

A World Bank Group Flagship Report



# TRADING FOR DEVELOPMENT **IN THE AGE OF GLOBAL VALUE CHAINS**



WORLD BANK GROUP

# The international fragmentation of goods production includes both goods parts and services tasks

Software development



Product design



Accounting



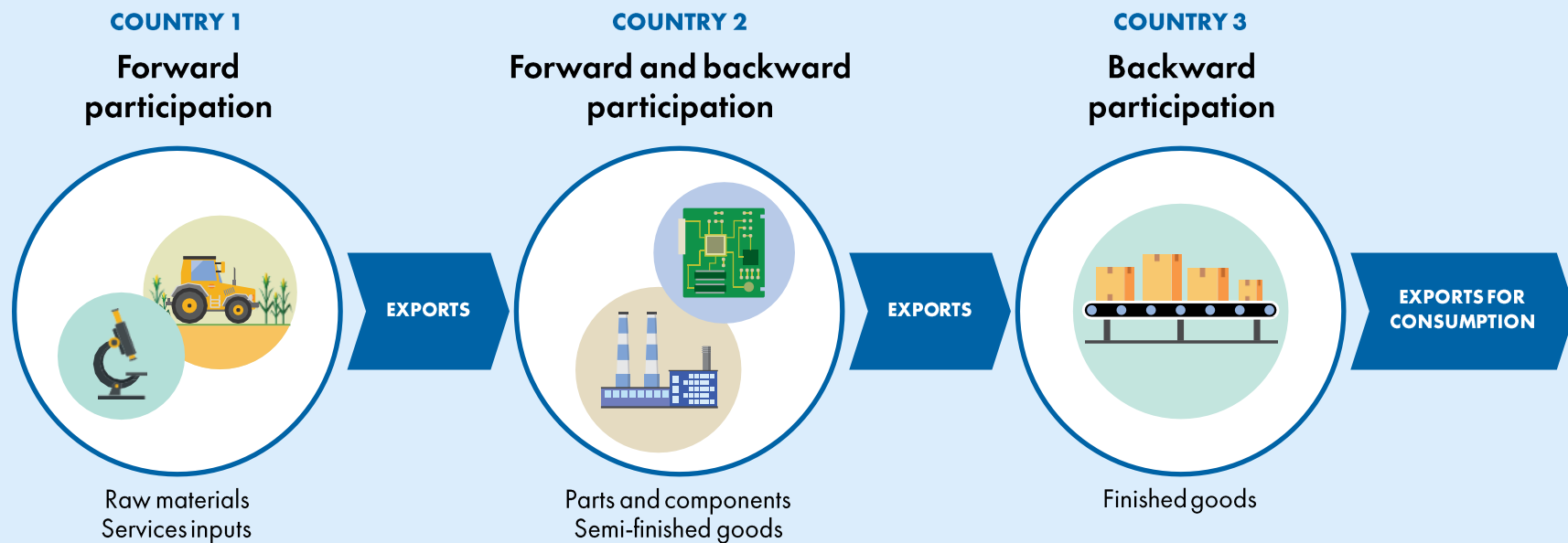
HR and payroll management



Driven by, and boosting demand for, information, communication and transport services



# What is a global value chain?

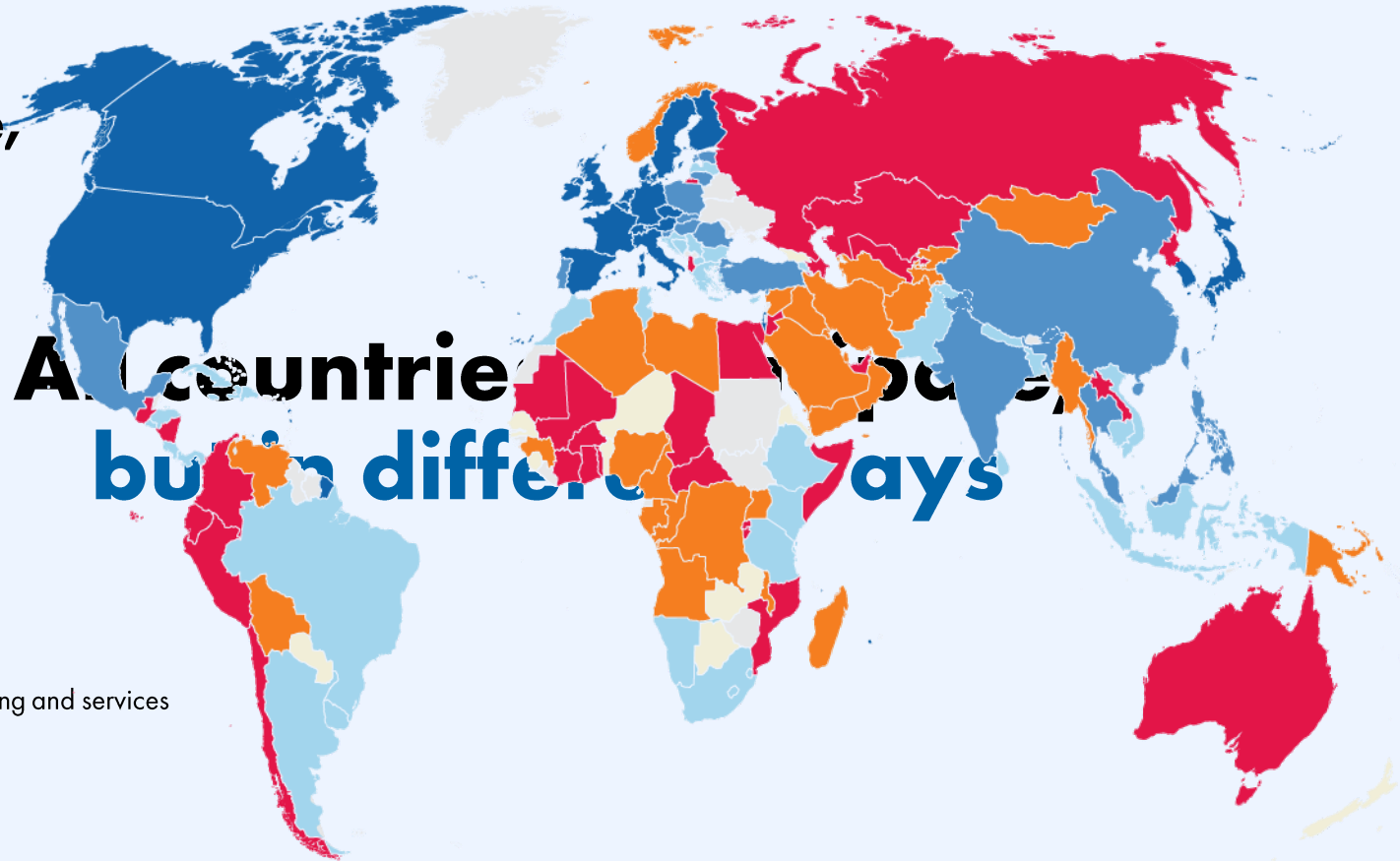


**All countries participate, but in different ways**

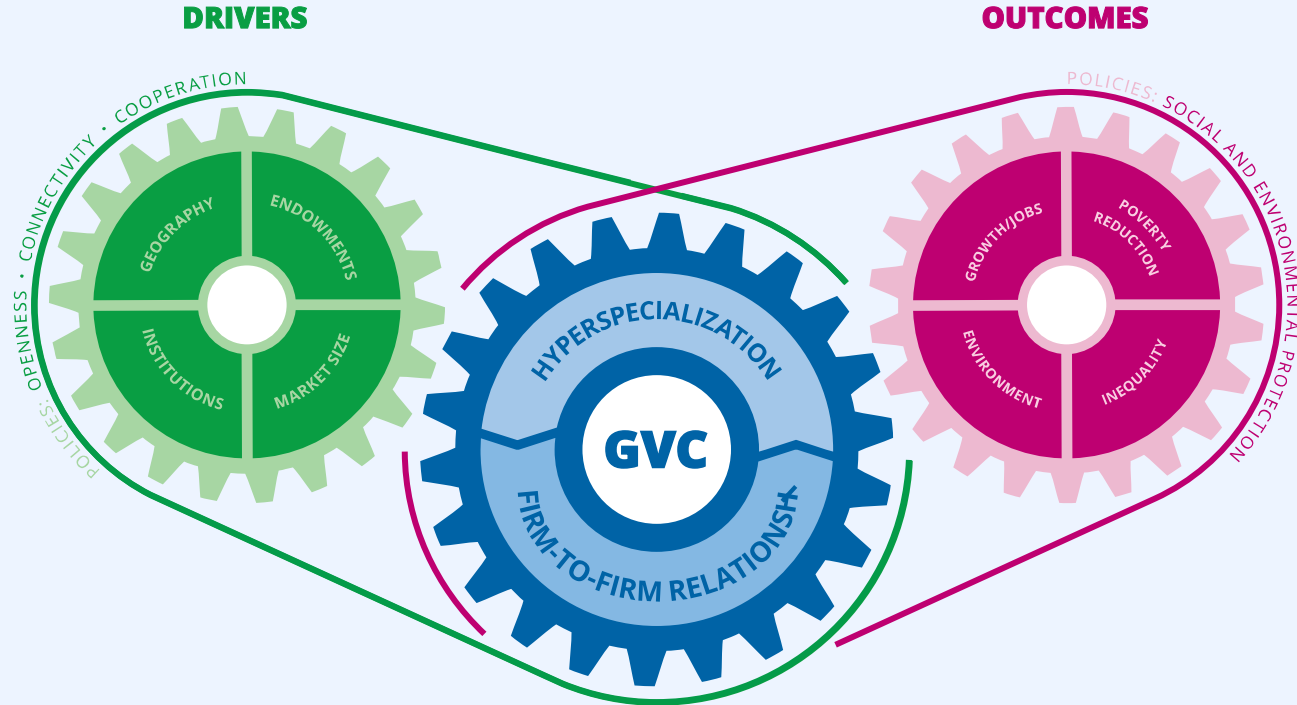
**All countries participate, but in different ways**

