B.6. Trade

Trade and COVID-19

After riding the crest of hyperglobalization since the early 1990s, EAP trade has been buffeted by several shocks. The *great recession* in 2008 was followed by a “great flattening”: trade growth barely kept pace with GDP growth and trade as a share of GDP stopped increasing (Figure B.6.1), though services trade was more buoyant than goods trade (Figure B.6.2). After that, the *trade tensions* in 2018-2019 between the great powers ushered in a period of protection and uncertainty that further inhibited investment and trade. Now, due to *COVID-19*, trade is contracting because both production and consumption have been disrupted across the world. In this section, we describe how COVID-19 has accelerated five recent trends in trade: contraction, regionalization, relocation, servicification, and protection. We also consider how policy should respond.

**Figure B.6.1.** After recovering from the Great Recession, trade growth barely kept up with GDP growth and has plunged faster in 2020

![Graph showing trade growth and GDP between 2006-Q2 and 2020-Q2.]

*Source:* World Bank Global Economic Monitor (WB GEM) and Eurostat - for trade in goods; World Trade Organization (WTO) - for trade in services; WB GEM for GDP current U.S. dollar.

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1 This analysis was conducted to inform the October 2020 East Asia and Pacific Economic Update.
Figure B.6.2. After recovering from the Great Recession, the share of goods trade in GDP declined while the share of services trade increased – until 2020

Source: World Bank Global Economic Monitor (WB GEM) and Eurostat - for trade in goods; World Trade Organization (WTO) - for trade in services; WB GEM for GDP current US dollars. International Monetary Fund’s International Financial Statistics (IFS) and WB GEM for exchange rates.

Contraction

EAP trade contracted significantly in the first half of the year, but less than that in other parts of the world.

All the major EAP countries (except Indonesia) saw a sharper decline in exports in 2020 compared to that in 2019, with only Vietnam experiencing continued but slower growth in exports. While the exports of China and the rest of developing East Asia saw smaller declines of 5.9 percent and 5.1 percent respectively in the first half of 2020 (January until July), global exports declined more than twice as fast, by 12 percent. Since the EAP countries experienced lockdowns in waves – China led the wave, other EAP countries followed as the virus spread across these nations –consumption losses from lockdowns were low as production continued to happen somewhere in the region (for example, Vietnam’s exports expanded while China was under lockdown in
Figure B.6.3. Growth of region’s exports in the first half of the year has, on average, contracted further compared to the same period last year.

Exports growth in the region was negative during the Jan-Jul period last year, with the exception of Philippines and Vietnam, and has turned further negative this year.

Trade is showing signs of recovery in June 2020

Trade showed signs of recovery globally in June 2020. Some countries globally and in the region, such as Japan, the EU, China, Vietnam, Malaysia and Thailand, were relatively successful in containing the disease and lifted the stringent restrictions that were stifling economic activity. Other countries, like the United States and Indonesia, were less successful in containing the disease, but nevertheless allowed economic activity to resume or continue (Figure B.6.4).

Figure B.6.4. EAP trade flows increased considerably in June 2020

Sources: World Bank Global Economic Monitor; World Bank staff calculations
Notes: Total merchandise exports. EAP includes Indonesia, Malaysia, Philippines, Thailand and Vietnam.
The impact on trade was driven by the COVID shock and the stringent policy response

The trade decline was caused by the disruption of production in source countries and the contraction of consumption in destination countries. High-frequency trade data reveal that exports growth is significantly related to declines in worker mobility and import growth is related to declines in retail mobility. Recent research finds that a 1 percent decline in worker mobility led to a 0.5 percent decline in exports growth, and a 1 percent decline in retail mobility led to a 0.25 percent decline in imports growth. These negative trade effects intensified over the early months of 2020 with the increase in the number of cases and the stringency of lockdown policies (Figure B.6.5).

