



Economic Brief

The Covid-19

Economic Implications for the CAREC Region

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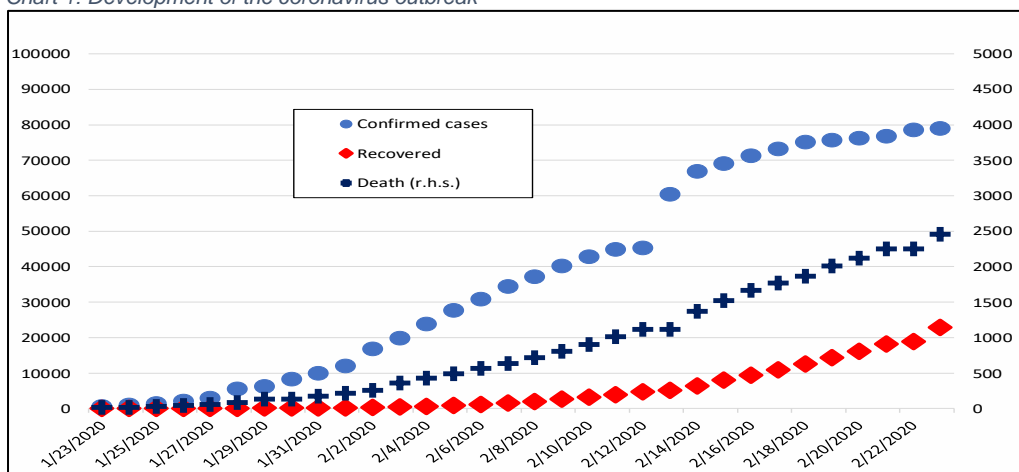
The Covid-19 Outbreak: A Preliminary Analysis of the Impact on the CAREC Region through Commodity Prices, Travel, and Trade

The outbreak of the coronavirus (Covid-19) epidemic has substantial economic consequences for the People's Republic of China (PRC), the world, and the CAREC countries. The PRC's position as a global production hub causes economic repercussions all over the globe. There are significant disruptions in supply chains of the electronics and car industries, among others. In the PRC, production and daily life have been seriously affected. The Chinese authorities have reacted decisively in support of the economy, mostly by cutting interest rates, pouring liquidity into the market and lowering gas prices for industries. Regulators have also asked banks to extend the terms on loans to businesses and allowed them to relax the classification of non-performing loans¹. The Government is likely to do more and has announced so. While this is necessary and offers relief in the short run, the reversal of these policies will make reforms harsher later.

CAREC countries are affected by the virus outbreak as well. Beside travel and trade disruptions, the economies of net commodity exporters might suffer from lower commodity prices as Chinese demand weakens. However, there are also offsetting factors: further rising tensions in the Middle East could, by contrast, cause commodity prices rise. Current events once again underline that CAREC countries need prudent resource management in order to mitigate price volatility. The Covid-19 epidemic will reinforce current trends in globalization such as reducing disruption risks by relocation of value chains closer to the main global demand and production centers. This will contribute to advancing the build-up of the Asian economic cluster. To be successful participants of this cluster, CAREC countries will have to work harder on improving their export performance, especially in the Asian direction. Situations, such as the current one, highlight the desirability of region-wide emergency arrangements for travel and trade, not only from an economic point of view, but also for further improving human relations and avoiding unnecessary hardship.

The outbreak of the Covid-19 epidemic is a big and growing public health challenge. Chart 1 shows the rise. By 25 February 2020, some 80,350 cases were confirmed globally, according to the Johns Hopkins CSSE web page². Of these, some 77,660 cases were in Mainland China, 2,666 dead and 27,354 recovered persons. The most affected Hubei region reported 64,768 cases, 2,563 deaths and 18,971 recovered. Meanwhile the virus is spreading quickly outside the PRC, namely, in South Korea (893 cases, 8 deaths), Japan (847 cases, 4 deaths, including a cruise ship), Italy (229 cases, 7 deaths), and Iran (61 cases 12 deaths).

Chart 1: Development of the coronavirus outbreak



Source: Johns Hopkins CSSE, author's calculations

The current outbreak is often compared to the Severe Acute Respiratory Syndrome (SARS) epidemic in 2003. Then, a total of 8,098 probable SARS cases were reported to the World Health Organization (WHO) from 29 countries during the November 2002-July 2003 SARS outbreak. There were 774

¹ <https://www.ft.com/content/deb2f19a-4d44-11ea-95a0-43d18ec715f5>

² <https://gisanddata.maps.arcgis.com/apps/opsdashboard/index.html#/bda7594740fd40299423467b48e9ecf6>

SARS-related deaths³. The coronavirus outbreak is much more serious than the SARS outbreak 17 years ago.

The PRC's economy is affected substantially, and the authorities react decisively

The medical personnel and the authorities of the PRC and other countries, the WHO and other multilateral institutions, businesses and individuals are engaged in the fight against the virus and will certainly prevail. There are signs of success: daily increases in Mainland China have significantly slowed. However, it is still too early to know how long the outbreak will last, how things will develop outside the PRC, and how much time it will take to fully overcome the epidemic.

The virus and the battle against it have economic implications, of course. Channels, through which the virus affects the economy include travel, transportation, and supply chain disruptions, the shut-down of production sites and offices, reduced household consumption, weaker investment because of uncertainty and lower corporate earnings.

The impact of SARS on the PRC's GDP growth was an estimated 0.8 percentage points, according to Qiu Xiaohua, Director of China's National Bureau of Statistics that time, Xinhua reported.⁴ Industries affected by SARS began to recover in June 2003. Growth in the service sector resumed in the third quarter, with an increase of 7.6% year-on-year. Rural population's income recovered at a growth rate of 6.5% in the third quarter after a decrease of 3.3% in the second quarter as workers coming from rural areas went back to work in urban areas.

Judging from the severity of the current outbreak, it might cost significantly more than the 0.8 percentage points of forgone real GDP growth due to SARS.

On 29 February 2020, the official National Bureau of Statistics Purchasing Manager Indices (PMIs) for manufacturing and non-manufacturing will be published, in early March the CAIXIN PMIs and foreign trade figures for Jan-Feb, and in mid-March industrial production. These indicators should give a first hint about the actual impact of the Covid-19 on the PRC's economy.

