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Keynote Presentation #3
Global Supply Chains under Geopolitical Tensions:
a View from East Asia

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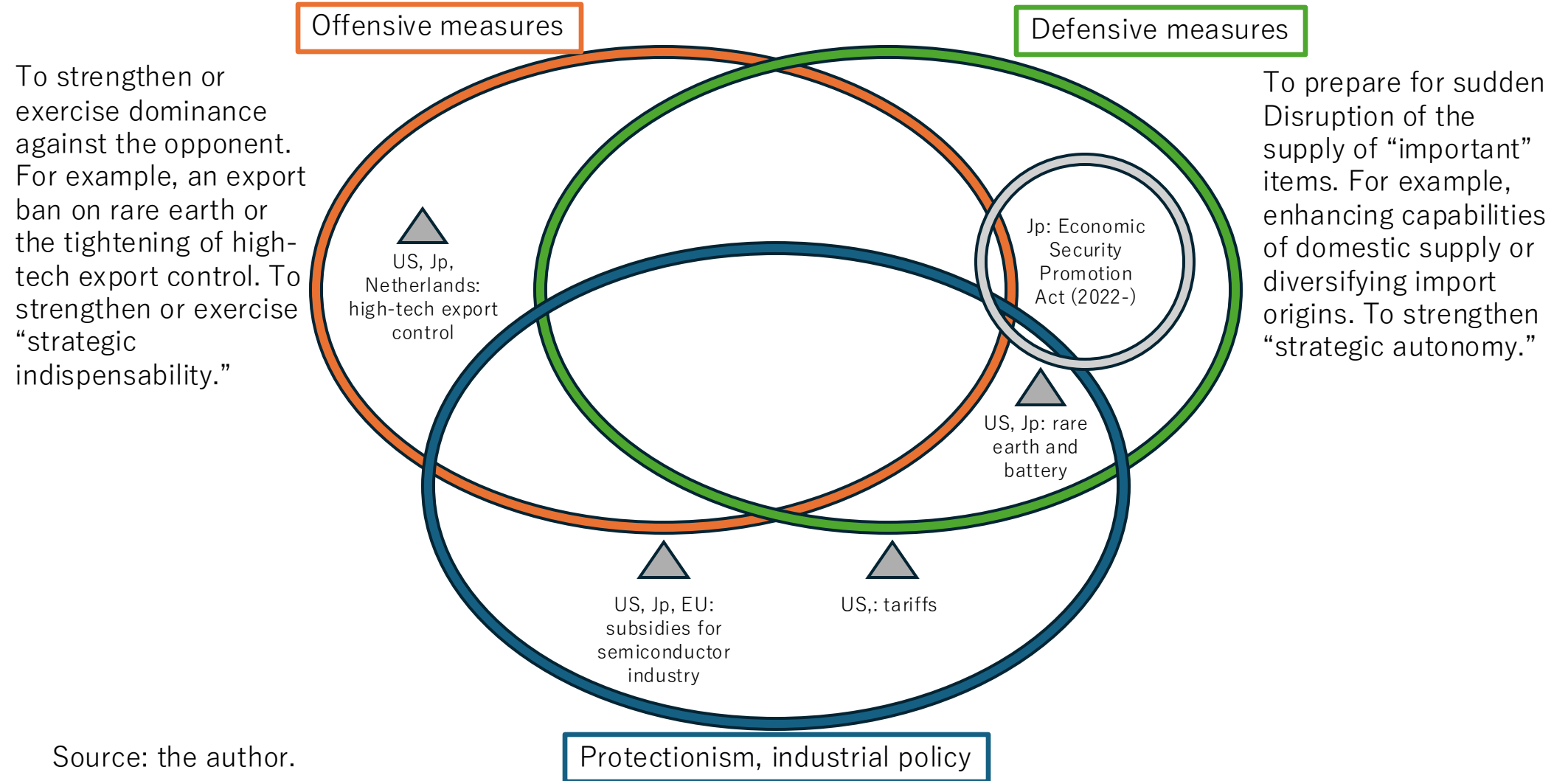
1. The US-China confrontation and the third countries

- Policy debates in Tokyo and Washington, DC have been predominated by national security arguments.
- However, the responses by the third countries are of variety; some of them such as ASEAN Member States (AMS) try to keep “proactive neutrality.”
 - Neither the US nor China may be able to force them to choose a side.
- If the whole world will not be divided into two at the end, vigorous economic activities must be retained as widely as possible.
 - Many newly developed and developing countries would like to grow with utilizing globalization.
 - Some respect for the trade norm still exist in most of the countries.