**GVC linkages, 2015**

- Low participation
- Limited commodities
- High commodities
- Limited manufacturing
- Advanced manufacturing and services
- Innovative activities

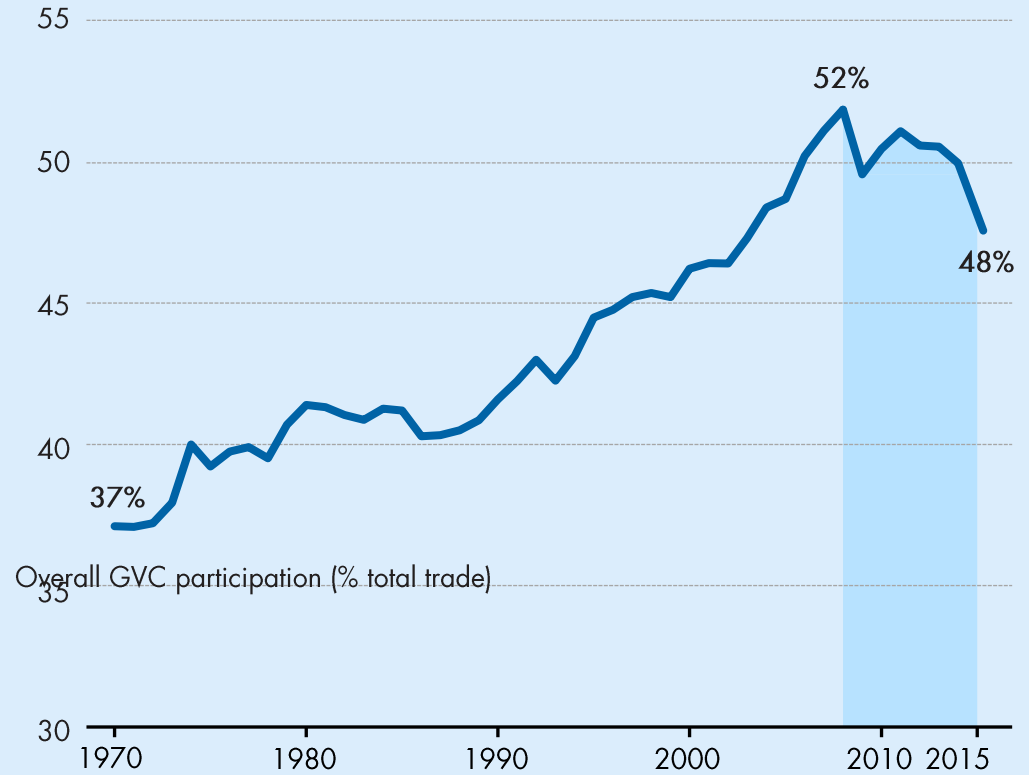


# Framework for GVC-led development



# Since 2008, GVC expansion has slowed

## GVCs' share of global trade (%)







# Why Care?

## Global Value Chains:

- Boosted incomes, created better jobs and reduced poverty
- Mixed impact on the environment and inequality
- Can continue to support development if developing countries undertake deeper reforms and industrial countries pursue open and predictable policies



# Main points 1

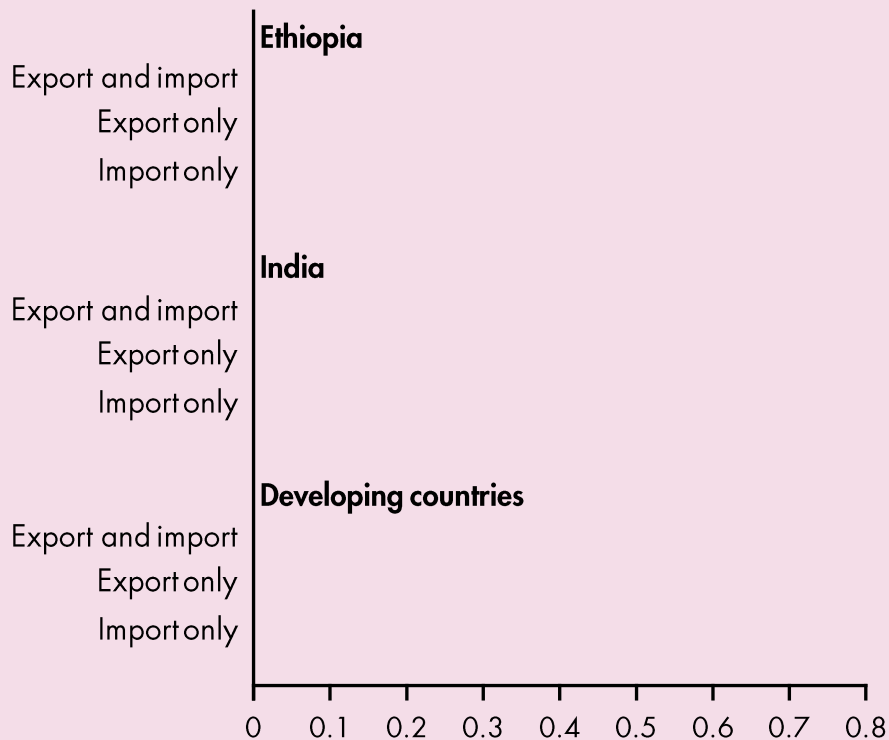
- *India has both underachieved and overachieved in GVCs.*
  - Failure to take full advantage of the first transition: from commodities to basic labor-intensive manufacturing GVCs
  - And precocious second transition: from basic manufacturing to advanced manufacturing and services GVCs
- *Two questions:*
  - Is it too late to engage more fully in basic manufacturing given the twin threats of automation and protection?
  - Is it possible to rely primarily on advanced manufacturing and services to deliver growth and jobs?

# Main points 2

- The answer to both questions is no.
  - Not too late. Technological change is at this stage more boon than curse. And protectionism is not inevitable.
  - Jobs for the less-skilled will not come from advanced manufacturing and services alone - unless there is an implausibly rapid growth in the skilled.
- Then what is to be done?
  - Deeper domestic reform to remedy weakness in manufacturing and to reinforce strength in services.
  - International cooperation to spur domestic reform and secure access to foreign markets.
  - But cooperation needs to extend beyond trade to ensure trade stays open and beneficial.