Figure B.6.5. Trade disruptions negative effects over exports and imports intensified during first months of 2020

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2 The negative on imports is mitigated by a higher share of durable goods in imports. Unlike in previous recessions, the shutdown has had a less adverse effect on imports of durable goods – possibly because demand for consumer durables like computers and televisions has increased and these products are relatively amenable to online purchase.
Exports growth is positively correlated with work mobility changes across exporting countries

Source: Espitia et al. (2020)
Import growth is positively correlated with retail mobility changes across importing countries

What were the implications of global value chains? The conventional concerns are legitimate but ignore important positive benefits. The disruption of production in source countries does adversely affect exports of products that rely on imported inputs. And the disruption of production in destination countries does adversely affects exports of products that are used as inputs in production by importing countries. But the negative impact of a disruption in production in exporting countries themselves is mitigated by greater backward participation in global value chains – i.e. a higher share of imported value added in exports. Thus, the diversification benefits of GVC participation reduce vulnerability to domestic shocks. These diversification benefits are particularly important because while COVID-19 is an aggregate world shock, its intensity has varied over time across countries.

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3 Results are robust to the use of different configurations of fixed effects, reliance on mirror-import data to quantify the trade effects on a larger number of developed and developing country exporters, and when the inclusion of monthly data for China in the analysis.
Regionalization

The COVID-19 shock is deepening the trend towards regionalization of EAP trade.

Since China first, and then many other countries in the region, contained the disease faster than other parts of the world, domestic shutdowns were phased out, and production and consumption also recovered faster than in other parts of the world. That meant intra-regional trade suffered less than trade in and with other parts of the world (Figure B.6.6; Figure B.6.7). The US willingness to end shutdowns before containing the disease also provided a boost to its trade, but the growth is lower than in the preceding year while the growth of trade with China has accelerated. The ambitious targets specified in the China-US Trade Agreement had the potential to divert China’s imports away from EAP and towards the United States but we see the opposite. In sum, the recent evidence suggests that COVID-19 has further boosted the trend towards the regionalization of EAP trade evident in the last two decades (Figure B.6.8; Figure B.6.9).

Figure B.6.6. China’s export growth to ASEAN5 has held up better than its export growth to US and even EU.

While the export growth has been lower than last year for all the country groups, it is more pronounced for the US.

Source: China Customs Administration
Notes: EU represents 27 European Union countries
Figure B.6.7. China’s import growth from the US has declined but from EAP has picked up this year relative to last year.

While there was a decline in imports from US and EU, imports from the ASEAN5 countries has improved by a sizeable margin. Imports growth from the US has picked up after the Phase One deal but EU remains at the downward trajectory.

Source: China’s customs administration
Notes: EU represents 27 European Union countries

Figure B.6.8. Developing EAP export growth to China has accelerated in the first half of the year compared with last year.
Developing EAP export growth to the US, though lower than a year ago, has remained strong for the first half of the year, whereas export growth to EU and other countries is negative.

Source: World Bank Global Economic Monitor (WB GEM)
Notes: EU represents 27 European Union countries.
Figure B.6.9. Developing EAP import growth from China has remained steady in the first half of the year compared with last year.

Overall, import growth of developing EAP countries has contracted sharply


Notes: EU relates to 27 European Union countries. Developing EAP includes Indonesia, Malaysia, Philippines, Thailand and Vietnam.

Relocation

COVID-19 could lead to a shift away from China of some manufacturing activity but some countries in the EAP region may be best placed to take advantage.

Real wages are increasing in China due to demographic change and growth, and that was already leading to a shift of some manufacturing activity to countries like Cambodia and Vietnam. Our analysis of past shocks suggests that importers do not bring production home but reduce excessive dependence on any single foreign source (Freund, et al., 2020). Thus the 2011 earthquake in Japan did not lead to reshoring, nearshoring, or diversification, but imports shifted away from Japan especially if it had a high share in imports, and towards developing countries that had a revealed comparative advantage in the input. These results cannot be mechanically applied to COVID-19, but the observed pattern of switching may be relevant. Import dependence on China was high before the coming of COVID-19, as was its export similarity with other developing countries (Figure B.6.10, Figure B.6.11).
Past trends suggest some regional countries were the primary beneficiaries of the relocation while others were not. Thus, in both automotive components and electronic products, shifts away from Japan in products where it had a high share, were towards China (a continued trend), Vietnam (an acceleration) but not towards Indonesia (declining or stagnant).