2. Policy measures in the US-China confrontation

- Major policy measures on the US side
 - 2018-: Tariff war
 - 2020-: Tightening of high-tech export control
 - 2022-: Import ban on forced labor products
 - Sept. 27, 2024?-: Raising tariffs on imports from China (EVs, semiconductors, medical products, iron and steel) to protect domestic industries.
 - A series of industrial policy.
 - More may come after the US presidential election.
- Countermeasures on the Chinese side
- Logic behind for each geopolitical tension-related policy is confusing, often simply summarized as “national security reasons.”
 - Three elements: offensive measures, defensive measures, industrial policy
- National security claim is stronger than economic argument in policy discussion.
- Policy uncertainties are enhanced.
- The rules-based trading regime is weakened.

Three elements in geopolitical tension-related policies: an illustration

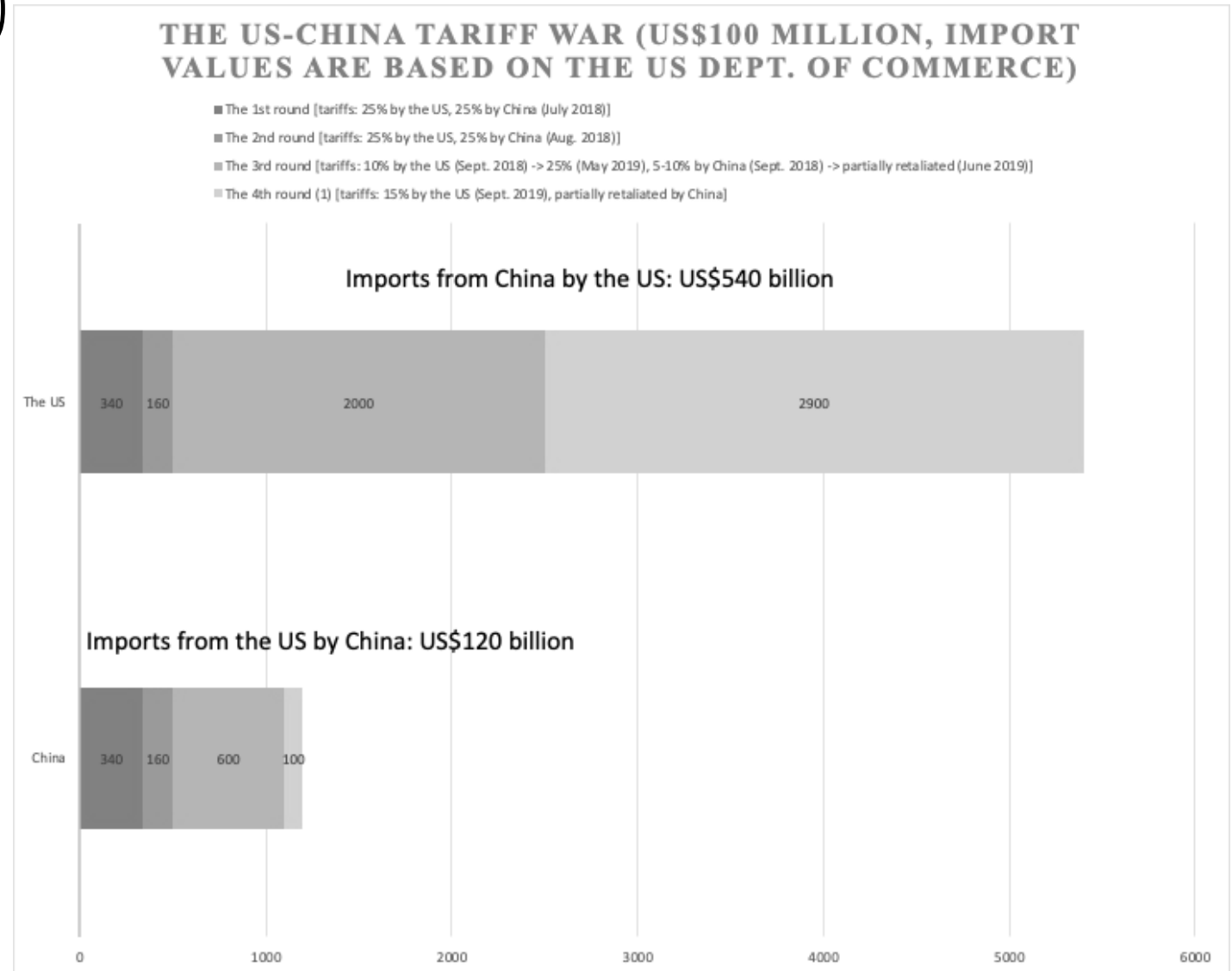


Source: the author.