The outbreak has been reflected in stock market volatility: the Shanghai Composite Stock Market Index fell 7.7% to 2747 on 3 February 2020, the first trading day after holidays. Stock exchanges in the PRC were closed from 24 January 2020 for the regular Chinese New Year holiday. Then, the government extended the holiday by another three days in an attempt to contain the spread of the virus. The 2747 reading was the lowest since 15 February 2019.

To calm markets and support the economy, the Peoples Bank of China cut the 7-day reverse repo rate by 10 bps to 2.4% from 2.5% previously on 3 February, and the 14-day tenor to 2.55% from 2.65%. In a fast move, the Central Bank injected CNY 1.7 trillion into money markets through reverse bond repurchase agreements⁵. The central bank also reduced the medium-term lending rate by 10 bps to 3.15%. This was followed by a 10bps cut on 20 February of the 1-year Loan Prime Rate (LPR) to 4.05% and the 5-year LPR by 5 bps to 4.75%. The Shanghai Composite recovered to 3,013 by 25 February.

The authorities continue to react, especially as there is the threat that real GDP growth might fall significantly below 5.6%, the target China needs to meet its goal of doubling real GDP between 2011 and 2020. At a meeting on 21 February 2020, chaired by President Xi Jinping, officials pledged to be more "proactive" in using fiscal policy and exercise "more flexibility" in monetary easing, Bloomberg reported.⁶

"More proactive fiscal policies will be enacted to prevent the economic growth rate slipping out of a reasonable range, and new measures will include introducing new policies to cut taxes and fees to

³ <https://www.cdc.gov/mmwr/preview/mmwrhtml/mm5249a2.htm>

⁴ http://www.chinadaily.com.cn/en/doc/2003-10/17/content_273199.htm

⁵ <https://www.reuters.com/article/us-china-markets-rates/china-central-bank-unexpectedly-cuts-reverse-repo-rates-to-help-economy-as-virus-spreads-idUSKBN1ZX05X>

⁶ <https://www.bloomberg.com/news/articles/2020-02-22/xi-pledges-easier-monetary-policy-for-economy-pummeled-by-virus>

boost production resumption and support small and medium enterprises,” said On Wuhan, Assistant Minister at the Ministry of Finance on 24 February according to the China Daily⁷.

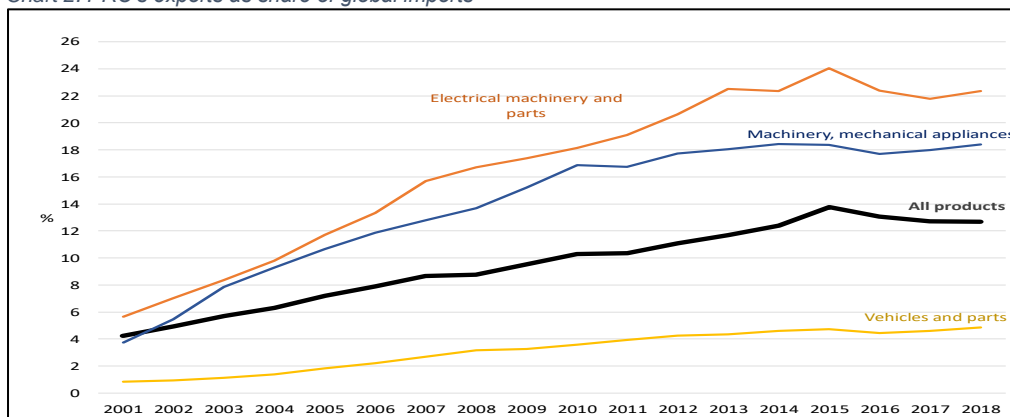
Local governments will expand the issuance of infrastructure project bonds, the central government will transfer more funds to local governments. Chen Yulu, Vice Governor of the People’s Bank of China, indicated that more commercial banks will be allowed to operate at preferential policy of reserve rates and that three policy banks, the China Development Bank, the Export-Import Bank of China and the Agricultural Development Bank will increase their financial support for companies.

Since the PRC has become an economic heavyweight, Chinese events are felt globally

In case the Covid-19 continues to spread globally, the world economy will be affected directly. Currently, the impact is mostly felt via the PRC. The PRC has become a critical hub for global value chains, a major supplier of goods worldwide and a significant purchaser of global travel and other services.

The PRC meanwhile accounts for the supply of 12-14% of global goods imports (Chart 2). The PRC exports provide 22-24% of global imports of electrical machinery/electronics. For mechanical machinery and appliances, the number is 18-20%, and for vehicles and parts about 5%. If trade disruptions and production cuts because of the Covid-19 are going to last long, the global economy might run short of supplies.

Chart 2: PRC’s exports as share of global imports



Source: TradeMap, author’s calculations

Supply shortages are felt already. The PRC’s automakers were operating at only 32% capacity in February 2020, according to a report by CRU consulting.⁸ The most affected Hubei province accounts for 8.4% of the PRC’s light vehicle production. Wuhan, its capital, is hosting production facilities for manufacturers such as Honda, Nissan, Renault, and General Motors, along with many auto parts suppliers.

There is a significant impact on the electronics industry. According to TrendForce estimates, the decline in shipments could reach 4.5% year-on-year for TV sets, 10% for smartphones, 12% for notebooks and 16% for smartwatches.⁹

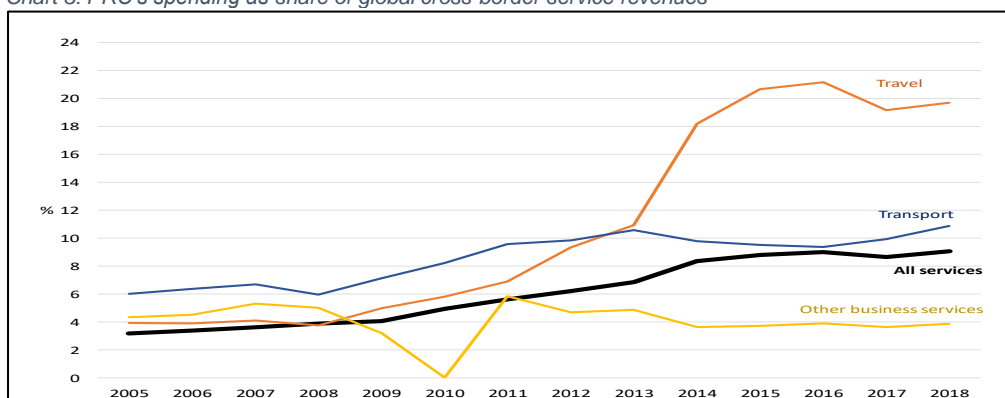
The epidemic has serious consequences for the global demand for services. The PRC purchases one-fifth of global cross-border travel now, and almost 10% of all cross-border services (Chart 3).

