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De-Globalisation Sentiment Carries Risks for ASEAN Economies

*Sanchita Basu Das**

EXECUTIVE SUMMARY

- Global trade has slackened since the 2008-09 crisis partly due to a reduction in the pace of trade liberalisation and to rising protectionism. Other aspects such as the slowing of the Chinese economy, the maturation of the global value chain and stringent banking sector regulations, are also contributing factors.

- Stagnant wages and rising income inequality being often perceived as the outcome of unfair foreign competition have now brought about an electoral backlash in the advanced economies.

- This is of concern to ASEAN economies, not due so much to their excessive direct exposure to the US as to their indirect linkage to China. Also, income inequality in some ASEAN countries has the potential to generate a future political backlash.

- We are unlikely to see an end to globalisation soon, although there will be a cautious approach towards economic integration. ASEAN countries should explore their policy options to boost regional demand, mitigate the adverse distributional effects of trade liberalisation and work for a more equitable society.

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INTRODUCTION

Since the 2008 Global Economic Crisis (GEC), trade growth has slowed significantly. After an average growth rate of 16% per annum (p.a.) in 2003-2008, merchandise trade grew by only 1.5% p.a. in 2010-2015. Trade in commercial services dropped from a growth rate of 15% p.a. during 2005-2008 to 4.4% p.a. in 2010-2015.

This issue was amplified following the Brexit referendum and the US presidential election in 2016 as world leaders fretted over a trend of de-globalisation. Years of soft economic growth and large income inequality fueled a voter backlash against the perceived unfair competition from foreign multinationals and workers in these advanced economies. 2016 thus witnessed a combination of economic and political risks, raising fears of throttling earlier efforts of globalisation. But will the trend of globalisation end soon?

This paper looks at the economics and politics governing the slowdown in cross-border activities. It discusses the risks of de-globalisation sentiments for ASEAN economies and concludes that although there are some signs of de-globalisation, we are unlikely to see an end to globalisation anytime soon. What we will observe is increased policy uncertainty that will weigh on trade and investment flows and a cautious approach towards economic integration.

STATE OF (DE)GLOBALISATION

The de-globalisation trend is measured by observing key economic indicators such as international commerce and flows of foreign direct investments (FDI). Other indicators are the application of tariffs and non-tariff barriers on trade, restrictions imposed by governments on labour movement and national policies for encouraging purchase of local goods. Many of these tools are used during times of crisis, such as in 2008-09.

Figures 1 to 4 show the trend of global trade and investment. Unlike other crises like that of 1997-98 or 2001, global trade and FDI growth did not accelerate to its earlier pace after the GEC of 2008-09. After a sharp recovery in 2010, the annual growth of global merchandise exports stayed stuck at around 1% in 2012-2014, before contracting in 2015. Growth in the export of commercial services also moderated from an expansion of 13.2% in 2011 to a contraction of 6% in 2015 (Figures 1a and 1b). FDI net inflows fell from a peak of US$3.1 trillion in 2007 to US$1.8 trillion in 2014, before rising moderately to US$2.2 trillion in 2015 (Figure 2).

Since 2011, the trade-to-GDP ratio has remained almost flat or declined (Figure 3). FDI net inflows as percentage of global GDP remained well below the mark of 5.3% from 2007, although it recently improved marginally relative to the output (Figure 4).

