COMPETING INTEGRATIONS IN SOUTHEAST ASIA

Is FDI-led industrialization the way forward? A labour perspective

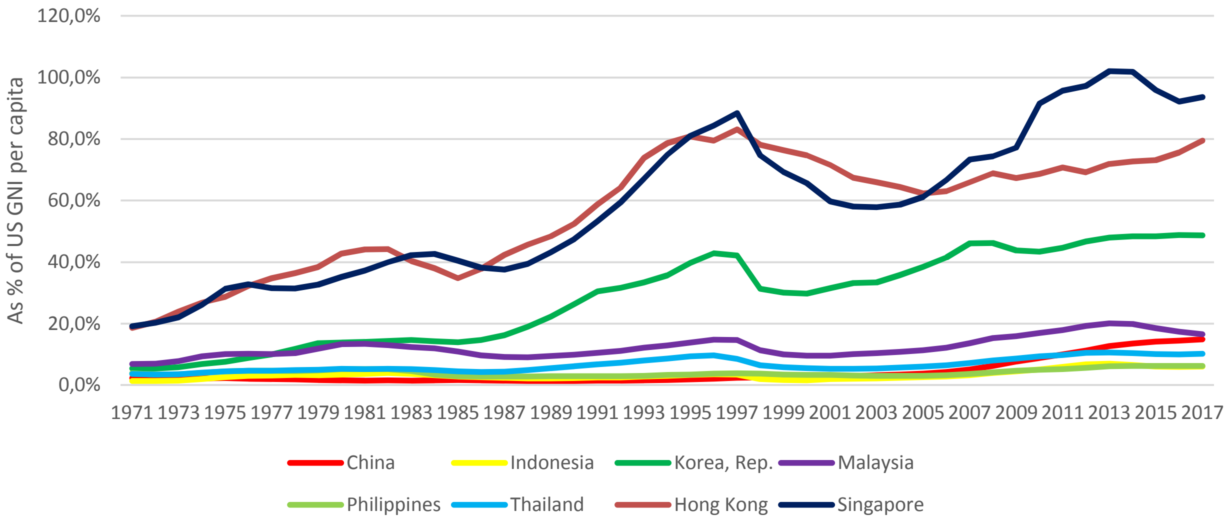
Pietro Masina, January 2020

INTRODUCTION

ASEAN countries have achieved high levels of GDP and GDP per capita growth over the last forty years. Growth was accompanied by a sharp decline in absolute poverty levels. This makes Southeast Asia, compared to other world regions, a success story. In the wider framework of East Asia (including both Northeast and Southeast Asia), however, the performance of the ASEAN countries emerges as more questionable. The regional crisis of 1997-98 represented a watershed rather than a temporary pain as growth rates did not return to previous levels. The poorest countries in the region – Cambodia, Laos and Malaysia – joined Vietnam as new actors in the regional production networks, but their growth model seems to repeat the pattern of ASEAN's more mature economies.

The fundamental problem is the failure to close the gap with industrialized countries, repeating the impressive catching-up achieved by Japan and then the four "tigers" – Hong Kong, Singapore, South Korea and Taiwan. Figure 1 measures the performance of several Asian countries as a percentage of the American GNI per capita in current US dollars. Figure 1 shows that while Singapore and Hong Kong have now GNI per capital levels similar to the Unites States and South Korea levelled at about 50%, Southeast Asian countries have failed to improve their relative position. The best performer, Malaysia, had the same GNI per capita as South Korea in 1980 and reaches now only 20% of the American one.

Figure 1 – GNI per capita growth, 1971-2017 (Current US$)



In recent years, the literature on Southeast Asian economies has used the expression "middle-income trap" to describe the challenges for these countries. The trap would be a result of competitive pressure from neighbours with lower labour costs and the inability to move upwards to more value adding productions. However, this concept describes the problem rather than explaining the difficulties involved in climbing the value chains. The present policy brief builds upon current CRISEA research looking at how the failed catching-up can be understood as a result of a development pattern where ASEAN countries and firms appear to be in a relation of dependence on foreign capital – a relationship in which ASEAN countries are locked in labour-intensive and low value-added productions. Contrary to prevailing wisdom, low wages and poor working conditions are not the temporary price to be paid to climb the value chain but tend to become a permanent feature of ASEAN industrial participation in regional and global production networks.