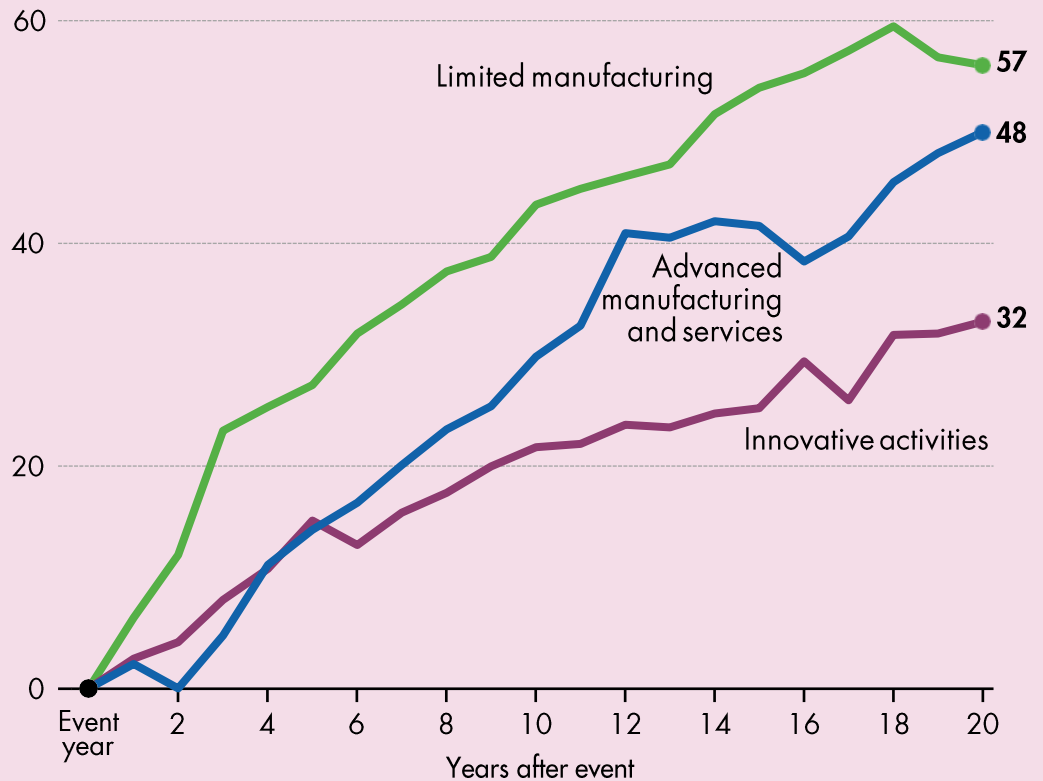
# GVC firms are more productive than one-way traders or nontraders

Productivity difference between trading and nontrading firms (%)



# Incomes grow most when countries break into simple manufacturing

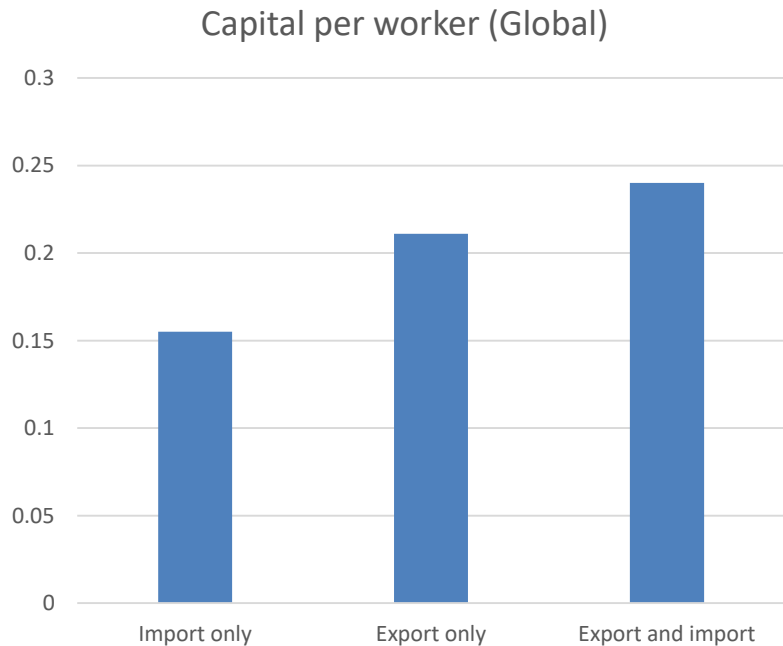
## Cumulated change in GDP per capita (%)



# GVC firms are more capital intensive but also see faster employment growth

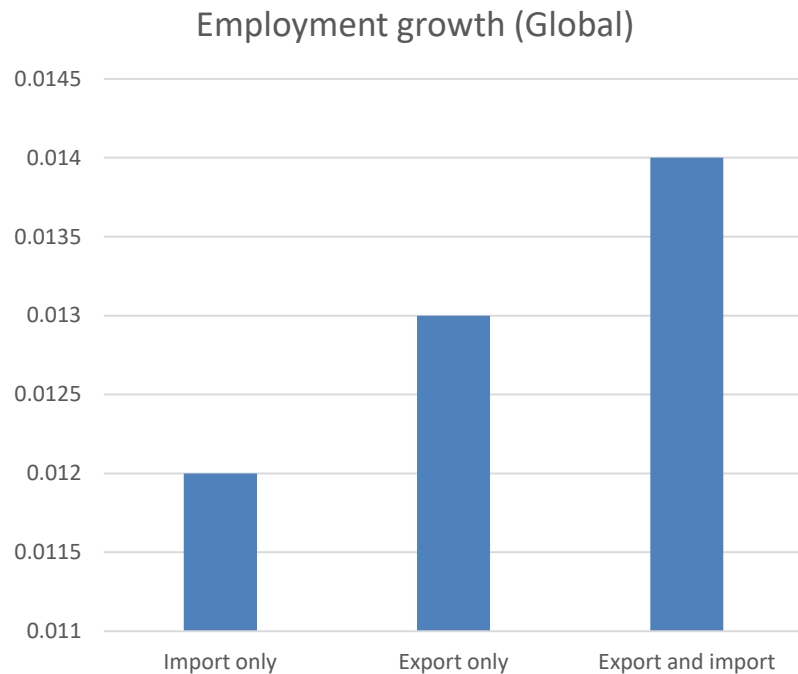
## Capital intensity

Difference between trading firms and nontrading firms (%)



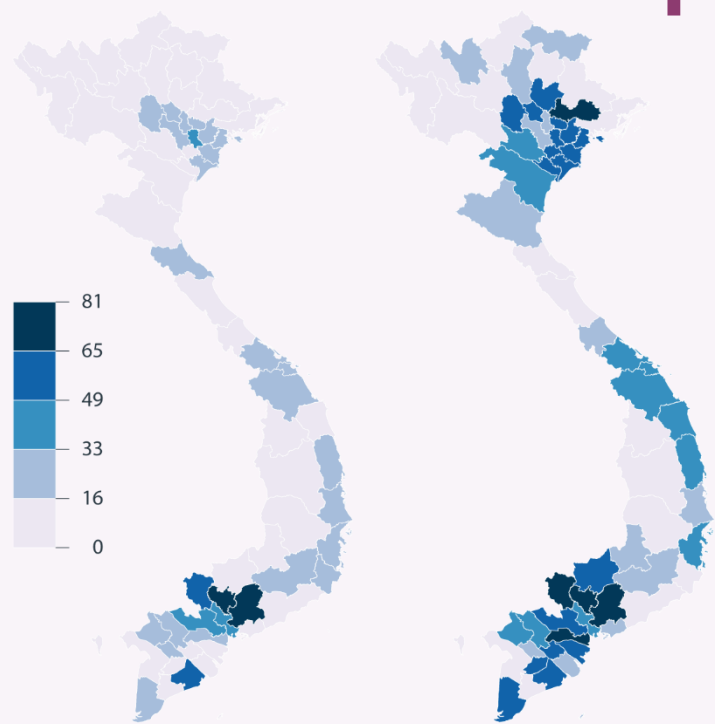
## Employment

Before-after difference for firms switching from not trading to trading (%)