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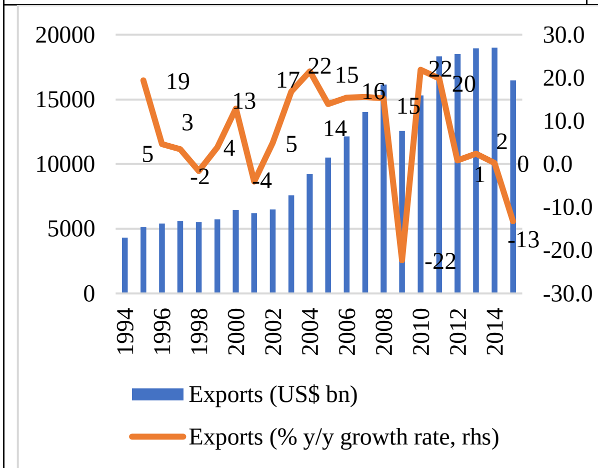
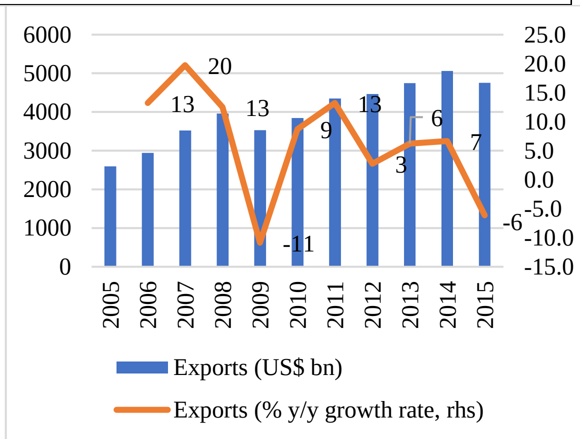
Therefore, the catalyst for cross-border movement of goods and services (globalisation) seems to have stalled, thereby raising the risk of de-globalisation. What can be causing this trend?

Figure 1a: Global Exports of Goods



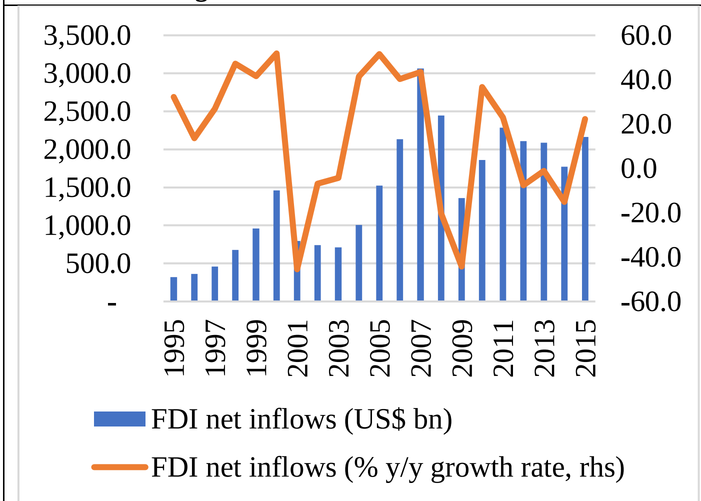
Note: Other than statistical discrepancies, global exports and imports are generally the same.
Source: WTO Statistical Database and author's calculation

Figure 1b: Global Exports of Commercial Services



Note: Other than statistical discrepancies, global exports and imports are generally the same.
Source: WTO Statistical Database and author's calculation

Figure 2: Global FDI Net Inflows



Source: World Bank

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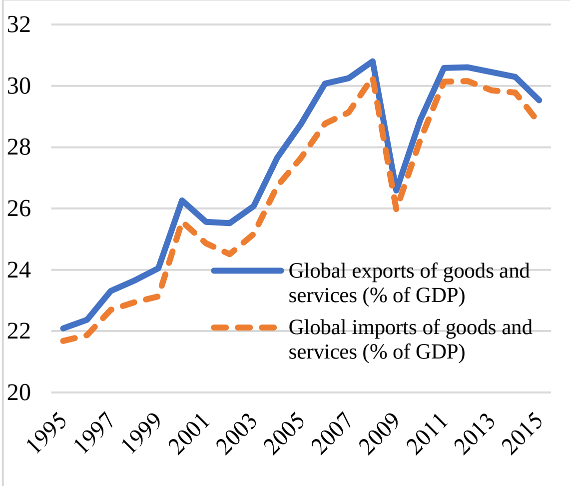
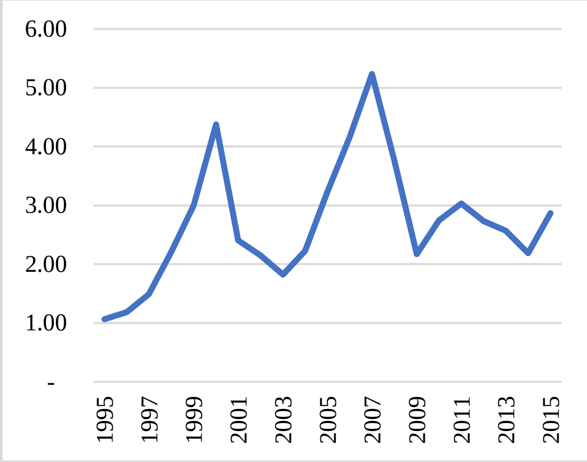
Figure 3: Global Trade in Goods and Services (% of GDP)