3. Economic effects of GT-related policies

(1) Tariff war 1.0

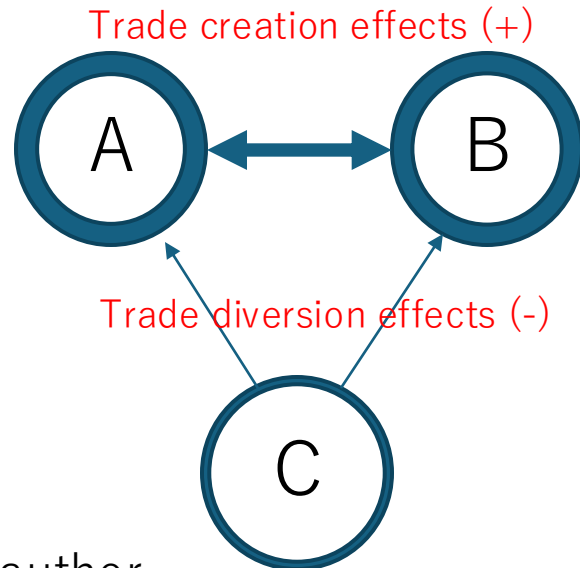
- Starting from July 2018, the US and China imposed additional bilateral tariffs reciprocally in four rounds.
 - Tariffs were imposed on virtually all items at the end.
- Most of the tariffs remain with some minor changes.



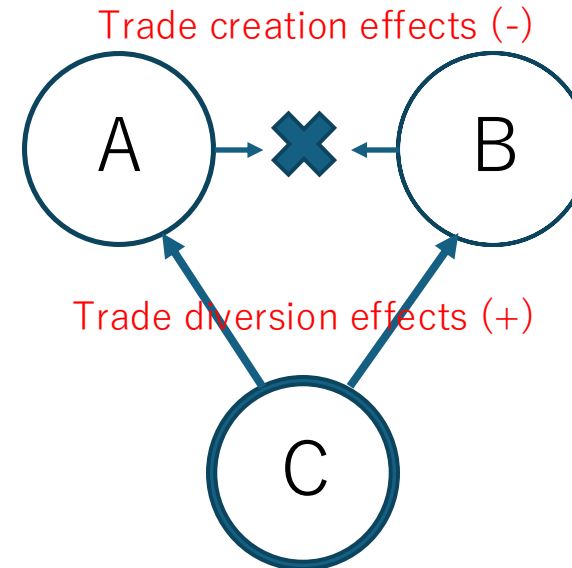
Sources: Various info. sources.