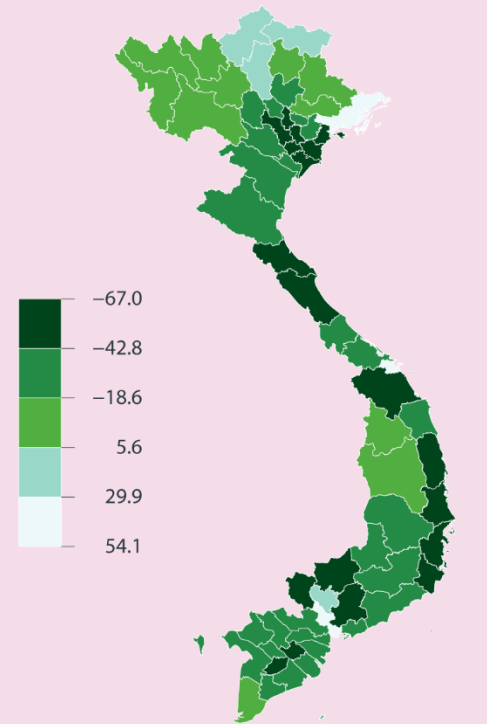


# In Vietnam, poverty reduction is greater where GVC firms are present

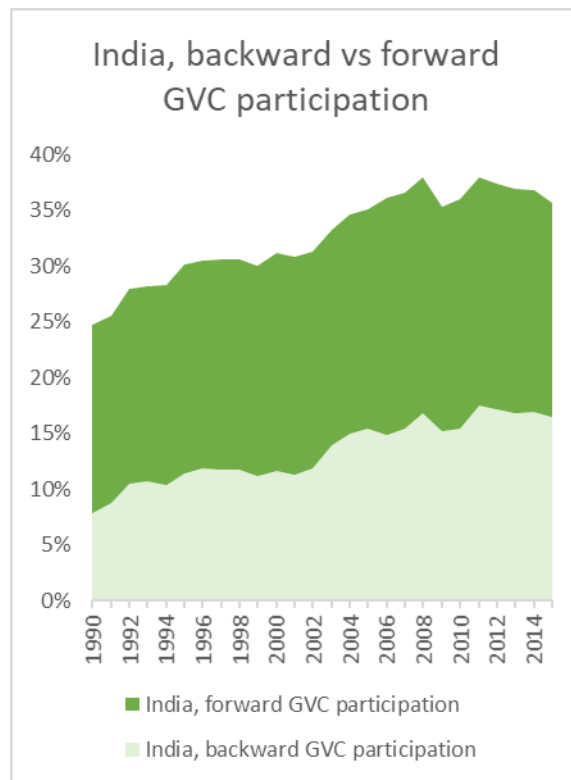
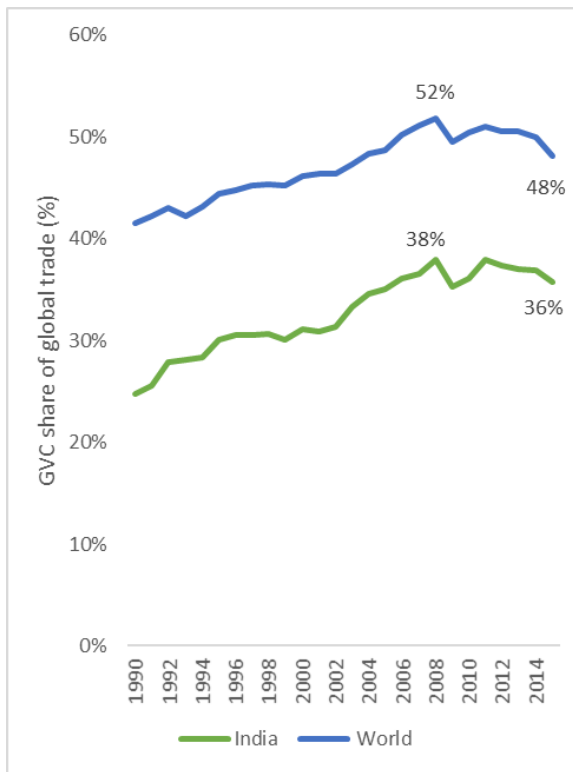
GVC firms in the top 10 provinces (2007-2014)



Change in expenditure poverty rate, 2004–14 (%)



# India's GVC linkages are about a quarter less than the global average





# India has underperformed in its transition to basic manufacturing

Figure 1(a). Exports of Apparel Post Take Off (Initial year = 100)

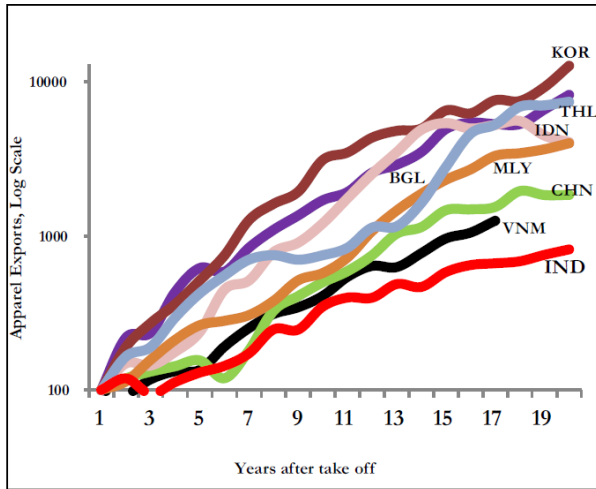
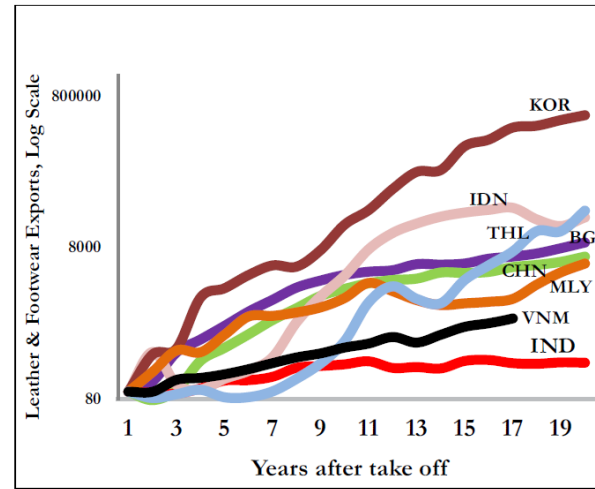


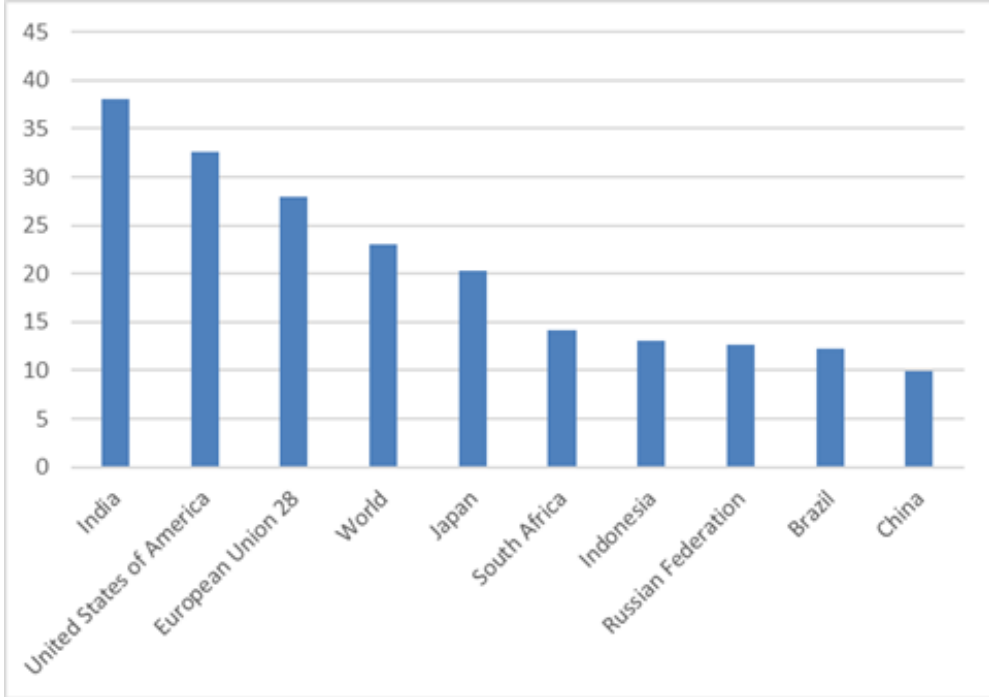
Figure 1(b). Exports of Leather & Footwear Post Take Off (Initial year = 100)