Source: World Bank, WDI Database

Figure 4: Global FDI Net Inflows (% of GDP)



Note: Other than statistical discrepancies, global exports and imports are generally the same.
Source: WTO Statistical Database and author's calculation

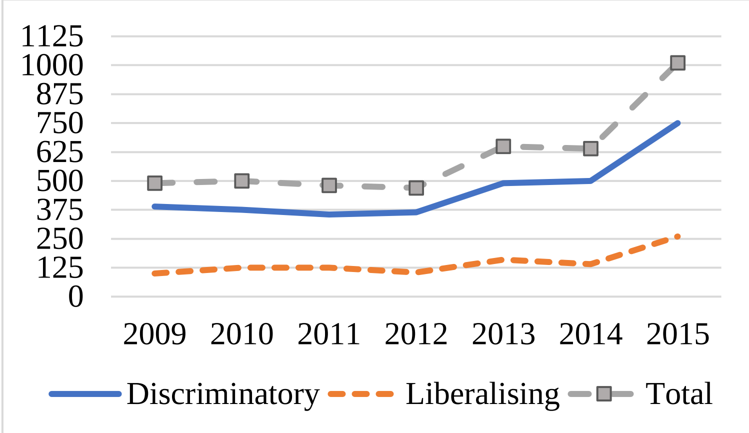
There are many underlying causes for the trade slowdown, including import moderation by big economies, structural factors and increased protectionism.

According to the Global Trade Alert Report 2016[1], incidents of protectionism have gone up recently. In 2015, the number of discriminatory measures applied was 50% higher than in 2014. This was also much higher than in 2009, when political leaders worldwide voiced concern about the global trading system (Figure 5). G-20 economies accounted for most of the trade-restrictive measures in 2015 (Table 1). Although subsidies, trade defence measures and import tariff increases were widely used as trade discriminatory instruments, there was a shift towards more opaque ones, such as localisation requirements and export incentives.

The 10 sectors hit the most by these discriminatory measures accounted for around 40% of world trade in 2015 (Table 2). Basic metals have been affected the most in 2015 (143 times), reflecting discriminatory policy measures of import tariffs and export incentives in the steel sector. Transport equipment, a significant sector in world trade at 7.5%, has also been harmed.

[1] http://www.globaltradealert.org/sites/default/files/GTA%2019%20-%20World%20Trade%20Plateaus_0.pdf

Figure 5: Number of Implemented Measures Worldwide



Source: Global Trade Alert Report 2016 (p. 25)

Table 1: Top 10 Countries Imposing Discriminatory Measures in 2015

Rank	Countries	No. of measures imposed in 2015	Share of world imports, 2014
1	USA	90	13.5%
2	Russia	86	1.6%
3	India	67	2.6%
4	Brazil	42	1.3%
5	Indonesia	42	1.0%
6	Argentina	36	0.4%
7	Japan	36	4.5%
8	UK	36	3.8%
9	Italy	34	2.6%
10	Canada	27	2.6%

Source: Global Trade Alert Report 2016 (p. 27)

Table 2: Top 10 Sectors Affected Most by Protectionist Measures in 2015

Rank	Sector	Number of times hit in 2015	% of world trade in 2014
1	Basic metals	143	5.4
2	Transport equipment	107	7.5
3	Agricultural products	100	2.2
4	Fabricated metal products	94	1.4
5	Special purpose machinery	90	5.3
6	Basic chemicals	86	5.3
7	Grain mill products and starches	69	1.5
8	Other chemical products	65	4.9
9	Meat, fish, fruit, vegetables, oils and fats	62	2.1
10	General purpose machinery	62	4.9
	All other sectors	835	59.4

Source: Global Trade Alert Report 2016 (p. 28)

The aversion to trade liberalisation is also observed in policy failures. The World Trade Organisation (WTO) Doha Round of multilateral trade negotiations launched in 2001 did not progress in the last 15 years. Advanced economies like the US and the EU decided to seek alternative arrangements, i.e. Trans-Pacific Partnership (TPP) and Transatlantic Trade and Investment Partnership (TTIP). However, these also failed to progress due to domestic backlash.

