TRADING FOR DEVELOPMENT IN THE AGE OF GLOBAL VALUE CHAINS
Why Care?

Global Value Chains:

- Boosted per capita incomes and created jobs in many developing countries
- Contributed to reduce poverty to historical low levels
- Can continue to create development if developing countries undertake deeper reforms and industrial countries pursue open and predictable policies
1990-2008: Unprecedented expansion of Global Value Chains

- GVCs grew swiftly, as manufacturers extended production beyond national borders
- Drivers: technological advances and lower trade barriers induced
Since 2008, expansion has slowed

- Decline in overall economic growth and investment
- Maturation of high-growth markets (e.g., China)
- Slowing pace and reversal of trade reform
What is Different about Global Value Chains?
What is a global value chain?

**COUNTRY 1**
Forward participation

Raw materials
Services inputs

**COUNTRY 2**
Forward and backward participation

Parts and components
Semi-finished goods

**COUNTRY 3**
Backward participation

Finished goods

EXPORTS

EXPORTS

EXPORTS FOR CONSUMPTION
Framework for GVC-led development
All countries participate, but in different ways

GVC linkages, 2015
- Low participation
- Limited commodities
- High commodities
- Limited manufacturing
- Advanced manufacturing and services
- Innovative activities
Is there still a GVC-path to development?

Outcomes
GVC firms are more productive than one-way traders or non-traders

Productivity difference between trading and nontrading firms (%)

- Ethiopia
  - Export and import
  - Export only
  - Import only

- Vietnam
  - Export and import
  - Export only
  - Import only

- Developing countries
  - Export and import
  - Export only
  - Import only
Incomes grow most when countries break into simple manufacturing
In Ethiopia, capital intensity is higher, but so is employment growth.
In Vietnam, poverty reduction is greater where GVC firms are present
Technologies are changing production and distribution
Increased adoption of industrial robots in the North has promoted imports from the South.

Change in parts imports from developing countries (%)

- Automotive
- Rubber and plastics
- Metal
- Electronics
- Machinery
- Chemicals
- Food products
- Other manufacturing
- Wood, paper, and printing
- Textiles
- Mining
- Education
- Agriculture
- Construction
- Utilities
- Other nonmanufacturing

More parts imported from South
3D printing has increased trade
What are the costs of participation?
GVC gains are distributed unequally across and within countries

- Lead GVC firms experience rising markups and profits
- Supplier firms in developing countries are being squeezed
- GVCs contribute to the declining labor share within countries
- GVCs rewards skilled over unskilled workers
- Women and youth are generally found in lower value-added segments
- Raising tax revenues is more challenging
Increasing GVC participation is associated with rising markups in developed countries but falling markups in developing countries.
GVCs have contributed to the declining labor share within countries

![Graph showing labor share over GDP (%)](image)

### Factors contributing to labor share decline (percentage points)

- **Total**
- **World demand**
- **Domestic within-industry factors**
- **GVCs**
GVCs favor women’s employment... but don’t break glass ceilings

Female workers in total workers, relative to non-GVC firms (%)

Production workers

Administrators or sales workers

Probability of female owners or managers, relative to non-GVC firms

Majority ownership

Top management

-0.20 -0.16 -0.12 -0.08 -0.04 0
Raising tax revenue is challenging in today’s globalized world

- Corporate income taxes have declined by nearly 50 percent since 1990
- As a share of GDP, non-OECD countries lose the most from profit shifting
Digital market places are on the rise, fostering participation and concentration

- Platform firms and e-commerce have uneven benefits
- Platforms create new regulatory challenges
GVCs can also be a mixed blessing for the environment

Disadvantages
• Excess transport
• Pollution haven
• Waste

Advantages
• New environmental goods
• Lead firms push standards upstream
While GVCs are a mixed blessing for the environment, production-related CO2 emissions drop in most countries.
GVCs are associated with... more shipping and more waste

The world produced 50 million metric tons of e-waste in 2018
Relational GVCs help alleviate environmental concerns