⁷ <http://global.chinadaily.com.cn/a/202002/24/WS5e537485a310128217279d44.html>

⁸ <https://www.prnewswire.com/news-releases/cru-covid-19-is-spreading-through-the-auto-industry-301008604.html>

⁹ <https://cdn.statcdn.com/Infographic/images/normal/20894.jpeg>

Chart 3: PRC's spending as share of global cross-border service revenues



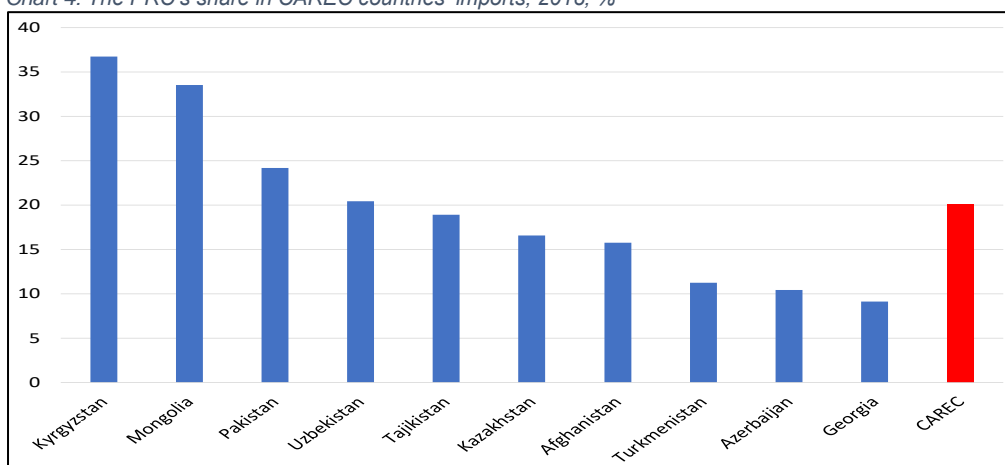
Source: TradeMap, author's calculations

The SARS analogy provides some indication for the impact of the coronavirus on travel earnings: “At the height of the SARS outbreak, in May 2003, revenue passenger kilometers of Asia-Pacific airlines dropped a staggering 35% from their pre-crisis levels but monthly international passenger traffic returned to its pre-crisis level within nine months, according to IATA data. On an annual basis, airlines in the region lost 8% of passenger traffic,” Aviation International News calculated.¹⁰ This time the impact is likely to be substantially larger, not only because of the severity of the Covid-19 outbreak, but also because the PRC's global travel share has grown so much.

The CAREC region is vulnerable to supply cuts from the PRC, but for the time being rather moderately

The PRC's share in CAREC countries' imports is substantial, and the PRC is for several CAREC countries the number one or number two provider of imports. However, the PRC's share does not exceed 20% in the region as a whole, and even for Kyrgyzstan the share is only roughly one-third (Chart 4).

Chart 4: The PRC's share in CAREC countries' imports, 2018, %



Source: TradeMap, author's calculations

For some goods, the PRC supplies very high shares (see Table 1 for Pakistan as an example). But even for these goods there is mostly some room to delay deliveries somewhat without very severe consequences. Potential help by the authorities to overcome shortages would have to focus on only a very few, really critical products in the short run.

¹⁰ <https://www.ainonline.com/aviation-news/air-transport/2020-01-27/iata-coronavirus-could-cause-sizeable-traffic-disruption>

Table 1: The PRC's share in Pakistan's imports, 2018, USD million

Product code	Product label	Pakistan's imports from the PRC	Pakistan's imports globally	PRC/ globally, %
'TOTAL	All products	14,545	60,163	24.2
'8603	Self-propelled railway or tramway coaches, vans and trucks (excluding those of heading 8604)	95	95	100.0
'8401	Nuclear reactors; fuel elements "cartridges", non-irradiated, for nuclear reactors; machinery ...	88	88	99.8
'5007	Woven fabrics of silk or of silk waste	15	15	99.6
'6001	Pile fabrics, incl. "long pile" fabrics and terry fabrics, knitted or crocheted	109	110	98.8
'1006	Rice	30	30	98.8
'6301	Blankets and travelling rugs of all types of textile materials (excluding table covers, bedspreads ...)	35	35	98.7
'8712	Bicycles and other cycles, incl. delivery tricycles, not motorised	11	12	98.6
'8513	Portable electric lamps designed to function by their own source of energy, e.g. dry batteries, ...	12	12	98.1
'5801	Woven pile fabrics and chenille fabrics (excluding terry towelling and similar woven terry ...)	15	16	97.3
'9609	Pencils, crayons, pencil leads, pastels, drawing charcoals, writing or drawing chalks and tailors' ...	19	19	97.2
'6405	Footwear with outer soles of rubber or plastics, with uppers other than rubber, plastics, leather ...	23	24	97.0

Source: TradeMap, author's calculations

Due to the region's economic structure, the most important potential economic impact on CAREC countries is via commodity prices

There are substantial earnings from travel in the CAREC region, especially for Georgia, Azerbaijan and Kazakhstan (Table 2). However, data suggest that arrivals from the PRC don't play a very large role and that most of these travel earnings are from travelers from Central Asian countries, Russia, and Europe.