There were other reasons contributing to the slowdown.[2] Lately, China's economy has slowed from 10% p.a. to less than 7% annually. It is rebalancing its economy away from exports and towards domestic demand. As a result, while China's exports contracted by 3%, imports declined by 14% in 2015 vis-à-vis 2014. This is significant, given that China accounts for 14% of world exports. The maturation of the global value chain (GVC) is another reason for the slowdown. During the 1990s and early 2000s, global trade was highly supported by a production process that is fragmented across multiple countries and hence increased trade particularly in intermediate products. However, since the GEC, the contribution of GVCs in global trade has plateaued with weakness in advanced economies.[3] The deceleration in GVC participation is significant in the US and Japan. Finally, since the GEC, there has been a sharp fall in international capital flows, mostly through reduced cross-border bank lending and borrowing as financial regulators imposed higher regulatory standards to mitigate risks of future crises.[4] This affected economic activities in countries that are largely dependent on foreign banks and have less developed stock and bond markets.

It is, thus, inconclusive that globalisation will reverse soon due to increase in protectionism. Going forward, while China's economic growth may slow down further and it may engage in world trade at a lower rate, there is unlikely to be a global trade war. The established GVCs will not be reversed immediately. Similarly, while international operation of banks may decline, FDI will continue to be an attractive mode of financing. One may observe sluggishness in economic integration though. There is a possibility of a re-calibration of globalisation, i.e. countries will integrate more deeply in their areas of comparative advantage and hold back in areas that are politically sensitive. The latter arises from the policy uncertainty of the West, exacerbated by recent electoral outcomes in the US and the UK.

POLITICS OF DE-GLOBALISATION

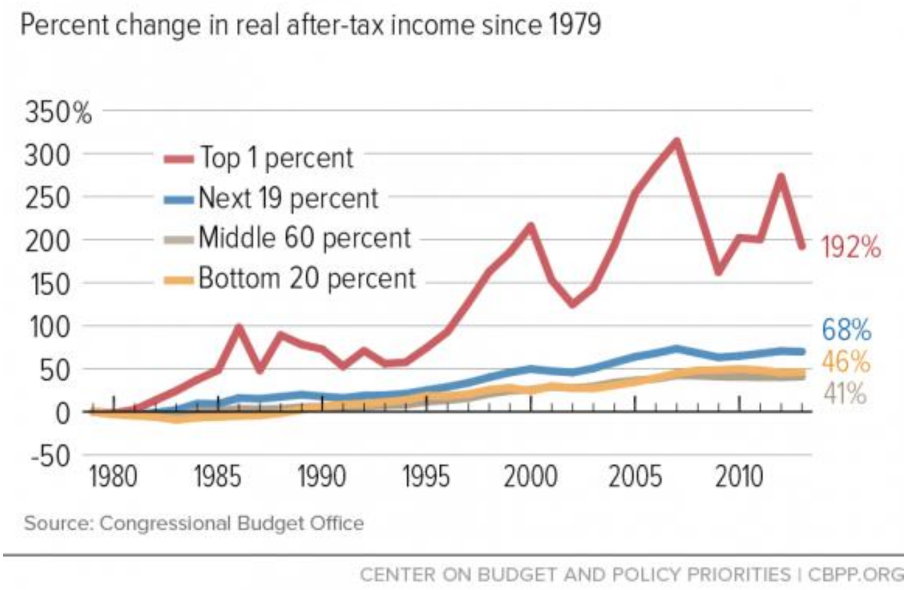
Of late, income inequality and immigration have been argued to be a threat to globalisation. There is a growing perception that both these issues are a result of trade liberalisation: while it is making a section of the society of some countries richer at the expense of others,

[2] For more details, please refer to https://openknowledge.worldbank.org/bitstream/handle/10986/25823/9781464810169.pdf
[3] https://www.oecd.org/eco/outlook/Cardiac-arrest-or-dizzy-spell-why-is-world-trade-so-weak-OECD-Paris-21-September-2016.pdf
[4] https://www.imf.org/External/Pubs/FT/GFSR/2015/01/index.htm

immigration is increasing competition for the same jobs and public resources. The outcomes of the Brexit vote and the US election in 2016 are reflections of voters' hostility towards liberalisation initiatives and globalisation.

