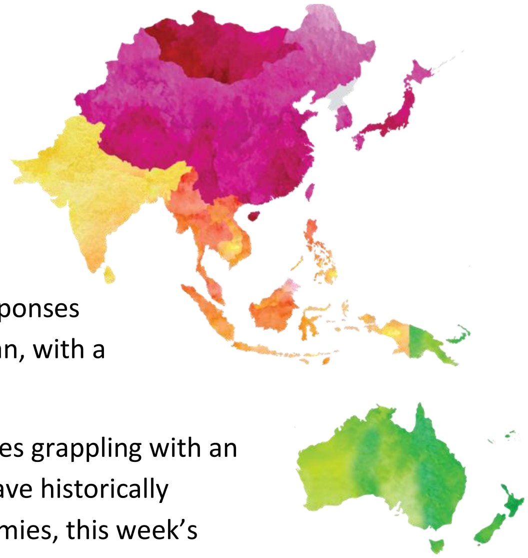
August 13, 2020



Dear BGA Clients,

Our report this week is the second in a series on the effects of Covid-19 on supply chains across the Asia-Pacific, perhaps the single most salient issue affecting economies around the Pacific Rim. This week's report will highlight the broader trends and how the wide range of responses are reflected in four markets: Australia, Malaysia, Singapore and Taiwan, with a special social intelligence highlight of Indonesia.

The markets highlighted this week exemplify export-oriented economies grappling with an increasingly threatening environment for the pro-trade policies that have historically propelled their growth. As a set of smaller and historically open economies, this week's underscored markets are threading the needle between responding to protectionist impulses at home and abroad while staying true to the principles that have brought them wealth. While each of the markets has taken steps to address visible issues in their medical supply chains, they are also cognizant of the need to remain interconnected in a rapidly evolving global landscape.

**In Australia, a country that had previously enjoyed an unparalleled run of economic growth on the back of strong exports to China and a robust relationship with the United States, boosting domestic production and diversifying trade supply chains are now at the forefront of the trade conversation.** Securing the supply of medical goods and equipment has dominated headlines, and the buildup of sovereign capability is likely to extend more broadly. However, once the initial panic subsides, the rush to build domestic capacity is likely to be tempered by the reality that Australia has benefited from remaining an open-trading nation and will continue to do so. Australia would struggle to find any market capable of replacing China's seemingly insatiable demand for its raw resources, and Australian leaders are conscious that the two economies will remain interlinked for the foreseeable future.

**In Malaysia, the Covid-19 pandemic has triggered the government to take strategic actions to ensure smooth supplies of medicine, food and other essential goods, both by bolstering domestic production and by securing trade relations.** Malaysia has outlined several incentive schemes to attract reshoring industries over the course of several special budgets. Domestically, the ministries are thinking of the best way to increase the country's self-sufficiency level to meet local consumption, particularly of agricultural and medical goods. Meanwhile, Malaysia has forcefully argued that ASEAN should deepen its internal trade relationships in the face of the pandemic.

**Singapore is doubling down on its posture of openness while pushing for increased resilience and diversification.** As a regional entrepot and manufacturing hub that has benefitted from liberalization over the past few decades, the city-state is a world leader in pushing back against the rising tide of trade skepticism. It has forged links with other smaller, pro-trade markets across the globe, from New Zealand to the United Arab Emirates, in an attempt to forcefully advocate for deepening international commerce. Singapore plans on creating a conducive environment for supply chains, biopharma and precision engineering sectors to invest for the long term by improving macro conditions and by strengthening links to the global markets for supplies, technology and talent.

**Taiwan had a head start on shifting its supply lines, as it was uniquely affected by the earlier U.S.-China trade war, and Taiwanese firms have undertaken some of the most significant reshoring developments.** Though increasingly confrontational rhetoric out of Beijing has rattled the island, Taiwan remains highly intertwined with mainland China thanks to an extensive network of manufacturing facilities. However, as the United States has stepped up its sanctions on China and the global environment has shifted toward more diversification, Taiwan's government and companies have led the way in relocating out of China. Most visibly expressed by TSMC's decision to cease production in China, Taiwanese firms are shifting some of that production either back home, elsewhere in the region or even to the United States, all while recognizing that some degree of economic linkage with the mainland is unavoidable.