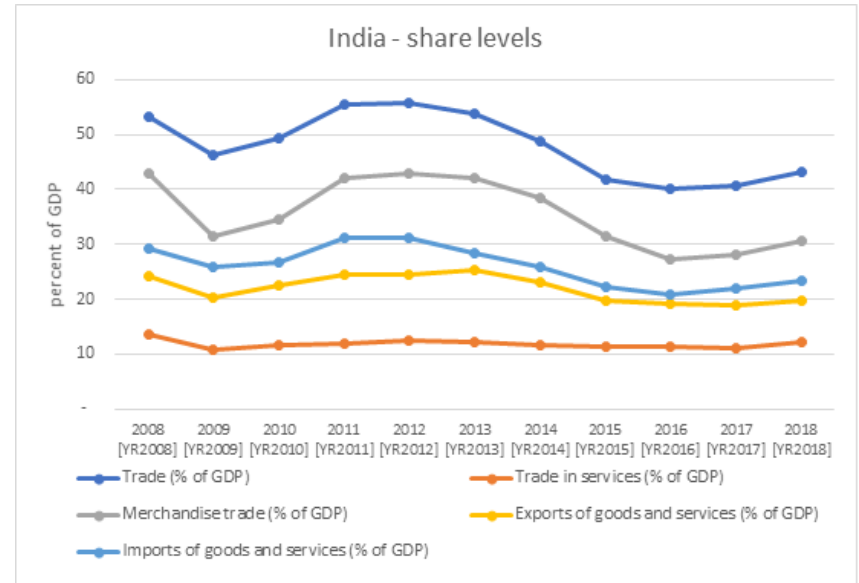
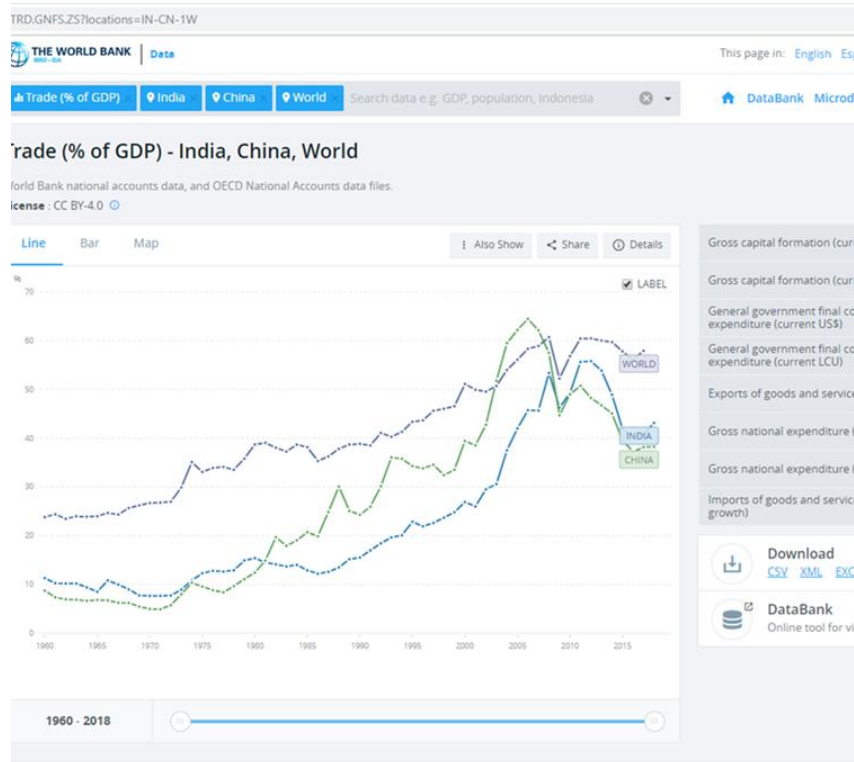
Source: Johnson, Ostry, Subramanian(2010) and World Bank Database

But has developed a strong comparative advantage in services trade

Share of services exports in total goods and services exports, 2018



# The declining share of India's trade in GDP



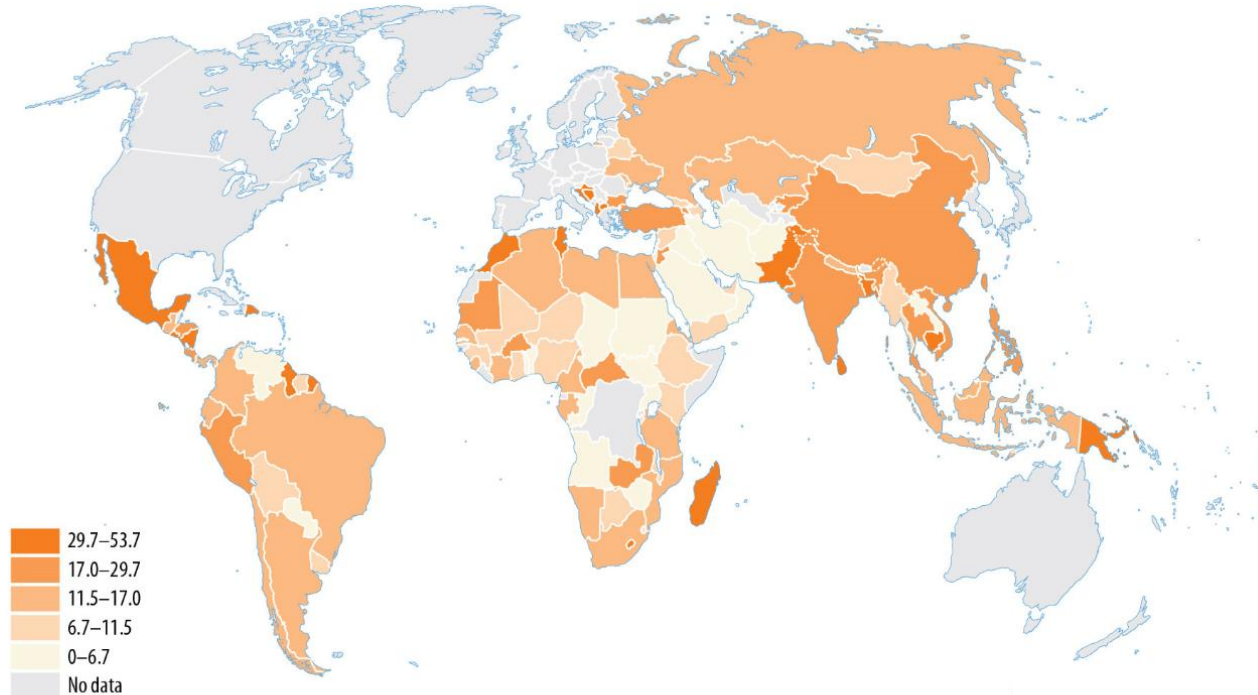
# Technologies are changing production and distribution



# Rapid Technological Change

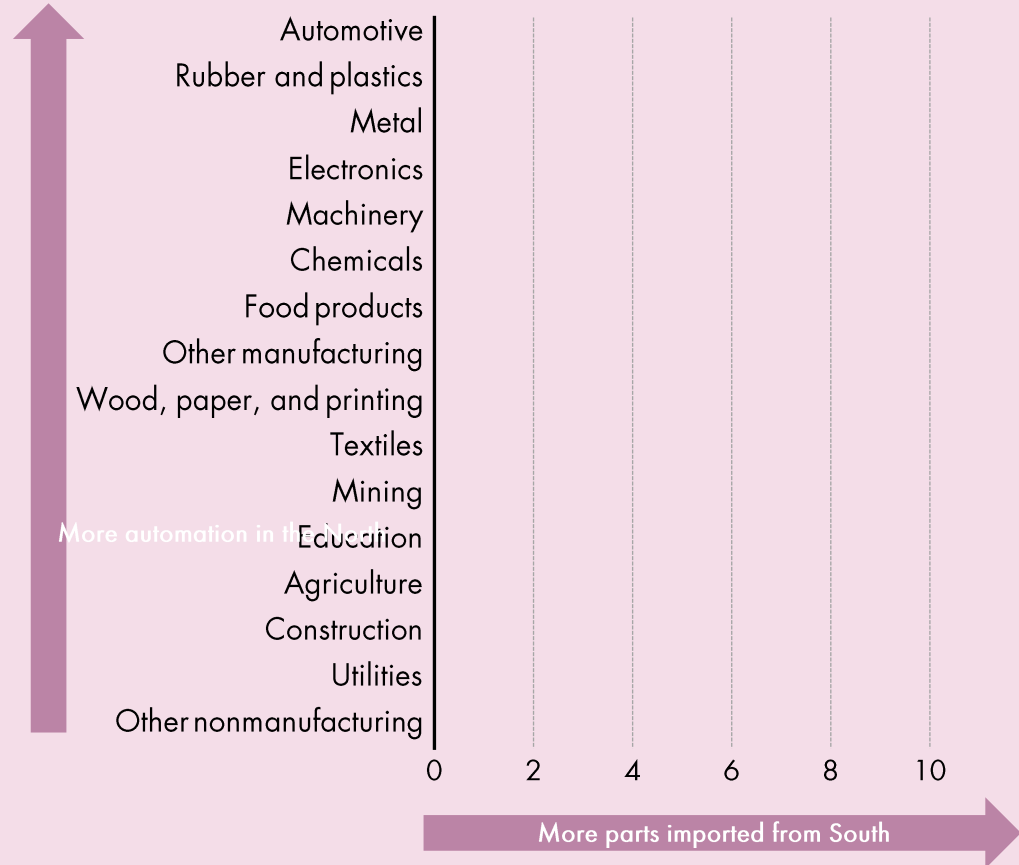
A significant share of India's goods exports can be produced by robots

Percent of total exports to OECD countries



# Increased adoption of industrial robots in the North has promoted imports from the South

Change in parts imports from developing countries (%)