Concentration of money in the hands of a few has indeed been a sensitive issue for a while. In a study of 46 major economies, it was found that while wealth inequality was on the rise in 12 of them before 2007, the number has since gone up to 35.[5] In the US, for example, income gains of the top 1% of the population had grown much higher since the early 2000s than those of the middle- and low-income households (Figure 6).

Figure 6: Income Gains of the Top-, Middle- and Low-Income Households



The discontent over inequality in the developed countries is often mentioned as a result of subdued growth for a long time. There are other reasons too, such as less purchasing power on account of low wage growth and uneven gains to individuals from the rise of asset values in the post-2008 period. The latter is largely caused by the Central Banks as they pump easy liquidity in the market raising asset prices, i.e. stocks, bonds and real estate. For example, in Britain, while wages are up only 13%, stock market is up 115% since 2008.[6]

However, trade liberalisation is the key offender for income inequality in the latest electoral outcomes of the advanced countries. This is because, broadly, trade liberalisation changes

[5] Wealth inequality is much higher than income inequality as it includes both wage income and capital/ asset income.
https://thenextrecession.files.wordpress.com/2014/10/cs_global_wealth_report_2014_vf.pdf
[6] https://www.theguardian.com/commentisfree/2016/jul/28/era-globalisation-brexit-eu-britain-economic-frustration

industry composition by reallocating resources from lower (import competing) to higher productive (export-oriented) firms. While the higher productive firms gain and expand with trade liberalisation, lower ones contract or exit the market. The higher productive firms also pay high wages and demand for better quality employees, unlike the lower productive firms, thus leading to wage inequality and unemployment in an economy.[7]

In the debate over Brexit, one of the arguments of the 'leave' campaign was greater control over immigrant flows in the UK from other EU countries. In the last 20 years, immigration had gone up significantly in the EU. During 1995-2015, EU immigrants living in the UK tripled from 0.9 million to 3.3 million. The share of EU nationals rose from 1.8% to 6.3% of the working age population (age of 16-64).[8] There was serious concern that the high level of immigration was putting pressure on jobs, wages and quality of life.

However, this does not mean that globalisation is coming to an end soon. Cross-border flows of goods and services were declining much before the incidents of Brexit and US election. What is happening is a cautious approach towards economic integration. Political leaders, while talking about open economies in international forums, are increasingly being careful on liberalisation initiatives. Worries over revolts, similar to Britain and America, are discouraging governments in developing countries from undertaking bold structural reforms. Businesses are working in uncertain environment as new barriers to trade and investment emerge globally. All this acts as a drag on international trade, FDI and hence growth.

IMPLICATION FOR ASEAN ECONOMIES

ASEAN has a trade-to-GDP ratio of around 100% (Figure 7), reflecting its high exposure to the global economy. There are significant variations though: Singapore and Vietnam have higher trade exposure compared to Indonesia and Myanmar (Table 3). The countries are also dependent on FDI as a major source of growth as seen by its share in total GDP (Figure 8). The slowdown in global trade and investment and a cautious sentiment over economic integration is unlikely to bode well for this group of countries.

[7] The relationship between trade liberalisation and income inequality may not be so monotonic, in practice. The gainers and losers can be within an industry or across an industry. On aggregate, the positives can outweigh the negatives. Often, gains/losses depend on skill-levels in the two trading countries. It is also possible that trade openness over a long period can reduce wage inequality as the number of firms operating in the domestic market reduces or firms move up the value-chain of activity and become more productive.

