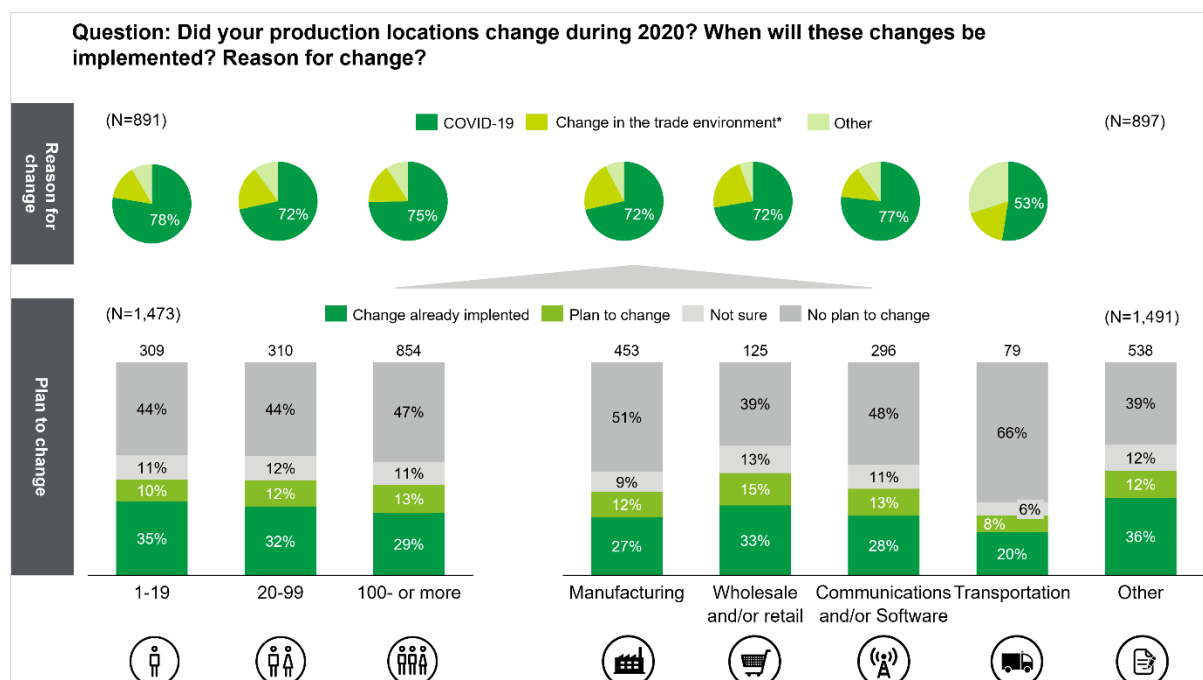
Figure 6.10: Changes Implemented or Planned in Production Location



COVID-19 = coronavirus disease.

Source: ERIA (2021).

Figure 6.11: Change in Production Location, by Industry Size and Type



COVID-19 = coronavirus disease. * = e.g. imposition of additional customs duties, US–China trade discord.

Source: ERIA (2021).

Supply chain measures against COVID-19

The most prevalent supply chain measure in the response to COVID-19 is cost reduction and/or optimisation (Figure 6.12). Some 63% of the respondents adopted this measure. Notably, only 23% of the responding firms adopted supply chain digitalisation (inter-firm digitalisation). Moreover, only about 31% of the respondents adopted remotely manageable operations (intra-firm digitalisation). The firms that implemented supply chain digitalisation tend to have implemented both supply chain optimisation and remote operations. If a firm is large or young, or has internationally diversified customers, it is more likely to adopt the supply chain digitalisation measure. The remote operations measure tends to be taken by firms that are foreign-affiliated or located in countries with a relatively high internet penetration rate.

Rebuilding relationships with customers and suppliers is the next most preferred measure to deal with the COVID-19 shocks. About half of the reporting firms chose the rebuilding customer relationship measure and about one-third of respondents chose the rebuilding supplier relationship measure. It is notable that firms' relationships or transaction links with customers were more flexible to change than with suppliers.