Total reported savings generated by the Swedish Textile Water Initiative in 5 partner countries, 2015-17

- Water (m3): 10,521,557
- Electricity (kWh): 79,587,701
- Thermal use (metric tons): 22,582,559
- Chemical use (kg): 27,360,768
- Waste water (m3):
- Natural gas (m3):
- Fossil fuel (metric tons):
- Coal (kg):
- GHG emissions (metric tons): 10,144,135
What are the drivers of participation and the appropriate response?
GVC-led development: Drivers and policies for participation
Factor endowments matter: foreign capital tends to increase with GVCs, especially in limited manufacturing.
Factor endowments matter: low-skilled labor is critical at early stages of GVC engagement.
Market size matters: trade liberalization can expand market size

Manufacturing tariffs are lower and preferential trade partners more in countries in more advanced stages of GVC participation
Improving customs and introducing electronic systems are as important as infrastructure for African trade.

Geography matters: overcoming remoteness by improving connectivity.
Institutions matter: Deep trade agreements are linked to GVC growth

- GVCs trade is more than four times larger between countries sharing a deep trade agreement than between countries with no trade agreements
What are the impacts of removing specific constraints?

If Africa...

<table>
<thead>
<tr>
<th>Region</th>
<th>Reduced Tariffs to Level in ECA (Best Performer)</th>
<th>Impact on GVC Part. Share in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia &amp; Pacific</td>
<td>-2.62</td>
<td>5%</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>-3.26</td>
<td>7%</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>-5.75</td>
<td>16%</td>
</tr>
<tr>
<td>South Asia</td>
<td>-7.98</td>
<td>20%</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>-5.54</td>
<td>13%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Region</th>
<th>Increased FDIs to Level in ECA (Best Performer)</th>
<th>Impact on GVC Part. Share in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia &amp; Pacific</td>
<td>0.13</td>
<td>1%</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>0.20</td>
<td>2%</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>0.10</td>
<td>1%</td>
</tr>
<tr>
<td>South Asia</td>
<td>1.32</td>
<td>16%</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>1.44</td>
<td>16%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Region</th>
<th>Increased Political Stability to Level in EAP (Best Performer)</th>
<th>Impact on GVC Part. Share in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Europe and Central Asia</td>
<td>0.07</td>
<td>1%</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>0.01</td>
<td>0%</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>1.15</td>
<td>28%</td>
</tr>
<tr>
<td>South Asia</td>
<td>0.89</td>
<td>20%</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>0.39</td>
<td>8%</td>
</tr>
</tbody>
</table>
## Not a one size fit all — policy priorities evolve

<table>
<thead>
<tr>
<th>Commodities to limited manufacturing</th>
<th>Limited manufacturing to advanced manufacturing and services</th>
<th>Advanced manufacturing and services to innovative activities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fundamentals</strong></td>
<td>Policy priorities</td>
<td></td>
</tr>
<tr>
<td><strong>Endowments</strong></td>
<td>Foreign direct investment: adopt supportive investment policy and improve the business climate</td>
<td>Finance: improve access to banks</td>
</tr>
<tr>
<td></td>
<td>Labor costs: avoid rigid regulation and exchange rate misalignment</td>
<td>Finance: improve access to equity finance</td>
</tr>
<tr>
<td><strong>Market size</strong></td>
<td>Access to inputs: reduce tariffs and NTMs; reform services</td>
<td>Technical and managerial skills: educate, train, and open to foreign skills</td>
</tr>
<tr>
<td></td>
<td>Market access: pursue trade agreements</td>
<td>Advanced skills: educate for innovation and open to foreign talent</td>
</tr>
<tr>
<td><strong>Location</strong></td>
<td>Trade facilitation and transport liberalization</td>
<td>Advanced logistics services</td>
</tr>
<tr>
<td><strong>Institutions</strong></td>
<td>Governance: promote political stability</td>
<td>Governance: improve policy predictability and enforcement</td>
</tr>
<tr>
<td></td>
<td>Standards certification: establish conformity assessment regime</td>
<td>Contracts: enhance enforcement</td>
</tr>
</tbody>
</table>
Facilitating GVC participation: factor markets

