

# Trade Adjustment in Asia: Past Experience and Future Risks

Matthias Helble, Senior Economist, Co-Chair, ADBI

UNESCAP Regional Dialogue on  
«Enhancing the Contribution of Preferential Trade Agreements to  
Inclusive and Equitable Trade»

22 June, 2017

# The Context

Brexit and Trump's election expressions of non-inclusive (perceived) globalization.

How to ensure that globalization is inclusive in Asia?

1. Past experience with trade opening in Asia.
2. Prospects for future trade adjustment.
3. Policies to ensure that trade integration delivers for everyone.

# Asia's past and current experience with trade opening



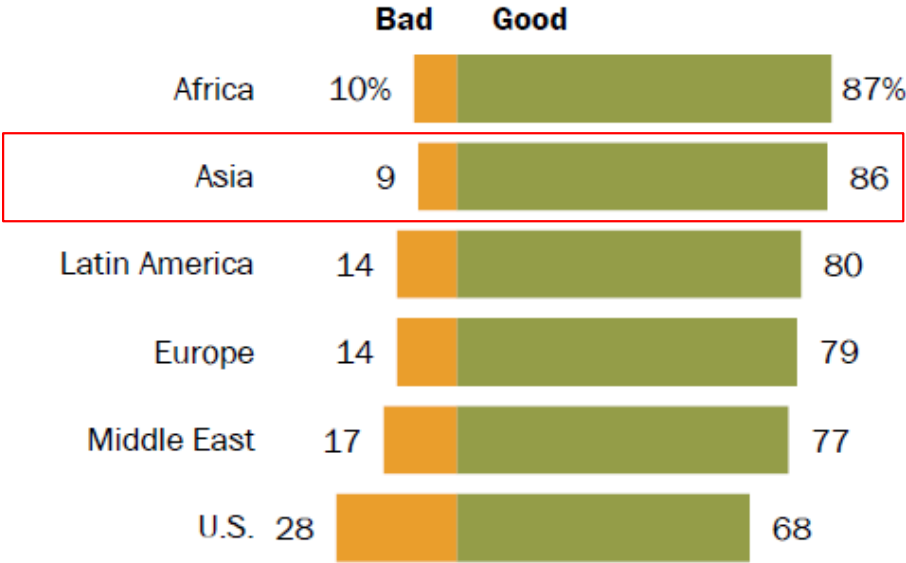
# So far, Asia has been embracing globalization...

- Large majority of Asians believes that **trade is good**, that it creates jobs and boosts wages (Pew Research Center, 2014).
- Stance is outcome of **positive experience** with globalization.
- **Export oriented growth strategies** allowed many Asian economies to successfully integrate into the global economy.
- **Benefits trickled down** and lifted hundreds of millions out of poverty.

# More than 85% of Asians believe in trade...

## Growing Trade Seen Positively

*Growing trade and business ties with other countries is \_\_\_ for our country*



Note: Median percentages by region. Russia and Ukraine not included in Europe median.

Source: Spring 2014 Global Attitudes survey. Q27.

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# Strong support for TPP in developing Asia

## Vietnam Most Enthusiastic Among TPP Countries

	<b>Trade is good</b>	<b>Trade increases wages</b>	<b>Trade creates jobs</b>	<b>Trade lowers prices</b>	<b>Foreign companies buying is good</b>	<b>Foreign companies building factories is good</b>
	%	%	%	%	%	%
Vietnam	95	72	78	31	59	80
Malaysia	87	47	57	9	45	78
Chile	85	27	52	28	53	68
Peru	81	42	55	24	59	70
Mexico	71	31	43	24	50	69
Japan	69	10	15	27	17	58
U.S.	68	17	20	35	28	75

Source: Spring 2014 Global Attitudes survey. Q27-Q32.

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# Asia has been able to adjust relatively well...

Adjustment has come at costs, but was facilitated by:

- Investment in **education and health**
- Investment in **infrastructure**
- Relative simple shift from **agriculture** to **manufacturing**
- Relative high **labor mobility**
- Rapid **urbanization**
- **Substantive** improvement of personal well-being (exiting poverty, improved health, education, etc.)

Adjustment to trade opening = Improved welfare

# India's experience with trade opening





# India's Experience with Trade Opening

Post WWII: Import substitution led industrialization with heavy government control

- Dismal performance of the public sector
- Massive growth of government expenditure
- External economic shocks in late 1980s and early 1990s
- Severe balance of payment crises

1991 IMF assistance conditional upon undertaking structural reforms and opening the economy.

- Initiated process of liberalization, including trade opening, in India until today.