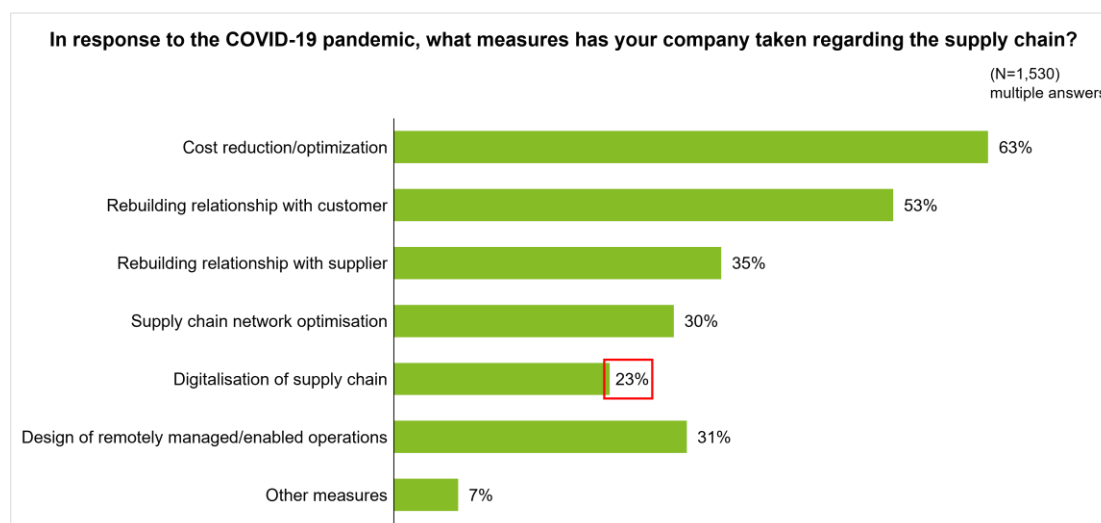
Rebuilding relationships with customers includes changing the way of doing business with customers. This measure includes stopping trading with existing customers/suppliers; starting trading with new ones; and renegotiating financial agreements with distributors and suppliers, e.g. payment terms, changing logistics arrangements, educating customers more intensively, etc.

The supply chain network optimisation measure allows a firm to improve its efficiency in the whole supply chain. However, larger firms employ this measure regularly so it may not be specific to the COVID-19 pandemic.

About two-thirds of respondents reported the cost reduction and/or optimisation measure in response to the COVID-19 pandemic.

Digitalisation and remote management of operations was the least preferred measure amongst the respondent firms. This will have important implications for policy inputs for the digital economy supply chains in the region.

Figure 6.12: Measures Undertaken by Firms to Reduce the COVID-19 Impact



COVID-19 = coronavirus disease.

Source: ERIA (2021).