A free trade agreement and a tariff war: economic effects on the third country

(a) Free trade agreement



(b) Tariff war

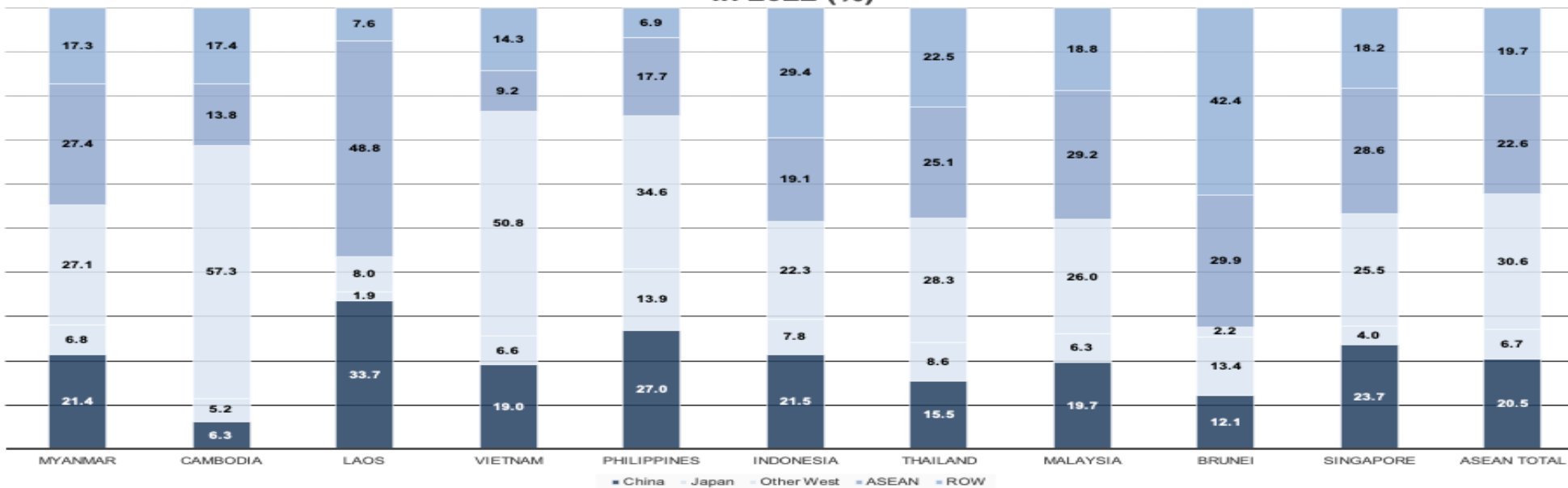


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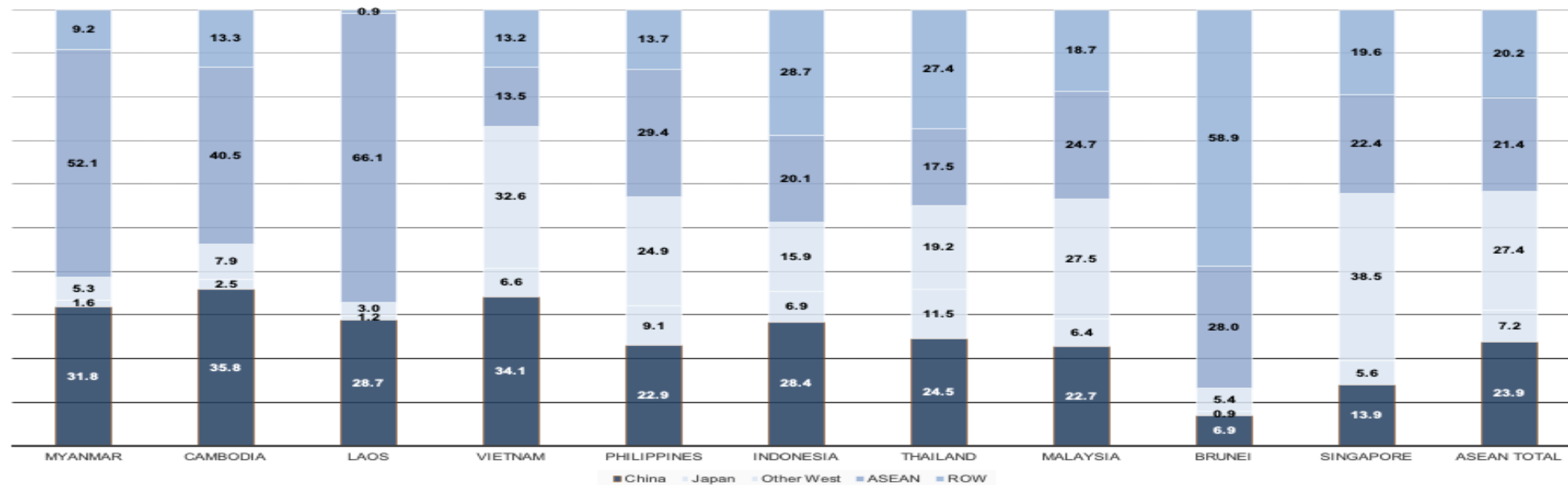
- Economic effects of tariff war is equivalent to those of a “negative” free trade agreement (FTA).
 - Trade creation effects: big negative between country A and country B, some negative spillovers to country C.
 - Trade diversion effects: possibly positive for country C
- With foreign direct investment (FDI), “investment diversion” would also occur.

- A series of empirical studies present that positive trade diversion effects benefit some third countries including Taiwan, Mexico, the EU, and Vietnam.
 - e.g., Nicita (2019); Fajgelbaum et al. (2024).
- Tariff pass-through on the US side is high; tariffs are borne by the US consumers (Mr. Trump: “I’m a tariff man!”).
 - However, due to a large domestic economy and some trade diversion, the US consumers do not feel the cost much….
- Kumagai, et al. (2023) conduct a simulation analysis with the Geographical Simulation Model and show that the East-West decoupling may generate positive trade diversion effects on some neutral countries such as ASEAN Member States (AMS).
 - Assuming that neutral countries can continue normal businesses.