Table 2: Earnings from cross-border travel in the CAREC region*, USD million

	Exported value in 2014	Exported value in 2015	Exported value in 2016	Exported value in 2017	Exported value in 2018
Georgia	1,787	1,868	2,111	2,704	3,222
Azerbaijan	2,432	2,309	2,714	3,012	2,634
Kazakhstan	2,000	1,632	1,858	2,135	2,255
Mongolia	215	246	316	396	445
Kyrgyzstan	423	426	432	429	438
Pakistan	282	317	322	352	390
Afghanistan	109	79	49	2	16
Tajikistan	1	1	4	8	9
Total	7,249	6,879	7,806	9,037	9,409

Source: TradeMap, *No data available for Turkmenistan, Uzbekistan

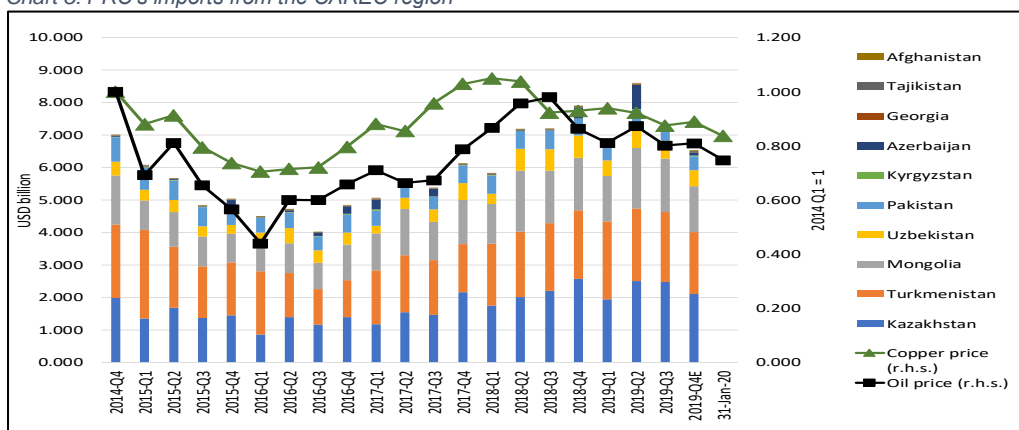
Much more important is that CAREC region's export to the PRC is highly concentrated on commodities, especially oil, natural gas, copper, and coal. The development of CAREC exports to the PRC is narrowly aligned with commodity prices (Chart 5).

A slow-down in the PRC is able to strongly influence commodity prices with a substantial impact on CAREC countries. Kazakhstan owes about 70% of its global exports to proceeds from exports of mineral fuels, Turkmenistan more than 90%, Mongolia about 45%. These countries are large net exporters of mineral fuels (Chart 6), with metal and ore exports having important share.

CAREC fuel net exporters might strongly lose from lower mineral fuel and other commodity prices. Net importers such as Pakistan would gain, however.

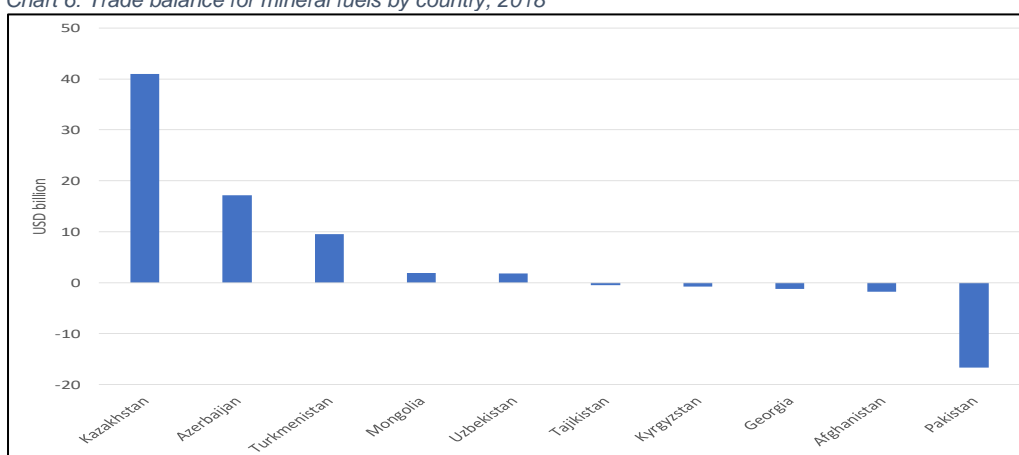
The PRC meanwhile accounts for about 13% of the global demand for mineral fuels, and for 28% for a metal such as copper (Chart 7). Accordingly, markets react highly sensitively.

Chart 5: PRC's imports from the CAREC region



Source: TradeMap, author's calculations

Chart 6: Trade balance for mineral fuels by country, 2018



Source: TradeMap, author's calculations

Crude oil Brent prices fell from a high of 70 USD per barrel on 7 January 2020 to USD 54 per barrel on 3 February 2020, while copper prices fell from 2.8 to 2.5 USD per LBS over the same period (Chart 8). This is a decline of 23% and 11%, respectively. However, while this is substantial, it remains within the volatility seen over the past years. By 25 February 2020, prices recovered to 55 and 2.6, respectively.

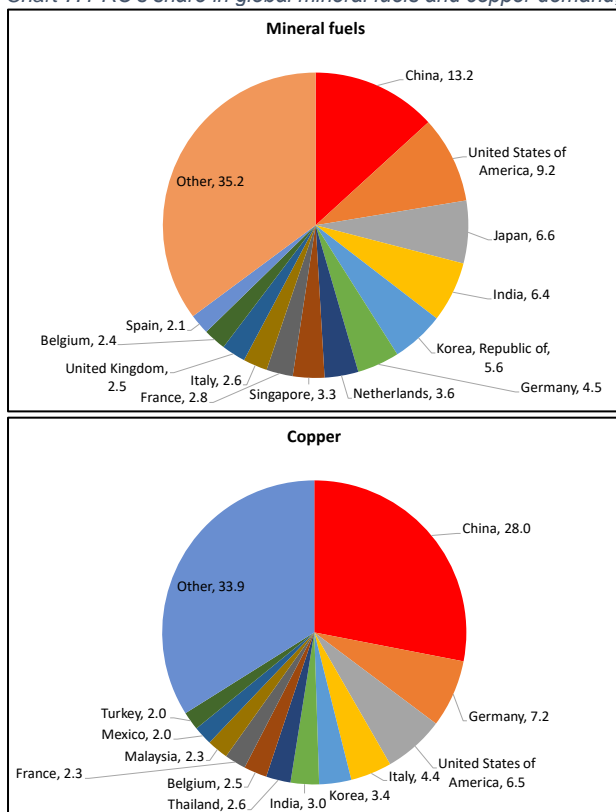
Events in other parts of the world might in contrast push fuel prices up: Middle East countries account for 27% of global mineral fuel exports, among them Saudi Arabia for 9%, Iraq for 4%, Iran for 3%. The current events such as the USA-Iran tensions, the political unrest in Iraq, the ongoing tensions in Yemen might have a large impact on mineral fuel prices as well. While the Covid-19 outbreak exerts downward pressures on oil prices, the Middle East events might increase them. The world is an uncertain place to live on, but the best we have. Let's wait and see.