## What has been the impact of Indian trade reforms?

# Trade Adjustment in India

## **Increase in firm productivity:**

- Positive impact on plant level productivity (Sivadasan, 2009), especially due to reduction of tariffs on inputs (Topalova and Khandelwal, 2011) as well as pro-competitive effect and technology spillovers (Gupta, 2016).

## **Decline in unemployment:**

- Positive effect if flexible labor markets and larger employment shares in net exporter industries (Hasan et al. 2012).
- For small and labor-intensive firms trade reforms led to increase in labor share. Impact found to be opposite for the larger and less labor-intensive firms (Ahsan and Mitra, 2014).

# Trade Adjustment in India

## Mixed evidence for poverty reduction:

- Districts more exposed to tariff reductions experienced **lower reduction in rural poverty** (Topalova, 2007).
- States more exposed to foreign competition **had lower rural, urban and overall poverty rates** (Hasan et al. 2007).

## No discernible impact on income inequality:

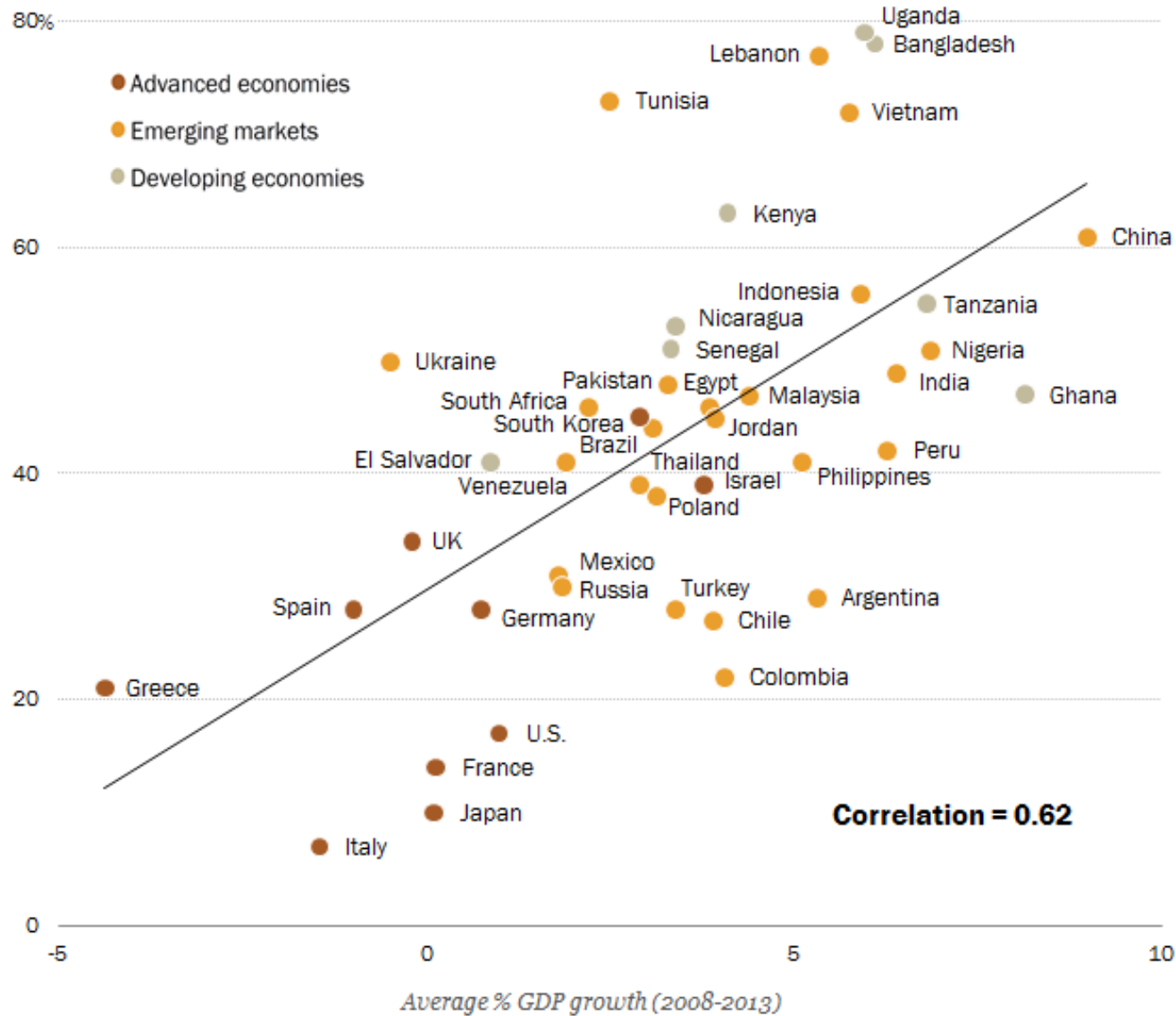
- **No discernible effect** of trade reforms on rural and urban inequality in India (Topalova, 2007).
- **No significant impact** of changes in state-level measures of trade protection on changes in inequality across households within states (Krishna and Sethupathy, 2011).