Shares in merchandise exports (FOB) of ASEAN Member States by Trading Partners in 2022 (%)



Shares in merchandise imports (CIF) of ASEAN Member States by Trading Partners in 2022 (%)



Notes: China includes Hong Kong and Macao. Other West consists of the US, EU, Korea, and Taiwan.
Data Source: IMF, Division of Trade Statistics (DOTS)

Further tariff war?

- Tariffs are likely to be utilized more extensively in the context of the US-China confrontation in the coming years.
- As is seen in the current plan of introducing further tariffs by the US, items with higher tariffs seem to be concentrated in industries that lose international competitiveness, which means that such tariffs may likely stay for long.
- As far as such tariffs are imposed only on the US imports from China, the third countries may respond to exploit possible positive trade diversion.
- However, the US may impose tariffs also on imported goods from the third countries as Mr. Trump is advocating.
- Or, if additional tariffs are imposed not only on the country origin basis but also on the firm nationality basis or on intermediate goods basis, things will be more complicated for the third countries.
- Further tariff war may cause a sudden increase in imports from China by ASEAN, which may trigger some protectionists moves in the third countries.
 - E.g., EVs in Thailand
- Middle powers in-between must watch carefully the politics in the US and China.

(2) Effects of high-tech export control

- The US policy related to supply chain decoupling
 - August 2018: strengthened export controls from the perspective of national security.
 - May 2019: added Huawei and its 68 affiliates to the Entity List (EL).
 - May 2020: requested firms (even outside the US [extra-territoriality]) to obtain prior permission of the exports of “direct products (using US-origin tech. or software)” if used in the production or development of chipsets and others designed by Huawei.
 - August 2020: requested prior authorization for exports to be used for the production or development of chipsets purchased or ordered by Huawei or its affiliates; particularly for foreign-produced items that are capable of supporting the development or production of telecom systems, equipment, and devices of the 5G level (including “indirect inputs”).
 - December 2020: added Semiconductor Manufacturing International Corporation (SMIC) to the EL.
 - August 2022: CHIPS Act was introduced (in exchange of receiving subsidy, the expansion or renewal of production capacity of high-end semiconductors in China is banned).
 - Oct. 2022: introduced export control in terms of the end-use (including any firm in China) for the development, production, or others of super computers or high-end semiconductors in China.
 - December 2022: added more than 30 Chinese firms to the EL. Further expansion of the EL followed.
- Japan’s export controls
 - March 2023: Japan announced the introduction of export control on semiconductor manufacturing equipment (plan to start in July 2023). Cf. The Netherlands had already introduced export control.
 - To cover items without using the US technologies.

- The purpose of the policy is to restrict flows of cutting-edge technologies.
- Extraterritoriality is partially imposed.
- Measures by the US include restrictions on FDI and the movement of people.

- Trade effects of export control are so far limited within the detailed product level (below HS 6 or 9-10 digit level).
 - DID analysis by Ando, Hayakawa, and Kimura (2024a, 2024b) and Hayakawa, Kimura, and Yamanouchi (2024) for (i) an entity list control for Huawei by the US in 2020, (ii) a control for semiconductor manufacturing by the US in 2022, and (iii) a control for semiconductor manufacturing equipment by Japan in 2023, respectively.
- However, chilling effects due to policy uncertainties in the short and middle run seem to become serious.
 - Inward FDI by the BOP statistics in China dropped by 81.7% in 2023 (provisional figure).

Further export control?

- From the viewpoint of ASEAN, direct effects of the US (and other) export control do not seem to exist so far.
 - Production plants located in AMS are not involved in real high-end semiconductor-related production yet.
- In the political turmoil, some AMS, notably Malaysia and Vietnam, recently attract new investment in semiconductor industry and try to upgrade their position in global value chains (GVCs).
- Once stepping into real high-tech, however, AMS may need to make its political stance clearer.

4. Concern

(1) Partial decoupling and “fence” setting

- The boundary of the restricted economy seems to differ even among the West allies.
 - Substantial economic links between the West and China are likely to survive.
- The third countries such as ASEAN may likely be allowed to keep the neutral position.
- Decoupling will be “partial.”
- To retain a vigorous economy, the “fence” between the restricted economy and free trade must be clearly shown to reduce policy uncertainties.
 - However, it seems difficult due to strong national security logic.
 - Can “small yard, high fence (Jake Sullivan, April 2023)” be achievable?
 - Unclear “fence” is particularly costly for middle powers like Japan.