Figure B.6.11. Impact of the 2011 Japan earthquake on market shares of selected countries.

In automotive components where Japan had a high market share

A. Japan Market Share pre>15
   China Share

B. Japan Market Share pre>15
   Vietnam Share

C. Japan Market Share pre>15
   Indonesia Share
In electronic products where Japan had a high market share

D. Japan Market Share pre>15 China Share

E. Japan Market Share pre>15 Vietnam Share

F. Japan Market Share pre>15 Indonesia Share

Source: Freund et al (2020)

These findings suggest that to take advantage of these opportunities, countries need to enhance their attractiveness by reducing trade restrictions and improving connectivity. COVID-19 may accelerate the arrival of opportunities that were already emerging due to changes in China, but deeper reform can equip developing countries to take advantage of these opportunities. This is particularly important since switching import sources is a more rational choice than bringing production back home.

Servicification

COVID-19 is likely to shift the pattern of services globalization from trade in face-to-face services, like tourism and international transport, to trade in digitally delivered services, like telecommunications, business, and software.

The information and communication technology revolution has already led to a rapid growth in business services exports from countries like the Philippines. Since COVID-19 is making face-to-face transactions difficult, firms and people are investing heavily in digital equipment and literacy. The result will be a levelling of domestic and international trade costs in a range of services, from education to health. Since digital investments are “sunk costs” – i.e. computers bought, and skills learnt are here to stay - the impact will be more durable than the pandemic. The result will be new opportunities for developing countries, like Malaysia and Thailand, which have successfully participated in manufacturing value chains, to now advance into services exports.

In addition, due to the digitization of communication, knowledge-intensive services have become easier to trade than ever before. An example of this is the beginning of various transcontinental exchange of ideas through online and open-to-all lectures, conferences, and seminars. Such
servicification reduces the costs of acquiring skills that can boost productivity and complement goods production as well going forward (Figure B.6.12, Figure B.6.133).

Figure B.6.122. COVID is hurting face to face transactions but not trade in digitally delivered services

![Bar chart showing the impact of COVID on various sectors](image)

Source: Mattoo and Taglioni (2020).
Notes: International trade in services for China, Japan and the US expressed in year-on-year change for June 2020

Figure B.6.133. The structure of services trade is changing: Shrinking face-to-face and growing digitally delivered services

![Graph showing the changing structure of services trade](image)

Source: Mattoo and Taglioni (2020)
But to take advantage of these opportunities, these countries need to be more open to trade and investment in services, and to develop stronger skills and even better digital infrastructure.

**Protection**

The failure to address growing inequality within countries through progressive domestic policies was already leading to a backlash against globalization. In addition, growing tensions between international powers and the erosion of multilateral disciplines were generating uncertainty that hurt all trade and investment. Now COVID-19 is creating a stronger craving for self-sufficiency in an uncertain environment. Since some countries will recover and export before others, and many governments will have subsidized their firms to cope with COVID-19, a sense of unfairness could spawn more trade restrictions. And the pandemic could also deepen great power divisions and renew calls for decoupling. Resisting these trends is important for recovery.

COVID-19 may lead to a range of old and new trade measures, some of which are already visible. To cope with scarcity, countries in the region and elsewhere are resorting to export restrictions to meet domestic demand, especially in personal protective equipment (PPEs) and some other goods. Examples include restrictions on face masks by Indonesia, Malaysia, and Thailand, Vietnam’s export curbs and China’s minimum purchase price on rice. As non-synchronized recovery creates competition for scarce demand, tariffs could be used to redirect demand towards domestic production. As states subsidize firms, we are likely to see increasing recourse to countervailing duties. To address rising aversion to various risks, e.g. health, security, privacy, increasing regulatory protectionism could also become a problem (Figure B.6.144).