Questions and comments are welcome and can be directed to BGA Head of Research Murray Hiebert at mhiebert@bowergroupasia.com.

Best Regards,

Murray Hiebert
Director of Research, BowerGroupAsia

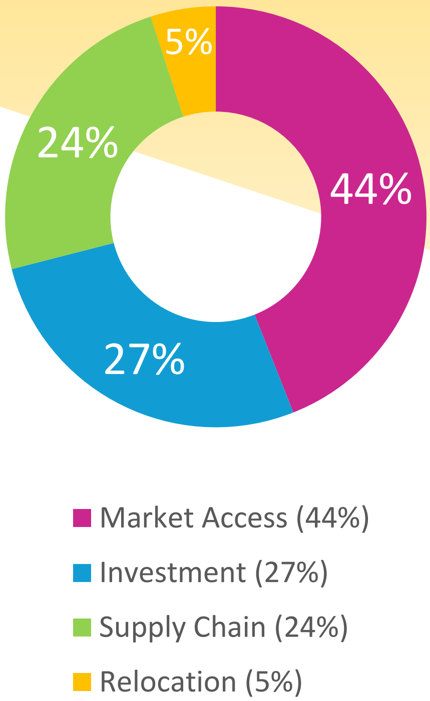
## Social Intelligence Spotlight: **Indonesia**

**This week's social intelligence spotlight evaluates how Covid-19 has shaped conversations in Indonesia's digital space on supply chains and related terms: investment, relocation and market access.** The bulk of the chatter referring specifically to supply chains (24 percent of mentions) highlighted the need for Indonesia to strengthen existing supply chains to weather the economic recession. Social media users touted the potential of big data analytics to achieve supply chain optimization to achieve that goal. Such sentiment runs parallel to the government's digital transformation initiatives, which officials believe may improve market access for Indonesian MSMEs.

**Prominent figures from the government and private sector agreed on the importance of strengthening Indonesia's supply chains to overcome the economic downturn.** Among notable key influencers, Minister of State-Owned Enterprises Erick Thohir proposed Indonesia bolster its supply chains and logistics systems by acquiring foreign firms that would allow Indonesia to enhance its position in the global value chain. In a similar vein, the chairman of Supply Chain Indonesia (SCI) and CEO of Ruang Logistik, Setijadi, called on the government to strengthen supply chains to support Indonesia's domestic steel industry, in part by relaxing import requirements for raw materials and limiting the quota for imported steel. Coverage of Indonesia's trade minister, Agus Suparmanto, also trended during the reporting period as the Regional Comprehensive Economic Partnership (RCEP) negotiations near a conclusion. While Suparmanto acknowledged that the RCEP may grant Indonesia greater market access, he also recognized the need for Indonesia to improve its logistics systems and the quality of its products.

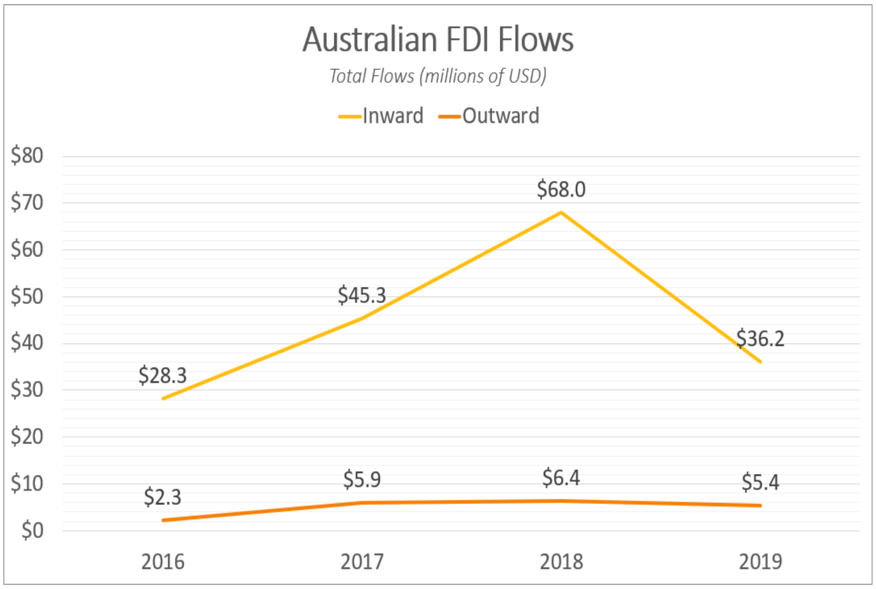
**Foreign investment tended to be viewed through the prism of economic recovery, uncovering a divergence of thought on its value.** A recent survey from Saiful Mujani Research and Consulting (SMRC), which found that 54 percent of Indonesians do not believe foreign investment has a positive impact on the economy, dominated much of this week's mentions feed. The survey spawned further conversations in the digital space, with some arguing that Indonesia must improve its regulatory environment to attract foreign investment — a necessary precursor to improving infrastructure and reviving the economy. Several users agreed that it will be difficult for Indonesia to capture foreign investment from China, claiming Indonesia cannot offer substantial value add beyond raw material exports. Others cited the recent relocation of 17 factories from China to Indonesia, valued at $37 billion, as evidence to the contrary.