Impact of COVID-19 and firms' expectations

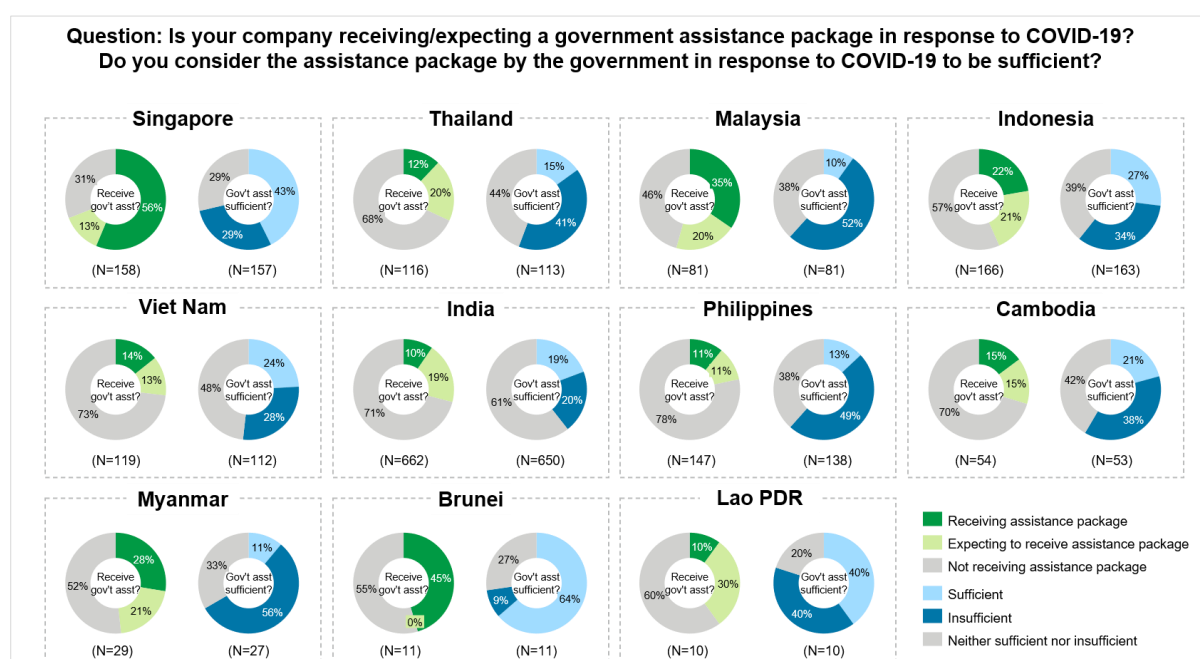
Government assistance to firms varies widely amongst countries in the ASEAN region. Overall, only 18% of firms in the ASEAN region have received assistance while another 17% expected to receive assistance. However, firms in countries like Singapore, Brunei, Myanmar, and Malaysia have received greater government assistance than their counterparts in other AMS (Figure 6.13). Significantly, satisfaction with the assistance is not proportionate to the assistance received. In other words, government assistance and its satisfaction levels vary across the countries, as noted for Malaysia and Myanmar. The results of whether the firms received or were satisfied with government assistance were largely same across firm size and industry type.

Most (58%) of the firms expected to receive tax reduction support from the government in response to the COVID-19 pandemic (Figure 6.14). The second and third preferences for government support were salary support (37%) and acceleration of business people's mobility across countries (32%). Some 61% of Malaysian and 58% of Singaporean firms preferred salary support from the government, while 52% of Thai respondents expected an acceleration in business people's mobility.

Smaller firms chose rent support as the preferred government support, as the rent cost share of a firm tends to be larger when the firm is small. Some 36.2% of manufacturing firms expected the government to accelerate people's mobility across countries, and were less likely than non-manufacturing firms to select wage and rent support as the expected government assistance since manufacturing firms' cost shares of labour compensation and rent are smaller than those of non-manufacturing firms. Manufacturing firms are more capital-intensive and larger than non-manufacturing firms.

Firms' country affiliation caused significant differences in expected government assistance. Foreign-owned/affiliated firms chose business people's mobility as the desired government assistance. In contrast, ASEAN and domestic firms chose other issues, including finance, salary, social security, and rent.

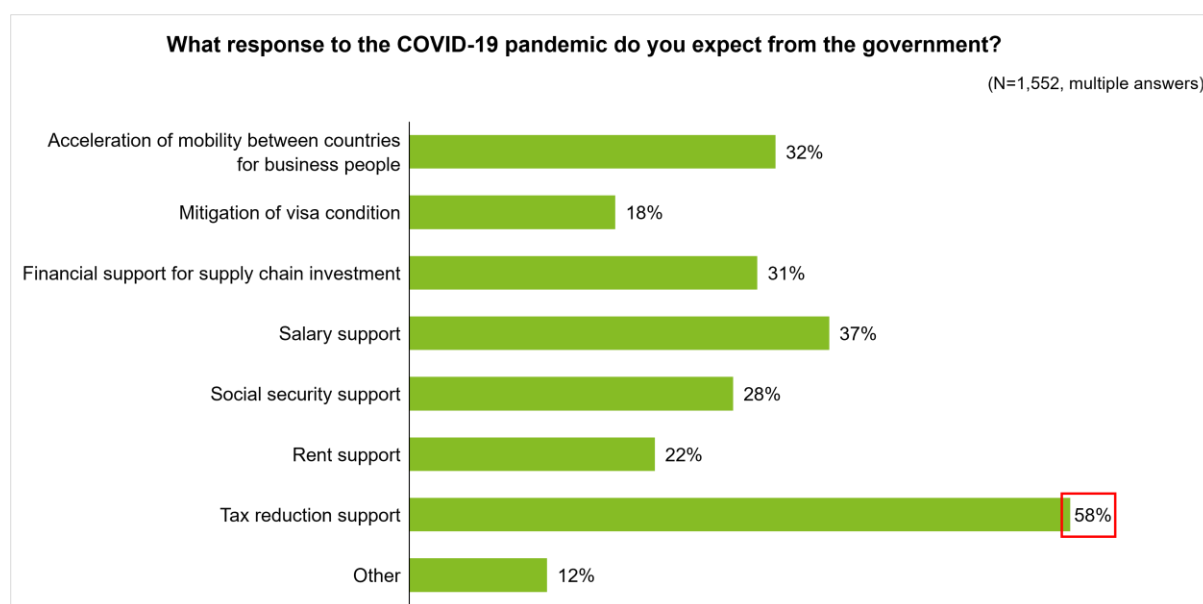
Figure 6.13: Status of Government Assistance and Firms' Satisfaction