# Future of Adjustment to Trade Integration



# GDP Growth & Views of Trade's Impact on Wages

Percent who say trade increases wages



Source: Pew Research Center

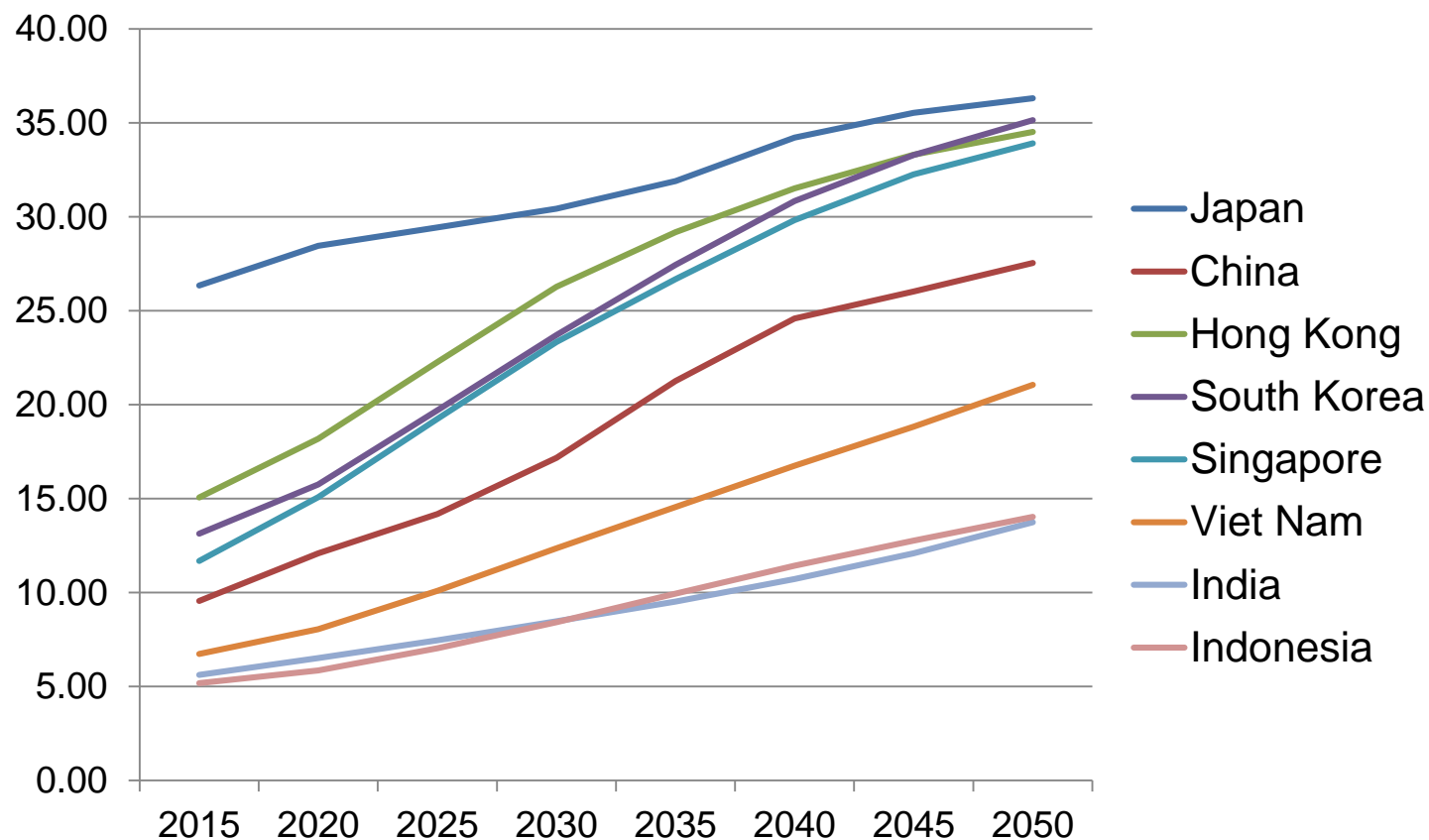
# Asia's future trade adjustment will become more difficult...

