The Strategic Role of Asian Countries in the Global Value Chains

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ABSTRACT

Asia is considered as the most dynamic continent in the world. Asia is also a huge market for attracting investment. It is true that many Asian countries have participated in the global production networks of multinational corporations. But not all of these countries could catch up with the world development because within Asian countries, there are conflicts in co-operation among countries, especially in many aspects such as religions, languages, ethnics, and culture... And this explained why many Asian countries could not participate and collaborate effectively in the global value chains even they have many strategic advantages. This paper, therefore, will depict the strategic role of Asian countries in the global value chain as well as the current linkages among these countries in the chains. Ultimately, this paper will imply the necessity of a reconciled Asia for the best optimization in the global value chains.

Keywords: Global Value Chain; Asia Value Chain; Asia Countries GVC; Asia Strategic Role.

Introduction

During the past three decades, the development of highly integrated global value chains (GVCs), in which products are supplied, manufactured and distributed across national boundaries, have created a new form of division of labor and other resources among Asian economies, especially in Northeast and South-East Asia.[2] For many Asian economies today, imports are increasingly a key complement of local production and exports. Many Asian countries have increasingly participated in GVCs at different levels of participation and served the GVCs with different advantages. Geographically, Asian continent makes up 8.7% of the Earth's total surface area. In the West, Asia is bordered by Europe, the eastern coastline of the Mediterranean Sea. In the East, it is bordered by the Pacific Ocean, and an almost endless stretch of bays and seas. The Arctic Ocean and a handful of seas front the Northern border, while the Bering Sea separates Asia from North America. To the Southwest, the Red Sea and the Isthmus of Suez separate the Asian continent from Africa. The Indian Ocean fronts most of Asia's southern borders, along with a series of bays, gulfs and seas. This region is rich in natural resources such as tin, petroleum, rubber, tea, spices, and valuable woods, which enables them to participate in GVCs as the main providers of raw materials. And due to the convenient natural position, the Southeast Asia is a vital crossroads of trade and commerce among Asia, Europe and America, which makes it an ideal region for outsourcing labeling, packaging and exporting. As the largest and most populous

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[2] IDE-JETRO, "Trade Patterns and Global Value Chains in East Asia: From Trade in Goods to Trade in Tasks," (Geneva: WTO, 2011).

continent in the world with just over 3.8 billion people, Asia is composed of a wide variety of ethnic groups, cultures, environments, economies, historical ties, and governmental systems. It is also the largest market of low-cost labor in the world, where all the MNCs want to locate their labor-intensive factories. In terms of political and economic advantages, Asia already had many bilateral and multilateral agreements such as ASEAN Free Trade Area (AFTA), FTA (ASEAN+3, ASEAN+1)… Thanks to those advantages, Asia nowadays has been recently known as the world's commodities trading hub and a promising destination for top investors.

Asian Countries in the Global Value Chains

GVCs first emerged as regional supply chain in East Asia in the 1970s, when American and Japanese investors took the lead positions in the region and triggered flying geese pattern of investments and trade there. At that time, a US semi-conductor firm, whose production was very labor intensive, located its assembly factories in East and South East Asia, and Japanese companies set up low-cost transistor radio production in Taipei—China and in Hong Kong—China (Khoi, 2009). Since then, Japanese investors expanded their production factories in a large number of countries in East Asia and later in Southeast Asia to access and to leverage locational advantages and develop export platforms for their components. The final assembly took place in a third country from where the finished products were exported either back to the home country or to the global markets under the Japanese brands. This fragmentation of production improved the cost competitiveness of the final products, which were then able to compete with the products from other developed countries.

Overtimes, MNCs from other developed countries, also aiming at improving their cost competitiveness, flocked the region and soon spread to other regions as well. What emerged from this phenomenon were GVC with production of a product spread across countries, regions and continents gathering cost advantages to become globally competitive.[3]

After years of participating in GVC, different Asian countries have applied different types of participation. In terms of GVC governance, Asian countries can be realized as two distinguished groups, namely "governing group" and "governed group."