COVID-19 = coronavirus disease, Lao PDR = Lao People's Democratic Republic.

Source: ERIA (2021).

Figure 6.14: Support Measures Expected from the Government



COVID-19 = coronavirus disease.

Source: ERIA (2021).

Trade and investment in supply chains in ASEAN in 2021 and beyond

The COVID-19 pandemic significantly impacted manufacturing and non-manufacturing firms in the AMS. While the impact was negative on average, most of the firms were able to quickly adjust trade with their customers and suppliers across countries and globally. Manufacturing firms showed better performance than other industries in 2020, which suggests that IPNs in the region have been relatively robust to negative supply shocks. Additionally, ICT services firms experienced better business outcomes and are more likely to expand their businesses and to hire more than other industries. This suggests that positive demand shocks have benefitted the ICT industry and its growth will continue.

The UK is pursuing an independent trade and investment roadmap for ASEAN and the East Asia region. The better than average performance of ASEAN markets – supported by policy measures such as the Hanoi Plan of Action to keep the market open to trade and investment – can help ASEAN's trading partners, including the UK, to plan and invest in the value chains of production in the region. The changing patterns of customer and supplier relationships amongst the firms in ASEAN present an opportunity for UK businesses to diversify their supply of goods and services and their markets away from the EU to the ASEAN region and the larger East Asia region, with which ASEAN shares a complex supply chain network and market. The increased mutuality between two economies will help both address the negative supply shocks and negative demand shocks. Importantly, for the UK, the positive demand shocks create an opportunity to provide its goods and services in the ASEAN region, which is also working on changes in supplier and customer relationships.

These findings from the ERIA survey of ASEAN firms will be useful for the UK and all the trading partners to better plan and respond to the post-COVID-19 developments and changes in the supply chains and markets in ASEAN and East Asia.

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Chapter 7

Conclusion and Policy Convergence

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A year and half have elapsed since the onset of the pandemic-led economic and health crises. During this time, there has been increasing policy convergence and a more unified regional response to the twin crises. The Hanoi Plan of Action on Strengthening ASEAN Economic Cooperation and Supply Chain Connectivity in Response to the COVID-19 Pandemic was adopted by the Association of Southeast Asian Nations (ASEAN) Heads of State/Government at a Special ASEAN Summit on 14 April 2020. It provided the mandate to implement the ASEAN Economic Ministers' Statement on Strengthening ASEAN's Economic Resilience in Response to the Outbreak of COVID-19, issued on 10 March 2020, and to explore a temporary arrangement to preserve supply chain connectivity during the coronavirus disease (COVID-19) pandemic.

Since then, more policy convergence has been facilitated and response mechanisms have been put in place in ASEAN and other parts of the world. The ASEAN Economic Community, ASEAN's Dialogue Partners, and international organisations have worked together to understand and respond to the twin crises over the past months. While the crises have not abated in Southeast Asia, or globally, several policy responses and business activities reaffirm the value of international cooperation and bring into focus the underlying strength of a partnership between the United Kingdom (UK) and ASEAN that would make the supply chains in ASEAN more resilient to the twin crises, deepen UK–ASEAN trade relations, and bring the UK–ASEAN partnership into relief in the emerging economic architecture of the Indo-Pacific.

