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Dialogue, Debate, and Discussion

De-Globalisation and Decoupling: Post-COVID-19 Myths versus Realities

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It has become fashionable to argue that the post-coronavirus world will see an acceleration in de-globalisation and decoupling and that companies will substantively re-localise their supply chains (Javorcik, 2020; McKinsey, 2020). The World Economic Forum recommended that companies should 'aggressively evaluate near-shore options to shorten supply chains' (World Economic Forum, 2020). This commentary argues that such predictions grossly exaggerate the extent to which such restructuring will happen in practice. Even more importantly, assuming that one of the main impacts of the pandemic will be to trigger de-globalisation, decoupling, and re-shoring in the aftermath is dangerous because it muddies the waters, obscuring a much more fundamental consequence: rapidly rising flows of data and knowledge around the world. This shift will have far-reaching implications that researchers, executives, and policymakers need to understand and then address.

EVIDENCE TO DATE

Let us begin with the data that are starting to come through about the impact of the COVID-19 pandemic on globalisation and global value chains (GVCs). In April 2020, the World Trade Organization forecast that world trade would decline by up to 32 percent in 2020, much more than the expected fall in world GDP (World Trade Organization, 2020a). By October 2020, their forecasts of falling trade were sharply cut back to a 9.2% decline in the volume of world merchandise trade for 2020, followed by a 7.2% rise in 2021 (World Trade Organization, 2020b). Spot-market rates for sending a container to America's West Coast, meanwhile, were up 127% year on year (*The Economist*, 2020).

The fact that trade volumes fell much less than expected and then began to rebound quickly reflects the fact that the globally interconnected economy helped in dealing with the corona epidemic. Vital raw materials, such as testing

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reagents, have moved across borders to where they were in short supply. Personal protective equipment and even ventilators from across the globe helped to alleviate shortages in many of the worst-hit countries. China, for example, exported 3.1 million patient monitors in the first quarter of 2020, a fourfold increase on the year before (Yu, Liu, & Mitchell, 2020). Contrary to dire predictions, GVCs, including for perishables such as food, held up well. Nestlé, for instance, reported in April 2020 that it had achieved its best quarterly global sales growth in almost five years (Evans, 2020). By contrast, it was local supply chains, whether bottlenecks in supermarket distribution or a shortage of delivery drivers, that have caused the most problems. Witness the fact that Europe's major ports soon began to face problems with storage capacity because cargoes were arriving from Asia but not being collected because of failing local logistics and lack of demand (Pooler & Keohane, 2020).

Given the longer lead times for implementing decoupling and reshoring, it is as yet unclear how much the COVID-19 pandemic will induce these adjustments. But even before the pandemic, evidence of long-predicted reshoring was limited. According to a recent Korean study of re-shoring, just 68 companies have returned their production back to Korea since 2014. By mid-2020, only 38 of those were still in business (Lee, 2020). The latest annual survey by the American Chamber of Commerce in China reports that some 28 percent of member companies said their investment in China would increase in 2020 (AmCham China, 2019). In the wake of the pandemic, the Japanese government created a $2 billion fund to assist businesses by covering two-thirds of the costs of re-shoring their supply chains to Japan. The reaction from corporate Japan, however, has reportedly been lukewarm (Beattie, 2020).

WHY DE-GLOBALISATION AND DECOUPLING WILL BE LIMITED

There are a number of reasons why we can expect de-globalisation, decoupling, and re-shoring in response to the pandemic to be limited. First, as has been pointed out Miroudot (2020), re-shoring and localised production cannot be expected to significantly improve the robustness of a supply chain. Robustness refers to the ability to maintain operations (and therefore supply) during a crisis. Capacity designed to supply a local market will, by necessity, be smaller scale and have less options to dramatically increase production in response to a crisis than a network of suppliers spanning different countries. When a disaster occurs, a global network can draw on supply from other locations to maintain deliveries. As we saw with the COVID-19 pandemic, even a global crisis is likely to hit different countries at different times, opening up options to compensate for a shutdown in any one location. Asia, and China in particular, restarted the bulk of its manufacturing by the time major shutdowns were implemented in Europe and the US in an attempt to slow the spread of the virus.

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A supply chain relying solely on limited local capacity hampered by a local lockdown, by contrast, would be unable to rapidly increase production to meet demand that might rise by ten or even one hundred times almost overnight. Moreover, a GVC will be able to identify and access countries where local institutions and infrastructure enable production to be expanded more flexibly and rapidly. China's more flexible labour laws compared with Europe, for example, enabled companies such as medical equipment producer Zoncare to respond to a flood of inquiries from Spain to Saudi Arabia in late February 2020 by drawing on China's huge and flexible supply base and running its assembly lines twenty hours per day to increase its weekly output sixfold (Yu et al., 2020). A GVC enables increased supply to be drawn from countries with the largest capacity and skills base in related industries that can be re-purposed to fill shortages arising as a result of a crisis. Following regulatory approval of a test kit for COVID-19, for example, Korea was able to increase production of test kits to one million per week within one month and three million per week within 45 days, 90% available for export. This was possible in large part because Korea was already producing in-vitro diagnostics products at large scale prior to the COVID-19 crisis (Kim, Kim, & Kim, 2020). As a result, it already had relevant international networks, skilled supply chain managers, and experience that could be redeployed at short notice to produce COVID-19 test kits. Re-shoring and localising production in countries lacking these options, therefore, would most likely reduce the robustness of the supply chain compared to a more diversified GVC that includes sources in locations with more available capacity, a more flexible institutional environment, and much larger ancillary industries on which to draw.