Factors hindering quick adjustment:

- **Ageing societies** (more difficult to retrain)
- More difficult shift from **low-skilled manufacturing** to **high-skilled manufacturing** or **services**
- Persistence of **SOEs**
- **Lower labor mobility**
- **Rudimentary social safety nets** (unemployment, health, etc.)
- **Limited access to financial services** (SMEs, start-up)
- **Incremental** improvements of personal well-being: Perceived adjustment costs > Welfare gains

# Ageing workers more difficult to retrain

Age 65 and above as a percentage of the total population



Source: United Nations, World Population Prospects: The 2015 Revision

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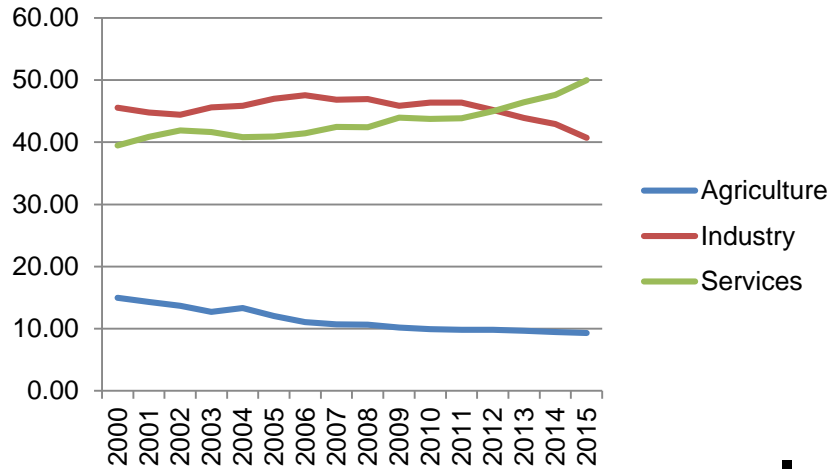
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# Growing importance of services' sector in Asia

Sectors as percentage of GDP (2000-2015)

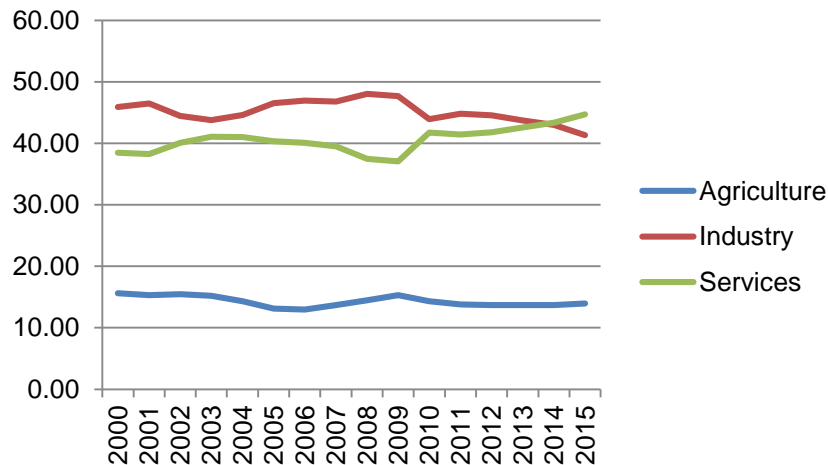
## PRC



## India



## Indonesia



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# High out-of-pocket expenditures for health in Asia