Impact on the PRC's reform trajectory: relaxing now, harsher and more decisive later

The PRC's economic situation is different now during the Covid-19 outbreak than it was during the SARS epidemic 17 years ago: growth has begun to slow, the middle-income-trap has to be avoided, serious structural reforms are on the agenda. Loosening economic, and especially monetary policy in response to the epidemic will delay reforms.

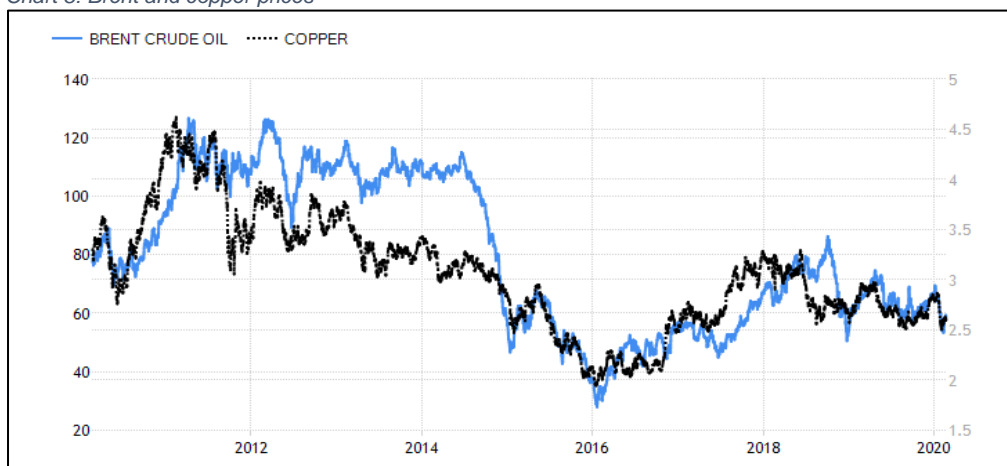
The PRC's gross domestic product (GDP) reached 99,086.5 billion RMB – equivalent to USD 14.3 trillion - in 2019, according to preliminary estimates by the National Bureau of Statistics of the PRC. This is a big achievement, for the first time in the PRC history, the GDP per capita exceeded USD 10,000. Household incomes and consumption also rose significantly. Per capita disposable income was at RMB 30,733 (about USD 4,450), 8.9% higher in nominal terms in 2019 than the year before, or 5.8% adjusting for inflation. Per capita consumption expenditures rose by 8.6% nominally and by 5.5% in real terms to RMB 21,559 (USD 3,125).

Chart 7: PRC's share in global mineral fuels and copper demand, 2018



Source: TradeMap, author's calculations

Chart 8: Brent and copper prices



Source: TradingEconomics

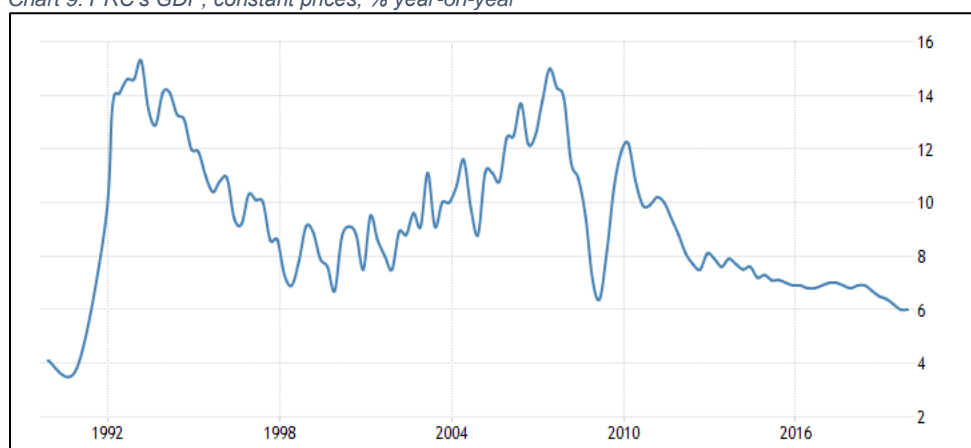
At constant prices, the GDP growth was 6.1% in 2019 as a whole, in line with the PRC target interval of 6.0-6.5%. However, growth slowed from 6.4% year-on-year in the first quarter to 6.2% in the second, and 6.0% in the third and fourth quarters. This continues the down-ward trend, which began in 2010 and is significantly lower than the double-digit growth rates seen in most of the first decade of this century (Chart 9).

The financial sector is one of the main areas, which needs reform. The PRC's macro-economic leverage ratio (debt/GDP) rose to impressive 245.4% in 2019, according to an analysis by the "National Institution for Finance and Development (NIFD)".¹¹ After a decrease by 1.9 percentage points in 2018, there was a re-increase by 6 percentage points in 2019 the report says, and also

¹¹ <http://www.nifd.cn/Interview/Details/1709>

“affected by the new crown pneumonia epidemic, economic growth will face greater pressure in 2020, and the probability of an increase in macro leverage will be higher than in 2019. According to preliminary forecasts, the macro leverage may rise by 10 percentage points in 2020.”

Chart 9: PRC's GDP, constant prices, % year-on-year



Source: TradingEconomics

The leverage ratio of the residential sector was 56% in 2019, of government departments 38%, that of the non-financial corporate sector 151%. The proportion of bank loans in corporate sector debt rebounded from 62% in 2017 to 66% in 2019, reflecting the decline in the size of shadow banking due to tightened supervision. According to NIFD estimates, state-owned enterprise (SOE) debt accounted for approximately 70% of all non-financial corporate debt in 2019, up from about 60% in 2017. The financial system is to a certain extent biased towards large companies, and SOEs in particular. This makes the pass-through of financial easing measures to smaller businesses more complicated and increases the amounts needed to achieve tangible results to counter-act the liquidity shortages brought about by the lock-downs due to the epidemic.

