

Opportunities & challenges in global value chains

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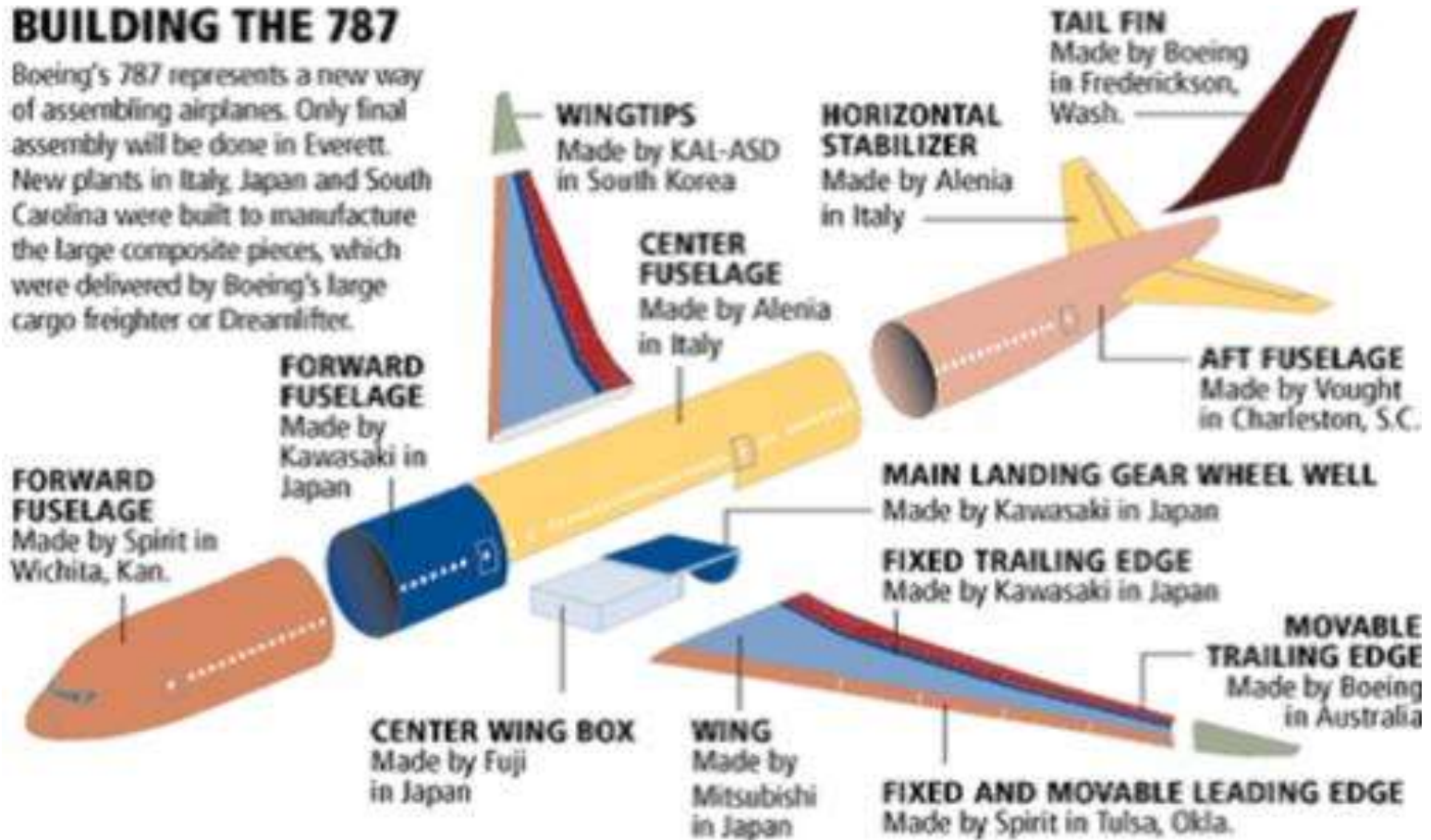
What this talk is about

- Governments cannot exploit the opportunities afforded by Global Value Chains (GVCs); neither can scholars like me
 - Only businesses and entrepreneurs can
- But I can give you a sense of the lay of the land, including what is not visible to the untrained eye
- Governments can create the conditions
 - Part of what we can do is to persuade the governments to do the right thing (or at least, not do the wrong thing)

Example of a Global Value Chain (or Global Production Network)

BUILDING THE 787

Boeing's 787 represents a new way of assembling airplanes. Only final assembly will be done in Everett. New plants in Italy, Japan and South Carolina were built to manufacture the large composite pieces, which were delivered by Boeing's large cargo freighter or Dreamlifter.