The promise of building back better should be at the core of UK–ASEAN policy engagement in the months ahead, while the ASEAN Economic Community would be the UK's natural partner in the regional architecture. The ASEAN Economic Community Vision 2025, the Master Plan on ASEAN Connectivity 2025, and the ASEAN Outlook on the Indo-Pacific would guide the implementation of the UK's objectives of expanding and deepening its trade relations in ASEAN and the Indo-Pacific. All the important economies of Southeast and East Asia (China, Japan, the Republic of Korea, Australia, New Zealand, and India) have several decades of ASEAN+1 processes in place. The United States (US) and Russia have also followed the Asian countries in greater engagement with ASEAN and East Asia since 2010. The UK will be able to bring unique policy convergence to this region through its trade in goods and services, and its core strengths in education, research, medicine, health equipment, digital technology, and low-carbon and green technology, amongst others. ASEAN would bring a reciprocal strength in manufacturing, infrastructure, agro-food, e-commerce, and new start-ups in the digital economy.

The sectoral composition of trade flows between the UK and ASEAN has remained relatively stable in the last decade. On a bilateral basis, there are deviations in the sectoral composition of UK exports to ASEAN, but the sectoral structure is more heterogeneous for UK imports across AMS partners, reflecting to a large extent the product specialisation of each ASEAN economy. The chapters on trade flow and trade integration between the UK and ASEAN establish that ASEAN is already a manufacturing hub, and closer trade relations with ASEAN would improve the integration of the UK in the global value chains (GVCs) outside the European Union (EU), in particular that of Asia. However,

GVCs are partial to efficiency. Product/sector matching can be achieved only through supply chain efficiencies and market demand. A case in point is the reduction of petroleum exports to ASEAN. The removal of infrastructure bottlenecks in the gulf coast countries reduced their cost of production when compared with the UK and the EU (US Energy Information Administration, 2014). This has increased US' petroleum exports to ASEAN, especially to the large consumers such as Indonesia and Malaysia.

On a structural basis, the GVC integration of ASEAN with other economies predominantly corresponds to backward participation, especially with the US and Japan. The nature of bilateral integration has changed over time, positioning ASEAN more upstream with respect to the EU and downstream with respect to China, accounting for a larger participation of Chinese inputs in ASEAN exports. GVC integration between ASEAN and the UK is asymmetrical in both its characterisation and evolution. Backward participation accounts for the largest share for ASEAN, while forward participation contributes more for the UK – emphasising its input export specialisation. From a country perspective, the most significant bilateral integration is with Singapore. For the rest of the AMS, it has remained relatively limited, particularly for commodity exporting countries such as Brunei Darussalam, Cambodia, and Indonesia.

The current basket of traded goods between the UK and ASEAN, however, can be expanded if the future needs of the region are taken into account. ASEAN is preparing to play a larger role in the value chains of the new digital economy. It is also committed to a growth model that is sustainable and inclusive. The UK's competitiveness in the digital economy, services components of goods trade, research and development, financial services, and low-carbon and green products is an important channel for integrating the UK economy into supply chains in ASEAN and East Asia. An important consideration in this roadmap would lie in the accession to the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). The Regional Comprehensive Economic Partnership (RCEP), although equipped with a provision for accession, may prove to be too regional and not deep enough to accommodate the UK's strength in the services sector. More immediately, trade agreements with Japan and Australia are important milestones for the UK. India would be an important addition too. Given the economic and institutional diversity within ASEAN, bilateral trade agreements with individual ASEAN Member States would be a better strategy in the near term. Viet Nam's free trade agreement (FTA) with the EU is a good example of mutual economic benefit. In the period leading to the EU–Viet Nam FTA entry into force in July 2020, Viet Nam replaced Thailand as ASEAN's largest exporter to the EU. This trade will likely increase further with zero duties on 99% of traded goods. The EU–Singapore FTA is similarly designed and complements the services economy on both sides.