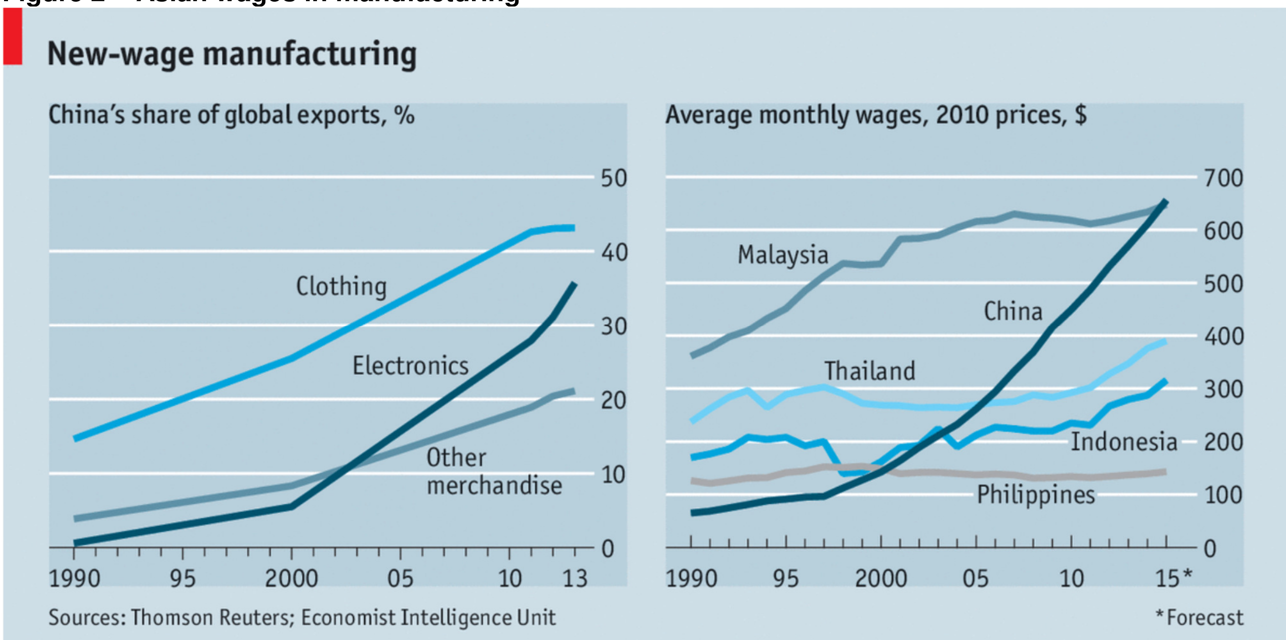
Evidence and Analysis

The inclusion of Southeast Asia in a Japan-led regional system of division of labour emerged in the second half of the 1980s. After the Plaza Agreements (1985), Japan, soon followed by South Korea and Taiwan, responded to currency appreciation and high labour costs by moving labour-intensive productions to Malaysia, Thailand, the Philippines and Indonesia (particularly the island of Batam). The role of Southeast Asia in regional production networks become even more relevant since the mid-2000s, when Vietnam emerged as a major manufacturing hub, first in garment production and then electronics. Eventually Cambodia and, to a certain extent, Laos were also integrated as garment producers. While the inclusion of Southeast Asia in the regional division of labour can be seen as the extension of the success story that allowed Singapore, South Korea and Taiwan to graduate as industrialised countries, key differences explain why ASEAN countries have not replicated the so-called miracle. The inclusion of Singapore, South Korea and Taiwan in a Japan-led production system was based on technology transfer which allowed locally-owned, independent firms to become subcontractors for foreign brands. The involvement of these firms in regional value chains was coherent with the development state-type industrial policies pursued by national governments and resulted in successful industrial upgrading. The involvement of Southeast Asia in a wider regional production system after the Plaza Agreement occurred in a radically different international environment, which was much less favourable to market-distorting national industrial strategies. Foreign direct investment (FDI) became an alternative to, rather than a medium of, technology transfer. In this context, FDI to Southeast Asia often results in the consolidation of already existing production networks, with key subcontractors following the lead firm in the same industrial park in the host country, while local firms remain confined to law value-added productions. Even in the relatively successful Malaysian electronics or in Thai automotive production, the involvement of local firms did not entail a substantial industrial upgrading – thus maintaining the country's dependence on cheap labour as a competitive factor.