Bloomberg News claims that a “survey of small- and medium-sized Chinese companies conducted this month showed that a third of respondents only had enough cash to cover fixed expenses for a month [February 2020], with another third running out within two months.”¹² It is difficult to know whether the situation is actually so bad, but fast transmission of monetary easing to final users is definitely a difficult problem.

The PRC's economic policy easing in response to the epidemic will likely keep real GDP to grow above 5% in 2020 as a whole, despite significantly lower readings for the first quarter. However, the reversal of this policy, needed to achieve a more rational resource allocation and to reduce overcapacities in real estate and other industries that need re-dimensioning, will weigh on growth rates in the medium term. Relaxing now, will have to be offset by harsher, more decisive reforms in future. GDP growth might thus be somewhat slower in the medium term than assumed before the Covid-19 outbreak.

For the CAREC region this means weaker demand for fossil fuels from the PRC, especially from such high energy-intensive industries as cement and steel. This will come in addition of the effect which the global decarbonization strategies might have.

¹² <https://www.bloomberg.com/amp/news/articles/2020-02-23/millions-of-chinese-firms-face-collapse-if-banks-don-t-act-fast>

Accelerating global value chain relocation

In September 2018, the McKinsey's Economic Conditions Snapshot Survey asked over 1000 executives which globalization-related challenges were the greatest concern for their companies over the next 12 months. About 14% of the executives responded, "disruption in global supply chains." For comparison, some of the other answers: 33% said uncertainty over trade policy, 30% changes in industry regulation, 19% exchange rate volatility, 9% backlash from workers or consumers.¹³ While even 14% is a significant number, the share of executives with this opinion has very likely increased after the Covid-19 experience.

Box 1: New trends in globalization and value chains

The McKinsey Global Institute identified new trends in globalization and value chain design since the mid-2000ies, among them (*NB: shortened, rearranged and highlighted by the author*):

- a) Goods producing value chains have become less trade intensive. Output and trade both continue to grow in absolute terms, but a smaller share of the goods rolling off the world's assembly lines is now traded across borders.
- b) Cross-border services are growing more than 60% faster than trade in goods.
- c) Less than 20% of goods trade is based on labor-cost arbitrage, and in many value chains, that share has been declining over the last decade.
- d) Global value chains are becoming more knowledge-intensive and reliant on high-skill labor.
- e) Goods-producing value chains (particularly automotive as well as computers and electronics) are becoming more regionally concentrated, especially within Asia and Europe. Companies are increasingly establishing production in proximity to demand.
- f) China and other developing countries are consuming more of what they produce and exporting a smaller share.
- g) Emerging economies are building more comprehensive domestic supply chains, reducing their reliance on imported intermediate inputs.
- h) Global value chains are being reshaped by cross-border data flows and new technologies, including digital platforms, the Internet of Things, and automation and AI.
- i) *With the costs and the risks of global operations shifting, companies need to decide where to compete along the value chain, consider new service offerings, and reassess their geographic footprint.***
- j) *Speed to market is becoming a key battleground, and many companies are localizing supply chains for better coordination.***
- k) *Regional integration offers one possible solution, and digital technologies also hold possibilities for new development paths.***

Source: McKinsey Global Institute, Globalization in Transition, The future of trade and global value chains, January 2019

The McKinsey Global Institute has identified several new trends in globalization, trade and value chain design since the mid-2000ies (see Box 1). The supply chain disruptions caused by the fight against the virus and the evidence of the costs associated with supply chain vulnerability will highly likely accelerate the trends already present in globalization and value chain location, especially with regard to closeness and speed to markets.

Concerns about supply chain vulnerabilities due to such events as the Covid-19 outbreak come on top of continued uncertainties about the future of trade. As one comment put it: "... planning for the impact of the coronavirus outbreak, a trade war, or even the supply chain upheaval tied to the financial crisis ... is no easy task. ... The problem with these mega-episodes is that disruption at a transportation level becomes one more argument for de-risking the supply chain overall...Part of the solution may be to flee from high-risk areas."¹⁴

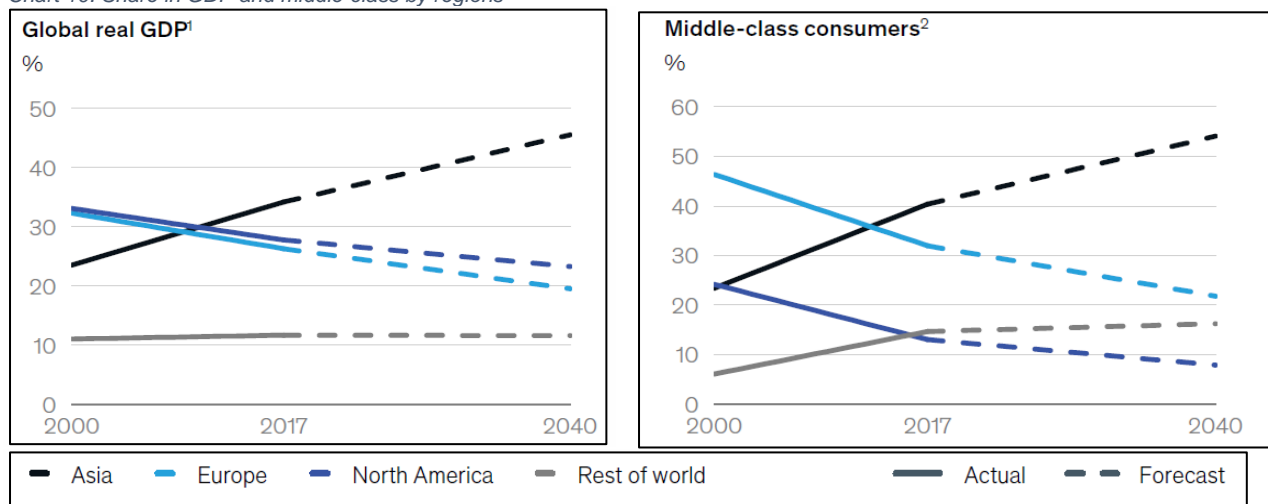
¹³ <https://www.mckinsey.com/featured-insights/innovation-and-growth/globalization-in-transition-the-future-of-trade-and-value-chains>