The second reason why we can expect de-globalisation, decoupling, and re-shoring in response to the pandemic to be limited is the power of fundamental economics (Buckley, 2019). Regardless of the forces of geopolitics or the desire of executives to increase their perceived control by re-localising supply or bringing it in-house, the principles of comparative advantage enunciated by David Ricardo still apply. US electrical goods retailer, Best Buy, has pointed out that unwinding its global supply chain would dramatically increase economic inefficiency. Analysis by Blue Silk Consulting estimates that moving iPhone production out of China could cost Apple as much as 30 percent in increased production costs (Rathke & O'Connell, 2020). In addition to the advantages of cost arbitrage, disaggregated GVCs allow companies to access clusters of specialisms to strengthen the capabilities harnessed by the supply chain helping to improve the functionality and quality of the output (Verbeke, 2020). Companies will have strong incentives to avoid these cost and quality impairments by resisting de-globalisation, decoupling, and re-shoring.

Third, innovation in many industries would also suffer from de-globalisation. Innovation in today's complex products and services require new sources of knowledge to be combined and integrated. This necessitates casting the net globally to identify and access specialist knowledge and capabilities scattered around the

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world, including looking beyond the traditional hotspots where advances in a particular technology have been concentrated in the past (Doz, Santos, & Williamson, 2001). Commenting on the challenge of corona virus, Germany's President, Frank Walter Steinmeier, summed up the importance of a global network in facilitating innovation: 'No single entity covers the medical, economic, and political elements required to produce a vaccine for all' (Steinnmeier, 2020).

The probable costs of de-globalisation and decoupling that would result from stifling innovation are evident in the consequences of rules recently implemented by the Trump administration requiring that even a chip designed and manufactured outside the US can only be sold with the approval of the US government if it uses any piece of US-origin equipment at any step in its production. These restrictions are reportedly aimed at crippling Chinese semiconductor fabricators and users of advanced chips such as Huawei. But the repercussions would harm innovation across the entire global industry, including major American firms. A report on the negative effects of de-globalising the semiconductor industry by The Boston Consulting Group in March 2020, commissioned by the US Semiconductor Industry Association, concluded that these rules would also result in severe cuts in R&D and capital expenditures by multinationals, and the loss of 15,000 to 40,000 highly skilled direct jobs in the US semiconductor industry. BCG also argued that they would cripple innovation by undermining in-depth, long-term collaboration between chip designers in the US, China, Europe, Singapore, Japan, and Taiwan and chip fabricators (Varas & Varadarajan, 2020). Semiconductor modules are highly interdependent, and no company or country can build up a comprehensive supply chain on their own. Given these potentially devastating impacts on innovation of de-globalisation and decoupling, it is likely that multinationals will think twice before implementing such strategies.

Finally, multinationals will be loath to surrender the potential to grow their sales offered by emerging markets that would be lost through de-globalisation and decoupling. China, for example, is already the largest market for many products from automobiles to pork, eggs, and luxury goods. Its GDP grew 4.9% in the third quarter of 2020 compared to the same time last year while the IMF forecasts for the global economy to shrink by 4.4% for 2020 (Hansen, 2020). It is unlikely that Western multinationals, many now heavily indebted as a result of losses associated with COVID-19, will choose to invest in re-shoring and localised production when the growth in demand for their products and services is almost solely in emerging markets such as China.

FROM PHYSICAL AND FINANCIAL FLOWS TO DATA AND KNOWLEDGE FLOWS

The value of world trade in goods and services as a % of GDP has stalled at just over 60% since 2008. Foreign Direct Investment inflows worldwide have fallen 48% since their peak in 2007 (The World Bank, 2020). Arguably these flows

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traditionally associated with globalisation are being replaced by cross-border flows of data and knowledge which continue to grow at a rapid, exponential pace (Manyika et al., 2014). These increasing flows of knowledge and data mean that multinationals' distinctive advantages as a more efficient conduit for cross-border transfer of data and knowledge assets is likely to be eroding as technologies and markets play an increasingly role (Canno-Kollman, Cantwell, Hannigan, Mudambi, & Song, 2016). Domestic firms are likely to be able to use these improved conduits for data and knowledge flows to gain better access to foreign technologies and know-how. At the same time, domestic firms often enjoy 'home team' advantage of better local integration, including superior capabilities in engaging deeply with, and educating, local customers and end users; partnering and co-creating with local suppliers; fostering the development of the local talent pool; shaping the regulatory and institutional environment; and participating in the broader development of the local society (Santos & Williamson, 2015). These developments will help domestic firms to improve their competitiveness relative to multinationals. Instead of focusing on possible de-globalisation and de-coupling in the post-COVID-19 environment, therefore, perhaps the key development to understand is the relentless growth of data and knowledge flows across the world and its implications (Santos, Doz, & Williamson, 2004).

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