WE HAVE A PROBLEM

We don't export enough . . .

88% (2000)

Trade as a proportion of GDP

48% (2016)

Less than competitors . . .

- Viet Nam's goods exports increased **x 9.5**
- While Sri Lanka's goods exports increased **x 2.1**

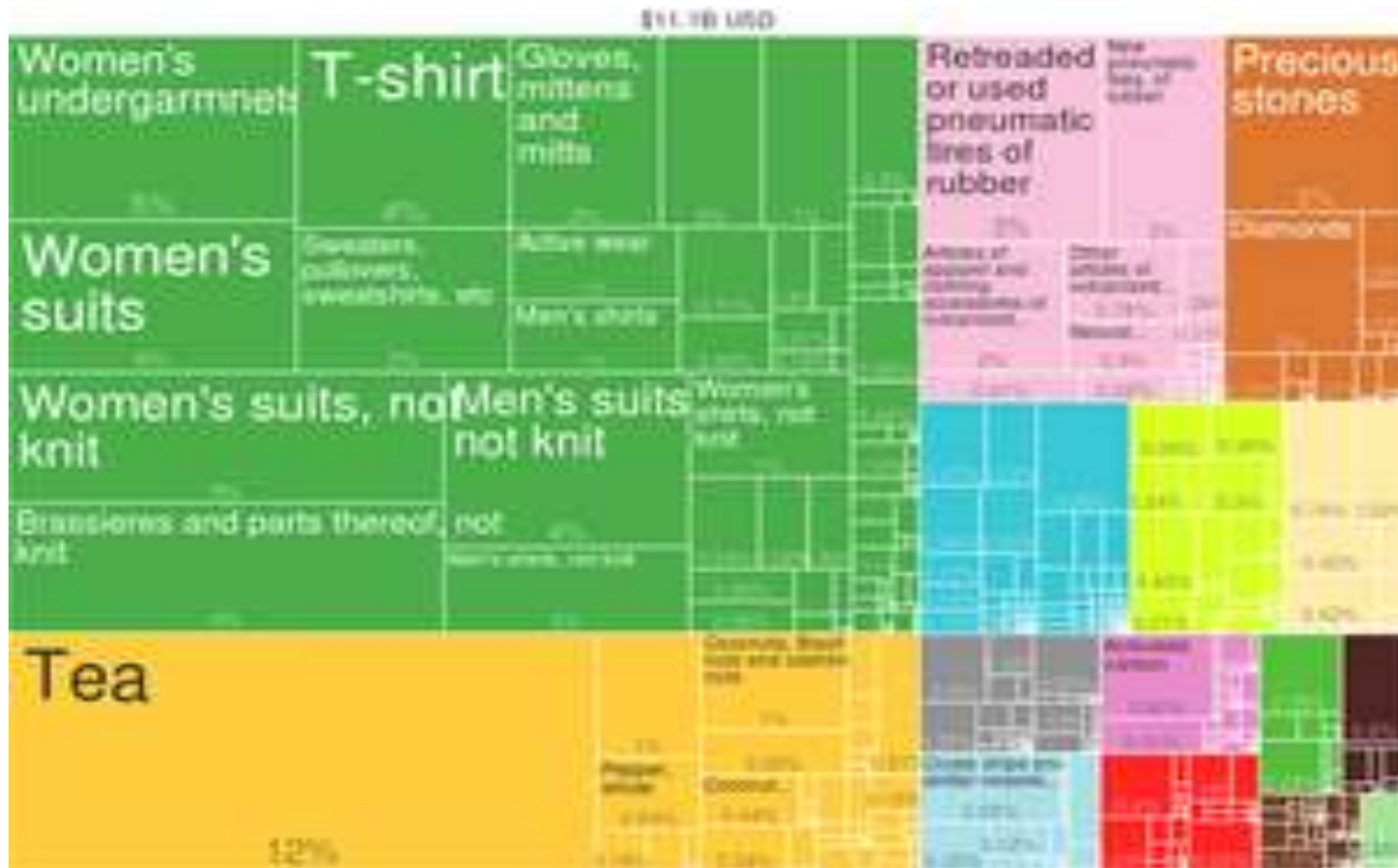
Between 2000 and 2014

And not the right things . . .