¹⁴ https://www.joc.com/maritime-news/container-lines/coronavirus-creating-unprecedented-container-shipping-disruption_20200221.html?utm_source=Eloqua&utm_medium=email&utm_campaign=CL_JOC%20Daily%20News%202%2F24%2F20%20_PC9156_e-production_E-55968_TF_0224_0846

The recent signing of the phase one deal between the PRC and the USA has strengthened business confidence. Perhaps less than the 33% of executives cited above are concerned about trade policy now. However, it remains to be seen how much the agreement brings in the longer term. The roots of the trade wars are deep ones:

- a) redistribution of global economic power in favor of Asia, especially the PRC. Chart 10 shows MGI's projection of Asia's shares in global GDP and in middle-class consumers by 2040. We know that predictions are difficult, especially of the future, but it seems pretty obvious that Asia's share is set to increase dramatically and that this can't progress without frictions.
- b) resistance of sunset industries and other industries, or parts of them, and affected regions against restructuring and losing sunk cost due to technological, climate and social change. In attempts to reduce domestic pain, this resistance spills over into protectionism at home and abroad.

Chart 10: Share in GDP and middle-class by regions



¹ Real GDP in 2017 US dollars. ² Defined as households with income between \$20,000 and \$70,000 (constant 2015 prices).
Source: McKinsey: The future of Asia: Asian flows and networks are defining the next phase of globalization¹⁵

While the Covid-19 epidemic clearly shows the necessity of good international coordination and cooperation for achieving good public health result and global prosperity, concerns about vulnerabilities in emergency situations due to over-reliance on global networks could add to the more fundamental reasons that cause trade disputes. This might speed up supply chain relocations, and also reinforce economic and political nationalism.

What are the lessons for CAREC, what can CAREC countries do?

CAREC countries have to be prepared to deal with outbreaks also in the CAREC region and need to adopt precautionary measures such as having sufficient medical devices on store, put appropriate procedures in place for how to keep the economy running at minimum required levels in case of longer quarantine and shut-down measures, for how to provide bridge-financing for businesses in times of a shut-downs, for how to organize support services for households.

Region-wide arrangements for dealing with emergencies such as the current one, the exchange of knowledge how to act in such situations and how to institutionalize best practices throughout the region would be of help - not only under the economic point of view, but also for further improvement of human relations and the avoiding of unnecessary hardship and disruptions in mutual relations.

¹⁵ <https://www.mckinsey.com/featured-insights/asia-pacific/the-future-of-asia-asian-flows-and-networks-are-defining-the-next-phase-of-globalization>

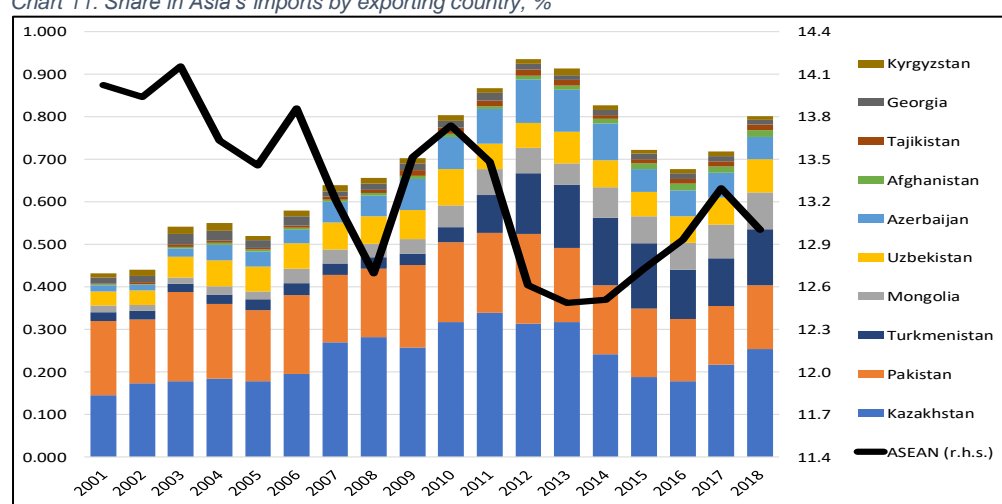
More fundamentally and longer-term, the current events show once again that:

- a) CAREC countries have to mitigate commodity price volatility through prudent resource management and rainy-day funds, including sovereign wealth funds.
- b) Intra-regional CAREC trade should be enhanced, including through trade facilitation measures, to allow better resilience and mutual support.

To live up to the acceleration of the long-term trends in globalization and global value chain reshaping, better results in diversifying CAREC's export structure need to be achieved, and stronger emphasis has to be put on Asia as export destination.

CAREC exporters (ex PRC) have managed to almost double their share in Asia's import from slightly above 0.4% in 2001 to 0.8% in 2018 (Chart 11). This was mostly achieved thanks to higher mineral fuel and copper exports, although with some volatility due to fluctuations in commodity prices. However, while this is a real achievement, CAREC's share in Asia's import is still very low, even after doubling. For comparison: the share of the ASEAN countries, although on the decline, was 13% in 2018 (see the right-hand side scale in Chart 11).

Chart 11: Share in Asia's imports by exporting country, %



Source: TradeMap, author's calculations

Table 3 shows that CAREC region (ex PRC) had 52% of ASEAN's population in 2018, 23% of ASEAN's GDP, but less than 10% of ASEAN's global exports. While it is understandable that CAREC has a stronger orientation towards Europe (includes also Russia) than ASEAN, the fact that CAREC exports only 6% of the ASEAN number to Asia, clearly puts CAREC in a disadvantaged position in a time when the global economy gets concentrated in Asia. Exports to Asia equal only 8.8% of CAREC's GDP compared to 34.5% for the ASEAN countries. This means that only a very low share of CAREC's production potential is dedicated towards the fastest growing region globally.

Trade with the PRC is an example of how CAREC countries have failed to capitalize sufficiently on new technological and economic developments. CAREC's share in the PRC's import grew from 0.7-0.8% in the early 2000ies to a peak of 1.8% in 2012 but has fallen back to around 1.1-1.3% since 2015 (Chart 12). CAREC exports predominantly fossil fuels, copper, and cotton. Three countries - Kazakhstan, Turkmenistan, and Mongolia - account for more than 80% of CAREC exports to the PRC.