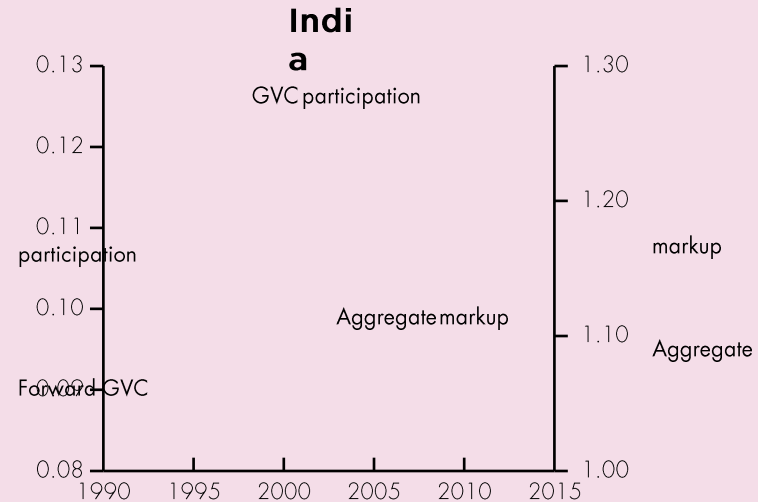
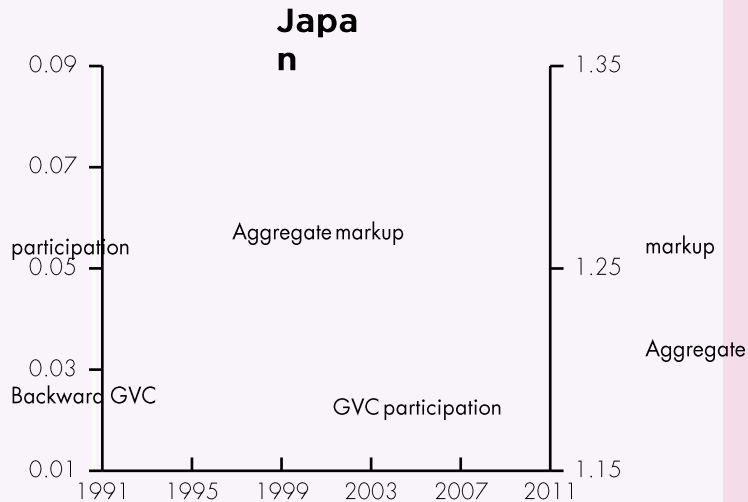


# What are the costs of participation?



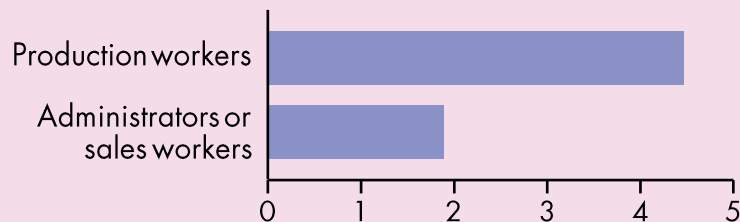


# Increasing GVC participation is associated with rising markups in developed countries but falling markups in developing countries

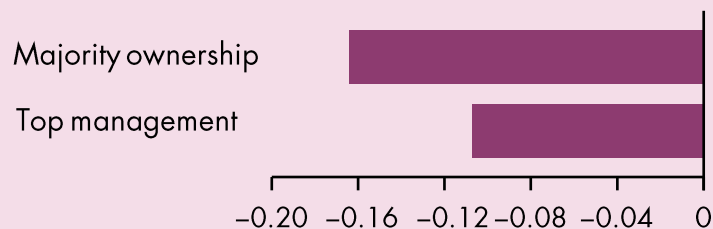


# GVCs favor women's employment... but don't break glass ceilings

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



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

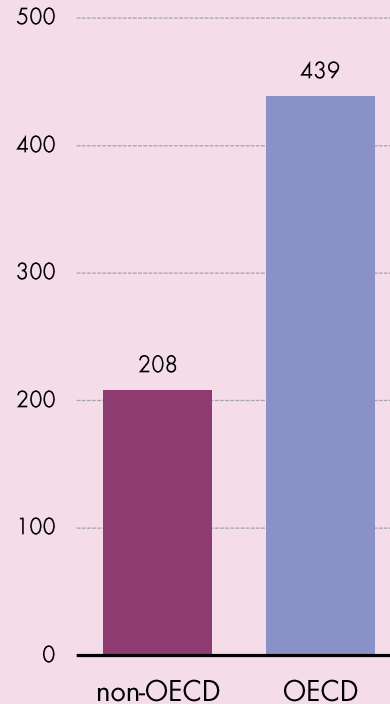


# Raising tax revenue is **challenging** in today's globalized world

- 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

## Revenue loss from profit shifting

US\$, billions

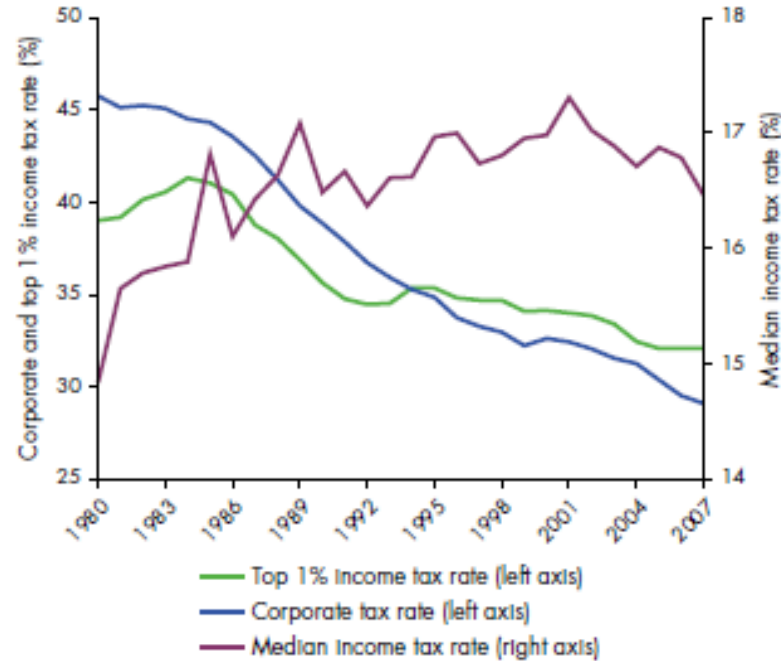


% of GDP



# Impact of globalization on tax structures: harder to tax winners and compensate losers

Corporate tax rates and personal labor income tax rates for top 1% and median workers in 65 economies over 1980-2007



Source: Egger, Nigal, and Strecker 2019.

# GVCs can also be a **mixed blessing** for the environment



## Disadvantages

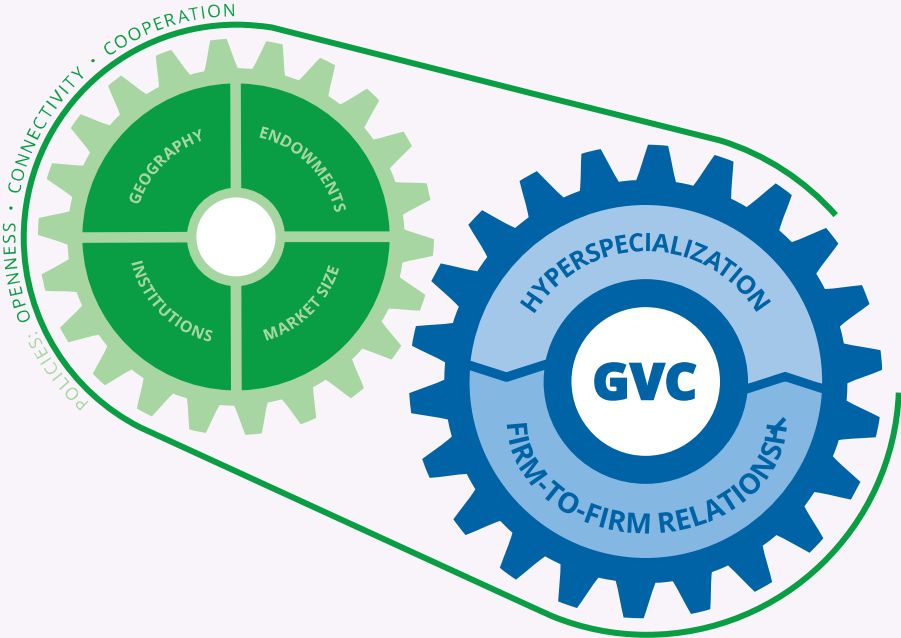
- Excess transport
- Waste
- Pollution haven