For the Governing Group, obviously, Asian entrepreneurs from Japan, China, Korea, Taiwan and India establish a large number of MNCs. According to the 2013 Fortune Global 500 report, 25.8% (equivalent to 129 companies) of the 500 big companies are from Asian countries. It also showed the increasing trend in the number of big MNCs in the future. For examples, in 2013, 90 Chinese companies made to the list, up from 73 in 2012, 61 in 2010, and 34 in 2008; three Chinese companies made to the top ten, beating the United States and 12 Chinese

[3] Rashmi Banga, "Measuring Value in Global Value Chains," Background Paper RVC-8, *Development Oriented Integration in South Asia*, (Geneva: UNCTAD, 2013), http://unctad. org.

companies stand in top 100. Japan presents 10 big brand names standing in top 10 of the list. Nevertheless, it is also witnessed new appearances of new emerging companies from India, Taiwan, Singapore, Thailand and Malaysia.

While those local MNCs create a large demand on outsourcing the production part or assembly plants to other Asian developing countries, the rest of Asia still account for downstream processes of GVC and take a small share in the final profits of products. As proved in the research of Gereffi and Korzeniewicz,[4] in low-wage labor-incentive production, the principal profits are not realized in manufacturing itself, but rather in the corporate coordination and control of the entire "global assemble line," especially design, marketing and retailing, which are typically done by MNCs based in core countries (including Western developed countries and Asian developed countries or Asian emerging economy).

Discussing about the main roles of Asian countries in GVCs, it is clear that in Asia production network, leading countries with advanced technology and the operation of big local MNCs such as Japan, South Korea, Taiwan, Singapore, China, India, take the second most important role in creating demands for outsourcing, offshoring and new markets seeking in Asia. Those countries act as governors of GVCs in the region, they increase regional investments and improve intra-trade between regional countries, simultaneously. As a good example, Japan faces intermediate goods surplus with all of its Asian trading partners containing South Korea, Taipei, China. It is the single most important supplier to over a third of Indonesia's intermediate goods imports from Asia. For high technology equipment or electronics as well as capital goods, Japan still plays a dominant role. Hong Kong (China) and Singapore also have become the core distribution and logistics hubs in Asian production and trade networks. As part of their business strategies, enterprises may also outsource some of their non-core business functions to other Asian developing countries.

On the other hand of the trend of specializing on core activities that makes outsourcing inevitable, small Asian developing countries (many regions of China, Thailand, Taiwan, and Malaysia are counted in) take the main responsibility for low-level of production. In those countries, there usually are "export processing zones" (EPZs), which are industrial zones with special incentives set up to attract foreign investors, in which imported materials undergo some degree of processing before re-exported (Khoi, 2012). In this complex chain of production functions, small Asian developing countries still remain primarily a common characteristic as "export platform" for simple low-technology, labor-intensive goods made by low-wage unskilled workers.

[4] Gary Gereffi and Miguel Korzeniewicz, eds., *Commodity Chains and Global Capitalism*, (Westport, CT: Praeger, 1994).

Up to now, the GVCs trend shows the larger and larger dependence of developed countries in the "Asia Factory." As an example, intermediate inputs from Asian countries represent 56% of goods trade and 73% of services trade in OECD countries[5] and imports of intermediate goods increasingly determine the export competitiveness of countries.[6] For the majority of OECD countries, more than half of the value of exports originates from products traded in the context of global value chains.[7] The research of Timmer et al.[8] showed that vertical specialization as measured by the share of imported intermediate inputs in manufacturing gross output has increased for almost all developed and emerging economies. In particular, East Asian economies are characterized by increasing two-way integration, i.e. trade in intermediate inputs increased in both directions between Japan, South Korea and Taiwan on the one hand and China on the other hand.