[8] http://cep.lse.ac.uk/pubs/download/brexit05.pdf

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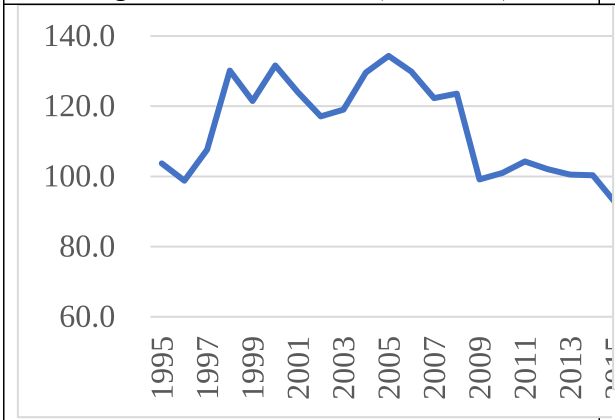
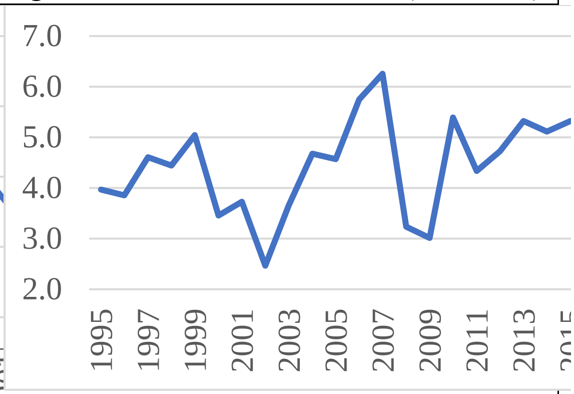
Figure 7: ASEAN Trade (% of GDP)



Source: World Bank

Figure 8: ASEAN FDI Net Inflows (% of GDP)



Source: World Bank

Table 3: Trade (as % of GDP) of Individual ASEAN Countries, 2015

Country	Ratio	Country	Ratio
Brunei	78	Myanmar	33
Cambodia	145	Philippines	44
Indonesia	34	Singapore	221
Laos	50	Thailand	106
Malaysia	127	Vietnam	171

Source: author's estimate using WTO Trade Database and IMF WEO, April 2016

Although IMF projects the ASEAN region to grow at an average rate of 5.3% in 2017-2018, downside risks remain from the increased uncertainty in the US and the EU.

A slowdown in trade flows from the US and the EU will weaken the economic outlook of ASEAN countries. Although the ASEAN countries now trade much less with the US and the EU, their significant linkage with China will impact economic growth (Figure 9). This is because while China exports final goods to the US (around 60% each of US' demand for capital and consumer goods), it imports approximately 50% of intermediate goods from neighbouring countries in Asia.[9] For the last few years, China is restructuring its economy to make it more domestic-driven and is systematically slowing it down from 10% in 2010-11 to 7.0% in 2014-16 and further to 6.0% in 2017-19. If the slowdown in China happens faster than expected due to weaker global trade, it will have a significant spillover effect on ASEAN economies. A one-time 1-percentage-point unexpected decline in Chinese growth rate will probably shave off around 0.4 percentage point after two years in Indonesia, Malaysia and Thailand. The magnitude can be higher if there is deterioration of confidence in these economies.[10]

Although the economic influence of the US in the ASEAN region has diminished in recent times, it remains a key trading partner. ASEAN enjoys merchandise trade surplus with the US (Figure 10). Hence, any import restriction by the US will hurt ASEAN. Individually,

[9] Rising Risk of Protectionism: Measuring the Impact, Morgan Stanley Research, 5 January 2017
[10] Global Economic Prospects, The World Bank, January 2017

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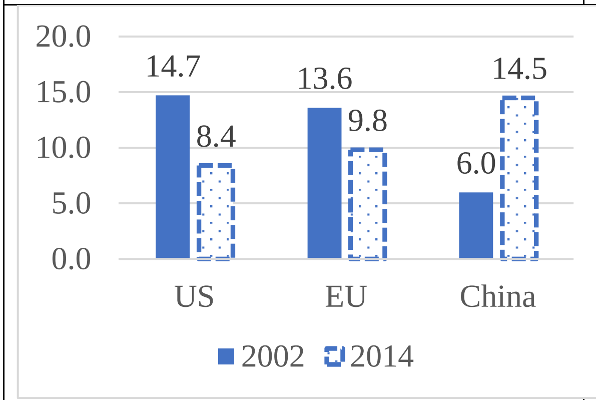
the US runs notable trade deficits with 4 ASEAN countries – Vietnam, Malaysia, Thailand and Indonesia – implying that these will be affected the most in case the new US administration decides to impose new import tariffs (Table 4).