Large FDI flows contributed to generate employment in export-oriented manufacturing industry, but did not contribute to a substantial expansion of national industry. Three related issues are critical. First, FDI-led, export-oriented production tends to be disconnected from national demand and – with lack of adequate industrial policies – do not create backward and forward linkages with national industry (that is, do neither integrate national firms in their supply chains nor sell their products locally). Second, market liberalization policies pursued by ASEAN countries to attract FDI expose national producers to strong competition in non-export-oriented sectors with a *deindustrialization* effect. Third, as ongoing CRISEA research indicates, workers tend to move in and out of manufacturing employment in a process that could be described as circular migration. Low wages, hard working conditions and high living costs in industrial areas keep workers only few years in manufacturing industry before moving back to rural areas or to the urban informal sector. In countries in which a substantial share of industrial labour force is made up of international migrants (particularly Malaysia and Thailand), legal constraints contribute to make the foreign labour force transient and vulnerable, thereby reducing labour costs.

The post-Plaza intensification of Southeast Asian participation in regional production networks was parallel to the involvement of China. To a large extent, China shares similar conditions of labour precarity and vulnerability. However, Chinese industrial wages have substantially increased in line with the national GNI per capita, as a result of successful industrial upgrading. In comparison, Southeast Asian wages have grown much less, even in the most prosperous countries of the region as the import of cheap labour from other Asian countries led to a continuous race to the bottom. As recently noticed by *The Economist* (see figure 2), average Chinese wages have closed the gap with Southeast Asia and are now higher than Malaysia's.

Figure 2 – Asian wages in manufacturing



In most Southeast Asian countries, there is a debate on the quality of foreign investment. The disconnection of current FDI-led processes with national demand and national production is confirmed by several studies published by the United Nations Industrial Development Organization (UNIDO). The debate about the "middle-income trap" has demonstrated that these countries are unable to maintain high growth levels and may even see a reversal of previous gains. However, the debate seems still far from addressing the root causes of the current difficulties. Our research suggests that these are related to a pattern of industrial development dependence, in which labour-unfriendly policies and practices contribute to weaken these countries and make them more vulnerable.

Policy Implications and Recommendations

FDI-led, export-oriented industrial processes contributed to make Southeast Asian countries more dependent on foreign capital and had a problematic impact on labour, contributing to a process described as a race to the bottom in terms of wages and workers' rights. A number of policy implications can be derived from this analysis.

Today, in most ASEAN countries there are debates regarding the *quality* of FDI. These debates focus on the need of increasing the contribution of foreign investment to technology transfers and strengthening the linkages between foreign-led productions and local firms. The aim is to promote industrial diffusion and technology upgrading allowing national firms to climb the value chain. However, these debates neglect the obvious fact that improving the position of ASEAN countries in regional and global production networks requires these countries to abandon their labour-unfriendly policies and to create a labour force with stronger skills, higher wages and better working conditions.

Secondly, the results of over thirty years of FDI-led, export-driven industrialization in Southeast Asia have been less than satisfactory. The experiences of the first generation of Asia's Newly Industrialized Economies (NIE; Japan, South Korea, Taiwan and Singapore) followed by China, have indicated that a more sustainable strategy conjugates export promotion with policies supporting the development of a national industry. This strategy implies strengthening national demand for national goods. A gradual increase of industrial wages is therefore essential to generate a stronger demand for local industrial products.