## Advantages

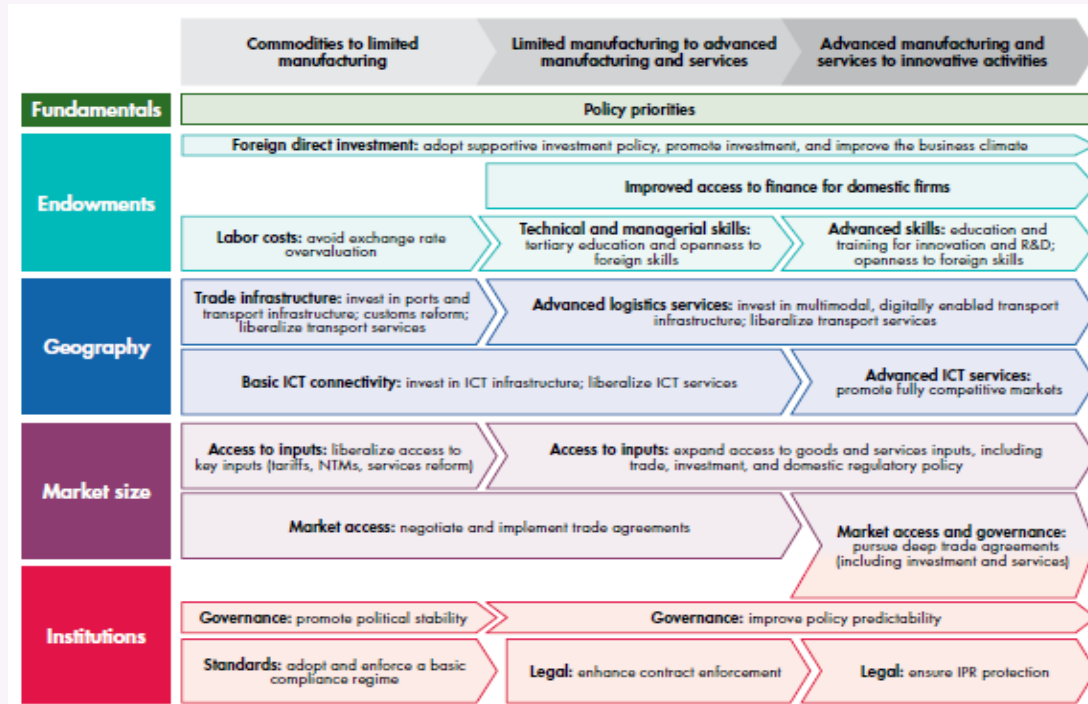
- Lead firms push standards upstream
- New environmental goods

# GVC-led development: Drivers and policies for participation

## DRIVERS



# Fundamentals need not determine destiny and transitions—policies matter



Source: World Bank 2019a

No one size fits all — policy priorities evolve



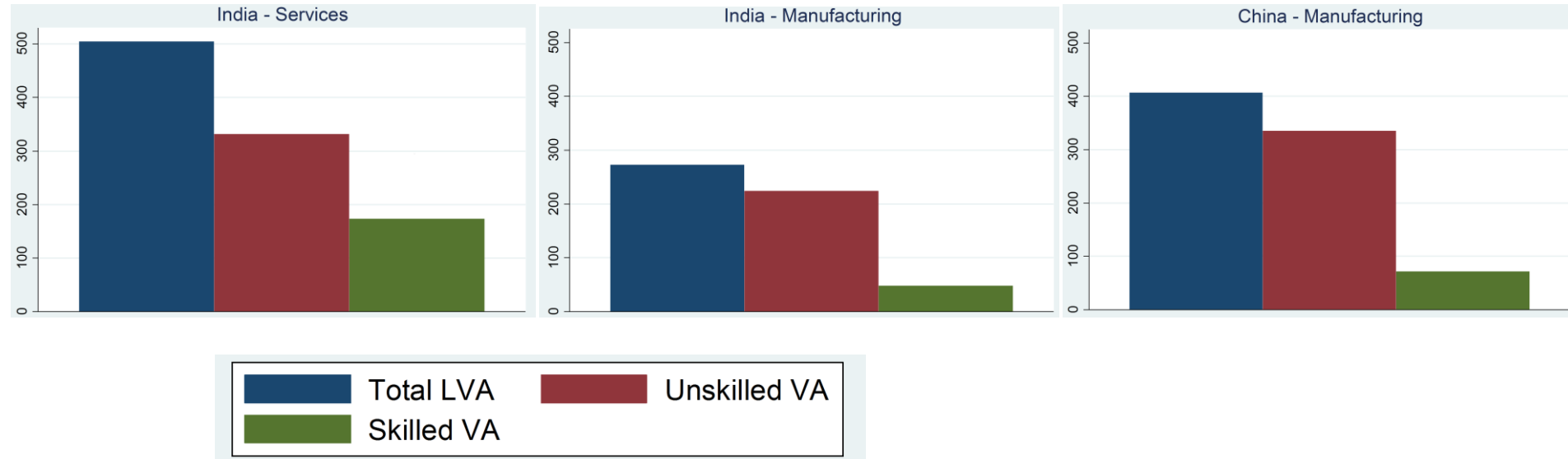
# Domestic distortions drive India's premature transition to “advanced manufacturing and services”

- Relative rigidity of the market for low-skilled labor.
  - Nearly 80 percent of firms in India employ less than 50 workers while in China only 15 percent have a similar small scale.
- Slow improvements in roads and ports on which trade in manufactures relies.
  - Logistics costs (US dollar per km of road transport) are three times higher in India than in China and two times higher than in Bangladesh.
- Restrictive trade policy
  - E.g. high tariffs on imports of yarn and fiber which increase the cost of producing clothing.
- Incomplete services reform
  - Especially in logistics, distribution, education and professional services.

# Binding constraint on job-creation is not services skill-intensity but skill scarcity

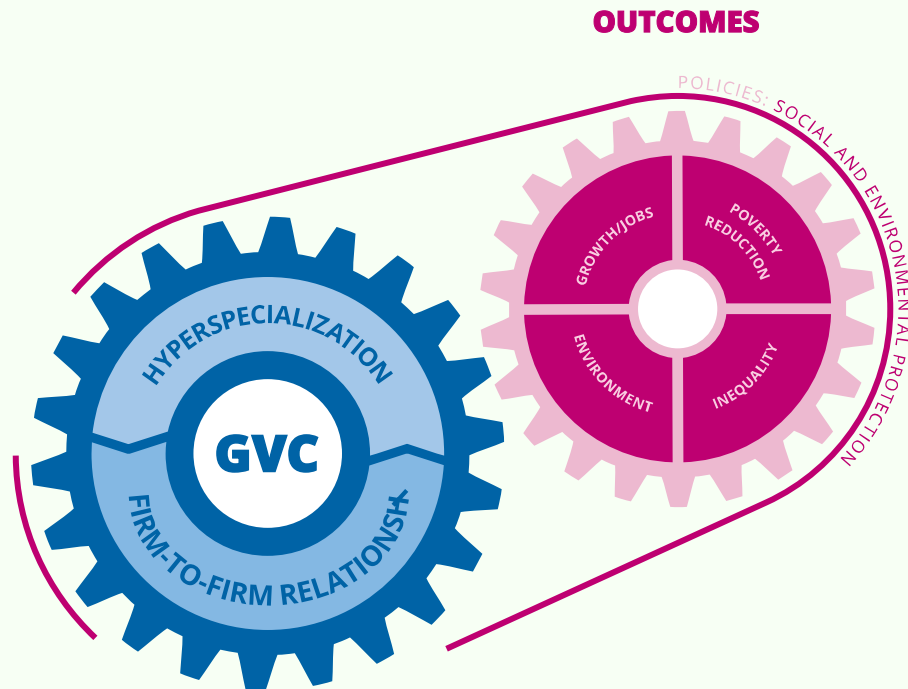
The surprisingly high unskilled labor value added in services exports

