Policies to Facilitate Upgrading in Global Value Chains

Submitted by: WTO
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Defining Upgrading

• Different types of upgrading...
  • Process upgrading: Improving production processes to increase productivity
  • Product upgrading: Improving products to obtain higher margins
  • Functional upgrading: Taking over higher-margin functions in GVCs
  • Channel upgrading: Making use of new distribution channels
  • Intersectoral upgrading: Entering higher-margin sectors

• ...might require different policies.

➢ The right upgrading policies tend to be case-specific but some policies apply broadly.
Upgrading trajectories

• Global Value Chain integration happens in most economies through the entry of foreign lead firms.

• Upgrading typically occurs when
  • knowledge spills over from lead firms to domestic firms (inter-firm) or
  • when lead firms expand their local activities (intra-firm).
Upgrading trajectories

• This can occur through different channels, e.g.:

  • Staff training,

  • Staff turnover (e.g. employee spinoffs use better technology and have a 4-year head start over other firms in accessing markets their parent firms serve),

  • Vertical and horizontal firm-to-firm relationships (e.g. a 10 p.p. increase in foreign presence is associated with an increase in the productivity of domestic firms in supplier sectors of about 9%).

• Policies can increase the likelihood of such spillovers.
Upgrading trajectories

Figure 4. Skills Transfer (Training)

Source: Calculations on World Bank Enterprise Surveys, 2010-2018; 30 most populous developing countries in the sample sorted by absolute performance of MNE 50. Note: High skills refers to the aggregate of high and semi-skilled workers.
Creating the right policy environment

• Economies should look beyond pure integration policies. To benefit from GVCs, an integrated policy approach to integrating and upgrading is needed.

➢ Policies should not only aim at attracting foreign investments but also incentivize the use of local resources.

• Lead firms tend to prefer local sourcing but require specific inputs (adequate quality, adherence to standards, etc.).

• Policies can increase the availability of such inputs.
Creating the right policy environment

• These policies can induce both intra- and inter-firm upgrading:

  • Human capital development:
    • Education,
    • Training,
    • R&D incentives.

  • Domestic market development:
    • Ease-of-doing business policies,
    • Procurement policies,
    • Open trade policies,
    • Environmental and social regulations.
    • R&D incentives.
Education

• Investments into education belong to the most profitable investments since they benefit all aspects of economy, not just trade.

• Global structural change and digitization continuously drives up demand for skilled workers.

• But returns from education investments take time to manifest.
Training

• Training policies in contrast can lead to immediate returns.

• Using resources of lead firms or chambers of commerce imply low costs.

• Policies should optimally be designed together with lead firms and provide incentives to lead firms (e.g. contingent tax credits).
Training: Samsung Viet Nam
Training: Samsung Viet Nam

• Since 2014, in collaboration with the Vietnamese government, Samsung has held an annual workshop known as the Samsung Sourcing Fair.

• Since 2015, Samsung has offered a 3-month technical consultation programme in which experts from Korea consult Vietnamese firms.

• Since 2020 under a four-year agreement with the Vietnamese government, Samsung holds two annual 14-week training courses.
Training: Samsung Viet Nam

- The number of local enterprises being Samsung’s tier-1 vendors has increased from 4 in 2014 to 42 in 2019. By 2020, the number is projected to reach 50.

- In 2020, Samsung started building a $220 million R&D center in Viet Nam.
Domestic market development

- A dynamic domestic business environment is, with human capital development, the most important enabler of spillovers.

- A variety of policies can help to develop the domestic market:
  
  - Ensuring demand through integration (→ open trade policies) and/or procurement: scale economies!
  
  - Ensuring access to affordable high-quality inputs (→ open trade policies ≠ local content requirements): e.g. lower input tariffs account on average for 31% of the new products introduced by domestic firms.

  - Supporting innovation through appropriate R&D policies.
Domestic market development

• Fast and transparent business regulations.

• Assistance with environmental and social standards demanded in major markets (e.g. evidence suggests that developing economies with better labour and environmental policies upgrade faster).

• Ensuring access to qualified staff (→ open trade policies: mode 4 services trade: e.g. in-person business travel can account for 20% of the higher patenting in Germany’s Greater Stuttgart area, compared to Portugal’s Algarve region).

• Human capital development also benefits domestic market development.
Thank you!

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