**Social Media Discussion Topics in Indonesia**
August 6 to 12




## Australia

The U.S.-China trade war wedged Australia between its closest ally and largest trading partner. There were short-term upsides as China restricted U.S. trade, but in the longer term the risk is that improved U.S. access to China will come at the expense of Australian exporters in key sectors like agriculture. Beyond China and the United States, the bulk of Australia's trade is with the rest of the Asia-Pacific, where it is a key commodity exporter.




*Source: UNCTAD*

Australia is a trade-dependent economy; over the past 20 years, manufacturing as a share of Australian GDP has fallen from 13.8 percent to 5.6 percent, making Australian companies and consumers reliant on imports for goods in almost every sector. It is also a major global exporter, particularly in mining and agriculture. However, shortfalls experienced during the global Covid lockdown (for example, of personal protective equipment) sparked an uncharacteristic rethink. A new strain of thinking is focused on building up and sustaining sovereign capability in key areas.

The Foreign Investment Review Board, which approves or rejects large foreign investments, was already in the spotlight before the Covid-19 pandemic, but in March 2020 the government reduced the threshold for review to zero dollars as a temporary measure to prevent the fire sale of assets, and additional national security provisions are in the pipeline.

A key factor shaping future supply chain discussions in Australia is its current overweight dependency on the Chinese market and the increasing willingness of the Chinese Communist Party to use that leverage coercively during periods of political disagreements. The physical shutdown of universities is already driving major transformations in the education sector, which relied heavily on Chinese students. In the technology space, the government was the first to ban Chinese telecommunications providers from participating in the nation's 5G build. But these are likely just the start of the conversation.

## Malaysia

The Malaysian economy is relatively dependent on primary products and trading, but much of that trade is also deeply integrated with global supply chains. Approximately 82 percent of large firms in Malaysia and nearly half of all small or medium enterprises participate in global value chains. Furthermore, China is one of the largest trading partners for Malaysia. This means that disruptions to the Chinese supply chain will have significant effects on Malaysian production and exports.

The Covid-19 pandemic has caused Malaysian policymakers to focus on self-sufficiency. The government has allocated MYR 1 billion ($240 million) to the Food Security Fund to ensure sufficient and guaranteed supply of food. It is helping farmers, breeders and fishers in the form of agricultural, livestock and fishery inputs to encourage domestic production. In addition, it is setting up infrastructure facilities for food storage and distribution as well crop integration programs with an allocation of MYR 100 million ($23.8 million). A special fund with an allocation of MYR 64.4 million ($15.3 million) was also initiated to develop short-term agricultural projects that can produce results within three to six months.

The government is offering special incentives to attract foreign companies to relocate their operations to Malaysia. The plan includes tax holidays for investments above MYR 300 million ($71.5 million), investment tax allowances for companies relocating facilities into Malaysia and special allowances for manufacturing and agriculture.