**Figure B.6.144. Protective measures in the region include exports and imports restrictions**

A. Export restrictions imposed by EAP  
B. Others’ export restrictions affecting the EAP
Avoiding a reversion to protection and a renewal of trade tensions is of vital macroeconomic significance at the present juncture and there are positive signs. Domestic trade policy reform and international trade cooperation could facilitate recovery from the COVID-19 crisis. It is noteworthy that COVID-19 has provided a practical example of gains from trade, as trade allowed consumption when domestic production was disrupted. This recognition led to the steepest percentage rise in import liberalizing measures since 2009 (by 39%) and the steepest percentage fall in import restricting measures (by 59%) in 2020 (Figure B.6.155).

**Figure B.6.155. Total annual import-related measures affecting goods trade taken by countries over the years.**

*Source: Global Trade Alert Database*

*Notes: Dashed vertical line represents World Average*

Expressed in total number of policy interventions in effect each year. 2020 includes information until August.
The China-U.S. trade agreement had averted a damaging trade war and provided relief from the trade tensions that hurt EAP region’s economic performance in 2019. Now COVID-19 will make it difficult at least in 2020 to meet the quantitative import expansion commitments made by China because of the contraction in China’s demand and the likely contraction in U.S. production (Figure B.6.17). Instead of renegotiating the bilateral commitments, all countries would benefit if China opens its market to all trading partners. That would provide a much-needed boost of an estimated 0.6 percent to global income. China’s income could be nearly 0.5 percent higher. Most developing countries in East Asia would also be better off, despite the partial erosion in their preferential access to the Chinese market. Turning the agreement into a model of non-discriminatory market opening could be a credible down payment towards the revival of a multilateral trading system – which is in the interest of both the region and the rest of the world (Figure B.6.16).

Figure B.6.166. US exports and China’s imports in 2020 of all goods covered by the phase one of US-China deal as of July 2020

<table>
<thead>
<tr>
<th>Month</th>
<th>US Exports</th>
<th>Chinese Imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan</td>
<td>$48.5 billion</td>
<td>$172.7 billion</td>
</tr>
<tr>
<td>Feb</td>
<td>$39.3 billion</td>
<td>$142.7 billion</td>
</tr>
</tbody>
</table>

**Note:** Numbers may not sum to total due to rounding. “Uncovered” products refer to China’s imports from the United States not addressed by Annex 6.1. Prorating the 2020 year-end target to a monthly basis is for illustrative purposes only. Nothing in the text of the agreement indicates China must meet anything other than the year-end target. The July data for US exports of all uncovered products to China will be available on September 3, 2020.

**Sources:** Constructed by the author with US export data from US Bureau of the Census, Chinese Import data from International Trade Centre (Trademap) for 2017 and from Chinese customs for 2020, and product categories set out in Annex 6.1 of Economic and Trade Agreement between the United States of America and the People’s Republic of China.

*Source: Peterson Institute for International Economics*
Other countries in the region seeking to take advantage of the relocation of global value chains, must also focus on goods and services trade policy reforms. For example, Indonesia is considering phasing out restrictions on foreign investment that had reduced inflows to a relative trickle (2 percent of GDP), and is investing in roads and ports enhance the competitiveness of non-resource sectors of the economy. However, Indonesia also needs to make it easier for firms to import-to-export by reform its pre-shipment inspection, technical standards, and port-pricing strategies.

Many countries in the region penalize their firms by restricting trade and investment in services, and depriving them of access to efficient transport, finance, communication and other business services (Figure B.6.177). Liberalizing services policies is essential also to take advantage of the new opportunities in services in the post-COVID-19 world.