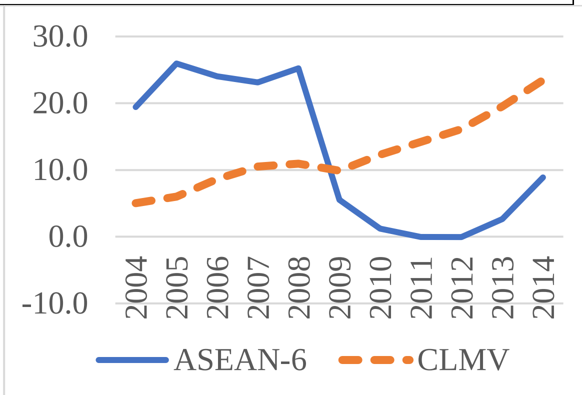
Also, it should be noted that US is deeply integrated into the global value chain, both in forward and backward participation.[11] Its participation is high in chemicals, business services, electronics and computers, apparel and leather products and motor vehicles. ASEAN countries are exporters of either final or intermediate products of electrical machinery (24% of total), apparel and clothing (15%) and footwear (4%) to the US. Any restrictions on trade for these products will thus hurt the region.

Figure 9: ASEAN's trade with the US, the EU and China (% of total ASEAN trade)



Source: ASEAN Statistical Yearbook, 2016, 2010, The ASEAN Secretariat

Figure 10: ASEAN Countries' trade balance with the US, US$ billion



Source: ASEAN Statistical Yearbook, 2016, 2010, The ASEAN Secretariat

Table 4: US' merchandise trade balance with ASEAN countries, 2016, (% of US GDP)

Country	Trade Balance	Country	Trade Balance
Brunei	0.0	Myanmar	n.a.
Cambodia	-0.01	Philippines	-0.01
Indonesia	-0.07	Singapore	0.04
Laos	0.0	Thailand	-0.09
Malaysia	-0.12	Vietnam	-0.16

Note: the numbers in the brackets give trade balance as % of US GDP
Source: www.census.gov, IMF WEO database, author's calculation

Rising protectionist sentiments create uncertainty about the future of institutionalised trading relationships. With WTO, members can legally raise import tariffs to a certain

[11] Forward participation – US exports often serve as production inputs in other countries for exports; backward participation – imports for final exports from the US.

extent[12]. ASEAN countries have already faced a setback since three out of four ASEAN members[13] have lost access to the US market due to the demise of the TPP. The future of an 11-member TPP remains uncertain. Nonetheless, ASEAN countries are more positive on the trade agreements as they continue to pursue the Regional Comprehensive Economic Partnership (RCEP).

As trade and FDI are often positively related to each other, trade contraction will affect FDI flows into the ASEAN region. Investment decisions will be affected due to uncertainty about the US' new trade and investment policies. However, ASEAN may also benefit from this. As President Trump has often marked China as a currency manipulator, but never mentioned any of the ASEAN countries, investors may get attracted to ASEAN as an alternative to China. Moreover, ASEAN is a low-cost production site vis-à-vis China.

Thus, while a slowdown in international trade and the de-globalisation sentiment is likely to challenge ASEAN, the positive factor is the region's limited exposure to the US compared to the early 2000s. Economies like the Philippines and Indonesia have significant domestic sources of demand, while Vietnam and Malaysia are more exposed to external demand, particularly to the US. Being a highly open economy, Singapore will be affected by policy uncertainty in the West, a slowdown in China and the global economy in general.