By 2011, intermediate goods have comprised over 50% of exports and over 60% of imports in Asia, since the year 2000.[9] Therefore, it is very important to measure trade in value-added terms, rather than just looking at the gross figures. By measuring exports in terms of their import content—we can understand domestic value-added. It becomes clear that so many products today comprise inputs from a number of countries. The reality which is not seen in gross trade statistics is that products today are "made in the world," rather than made in a single country. To understand how large the number of Asian countries joining in GVCs, UNCTAD has created a dataset containing all countries based only on gross levels of trade. Thus, there are uncertainties embedded in results, but this is to date the only attempt at estimating all developing countries' integration in GVCs including Asian countries. According to UNCTAD, there are some of elementary findings:

- In recent years, Asian countries' share in trade measured by value added is twice as much as it was in the past.
- There is great variation in Asian economies' GVC participation. The small number of examples from West and Central Asia found in the paper reinforces this conclusion.

[5] Sebastien Miroudot, Rainer Lanz, and Alexandros Ragoussis, "Trade in Intermediate Goods and Services," OECD Trade Policy Working Paper, No. 93 (2009).
[6] Andrea Beltramello, Koen De Backer, and Laurent Moussiegt, "The Export Performance of Countries within Global Value Chains (GVCs)," No. 2012/2, (OECD Publishing, 2012).
[7] Koen Backer, and Sébastien Miroudot, "Mapping Global Value Chains," (OECD Publishing, 2013).
[8] M. P. Timmer, A. Erumban, B. Los, R. Stehrer, and G. de Vries, "New Measures of European Competitiveness: A Global Value Chain Perspective," Groningen Growth and Development Centre, (University of Groningen, The Netherlands, 2012).
[9] IDE-JETRO, "Trade Patterns and Global Value Chains in East Asia: From Trade in Goods to Trade in Tasks," (Geneva: WTO, 2011).

	Import		Export	
	P&C trade	Network trade	P&C trade	Network trade
Emerging Asia	694, 987	1,399,976	788,501	1,733,803
Emerging Europe	229,087	341,216	194,651	276,238
Armenia	210	512	38	46
Azerbaijan	1,337	2,080	43	36
Georgia	590	1,772	31	675
Kazakhstan	5,245	9,059	409	616
Kyrgyz Republic	317	1,017	77	154
Malaysia	45,666	69,489	44,230	84,219
Slovakia	19,493	27,368	16,246	37,148
Vietnam	**13,816**	**28,123**	**10,678**	**29,099**

TABLE 1: Trade in Parts and Components, and Value of Network Trade.[10] (USD million, 2012)

One strategy recommended and applied by an increasing number of SMEs in developing countries is that cooperation enables to create a difference and serve as a way to drive up the value chain. Yet, it is more beneficial to consider beyond the firms as actors to check the role of public and private institutions in order to nurture an appropriate environment for business activities as well as learn experience and maintain promotion such as the policy of export promotion.[11] Other important fields of supporting between countries in global chain are technological and financial support, training course.[12] Cooperation and the creation of local external economies, through promoting clustering and denser horizontal inter-firm relation, exhibit a significant way to counterbalance. Firms can cooperating or enjoy business associations and other emerging group, small and medium enterprises so as to improve investment capital and

[10] Source: Authors' calculations, based on COMTRADE data.
[11] Meenu Tewari, "Successful Adjustment in Indian Industry: The Case of Ludhiana's Woolen Knitwear Cluster," *World Development* 27, no. 9 (1999): 1651-1671; Luiza Bazan and Lizbeth Navas-Alemán, "The Underground Revolution in the Sinos Valley: A Comparison of Upgrading in Global and National Value Chains," *Local enterprises in the global economy: Issues of governance and upgrading* 3 (2004): 110-139.
[12] Jörg Meyer-Stamer, Claudio Maggi, and Silene Seibel, "Improving Upon Nature: Creating Competitive Advantage in Ceramic Tile Clusters in Italy, Spain and Brazil," (2001).

bargaining power, which are required factor for upgrading successfully.[13] The integration of new suppliers into global value chains simultaneously raises coordination challenges. As mentioned above, there are three factors determining the governance of value chains: the complexity of information, the ability of codifying transaction and the effectiveness of industry, all of which are the keys to open the door for government's restrictions and corporate strategy.