**Figure B.6.177. EAP countries still maintain relatively restrictive services trade policies**

EAP has been strongly affected by the policy measures by other countries but has shown restraint in retaliating. Countries around the world have resorted to extreme policy measures of restricting exports and relaxing quality requirements for imports of Personal Protective Equipment and Medical Devices (PPEs). This is done with the intention of ensuring availability of these products for their citizens. East Asia and Pacific region have been intensively affected by the measures implemented by other countries. On the extensive margin, major trading countries such as China, Vietnam and Indonesia have been at the receiving end of such drastic export curbing
measures more so than average country in the world. On the other hand, EAP countries have enacted fewer policy measures restricting exports relative to the average country in the world.

However, some policy measures harm regional trading partners more deeply than other partners. This increases the risk of retaliation and escalation of trade tension. It also damages the reputation of countries as reliable trading partners. Examples of such measures include Indonesia’s export ban of masks, raw materials for masks, antiseptics and medical protective garments, and Ethyl Alcohol which affected fellow ASEAN members indiscriminately along with other trading partners.

Another cause for concern is the extension of trade restrictions over and beyond the PPEs as countries retaliate on the goods in which they have the comparative advantage or of which they are major buyers. Examples of such policies include Vietnam’s export curbs and China’s minimum purchase price on rice (latter only affected Myanmar). This comes at the cost of trade tensions possibly widening in scope.
Annex B.6.1

Figure B.6.1.A1: Bilateral Trade in goods of Developing EAP countries, Selected Patterns

A. Exports to China (% gross exports)

B. Imports to China (% gross imports)

C. Exports to Developing EAP (% gross exports)

D. Imports to Developing EAP (% gross imports)

Source: Constantinescu, Mattoo and Ruta (2018)

Notes: Panels A and B represent bilateral trade with China, panels C and D represent bilateral trade with EAP region excluding China
Figure B.6.1.A2: China’s Role in Developing EAP participation in GVCs

A. China’s share in total Foreign Value Added (FVA) embodied in a country’s gross exports (percent)

B. China’s share in total Domestic Value Added (DVA) embodied in a country’s gross exports (percent)

Source: Constantinescu, Mattoo and Ruta (2018) using OECD TiVA
Notes: Trade refers to goods and services. 45-degree line shown as dotted line.
Annex B.6.2: Industrial Production

Figure B.6.2.A1: Changes in industrial production are positively correlated with changes in work mobility

Source: Espitia et al. (2020)
Figure B.6.2.A2: Changes in export growth are positively correlated with changes in industrial production across exporting countries

Source: Espitia et al. (2020)
Figure B.6.2.A3: Changes in import growth are positively correlated with changes in industrial production across importing countries

Source: Espitia et al. (2020)
Annex B.6.3: Examples of Interventions (by EAP):

Export Restrictions

Indonesia:
Export ban of masks, raw materials for masks, antiseptics and medical protective garments, announced on 17th March and enacted on 18th March to last until 30th June. This affected 29 importing countries including other ASEAN members.
Export ban of ethyl alcohol announced on 26th March and enacted on 27th March to last until 30th of June. This only affected Japan, China, Philippines and Malaysia.
Increased Plantation Fund Tariff for Export of Palm Oil and Its Derivative Products announced and enacted on 1st June that is still in force. This affected 85 countries.

China:
Ministry introduces strict quality controls on COVID-19-related medical exports, announced on 31st March and enacted on 1st April. This affected 102 countries.

Vietnam:
Exports of medical masks restricted due to the COVID-19 pandemic, announced on 28th February and enacted on the same day to last until 28th April. This measure affected 70 importing countries.
Temporary suspension of new rice exports due to the COVID-19 pandemic announced on 24th March and enacted on 25th March, lasted until 10th April. This measure affected 42 importing countries. Additional export quota for rice for the month of April announced on 21st April and enacted on the same day to last until 30th April.