(2) The weakening of the rules-based trading regime

- Some of the recently introduced trade/industrial policies in the G7 may be inconsistent with their WTO commitments or conventional trade norms.
 - These moves are weakening the rules-based trading regime.
- Some countries in the Global South start introducing policies that seem to violate trade norms.
 - The issue of the WTO Appellate Body affects the policy discipline.
 - The US blockage of the appointment of AB members stops AB to work.
 - 24 cases have become “appeal into void” by the end of 2023.
 - E.g., India in tariffs on ICT products (DS584), Indonesia in export ban on nickel (DS592)
 - The number of WTO DS cases reduced after 2020 into single digit per year.
- The rules-based trading regime must be retained at least for the “rest” of the economy.

- The commitment of East Asian countries, particularly ASEAN, to international production networks (IPNs) is strong.
 - A simple gravity equation exercise (Ando, Kimura, and Yamanouchi 2022) reveals the importance of machinery IPNs in ASEAN.
 - Machinery IPNs are still well connected between East Asia and Europe/Americas, particularly East Asian exports of general and electric machineries to other regions (Ando, Hayakawa, and Kimura 2024c, Ando, Kimura, and Yamanouchi 2024).
- The rules-based trading regime is crucial to IPNs.
 - Although ASEAN and East Asia have been freeriding the rules-based trading regime, they must now realize that they must be proactive for defending it.

Gravity equation: actual and predicted machinery trade, 2019

Exporter/Importer	Value (millions US\$, %)	China	Japan	Korea	ASEAN	Australia and New Zealand	India	North America	Europe	Rest of the world	Total (World)
China	Actual (A)		75,889	58,515	161,657	7,708	37,831	296,546	249,381	476,571	1,364,100
	Predicted (B) (A)/(B) (%)		118,568 64	65,893 89	72,285 224	9,463 81	50,069 76	163,984 181	177,079 141	295,714 161	953,054 143
Japan	Actual (A)	81,031		20,245	59,962	2,582	5,817	126,272	64,669	110,199	470,778
	Predicted (B) (A)/(B) (%)	74,293 109		22,386 90	21,715 276	3,928 66	7,176 81	64,147 197	60,411 107	84,697 130	338,752 139
Korea	Actual (A)	84,679	9,161		54,181	744	6,551	66,569	36,682	77,051	335,618
	Predicted (B) (A)/(B) (%)	45,860 185	24,865 37		8,639 627	1,307 57	2,996 219	21,772 306	22,348 164	35,613 216	163,400 205
ASEAN	Actual (A)	83,070	39,456	24,559	122,552	4,107	17,733	117,662	83,934	151,101	644,176
	Predicted (B) (A)/(B) (%)	39,799 209	18,528 213	6,644 370	45,225 271	2,846 144	8,388 211	34,797 338	38,940 216	65,409 231	260,576 247
Australia and New Zealand	Actual (A)	114	57	66	373	11	45	1,215	930	8,395	11,206
	Predicted (B) (A)/(B) (%)	2,694 4	1,766 3	531 12	1,521 25	300 4	540 8	7,916 15	5,269 18	13,322 63	33,859 33
India	Actual (A)	1,971	792	566	9,107	228		13,273	11,687	27,601	65,224
	Predicted (B) (A)/(B) (%)	56,238 4	12,864 6	4,836 12	18,953 48	2,042 11		32,905 40	45,745 26	87,819 31	261,402 25
North America	Actual (A)	63,106	28,621	23,338	43,379	5,678	9,328	617,230	161,678	177,220	1,129,577
	Predicted (B) (A)/(B) (%)	105,297 60	65,732 44	20,088 116	42,259 103	15,982 36	18,806 50	591,802 104	291,501 55	327,579 54	1,479,047 76
Europe	Actual (A)	144,804	37,144	30,659	64,599	8,846	24,562	286,773	1,517,637	428,107	2,543,132
	Predicted (B) (A)/(B) (%)	122,616 118	66,879 56	22,266 138	51,213 126	11,851 75	27,976 88	318,751 90	1,298,753 117	542,040 79	2,462,344 103
Rest of the world	Actual (A)	92,501	22,859	16,508	60,029	8,727	21,201	95,207	180,288	192,063	689,382
	Predicted (B) (A)/(B) (%)	137,665 67	59,758 38	23,082 72	55,204 109	17,478 50	38,627 55	227,839 42	380,672 47	360,433 53	1,300,757 53
Total (World)	Actual (A)	551,277	213,978	174,456	575,838	38,631	123,069	1,620,747	2,306,885	1,648,311	7,253,193
	Predicted (B) (A)/(B) (%)	584,462 94	368,959 58	165,726 105	317,013 182	65,196 59	154,578 80	1,463,914 111	2,320,719 99	1,812,625 91	7,253,192 100