Another aspect of problem, the literature capitalism becoming widely from political science, [14] simultaneously indicates that national-level restriction in finance and corporate governance deeply impact the industrial characters. Moreover, various geographically rooted characteristics are implemented oversea, as foreign direct investment (FDI) in Asian developing countries from multinational corporations or non-government profits. It is necessary for government of Asian developing countries to consider of emerging organizational forms like large-scale outsourcing, which is an efficient long-standing corporate strategies and institutions.

The Governance of Global Value Chain in Asia

In fact, the headquarters of big MNCs are mostly located in three regions, namely North America, Europe and Asia, in which, 28% of MNCs is located in Asia. The first two regions and the 28% of the latter are primarily the centers of demand for outsourcing labor intensive stages and lower-level production, while the 72% left of the latter act as the center of supply for low-cost labor and geographical advantages.

Chain governance or pattern of a chain impacts upgrading opportunities and it is closely involved in the extent to which the consumer determines the product or the risk of supply chain failure. Hence, it is link generates between the kinds of products and the buyer degree of control over suppliers. Knowledge-intensive seemly distinguishes with standardized manufacturing or the main material resource of products and the final structure of the chain. The term upgrading here is with respect to the three possible upward moves in the value chain. Firstly, it refers to efficiency growth of the production process, such as through reorganization or investing in more advanced technology. Secondly, product upgrading correlates a shift to more complicated product lines with rising unit value. Finally, functional upgrading is the process by which firms obtain new, more strategic functions in the chain such as design or marketing or by which they switch buyers, by moving to those chains to move complex market.[15] The relationship between different

[13]Hubert Schmitz, "Does Local Co-operation Matter? Evidence from Industrial Clusters in South Asia and Latin America," *Oxford Development Studies* 28, no. 3 (2000): 323-336.
[14] Suzanne Berger and Ronald Philip Dore, eds., *National Diversity and Global Capitalism*, (Ithaca: Cornell University Press, 1996).
[15] John Humphrey and Hubert Schmitz, "Governance and Upgrading: Linking Industrial Cluster and Global Value Chain Research," Vol. 120, (Brighton: Institute of Development Studies, 2000).

forms of buying relationships and the scopes for small and medium enterprises (SMEs) upgrading has been developed, establishing for five types of chain governance (see below table).

Markets	Describe a relationship where there are potentially many buyers and sellers for equivalent products, even though particular buyers and sellers may engage in repeat transactions. This implies that the producer either makes a standard product or designs the product without reference to the needs of any particular customer. The customer is a "design taker." It also implies that there is no transaction-specific investment required by either party to the transaction.
Modular value chains	Occur when the supplier and buyer join complementary competences. They may jointly design the product, using their different competences, and transaction-specific investment will be made. This type of relationship is particularly evident when both buyer and supplier are innovators, close to the technology or market frontiers, but this situation also arises when firms focus on their core competences and outsource important activities to suppliers.
Captive value chains	Small providers are transitionally dependent on much larger consumers. Producers obtain considerably switching costs and are, therefore, "captive." The outstanding character of that network is the high degree of taking charge by leading firm.
Relational value chains	Occur when one party to the transaction (usually the buyer) exercise a high degree of control over the other. This often includes specifying the design (or the general specification) of what is to be produced and also process parameters such as quality systems. Materials, etc. The introduction of monitoring and control procedures and the transmission of product design features require transaction specific investment.
Hierarchical relationships	Occur when the buyer takes ownership of the producers in the cluster on establishes its own companies within the cluster, or when firms in the cluster integrate forwards, establishing production facilities in the other countries.