The government has set up the Cabinet Committee on Food Security comprising industry players and appointed 12 advisers, dubbed the National Agriculture Advisory Council, to hear the industry's recommendations. Furthermore, the government has entrusted Malaysian Investment Development Authority (MIDA) with attracting investments in new and high technology areas post-Covid-19. MIDA is currently focusing on companies from countries that are affected by the trade war and the pandemic to shift their operations to Malaysia as a hub to penetrate the Southeast Asian market.

During the ASEAN Summit on Covid-19 on April 14, Malaysia proposed to the ASEAN countries to formulate a Regional Economic Recovery Plan that emphasized supply chain connectivity to ensure the flow of food and medical and essential supplies within the region. The government is supporting and committed to sign a free trade deal by this year with the Regional Comprehensive Economic Partnership (RCEP) countries to ensure the future economic development in Malaysia, promote the flow of investment and create a resilient supply chains network.

**Total impact from COVID-19**

| Sector | Shorter-containment scenario | | Longer-containment scenario | |
|---|---|---|---|---|
| | *as % of sector GDP* | *in $ millions* | *as % of sector GDP* | *in $ millions* |
| Agriculture, Mining and Quarrying | -6.2 | -$3,683 | -9.2 | -$5,459 |
| Business, Trade, Personal, and Public Services | -6.5 | -$10,740 | -9.7 | -$15,954 |
| Light/Heavy Manufacturing, Utilities, and Construction | -5.7 | -$5,830 | -8.5 | -$8,680 |
| Hotel and restaurants and Other Personal Services | -26.4 | -$4,933 | -38.5 | -$7,188 |
| Transport services | -16.9 | -$2,132 | -24.7 | -$3,115 |
| **TOTAL (Economy-wide)** | **-7.6** | **-$27,319** | **-11.3** | **-$40,395** |

*Source: Asian Development Bank*

## Singapore

As an important manufacturing and innovation hub, Singapore's export-reliant economy is highly susceptible to external demands and has already encountered supply-chain disruptions due to U.S.-China trade tensions prior to the pandemic. Singapore's Minister of Trade and Industry Chan Chun Sing warned companies in early 2019 to diversify sectors and markets because of the shift in global trade flows brought about by the conflict, and he suggested businesses upgrade their capabilities and workers' skills.

Ranked as the top logistics hub in Asia for the past decade by the World Bank, Singapore has greatly benefited from a boom in regional cross-border trade and an increase in regional consumption as Singapore's free trade agreements within ASEAN and the rest of the world entrenched Singapore in global value and supply chains. Naturally, the pandemic greatly challenged this ease in connectivity as borders started closing. Singapore then worked with like-minded countries such as New Zealand in issuing a joint ministerial statement calling for the importance of open supply chains, and other countries including Australia, Canada, Chile, China, Myanmar, New Zealand joined them in making a commitment to the free flow of goods and essential supplies.

Although Singapore's borders remain closed to travelers, barring green lane arrangements with Malaysia and China for business and official travel accompanied by strict requisites, Singapore is committed to keeping critical infrastructure such as air and seaports open. Plans to maintain its aviation and port hub status will be revealed in the coming weeks.