Notes: ‘Actual (A)’ denotes the actual values of specific country/region pairs, ‘Predicted (B)’ denotes the corresponding predicted values, and ‘(A)/(B) (%)’ denotes the ratio of actual to predicted values in percentage. North America refers to Canada, Mexico, and the United States; Europe refers to the 27 European Union member countries and the United Kingdom; and ‘Rest of the world’ refers to 128 countries and regions, including Hong Kong, Macao, and Taiwan. The predicted values for regions are calculated by totalling the member countries’ predicted values.

Source: Ando, Kimura, and Yamanouchi (2022).

Gravity equation: actual and predicted machinery trade for ASEAN Member States, 2019

Exporter/Importer	Value (millions US\$, %)	Singapore	Brunei	Malaysia	Thailand	Indonesia	Philippines	Vietnam	Laos	Cambodia	Myanmar	ASEAN	China, Japan, and Korea	Total (World)
Singapore	Actual (A)		393	13,234	3,955	5,543	4,543	3,470	30	338	815	32,321	34,364	156,011
	Predicted (B)		128	5,444	678	1,469	274	210	34	59	150	8,446	6,468	34,514
	(A)/(B) (%)		309	243	583	377	1,657	1,653	88	572	543	383	531	452
Brunei	Actual (A)	90		55	4	2	0	4	0	0	0	155	42	250
	Predicted (B)	74		70	25	38	19	10	1	2	6	245	327	1,416
	(A)/(B) (%)	122		79	15	5	1	38	2	0	0	63	13	18
Malaysia	Actual (A)	19,879	110		6,593	1,785	1,609	2,958	8	97	86	33,125	27,355	147,174
	Predicted (B)	8,476	188		1,486	2,124	269	214	36	62	161	13,015	6,308	38,377
	(A)/(B) (%)	235	59		444	84	598	1,384	22	156	54	255	434	383
Thailand	Actual (A)	3,786	49	4,377		3,574	3,860	4,798	915	1,581	827	23,768	22,145	113,417
	Predicted (B)	1,310	82	1,844		1,114	435	513	231	283	538	6,348	11,006	44,997
	(A)/(B) (%)	289	59	237		321	888	935	397	559	154	374	201	252
Indonesia	Actual (A)	3,471	40	1,210	2,311		3,226	1,851	21	91	147	12,367	4,551	30,530
	Predicted (B)	3,323	150	3,087	1,305		691	455	71	109	171	9,361	16,248	70,177
	(A)/(B) (%)	104	26	39	177		467	407	30	83	86	132	28	44
Philippines	Actual (A)	5,852	2	1,497	2,189	473		1,061	0	10	6	11,090	17,663	62,111
	Predicted (B)	608	74	383	499	678		239	32	44	65	2,623	9,235	27,307
	(A)/(B) (%)	962	3	391	438	70		445	0	23	9	423	191	227
Vietnam	Actual (A)	1,718	20	1,493	2,535	1,122	1,073		105	295	244	8,606	40,332	131,657
	Predicted (B)	492	40	322	623	472	252		225	162	85	2,674	11,129	28,431
	(A)/(B) (%)	349	51	464	407	238	425		47	182	286	322	362	463
Laos	Actual (A)	6	0	8	397	4	0	27		1	0	444	82	770
	Predicted (B)	45	3	30	159	42	19	127		17	19	462	814	2,460
	(A)/(B) (%)	13	0	28	250	9	0	21		8	1	96	10	31
Cambodia	Actual (A)	8	0	16	202	1	62	47	1		2	341	346	1,403
	Predicted (B)	91	6	62	225	74	30	107	19		10	624	658	2,906
	(A)/(B) (%)	9	0	27	90	2	206	44	7		18	55	53	48
Myanmar	Actual (A)	133	0	13	113	6	11	60	0	0		336	205	852
	Predicted (B)	304	19	209	564	153	60	74	30	13		1,426	2,777	9,993
	(A)/(B) (%)	44	0	6	20	4	19	81	0	1		24	7	9
ASEAN	Actual (A)	34,944	614	21,904	18,299	12,510	14,385	14,276	1,082	2,412	2,126	122,552	147,085	644,176
	Predicted (B)	14,723	690	11,451	5,563	6,163	2,050	1,948	679	752	1,205	45,225	64,971	260,576
	(A)/(B) (%)	237	89	191	329	203	702	733	159	321	177	271	226	247
China, Japan, and Korea	Actual (A)	49,071	427	34,230	41,200	31,174	25,148	86,404	995	2,485	4,664	275,800	329,520	2,170,496
	Predicted (B)	18,495	1,609	11,602	16,517	20,509	11,853	14,692	1,893	1,236	4,234	102,639	351,865	1,455,207
	(A)/(B) (%)	265	27	295	249	152	212	588	53	201	110	269	94	149
Total (World)	Actual (A)	154,458	1,729	86,621	81,632	58,174	57,501	119,042	2,257	6,313	8,112	575,838	939,711	7,253,192
	Predicted (B)	72,025	5,168	47,512	50,633	65,241	27,378	28,933	4,342	4,069	11,713	317,013	1,119,147	7,253,192
	(A)/(B) (%)	214	33	182	161	89	210	411	52	155	69	182	84	100