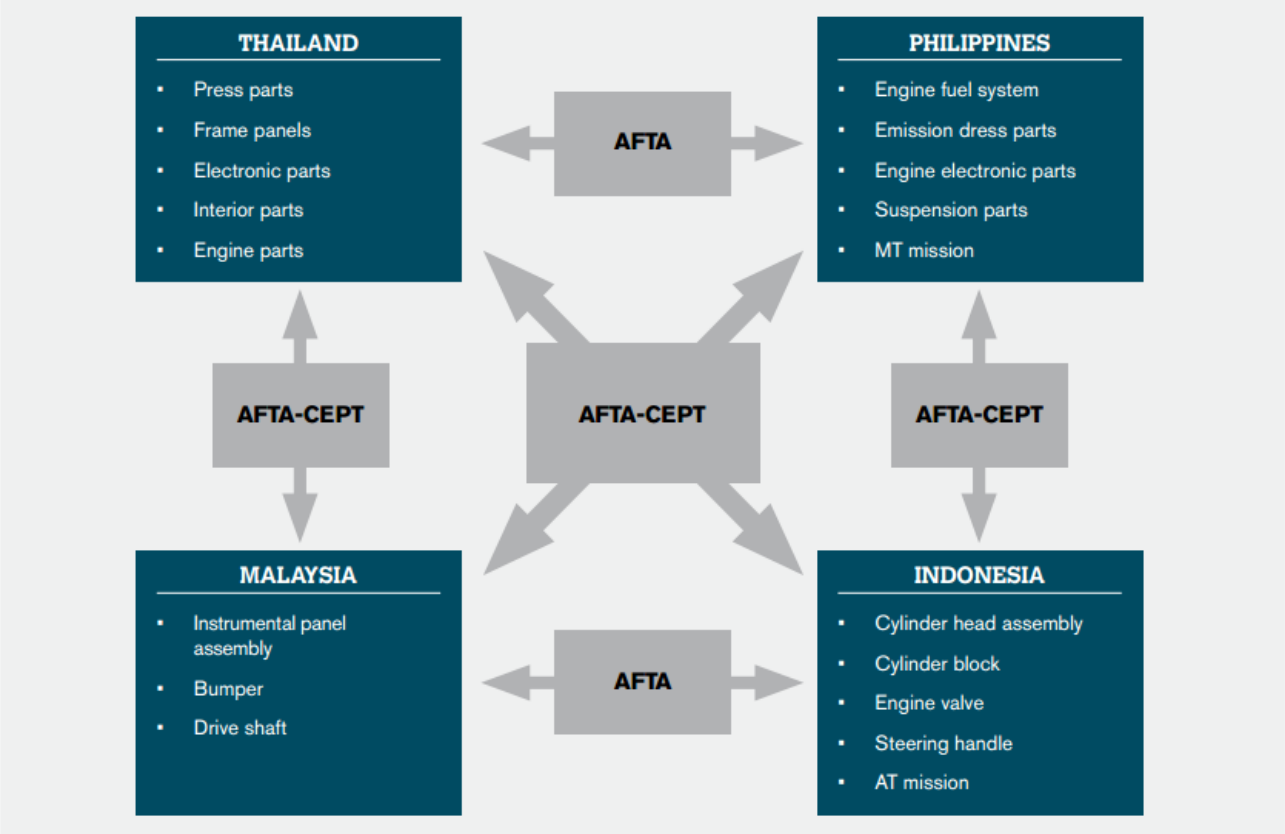
TABLE 2: Five Types of Chain Governance.[16]

When investing in Asia, MNCs firms may pursue two different types of governance: some choose to pursue the logic of trade in tasks and geographical fragmentation by staging production along a global supply chain (known as vertical specialization) while others produce the same type of goods that they do at home to enter Asian markets basing on the "build – where – you – sell" strategy (known as horizontal diversification of production). In particular, whilst the automotive consumer is served with cars produced by horizontal diversification: a Mercedes produced in the United States probably differs from the other in France; the electronics industries

[16] Ibid.

are accounted as a representative for vertical specialization pattern, which makes firms supply branded products in final market. In fact, many foreign firms operating in East Asia have progressively adopted the characteristics of both vertical and horizontal governance of GVCs.[17] And thanks to the convenient trade policies of Asian countries, as well as their variety regional contractual, they allow MNCs to take advantages from the flexibility in sourcing components from various countries and export the resulting final goods. Therefore, both horizontal and vertical production pattern can co-exist together in a GVCs governance strategy in Asia. Take Japanese automobile assemblers as an example, Japanese company established its GVC according to the key parts from four Asian countries, leveraging the advantages of the Asian FTA.