Labor value added (LVA) in \$1000 of exports



Hence, the vital importance of improving India's skill production capacity

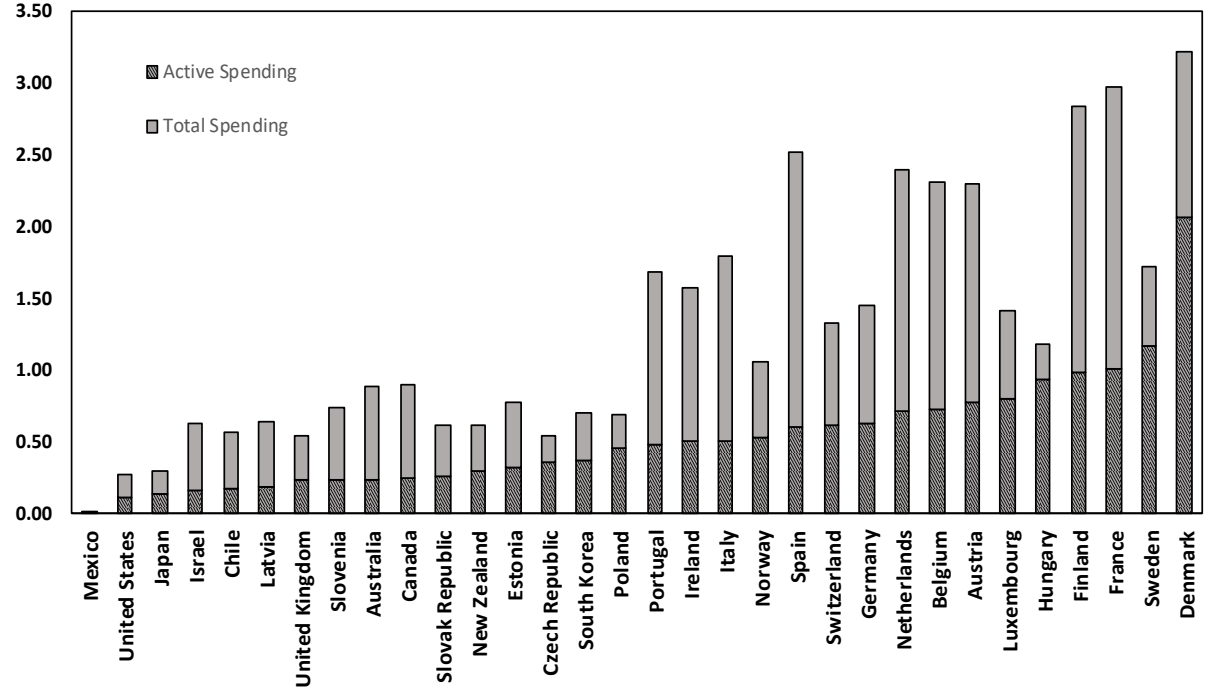
# GVC-led development: Policies for benefitting from GVCs



# Policies can help ensure benefits are shared and sustained

- Expand adjustment assistance
- Support active labor market programs to assist with retraining and job search
- Avoid rigid labor market regulation

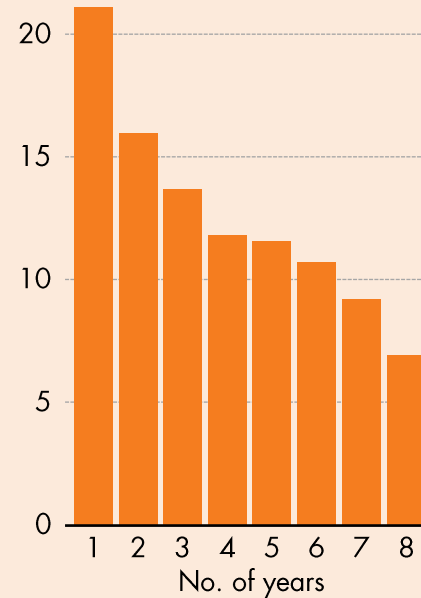
Spending on total and active labor market policies as a percentage of GDP, 2016



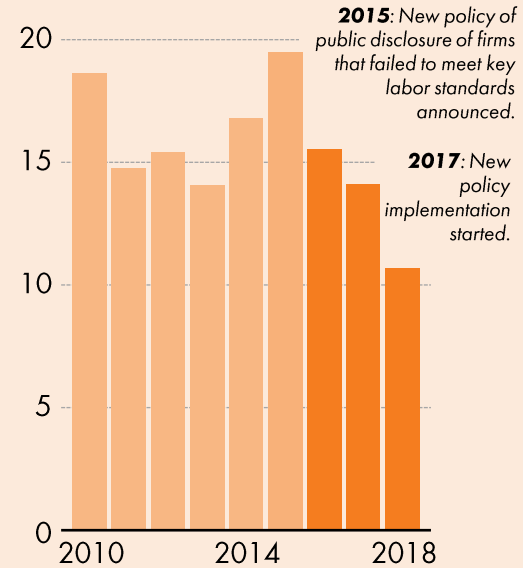
# Working with firms improves working conditions

## 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 (%)



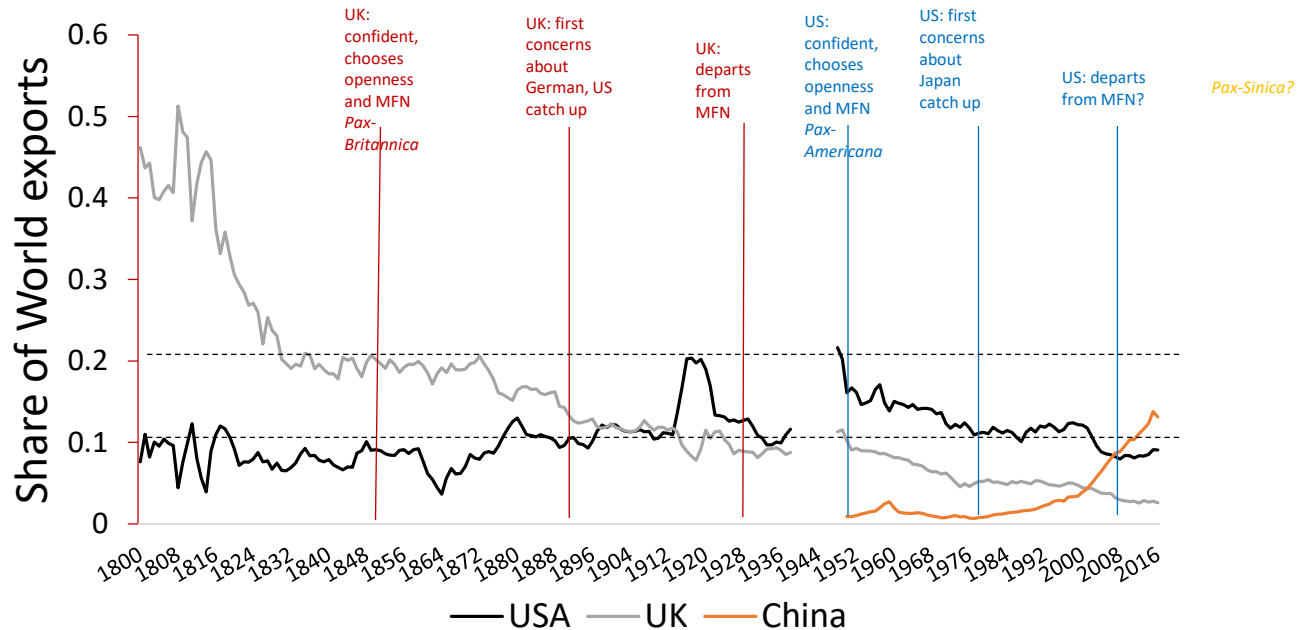
Average non-compliance rates, all firms (%)



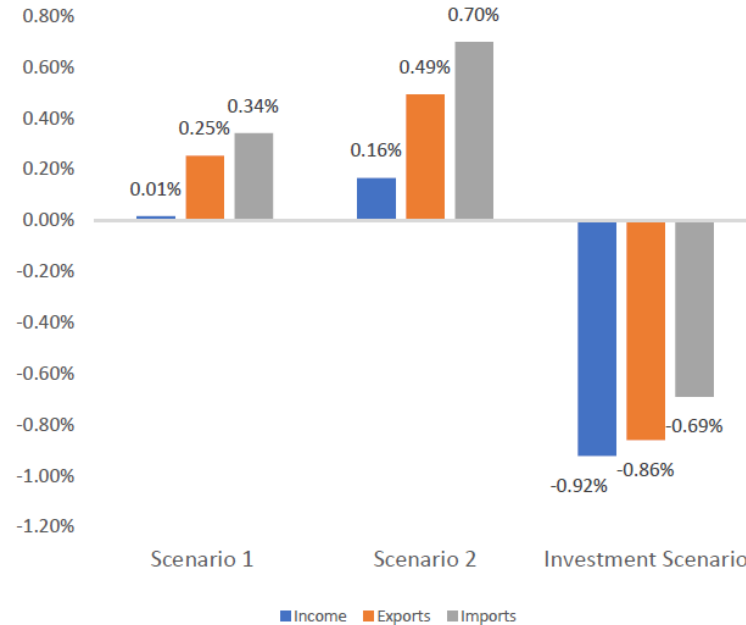
# The threat to rules-based trade may be a historical inevitability

Shifts in trade shares and changes in policy stance

The UK and US Share of World Trade, 1800-2016



# The impact of a trade war on India's trade and income



Source: Freund et al. (2018)



# 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

# Deeper trade cooperation matters for GVCs

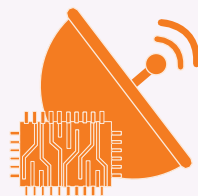
GVC trade is greater between countries sharing a deep trading agreement



# Look beyond trade to keep trade open and beneficial



**Taxes**



**International  
data flows**



**Competition**



**Environment**

# Innovative approaches to regulatory cooperation

