Global Value Chains
- What are the Policy Questions -

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Key Policy Questions

- To what extent are firms and industries involved in GVCs?
- What is the impact of GVC involvement?
- What factors influence the level of GVC participation?
- What factors influence the outcomes?
To what extent do industries and economies participate in GVCs?

GVC participation across countries, 2009

- Forward Participation
- Backward Participation

Share of Foreign Value-added in Gross Exports

- 2009
- 1995

- Are Canadian firms under participating in GVCs?
What is the impact of participating in GVCs?

- Type of firm:
  - Lead firms, foreign controlled firms and supplying firms

- Impacts on:
  - Productivity
  - Employment
  - R&D/Innovation
  - Competitiveness
It is unclear what a lead firm is
The impact of lead firms

- Foreign-controlled firms are more productive and pay higher wages and are more innovative than purely domestic firms.

- Foreign-controlled firms are an important source for positive economic spillovers.

- MNEs (domestic firms with investments abroad) are the most productive domestic firms and pay the highest wages. They generally look similar to foreign-controlled firms.

- Foreign controlled firms and MNEs account for most exports.

- The impact of these firms on SME participation in GVCs is unclear.
Sales by foreign affiliates are more important than exports for most markets

Canadian Exports and Foreign Affiliate Sales

Data: Statistics Canada, 2012
Source: Office of the Chief Economist, DFATD
Many SMEs export - directly or indirectly...

Direct and Indirect SME Exporters

- 9.1% Export
- 1.3% Export and Sell Inputs
- 3.7% Sell Inputs which are then Exported
- 5.0% Share of SMEs that Export Indirectly
- 10.4% Share of SMEs that Export

Data: Survey of SME Financing and Growth, data for 2011.
Source: Office of the Chief Economist, DFATD
All SMEs

3.2%

Percent of SMEs

Outsourcing by Canadian SMEs

Data: Survey on Financing and Growth of SMEs, data for 2011.
Source: Office of the Chief Economist, DFAIT

...and a few outsource
The impact of SME participation in GVCs

- SMEs account for most employment, but only about 30% of exports
- SMEs are less productive, less innovative and pay lower wages
- 10.4% of SMEs exports (increases to over 30% in manufacturing)
- SMEs that export are more productive than those that do not.
- SMEs that import are more productive than purely domestic firms.

**Depth of International Engagement**

1. Importer
2. Supplier Exporter
3. Indirect Exporter
4. Occasional Exporter
5. Alternate Modes of Entry
6. Single Product or Market
7. Multiple Products and Markets
8. Investor

**Level of Productivity and Innovativeness?**

- How to get more SMEs to internationalize or participate in GVCs?
- How to increase their depth of internationalization / GVC participation?
Canada is more important as a destination than as a source of R&D

Cross-Border R&D Shares

Percent

Canada | Europe | U.S. | Japan | Other A/P | Africa & ME | Latin America

Data: OECD
Source: Hall (2011)
What factors influence the level of GVC participation?

- GVC participation largely seen as a positive – international activity that contributes to more effective allocation of resources, increased pressure to innovate, and improved productivity leasing to higher wages and standards of living.
  - SMEs appear to realize the risks and benefits of supplying large firms/MNEs.
  - An opportunity to expand sales, gain economies of scale and become more competitive.
  - The risks associated with serving a dominant customer.

- Primary policy focus has become a perceived lack of GVC participation, and in particular, by SMEs.

- Barriers identified are varied and differ by industry (and how GVC participation is defined).
Trade policy

- In budgets 2009 and 2010, Canada unilaterally eliminated tariffs on all intermediate manufactured products and machinery and equipment.

- FTAs concluded with EU (CETA), Asia (TPP)

- Taken with NAFTA will result in agreements with three main GVC regions

- But, overlapping rules of origin and gaps (government procurement).

- Services, movement of people and investment not as free.

- Evolution of NAFTA is telling:
  - Declining use of NAFTA by Canadian exporters
  - Remaining areas for further liberalization are in areas traditionally considered to be “domestic”. (North American Competitiveness Work Plan, Beyond the Border)
Trade promotion

- Increasing focus on SMEs
- Increase internationalization of SMEs, including through GVC participation
- What is the path to internationalization?
  - Import => indirect export => direct export
  - U.S. first vs born global
  - Multinational pull
- What are the barriers?
  - Informational (trade commissioner service)
  - Financial (Trade finance, general access to capital)
  - Risk aversion, managerial skill/experience
“Domestic” economic environment

- Blurring of the line between domestic and international.

- Firms must compete not just in foreign markets but in domestic markets as well.

- “Domestic” economic environment is the most important factor for international competitiveness and to attract foreign investment.

- Most “domestic value-added” in exports is from supporting industries.

- Many barriers to increased trade openness are the responsibility of “domestic ministries”.
What factors influence the outcomes of GVC participation?
Other issues

- The risks of GVCs
  - Natural disasters
  - Complexity
  - Contagion

- Evidence suggests that slowdown in growth of global trade was due in part to slowing GVCs
  - Maturity of the business strategy?
  - Changing in driving factors:
    - Innovation (containerization, telecommunications)
    - Trade Openness (trade deals, opening of closed economies)
    - Geographic (China)