Source: Ando, Kimura, and Yamanouchi (2022).

Supporting the WTO

- Voice to support the WTO is substantially weakened in the US; middle powers including ASEAN must be proactive to reconfirm its value.
- Issue 1: dispute settlement mechanism
 - The Appellate Body issue must be taken care of.
 - The expansion of membership of MPIA (Multi-Party Interim Appeal Arbitration Arrangement) must be promoted in Asia.
 - The current members in extended East Asia: Japan (March 2023-), China, Hong Kong, Macao, Philippines (May 2024-), Singapore, Australia, and New Zealand
- Issue 2: WTO as a rule maker
 - Cooperation in JSI (Joint Statement Initiatives) can be enhanced.
 - Particularly, JSI on e-commerce is important.
 - 91 WTO members including Malaysia are participated.

Promote regional initiatives

- The link among AMS can be further strengthened.
- RCEP (Regional Comprehensive Economic Partnership) can be utilized for
 - Supporting the rules-based trading regime
 - Reducing policy uncertainties for the private sector
- Any move to promote the rules-based trading regime must be supported.
 - E.g., Indonesia's interest in OECD, CPTPP
 - CPTPP
 - Pro-trade gathering of middle powers (without the US or China)
 - OECD
 - Less binding setting but a good basis of overall policy reform toward fully developed economies.
 - Indonesia (Feb. 2024) and Thailand (June 2024) started accession discussions. Malaysia expresses interest.
 - Recent new members: Latvia (2016), Lithuania (2018), Colombia (2020), Costa Rica (2021)
 - Under negotiation: Argentina, Brazil, Bulgaria, Croatia, Indonesia, Peru, Romania, Thailand
 - OECD Secretary-General: switched from Jose Angel Gurría (Mexico) to Mathias Cormann (Belgium->Australia) in June 2021.

5. Rules in the middle and long run?

- At the end, China must get involved with the rules-based trading regime.
- A question is how the current issues could be resolved by the rules.
 - State-owned enterprises
 - Digital governance
 - “National security exceptions” in the context of trade rules
 - Interpretation of GATT XXI: from self-judgment to disciplined borderline
 - Panel decisions on Russia transit transport (DS512, 2019), the US Section 232 (DS544+, 2022).
 - May need to set a borderline of national security exceptions for each individual policy mode.
 - “Subsidy + over-production” vs. “Marshallian externalities + adjustment costs + international income distribution”
 - Current argument on iron and steel, solar panels, EVs, and others.
 - Different economic logic would apply. May need new trade rules.

6. Way forward and the role of the third countries

- It is important for the third countries such as ASEAN to maintain the neutral stance not only for its own sake but also for the world.
- ASEAN should take advantage of positive trade diversion; it's good for the world.
- It can try to penetrate deeper into high-tech value chains.
- Together with other pro-trade middle powers, ASEAN may want to be proactive in:
 - Reducing policy risks and
 - Retain the rules-based trading regime as widely as possible.
- Japan and the EU should get together with pro-trade players in Global South and retain vigorous economic activities as widely as possible.

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