- Export of labor yielded USD 7.2 billion in 2016
 - 70% of earnings from goods exports)
 - **About the same** as service exports USD 7.1 billion

- Composition of goods exports has remained stale with over reliance on garments

Sri Lanka's exports in 2014 look little different from exports in 1994



Few are in GVCs, and even the GVCs that we're in are not very complex

- Apparel sector is already embedded in GVCs, importing inputs, adding value and assembly in Sri Lanka and exporting
- Fast growing agricultural exports such as gherkins involve rudimentary value chains
 - Gherkins grown in Bangladesh
 - Processed in Biyagama
 - Exported to Japan

What does it take to participate in Global Value Chains?

- Firms signing contracts and getting down to business
- But if this is not happening at desirable levels, one has to look at structural constraints

What does it take to participate in Global Value Chains?

- Greater certainty (→ trade agreements)
- Low-cost labor, which we do not have; If not based on low-cost labor, skilled and productive workers (→ education reforms)
- A big enough pool of workers (→ education reforms; agricultural reforms; increasing labor participation by women; SOE reforms . . .)
- Right kind of infrastructure, including excellent logistics industry (→ SOE reforms)

What can be done to enhance ability to participate in GVCs in short term?

- Greater certainty (→ trade agreements)
- Low-cost labor, which we do not have; If not based on low-cost labor, skilled and productive workers (→ education reforms)
- A big enough pool of workers (→ education reforms; agricultural reforms; increasing labor participation by women; SOE reforms . . .)
- Right kind of infrastructure (→ SOE reforms)

Greater certainty through trade agreements

- A world incapable of multilateral trade liberalization under the WTO is moving toward plurilateral and bilateral trade regimes that cover goods, services, investment and trade-related matters
 - ASEAN is looking at RCEP and TPP(-US)
 - India has entered into a large number of bilateral agreements; in RCEP; considering TPP(-US)
- All Sri Lanka has are opportunities for a few bilaterals, despite having been member of GATT since 1947 and GATS since 1995
 - Many disadvantages to negotiating multiple bilateral agreements, but better than being excluded from benefits of agreements

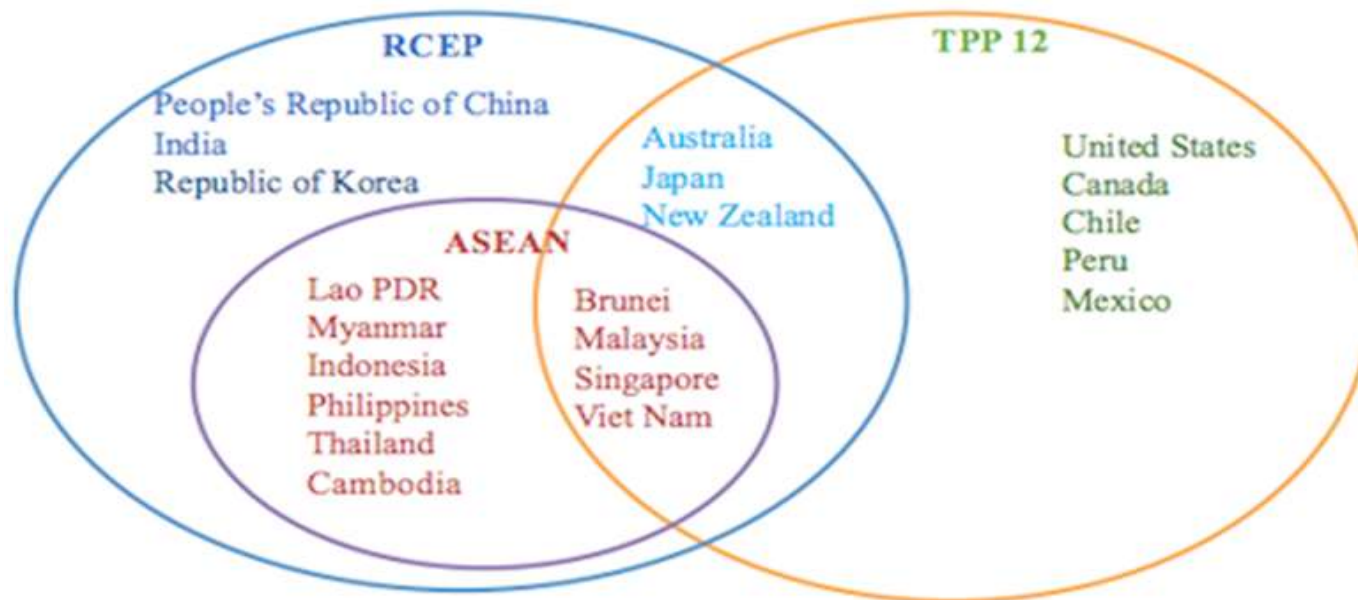
International trade is a competitive sport