Supply chains in ASEAN are likely to remain intact in the post-COVID-19 period. It is still too early to say to what extent GVC integration has been affected by the COVID-19 pandemic, as rigorous data will only be released after a delay of some years (Shepherd and Prakash, 2021). However, the available trade data show that there has been a major drop in trade, particularly in services requiring personal contact. It is still unclear why the recovery is happening at radically different rates in different countries. The survey of domestic and international firms in ASEAN and India, led by the Economic Research Institute for ASEAN and East Asia (ERIA), largely confirms that supply chains have been impacted to some degree across the sectors, but the business outlook amongst firms remains cautiously optimistic.

The ASEAN region has shown, so far, that supply chains have been fairly able to withstand the supply and demand shocks. From a supply chain integration standpoint, technology (digital, robotics, and automation) has the potential to move production closer to the location of final consumption, but existing production locations are still preferred. The pandemic experience will likely lead to a reassessment of the risks associated with dispersed production and just-in-time management practices, but anecdotal evidence and surveys suggest that businesses resolved those problems rapidly and retooled to meet increased short-term demand for pandemic-related products. The implications of the pandemic are more macroeconomic in nature, with some difference across sectors (Shepherd and Prakash, 2021). So far, Southeast Asia has shown that it is particularly well placed to take advantage of improved global demand later in 2021, as this region has seen fewer and shorter restrictions to economic activity than other parts of the world, in particular Europe and the US. However, in the case of a prolonged pandemic, gaps in health services, non-availability of vaccines, lack of social security mechanisms, social distancing measures, and restricted mobility of people across borders may still cause lasting damage to economic activities.

Trade and investment policies will assume more significance in the coming months as they determine the ability of firms to contest foreign markets or to source intermediate inputs from foreign suppliers. For the UK and ASEAN, trade and investment facilitation would be crucial as it can increase backward and forward linkages and deepen trade integration. Nurturing the business environment would also play a role in structuring the trade relations.

A UK–ASEAN trade and economic cooperation plan must consider China. In 2019, China became ASEAN’s largest trading partner (surpassing intra-ASEAN trade) and is now the fifth largest investor in the region. Closely integrated value chains between China and ASEAN cast a shadow on some trade and investment partnerships with ASEAN, e.g. with Japan, the EU, and most noticeably with India. The negotiations for trade in goods in RCEP reflected these concerns at several points before the conclusion of the FTA. It is also an important reason why India stayed out from the conclusion of RCEP. The emerging economic architecture in the Indo-Pacific, in which ASEAN has a central role, would also face the inevitability of supply chain integration between ASEAN and China. As the Indo-Pacific looks towards diversified supply chains in the region, it underlines the recommendation that the UK prepare for integration in the value chains of the digital economy in ASEAN, as there is both the scope and immediate need for efficient and trusted partners. Value chains of the green economy, high-tech production, research and development, and financial markets are other strong prospects. Investments in infrastructure for the digital economy and cybersecurity are the two most pressing needs in the region for it to grow as a digital economy hub. The UK should be ready and able to fulfil both the capacity needs and trust issues required in this industry. On a similar note, new supply chains emerging in the region – such as Australia–Japan–India, the Mekong Subregion, and India–Myanmar–Thailand – will function via ASEAN. Keeping the UK’s interest alive in these emerging activities will be important.

The UK and ASEAN are some of the most open markets for both trade and investment. Regulatory coherence and mutual recognition would not be painful to negotiate. Preferential trade and investment arrangements and regulatory connectivity focusing on identified core sectors will be better than wide-ranging FTAs. Concessions in the mobility of people and capital should be favourable in all plans, given that most regional trade arrangements have nearly by-passed these issues due to their emphasis on trade and tariffs, and less than meaningful services components. While trade facilitation can increase backward and forward linkages, negotiating investments will be important as

restrictive regulatory regimes governing foreign direct investment are associated with a lower degree of GVC integration, especially backward GVC participation (Shepherd and Prakash, 2021).

Reviving the UK's historical presence in the businesses of Southeast Asia through contemporary and future-ready cooperation plans – and promoting ASEAN's core competency in manufacturing in the UK – is the foreseeable and practical direction ahead for the UK–ASEAN partnership.

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