*Minister of Trade and Industry Chan Chung Sing*

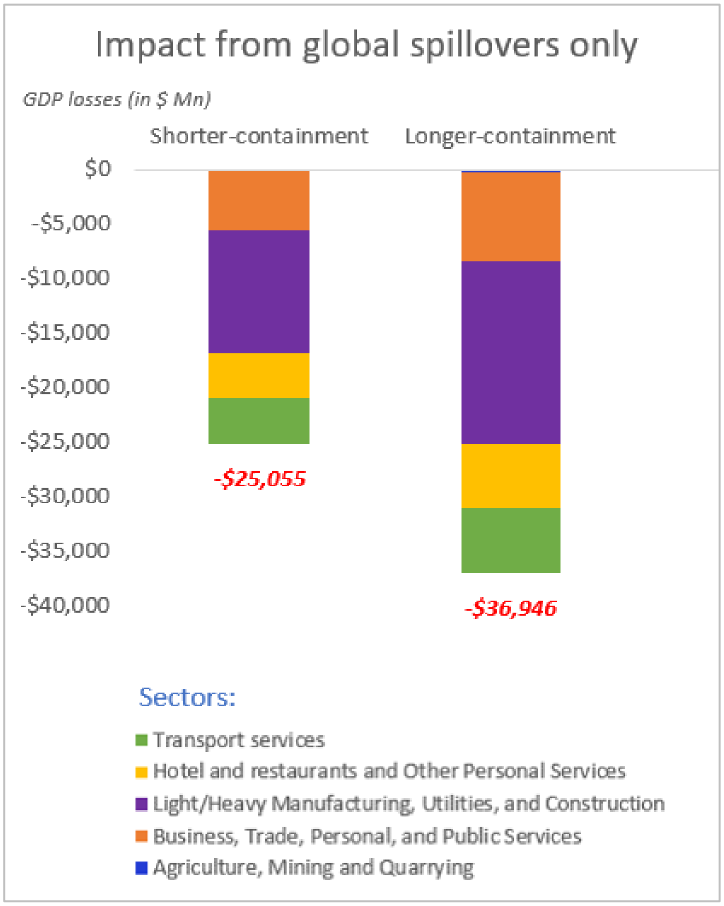
Minister of Trade and Industry Chan acknowledged that there was no returning to a pre-Covid-19 world; Singapore must chart a new path by building a new economy. For example, Singapore expects the digital free trade agreements that it has signed with Australia, Chile and New Zealand to open more markets for its businesses and preserve access to conventional markets. Singapore will enhance its intellectual property protection and legal certainty. Chan also remarked that the changing nature of tax, such as taxing digital taxes, could factor into companies' decisions to invest in Singapore.

In areas such as food security, Singapore is increasing its own production and diversifying its sources of food. In a recent discussion on Covid-19 vaccines, Singapore and the United States discussed collaboration on research and development and the manufacturing and distribution of vaccines. Singapore and China also agreed on a bilateral partnership in public health including Covid-19 vaccines, treatments and diagnostics. For businesses in especially hard-hit sectors, Singapore introduced measures giving wage subsidies for local employment and rental relief schemes, and Singapore's Deputy Prime Minister and Finance Minister Heng Swee Keat reassured businesses and union leaders of its support for companies and workers. Government agencies are in intense discussions to review and adjust support schemes as the situation develops.

## Taiwan

Taiwan has been incentivizing its firms to reinvest their assets back into Taiwan since June 2019. A single window to serve Taiwanese firms has been set up to help them move their asset back home. More recently, the government has been assisting Taiwanese companies to shift their supply chains out of China and seek suppliers in Europe and India in the pharmaceutical and manufacturing sectors. Only the production of personal protective equipment has been reshored to Taiwan to increase self-sufficiency.

Taiwan's Executive Yuan has also rolled out a TWD 16 billion ($542 million) subsidy program to attract the semiconductor, AI and 5G industries to Taiwan. The government has designated these industries, along with the defense industry, as strategically important in the larger scheme of the U.S.-China trade war and the shifting geopolitics in the Indo-Pacific.




*Source: Asian Development Bank*

Due to Taiwan's successful track record on the pandemic, its economy has not suffered a lockdown or shutdowns in production, allowing critical industries to maintain operations. As of now, capital is not leaving Taiwan but flooding in, evidenced by Taiwan's increasing inflation rate (5.7 percent) since September 2019.

Taiwan's semiconductor industry's decoupling from China and closer integration with the United States will certainly be a development to follow. The source of bulk material for pharmaceuticals will continue to shift from China to Europe and India. The most notable example has been Taiwan's TSMC, which used to manufacture chips for Huawei, but it has stopped taking Huawei's orders since May 15, 2020 and will finish its last on September 14, 2020, due to U.S. sanctions. As a result, Huawei's advanced smartphone chip, Kirin, will no longer be produced after September. The government has banned Huawei from participating in its 5G infrastructure.

Additional policy reviews of investments from China — already scrutinized more than other foreign investments — are being considered to deny entrance to Chinese over-the-top video streaming services such as iYIQI. On the automobile manufacturing front, the Yulon Group, one of Taiwan's largest car companies that also produces cars for Nissan, is making strategic adjustments including withdrawing from the Chinese market. Yulon's difficulties selling its own Luxgen-brand cars is a sign that Taiwan's automobile industry continues to struggle despite government support.