- Let's look at a competitor: Vietnam

Vietnam has many firms that compete with Sri Lanka firms

- “Overall apparel import growth used to come from China and Bangladesh, but today **Vietnam is the main driver**. I don’t think you will see that trend abate in the short term.”
 - Nate Herman, Vice President of International Trade, American Apparel & Footwear Association
- In 2017 AT Kearney Global Services Index (higher is more attractive for BPO sourcing)
 - Vietnam is 6th (advanced from 11th)
 - Sri Lanka is 11th (advanced from 14th)

Vietnam in RCEP & TPP; India & China in RCEP; and Sri Lanka?



Vietnam joined WTO in 2006. Additional Trade agreements since then

- TPP (signed, not yet in effect)
- Russia, Kazakhstan, Belarus (signed, not yet in effect)
- ASEAN Free Trade Area
- ASEAN-Australia+NZ FTA
- ASEAN-India CECA
- ASEAN-Japan CEP
- ASEAN-China CECA
- ASEAN-Rep of Korea CECA
- Chile-Vietnam FTA
- Japan-Vietnam ECA
- Rep of Korea-Vietnam FTA

And Sri Lanka . . .

- First bilateral FTA with India in 1998
- Second study group report to expand FTA in 2003
- Pakistan goods FTA in 2003
- . . . Then everything stops



Results: Exports increased x 9.5 (v x 2.1 for Sri Lanka) in 2000-2014

	Vietnam (2000)	Vietnam (2014)	Multiple	Sri Lanka (2000)	Sri Lanka (2014)	Multiple
FDI (USD millions)	1,298	9,200	7.1	173	1,616	9.3
Exports (USD billions)	17	161	9.5	5.5	11.3	2.1

Source: Sri Lanka BOI

**WHY IS VIETNAM GOING FOR
PLURILATERAL AGREEMENTS? WHY
SHOULD THAT BE OUR END GAME?**

GVN → GPN

Name	Definition	Other Names
Value Chain	Sequence of productive (i.e., value added) activities leading to end use.	<ul style="list-style-type: none">• Supply chain• Commodity chain• Production chain• Activities chain• Pipeline
Production Network	Two or more value chains that share at least one actor (network linkage)	<ul style="list-style-type: none">• Value network• Input-output matrix• Supply-base

Rules of origin (ROO)

- Criteria to determine nationality of goods (where they are made, produced etc.). They are crucial in any bilateral or regional preference or free trade arrangement in order to prevent trade deflection (i.e. to ensure that such arrangements are not used to route third country products to the participating countries)

ROOs are hard enough in bilateral trade agreements

- They make trade not worth the trouble when inputs from multiple countries are involved as is the case with GPNs

Government is beginning to talk the talk

- For the first time, the Vision 2025 document presented in September 2017 makes reference to GPNs

“We will position Sri Lanka as an export-oriented economic hub at the centre of the Indian Ocean. We recognise the fundamental reality that Sri Lanka has a domestic market of only 20 million consumers with a modest per capita income, and must rely on external demand for sustained, high, and long-term growth. We will strategically position Sri Lanka as the hub of the Indian Ocean, **securing opportunities for local businesses in global production networks (GPNs)**. This outward-looking approach will increase the efficiency of the domestic economy, contributing to a better life for all Sri Lankans.”

But is it ready to walk the talk?

- Trade agreements cannot be entered into unilaterally
- All we've received are invitations to negotiate from India, China, Singapore, Bangladesh, and Afghanistan (all bilateral)
 - India study group completed its work in 2003 (14 years ago); still no agreement
 - China study group completed its work in 2014 (3 years ago); still no agreement
- Modern trade agreements almost always include services, which require complex drafting of schedules → unlikely we can handle multiple negotiations simultaneously
 - Even if we have the experts

Ideal solutions are . . .

- To enter into a plurilateral agreement, such as RCEP or BIMSTEC
- But RCEP is ASEAN+
 - An attempt to merge all the agreements ASEAN has entered into
 - So our first step has to be entering into an agreement with ASEAN (Singapore is a start)
 - But small market size and government's lack of capacity makes this unlikely
- BIMSTEC agreement may be easier, but requires India and Thailand, the big actors, to agree