Complementary parts supply system of an automobile assembler in ASEAN



Note: the ASEAN Free Trade Area - Common Effective Preferential Tariff (AFTA-CEPT) is a cooperative arrangement among ASEAN member states to reduce intra-regional tariffs and remove non-tariff barriers.

Source: Hiratsuka (2010).

FIGURE 1: Japanese Supply System of Automobile Assembler in Asia.

[17] IDE-JETRO, "Trade Patterns and Global Value Chains in East Asia: From Trade in Goods to Trade in Tasks," (Geneva: WTO, 2011).

During the time that Japanese companies located its value chain in Asia (from 1970s to 2001), the proportion of Japanese companies' overseas production in Asia went to local customers in Asia was 40% of total product. After years, as household income in developing Asian countries rose, so did FDI for horizontal diversification, the figure reached 62%.[18] Therefore, Japanese company has successfully built a domestic market with related consumption capacity in the developing countries' territories.

It is clear that while small Asian developing countries (such as Myanmar, Vietnam, Indonesia, some regions of China and so on) play a predominant visible role in global trade of global manufactured goods, in reality it is the part of a highly integrated and sophisticated intra-Asian patchwork of production and specialization.[19] Prior to China's reception of huge amounts of FDI in the 1990s, Japanese, Korean, Taiwanese and Western investments had poured into a number of the ASEAN countries, especially Malaysia and Thailand. Penang in Malaysia emerged as the global IC (integrated circuit) hub, while Thailand focuses especially on automotive components. Other ASEAN countries also became included in the regional production process. Thus while the label "Made in China" has become globally ubiquitous, in fact in many cases it is not accurate and instead should read "Made in Asia—Finally Assembled in China."

The table on the next page revealed a trend that Asian merchandise's exports are mostly intra-regional trade. The volume of regional trade of Asia is always as high as twice that of trade to the rest of the world, as it is shown in the table of intra and inter-regional merchandise trade.

[18] Ibid.
[19] Ibid.

Origin	Destination							
	North America	South and Central America	Europe	CIS	Africa	Middle East	Asia	World
Value								
World	**3035**	**787**	**6564**	**550**	**580**	**714**	**5333**	**17930**
North America	1151	217	380	18	38	75	488	2371
South and Central America	187	202	128	8	21	17	172	750
Europe	492	124	4383	245	211	208	643	6385
Commonwealth of Independent States (CIS)	37	7	430	149	14	20	127	805
Africa	74	30	240	2	81	17	160	630
Middle East	118	11	148	7	39	116	732	1349
Asia	975	196	855	121	177	260	3012	5640
Share of regional trade flows in each Region's total merchandise exports								
World	**16.9**	**4.4**	**36.6**	**3.1**	**3.2**	**4.0**	**29.7**	**100.0**
North America	48.6	9.1	16.0	0.8	1.6	3.2	20.6	100.0
South and Central America	24.9	26.9	17.0	1.1	2.8	2.3	23.0	100.0
Europe	7.7	1.9	68.6	3.8	3.3	3.3	10.1	100.0
Commonwealth of Independent States (CIS)	4.6	0.9	53.4	18.5	1.7	2.5	15.7	100.0
Africa	11.7	4.8	38.2	0.3	12.8	2.7	25.3	100.0
Middle East	8.7	0.8	11.0	0.5	2.9	8.6	54.2	100.0
Asia	17.3	3.5	15.2	2.1	3.1	4.6	53.4	100.0
Share of each region's exports in world merchandise exports to the region								
World	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
North America	37.9	27.6	5.8	3.3	6.5	10.5	9.2	13.2
South and Central America	6.2	25.6	1.9	1.5	3.6	2.4	3.2	4.2
Europe	16.2	15.7	66.8	44.6	36.3	29.2	12.0	35.6
Commonwealth of Independent States (CIS)	1.2	0.9	6.6	27.0	2.4	2.8	2.4	4.5
Africa	2.4	3.9	3.7	0.3	13.9	2.4	3.0	3.5
Middle East	3.9	1.4	2.3	1.3	6.8	16.2	13.7	7.5
Asia	32.1	24.9	13.0	21.9	30.4	36.5	56.5	31.5
Share of regional trade flows in world merchandise exports								
World	**16.9**	**4.4**	**36.6**	**3.1**	**3.2**	**4.0**	**29.7**	**100.0**
North America	6.4	1.2	2.1	0.1	0.2	0.4	2.7	13.2
South and Central America	1.0	1.1	0.7	0.0	0.1	0.1	1.0	4.2
Europe	2.7	0.7	24.4	1.4	1.2	1.2	3.6	35.6
Commonwealth of Independent States (CIS)	0.2	0.0	2.4	0.8	0.1	0.1	0.7	4.5
Africa	0.4	0.2	1.3	0.0	0.5	0.1	0.9	3.5
Middle East	0.7	0.1	0.8	0.0	0.2	0.6	4.1	7.5
Asia	5.4	1.1	4.8	0.7	1.0	1.5	16.8	31.5