Thailand:
Export of face masks banned in relation to the COVID-19 outbreak announced on 21st February and is still in force. This affected 16 other countries.
Exports of certain bird eggs banned temporarily due to the COVID-19 pandemic announced on 26th March and enacted on the same day to last until 30th April. This only affected Hong Kong, SAR, China and Singapore.

Malaysia:
Export restriction imposed on face masks in response to the COVID-19 pandemic announced on 19th March and enacted on 20th March, is still in force. This affected Singapore, US, Thailand, Japan, Germany, France, Australia.

Import Restrictions

Indonesia:
Import ban for certain type of sugar announced on 18th February and enacted on 19th March, currently in force. This affected Thailand, Australia, Brazil and Korea. 2020 update on import
provisions for steel and iron products announced on 31st January and enacted on the same day, still in force. This affected India, Thailand, Vietnam, Singapore, Malaysia, Japan, China, Korea and Australia.

China:
2020 minimum purchase price for rice increases, announced on 28th February and is still in force. This only affected Myanmar. Quotas on tax-free imports of equipment in the terrestrial oil/gas exploration sector removed, announced on 20th March and enacted on the same day, set to expire at the end of 2020. This adversely affected 53 countries.

Vietnam’s measures were anti-dumping related and were announced before 2020.

Thailand:
Measures and incentives announced to accelerate investments in the medical sector in response to the COVID-19 outbreak announced on 13th April to last until 30th June.

Malaysia:
Fourth Stimulus Package announced in response to the COVID-19 pandemic (June 2020) was announced on 6th June and is currently in force, set to expire at the end of the year. This is measure of internal taxation of imports and it affected 12 motor cars exporting countries.

**Import Liberalization**
Indonesia:
Temporary scrapping of licenses for imports of onions and garlic announced on 18th March and enacted on the same day to last until 31st May. This affected China, India, New Zealand and Netherlands. Temporary import barrier removal for products related to COVID-19 pandemic was announced on 20th March and enacted on 23rd March to last until 30th June. This affected 15 countries. Temporary import license exemption for used ventilators announced on 2nd April and enacted on the same day, to last until 30th June. This affected 12 countries. Tax Exemption for import of medicine and health equipment announced on 17th April and enacted on the same day and is still in force. This affected 37 countries. Removal of Import Ban on Dichlorofluoromethane and Other Related Chemicals announced on 25th February and enacted on 24th April and is still in force. This only affected China.

China:
Government announces tax-free imports for certain goods related to prevention and control of COVID-19 epidemic announced on 13th March and enacted on the same day, to last until 30th September. This affected 102 other countries. Tax-free imports enacted for certain epidemic prevention materials was announced on 1st February and enacted on the same day to be last until
30th September; this affected 44 countries. Quotas on tax-free imports of equipment in the terrestrial oil/gas exploration sector removed, announced on 20th March and enacted on the same day, set to expire at the end of 2020. This favorably affected 60 countries. Second batch of tariff exemptions for US imports affect by 'trade war' announced on 12th May and enacted on 19th May and is still in force.

Vietnam:
Reduction of MFN Tariffs on Wheat and Select Agricultural Products announced on 25th May and enacted on 10th July and is still in force. This affected 37 countries.

Thailand:
Import duty exemption on face masks during COVID-19 pandemic announced on 24th March and enacted on the same day, set to expire on 20th September. This affected 12 countries.

Malaysia:
Temporary import duty exemption on face masks in response to the COVID-19 pandemic announced on 21st March and enacted on 23rd March and is still in force. This affected Singapore, US, Thailand,

Vietnam, Hong Kong, SAR China and China:
Exemption from import tax on medical products for the Ministry of Health due to the COVID-19 pandemic was announced on 24th March and enacted on 25th March and is still in force. This affected 28 countries.

EAP was affected more severely by all kinds of policy interventions relative to average country, but EAP itself enacted fewer policy measures relative to average country. Also, policy restrictions that began in medical products have now transcended into other products. Policy Interventions were swift, indiscriminate, and mostly of short duration.
References