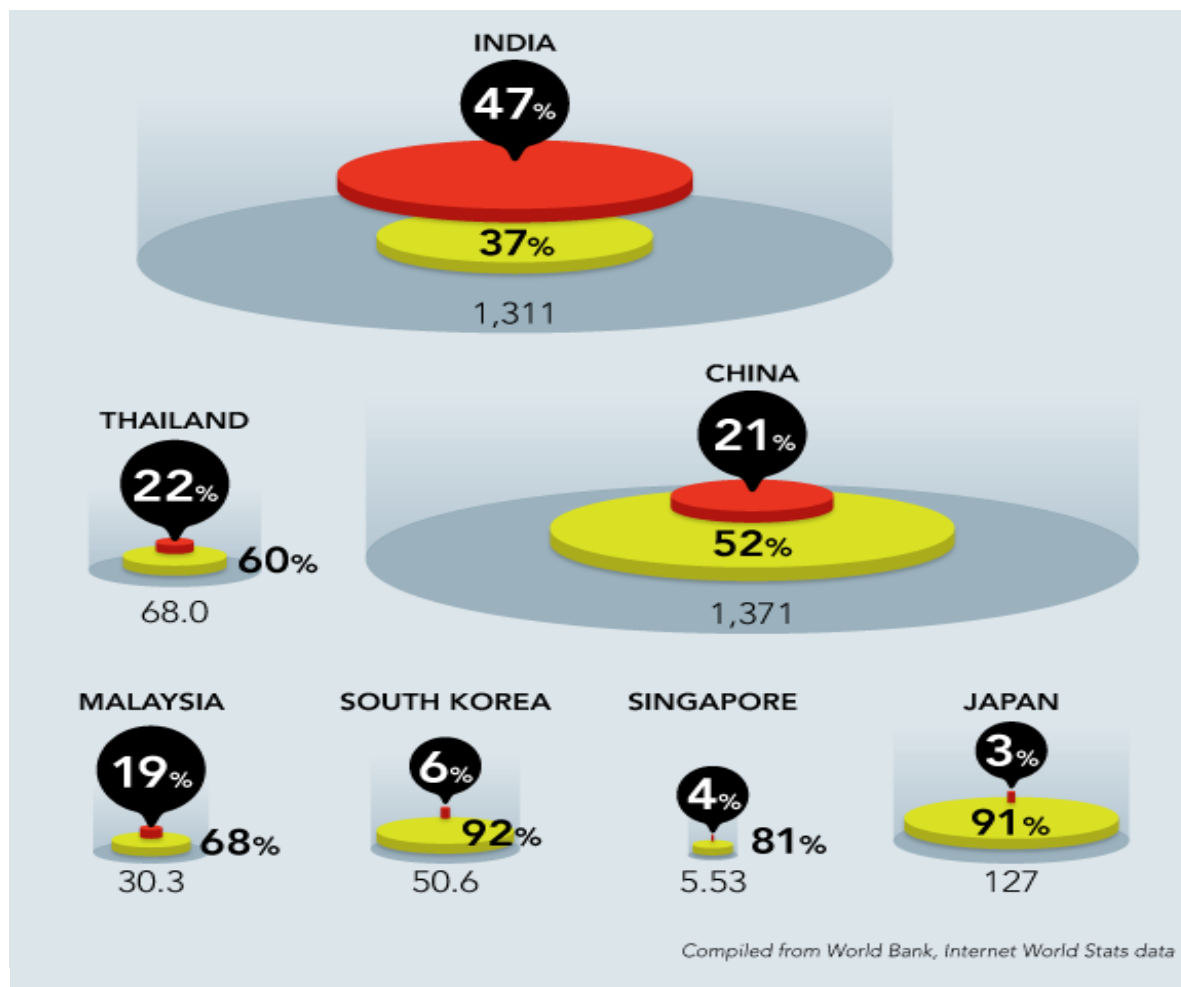
Source: WHO, 2013

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# Lack of access to financial services in Asia



Source: Nikkei Asian Review, 2016

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(Perceived) adjustment costs > Welfare gains

# Policies to make trade inclusive



# Fill knowledge gaps

- **Dynamics** of trade adjustment not well understood (recent literature)
- Existing empirical studies on adjustment dynamics are mostly on the **United States**.
- Benefits and costs of trade opening at individual level not easy to quantify and separate from **technological change**.
- **Adjustment speed** differs across sectors, industries and firms. Empirical estimation:

$$Y_t^A - Y_{t-1}^A = \lambda_A (Y_t^{*A} - Y_{t-1}^A)$$



# Ease trade adjustment

- **Trade agreements:** Ex. Different adjustment speeds across sectors (phase-out of tariffs): ex. agriculture (10 years), automobile (5 years), finance (2 years)
- **Adjustment funds** (ex. EU, PRC, USA)
- **Domestic policies:**
  - Education
  - Vocational training
  - Retraining
  - Land reform
  - Exchange rate policies (ex. market-oriented or basket)
  - Tax collection and redistribution (to mitigate income inequality)
  - ...
  - Policy coherence

**Thank you very much for  
your attention**



# How can India make trade opening inclusive?

- Investment in **education**
- Investment in **health**
- Investment in **infrastructure**
- **Flexible labor markets**
- Encourage **labor mobility**
- Well-managed **urbanization**
- **Ensure that benefits are distributed evenly to allow for substantive** improvement of personal well-being.