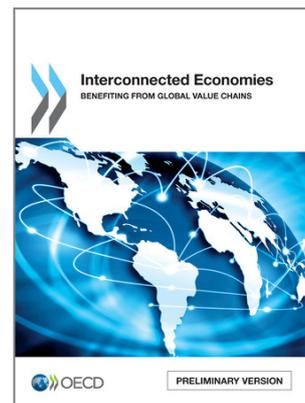


## Interconnected Economies. Benefiting from Global Value Chains

*Summary in English*



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- Today, “what you do” (the activities a firm or country is involved in) matters more for growth and employment than “what you sell” (the final product).
- Global value chains (GVCs) allow firms and economies to “do” the part of the process they are best at, using intermediate goods and services from elsewhere without having to develop a whole industry.
- Outsourcing and offshoring enhance competitiveness by providing access to cheaper, more differentiated, and better quality inputs.
- The growing interconnectedness among economies creates important opportunities but also new policy challenges.

## *Competitiveness*

- Competitiveness in GVCs requires strengthening factors of production that are “sticky” and unlikely to cross national borders. This implies investment in human capital and skills and high-quality infrastructure, and encouraging strong industry-university linkages and other tacit knowledge. The quality of institutions and government are also important in firms’ investment decisions.
- Small and medium-sized enterprises (SMEs) play an important role in niche areas of GVCs and contribute to the exports of larger firms.
- Manufacturing remains a core activity in GVCs, even if much value creation now involves services.
- Old-style support policies ignore the interconnected nature of production in GVCs and the need for international competition and openness. They raise the risk of protectionism, whereas success in international markets depends as much on the capacity to import high-quality inputs as on the capacity to export.

## *Trade*

- In most economies, around one-third of intermediate imports end up in exports. In GVCs, tariffs and other import barriers are effectively a tax on exports. Export restrictions can also affect the efficient functioning of GVCs and raise costs. The negative effects of trade protection are compounded when parts and components cross borders many times.
- Trade-facilitating measures, such as fast and efficient port and custom procedures, permit the smooth operation of value chains. Convergence of standards and certification requirements and mutual recognition agreements can alleviate burdens on exporting firms.
- While liberalising tariffs can create new trade opportunities, GVCs also require efficient services and the possibility to move people, capital and technology across borders.
- Services account for over half of value creation in GVCs in many OECD countries and over 30% in China.

## *Investment*

- Given the important role of multinational enterprises (MNEs), lowering investment barriers is an efficient way for a country to become integrated in GVCs. By inhibiting the efficient functioning of GVCs, impediments to cross-border investment can have negative welfare impacts in both home and host countries.
- A regime built on thousands of bilateral and regional investment agreements does not adequately reflect the interconnected nature of economies in GVCs.
- Investment promotion and facilitation need to focus more closely on activities undertaken in GVCs than on industries. Policies must recognise that success depends on both inward and outward investment.
- Large MNEs, including some state-owned enterprises (SOEs) are prominent players in GVCs, raising policy concerns, for example about the effects on competition and markets further downstream.
- GVCs can support the spread of ideas on responsible business conduct; it is essential that business be conducted in a manner respectful of human rights and dignity as prescribed by the OECD Guidelines for Multinational Enterprises, ILO and UN recognized standards.

## *Development*

- Through access to networks, global markets, capital, knowledge and technology, integration in a GVC can be a first step to economic development.
- Since GVCs involve activities contracted within and between MNEs and independent suppliers, the ability to enforce contracts is crucial. Countries with sound legal systems tend to export more in more complex industries. Tasks that require more complex contracts are more easily carried out in countries with well-functioning contractual institutions.
- Many low-income countries remain excluded from GVCs, due to their location, lack of natural resources, lack of infrastructure, or business environment.

### *Adjustment and risks*

- International competition in GVCs will entail adjustment costs, as some activities grow and others decline, and as activities are relocated across countries.
- Policy needs to facilitate the adjustment process through labour market and social policies and through investment in education and skills. Structural policies also help strengthen the flexibility and hence the resilience of economies against future shocks.
- The growing interconnectedness of economies is a source of resilience. It can also lead to contagion if events in one part of the GVC feed through the entire system.
- Given the broad welfare implications of GVCs, governments, enterprises and other stakeholders need to remain mindful of their respective roles and responsibilities with respect to governance.

### *Key recommendations*

- Reinforce multilateral co-operation and co-ordination to maintain the open and predictable international investment climate that has supported investment in GVCs, and to help reconcile national policies with the global nature of economic activity.
- Keep markets open and resist protectionist pressure. Advance trade liberalisation, ideally multilaterally to maximise upstream and downstream linkages. Trade facilitation measures should be taken, including through a WTO Agreement.
- Avoid incentive wars to attract high-value stages of a GVC.
- Support SMEs by policies that encourage the development of linkages with international firms, foster their supply capacity and ability to innovate, and facilitate the adoption of product standards.
- Invest in skills and advanced manufacturing technologies, including in traditional industries, through policies that strengthen networks and co-operation to help anchor production and value creation.
- Support investment in knowledge assets such as R&D and design, and foster the development of important economic competencies, notably skills and management.
- Reform regulation and liberalise trade and investment in services to enhance competition and increase the productivity and quality of services.
- Lower investment barriers to help developing countries become integrated in GVCs.
- Provide support to emerging economies to improve their business environments and to build their capacities for engaging in international trade.
- Support capacity building through “aid for trade” initiatives to help the poorest developing economies.
- While firms have the first responsibility to address potential risks, encourage a multi-stakeholder approach that involves governments to support information sharing and capability building.
- Initiate further work to measure the role of investment in GVCs, and the impacts of GVCs on employment, skills and incomes.

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