- Avoid excessive regulations and overvalued exchange rate

Manufacturing labor costs are out of line with national income levels in Sub-Saharan Africa but not in Bangladesh
Facilitating GVC participation: standards

- Higher quality standards help knowledge and technology transfer from FDI to firms and workers in the host country

Certification has had long lasting effects on quality in Mali’s cotton sector

- Difference = 23.71 pp, of which 8.75 pp attributable to Fairtrade quality certification

Average % of "premium quality" cotton

<table>
<thead>
<tr>
<th></th>
<th>Series1</th>
<th>Series2</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>97.84</td>
<td>82.88</td>
</tr>
<tr>
<td>2</td>
<td>55.91</td>
<td>32.2</td>
</tr>
</tbody>
</table>

difference = 14.96 percentage
Facilitating GVC participation: linkages

- In undertaking proactive (industrial) policies minimize use of “traditional” instruments (subsidies, local content requirements)
- Focus instead on promoting domestic supply chain linkages and FDI spillovers

In Bangladesh, local suppliers grew as FDI grew from 1985 to 2003
### Facilitating GVC participation: SEZs

<table>
<thead>
<tr>
<th>Driver for Success</th>
<th>Hawassa Industrial Park (Ethiopia)</th>
<th>Garri Free Zone (Sudan)</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Legal and regulatory framework</td>
<td>✓</td>
<td>✗</td>
</tr>
<tr>
<td>✓ Government support</td>
<td>✓</td>
<td>✗</td>
</tr>
<tr>
<td>✓ Zone-level governance</td>
<td>✓</td>
<td>✗</td>
</tr>
<tr>
<td>✓ Industrial infrastructure</td>
<td>✓</td>
<td>✗</td>
</tr>
<tr>
<td>✓ Location and connectivity</td>
<td>✓</td>
<td>✗</td>
</tr>
<tr>
<td>✓ Human resources</td>
<td>✓</td>
<td>~</td>
</tr>
<tr>
<td>✓ Market demand</td>
<td>✓</td>
<td>~</td>
</tr>
</tbody>
</table>
GVC-led development: Policies for benefitting from GVCs
National policies can help ensure benefits are shared and sustained

- Expand adjustment assistance
- Support active labor market programs to assist with retaining
- Avoid rigid labor market regulation

Industrial development was uneven across regions of Mexico during the period of strong international market integration

Regional share of manufacturing employment (%)
Working with firms improves working conditions and health and safety standards, among other benefits

Working conditions improved in apparel sector firms participating in the ILO-IFC Better Work Vietnam program

Average non-compliance rates, by years of firms participation in program (%)

Average non-compliance rates, all firms (%)

2015: New policy of public disclosure of firms that failed to meet key labor standards announced.

2017: New policy implementation started.
Work with firms and the international community to protect the environment

Pricing the environment would reduce the misallocation of resources:

- Reduce energy and production subsidies
- Encourage innovation in environmental goods
- Tax carbon
- Stronger regulations on specific industries and pollutants
International cooperation is critical

• GVC goods criss-cross borders multiple times >> greater cost of protection

• Coordinated reduction of trade barriers is even more important

• Open investment climate (especially important in capital-scarce countries)
All countries have benefited from the rules-based trade system

Continuing trade conflict and policy uncertainty could push more than 30 million people into poverty

Global income could fall by as much as $1.4 trillion
Deepen traditional trade cooperation

Reduce tariff and nontariff barriers, especially in agriculture and services (especially air and maritime)

Combat tariff escalation

Stronger rules on subsidies and SOEs

Reconsider special and differential treatment
Look beyond trade to keep trade open and beneficial

Taxes

International data flows

Competition

Environment