TABLE 3: Intra- and Inter-regional Merchandise Trade, 2012 (Billion dollars and percentage).[20]

[20] Source: International Trade Statistics 2013 by World Trade Organization.
Note: Commonwealth of Independent States (CIS).

The key determinants of global value chain governnace includes three factors as follow: complexity of information and knowledge transfer, ability of codifying transactions and the capabilities in supply-base are allowed only two values—high or low. As a result, each governance kind supplies trade-off between advantage and disadvantage of outsourcing in their own ways.

Governance type	Complexity of transactions	Ability to codify transactions	Capabilities in the supply-base	Degree of explicit coordination and power asymmetry
Market	Low	High	High	Low ↓ High
Modular	High	High	High	
Relational	High	Low	High	
Captive	High	High	Low	
Hierarchy	High	Low	Low	

TABLE 4: The Key Determinants of Global Value Chain Governance.[21]

It is true that the more knowledge-intensive a product is, the more dependent the buyers become on highly specialized and reliable suppliers and vice versus. Consumer's payment willingness switches from one supplier to another solely base on cost. All conditions considered, buyers seem to seek a relationship based on cooperation with suppliers and strive improving the learning process of their supplier base. The software and electronics industries can be seen as relevant evidence in this regard. Buyer-provider relationship in these industries is characterized by interdependent, but not dominate.

Obviously, the global-scale adjustments and the "rule of the game" asset have strong influence on the shape and tendency of changes in the global value chains. In a broaden categories of industries, from electronics to household equipment including section 807 and most-favored-nation status (MFN status) give incentive to carry out the geographical fragmentation of global value chains. Yet political pressures in developing countries containing the Asian-developing countries to spread risk through geographical diversification, seems to

[21] Source: Gary Gereffi, John Humphrey, and Timothy Sturgeon, "The Governance of Global Value Chains," *Review of International Political Economy* 12, no. 1 (2005): 78-104.

make those industries to more fragmented than it would be if production decisions depended mainly on economic criteria alone.[22]

While there are a huge number of factors that impact the evolutions of the global economy, global value chain is significantly affected by the variables internal to the model in term of shape and governance, no matter which the institutional context it is situated for. The governance of framework as recommend, tend to move a more systematic acknowledge of global value chains, but much maintains to be completed. One of the most outstanding aspects is the innovation of policy tools for industrial upgrading involving the framework.[23] Value chain indicates that the developed country markets have become more and more dependent on integrating global production networks with developing countries. Hence, it is beneficial for Asian countries to understand the governance and the profit in the global value chains to efficiently and dynamically cooperate in the future.

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