As an EU-funded project, CRISEA has also been looking at the implications of bilateral trade agreements currently pursued with ASEAN countries. There is a serious risk that these agreements support a race to the bottom both for Asian and European workers – leading to the intensification of export-driven industrial strategies in Asia; and an uneven competition in Europe from goods produced by workers with low wages and limited labour rights. From a labour-informed perspective, it is paramount that trade agreements become an instrument of co-development addressing the societal needs of the two regions. At a time when the European Union launches a new green deal, it is important that human and environmental sustainability are coherently pursued in the external economic relations and become the cornerstone of win-win cooperation with developing countries.

Finally, in most Southeast Asian countries trade unions and labour-related civil society organizations are repressed or face obstacles in representing grassroots voices at the policy table. This is a matter of concern for CRISEA researchers, too, as our macro-micro analysis has led to a better understanding of grassroots conditions, needs and perspectives. Strengthening the ability of Southeast Asian countries to incorporate these grassroots interests in policy debate would make an important contribution to sustainable development. It would also increase the quality of the policy debate with foreign partners, including the European Union.

Research Parameters

Competing Regional Integrations in Southeast Asia (CRISEA) is an interdisciplinary research project that studies multiple forces affecting regional integration in Southeast Asia and the challenges they present to the peoples of Southeast Asia and its regional institutional framework, ASEAN.

CRISEA innovates by encouraging 'macro-micro' dialogue between disciplines: global level analyses in international relations and political economy alongside socio-cultural insights from the grassroots methodologies of social sciences and the humanities.

Coordinated by the Ecole française d'Extrême-Orient (EFEO) with its unique network of ten field centres in Southeast Asia, the project brings together researchers from seven European and six Southeast Asian institutions, with three objectives:

1. Research on regional integration

Multiple internal and external forces drive regional integration in Southeast Asia and compete for resources and legitimacy. CRISEA has identified five 'arenas of competition' for the interplay of these forces, investigated in the project's five research Work Packages. It further aims to assess the extent to which they call into question the centrality of ASEAN's regional model.

2. Policy relevance

CRISEA reaches beyond academia to engage in public debate and impact on practitioners in government and non-government spheres. By establishing mechanisms for dialogue with targeted audiences of policymakers, stakeholders and the public, the project furthers European science diplomacy in Southeast Asia and promotes evidence-based policymaking.

3. Networking and capacity-building

CRISEA reinforces the European Research Area (ERA) in the field of Asian Studies through coordinated EU-ASEAN academic exchange and network development. It connects major research hubs with emerging expertise across Europe and Southeast Asia. CRISEA also promotes participation of younger generation academics in all its activities, notably policy dialogues.

PROJECT IDENTITY

PROJECT NAME	Competing Integrations in Southeast Asia (CRISEA)
COORDINATOR	Andrew Hardy, EFEO, Paris, France, hardyvn25@yahoo.com.
CONSORTIUM	Ecole française d'Extrême-Orient – EFEO – Paris, France University of Hamburg – UHAM – Hamburg, Germany University of Naples l'Orientale – UNO – Naples, Italy Institute of Social and Political Sciences – ISCSP - Lisbon, Portugal University of Lodz - UL – Lodz, Poland University of Oslo – UiO – Oslo, Norway University of Cambridge – Cam – Cambridge, UK Chiang Mai University – CMU – Chiang Mai, Thailand The Centre for Strategic and International Studies - CSIS – Jakarta, Indonesia Ateneo de Manila University – ADMU – Quezon City, Philippines University of Malaya – UM – Kuala Lumpur, Malaysia Vietnamese Academy of Social Sciences – VASS – Hanoi, Vietnam The University of Mandalay – MU – Mandalay, Myanmar
FUNDING SCHEME	H2020 Framework Programme for Research and Innovation of the European Union – Research Innovation Action (RIA) – Europe in a changing world, Engaging together globally
DURATION	November 2017 – October 2020 (36 months).
BUDGET	EU contribution: €2,500,000.00
WEBSITE	www.crisea.eu
FOR MORE INFORMATION	Contact: Jacques LEIDER, CRISEA scientific coordinator – jacques.leider@efeo.net Elisabeth LACROIX, CRISEA project manager – ideas.lacroix@gmail.com

FURTHER READING

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