The ASEAN governments may also get worried over the consequences of income inequality in the region as it can hamper long-term growth prospects. It can have a hollowing-out effect on the middle class, thereby dragging down consumer demand, or adversely affect labour productivity. However, as Krugman argues, the significant fallout of inequality is political.[14] As income inequality rises, economic elites whose political influence rise along with wealth, lobby for public policies that will benefit a small proportion of the population. The resulting discontent among the masses can have significant repercussions for social cohesion.

In the last two decades, while poverty has reduced in ASEAN countries, inequality has been rising. Table 5 shows that out of the 8 countries, Indonesia and Laos has had a significant increase in inequality. Uneasiness over income inequality is found in Malaysia, the Philippines, Thailand and Singapore, if one considers 40 as the transition point between an 'equal' and 'unequal' society[15]. Separate from the Gini Coefficient that is often used to measure inequality, a study in 2014 reported that Indonesia, Malaysia, the Philippines and Thailand suffer from 'very high' wealth inequality, while Singapore is challenged by 'medium' inequality.[16]

[12] In WTO, two tariff rates are negotiated - MFN and Bound. The bound tariff, generally higher than the applied MFN, is the maximum MFN tariff level that a country can apply. Anything above that could be reported to dispute settlement mechanism.
[13] Singapore has a bilateral trade agreement with the US.
[14] http://www.nytimes.com/2013/12/16/opinion/krugman-why-inequality-matters.html
[15] http://www3.ntu.edu.sg/rsis/nts/resources/db/uploadedfiles/Matthew%20Bock.pdf
[16] The study defines 'very high' inequality as top decile (10% of the population) share >70%, 'medium' inequality refers to a top decile share of 50%–60%; https://thenextrecession.files.wordpress.com/2014/10/cs_global_wealth_report_2014_vf.pdf.

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Table 5: Income Inequality in ASEAN Countries (Gini Coefficients)

	Initial Year	Final Year	1990s	2000s
Cambodia	1994	2012	38.8	30.7
Indonesia	1990	2013	29.2	39.5
Laos	1992	2012	30.4	37.9
Malaysia	1992	2009	47.7	46.2
Philippines	1991	2012	43.8	43.0
Singapore		2014		41.1
Thailand	1990	2013	45.3	39
Vietnam	1992	2014	35.7	37.6

Source: updated from http://www.ide.go.jp/English/Publish/Download/Brc/pdf/14_01.pdf

Income inequality is likely to get more attention from ASEAN policy makers going forward. Thanks to the media, the countries are not completely insulated from the spillover effect of people's sentiments in the advanced economies. A possible backlash will remain a concern, perhaps pushing the governments to limit liberalisation policies.

CONCLUSION

Since the 2008-09 crisis, global trade growth has slowed down for both goods and services. While this is explained by reduction in trade liberalisation initiatives and rising protectionism, other reasons may be just as important. In 2016, economic risks were intensified by political risks as years of low growth, stagnant wages and income inequality resulted in a political backlash in the US and the UK.

However, at this juncture, these cannot be interpreted as indicators for retreat from globalization, and are more correctly seen as signs of slowdown in the pace of economic integration. Going forward, while countries will continue to integrate in their areas of comparative advantage, they will hold back in politically sensitive areas. This will of course raise policy uncertainty that will have growth repercussions.

A slowdown in globalisation is unlikely to sit well with ASEAN countries. While the countries may not be directly affected much by US protectionism, they have indirect linkage through China. However, concern over a similar political backlash in their own backyard may hamper them from undertaking significant liberalisation initiatives.

The ASEAN governments should use this period of uncertainty to stimulate domestic and regional demand. This can be done by raising consumption demand, especially of the middle class, increasing infrastructure investment and exploiting the growing capacity of ASEAN as an integrated market.

In addition, ASEAN governments should distribute the gains of economic growth, particularly those derived from liberalisation policies, by devising fiscal policies targeting education, health, social protection scheme and conditional cash transfer to the poor. They

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should also broaden the tax base and improve tax administration. They should target economically lagging provinces and develop policies to improve connectivity, identify new sources of growth, support SMEs and institutionalize skill development programs. The government should also strengthen labour market institutions and introduce temporary public employment schemes as a mechanism to address sudden job losses in their economy.