At the same time, Vietnam's share in the PRC's import rose from 0.4% in 2001 to 3.0% in 2018. Vietnam alone exports more than twice as much to the PRC now than the CAREC region as a whole. A major reason for this achievement is Vietnam's export structure. "Electrical machinery" accounted for 53% of the PRC's imports from Vietnam in 2018, up from 8.8% in 2008 and only 1.1% in 2001. Within "Electrical machinery" the share of "telephone sets, incl. telephones for cellular networks or for other wireless networks" rose from 7.8% in 2001 to 49.8% in 2018. While the overall share of electrical machinery in the PRC imports has changed relatively little and has remained in the 12-15% range over the past 20 years, there was a significant shift towards high-tech within this category. The

share of “electronic integrated circuits” in “electrical machinery” imports increased from 30% in 2001 to 53% in 2013 and further to 60% in 2018.

Table 3: Indicators of CAREC (ex PRC) exports to Asia, 2018*

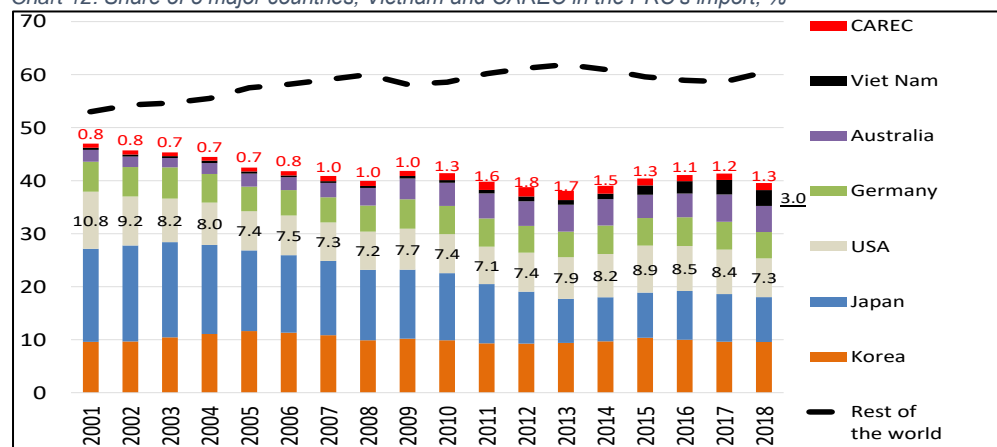
Country	GDP USDmn	Population, mn	GDP per capita, USD	Exports global, USDmn	Exports to Asia, USDmn	Exports global/GDP, %	Exports to Asia/GDP, %	Exports to Asia/Exports global, %
Pakistan	312,570	212.2	1,473	23,631	11,281	7.6	3.6	47.7
Kazakhstan	170,539	18.3	9,331	60,956	19,083	35.7	11.2	31.3
Uzbekistan	50,500	33.0	1,532	10,919	5,844	21.6	11.6	53.5
Azerbaijan	46,940	9.9	4,721	19,459	3,975	41.5	8.5	20.4
Turkmenistan	40,761	5.9	6,967	10,490	9,894	25.7	24.3	94.3
Afghanistan	19,363	37.2	521	1,769	1,147	9.1	5.9	64.9
Georgia	16,210	3.7	4,345	3,354	862	20.7	5.3	25.7
Mongolia	13,010	3.2	4,104	7,012	6,537	53.9	50.2	93.2
Kyrgyzstan	8,093	6.3	1,281	1,835	606	22.7	7.5	33.0
Tajikistan	7,523	9.1	827	1,074	1,036	14.3	13.8	96.5**
CAREC	685,509	338.7	2,024	140,499	60,267	20.5	8.8	42.9
ASEAN	2,969,014	653.5	4,543	1,449,517	1,023,407	48.8	34.5	70.6
CAREC/ASEAN, %	23.1	51.8	44.5	9.7	5.9			

* Red figures indicate very low ratios (cut of point is 15.0), purple figures a dangerously high ratio

**The ratio between exports to Asia and global exports for Tajikistan could be overstated as final destination might to a significant extent be Russia, but shipments are registered for CAREC countries.

Source: TradeMap, WB, author's calculations

Chart 12: Share of 5 major countries, Vietnam and CAREC in the PRC's import, %



Source: TradeMap, author's calculations

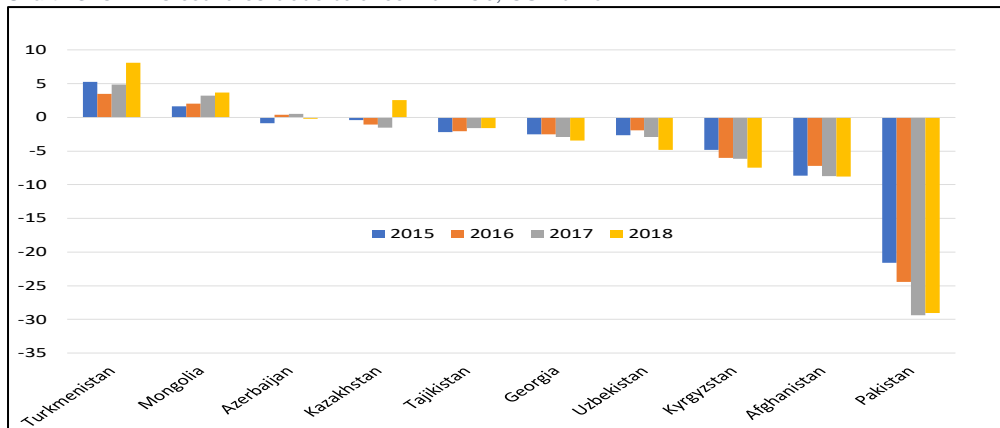
This is not to advocate that CAREC should follow closely Vietnam's example. The CAREC countries have to build on their own historically developed capabilities and on their own current and potential comparative advantages. Focusing only on few products has its problems and dangers, and Vietnam will also have to diversify. Vietnam runs a large trade deficit with the PRC. However, the example shows that Vietnam was able to find at least one specific high-tech niche for its exports to the PRC, and that this allowed it to overtake the value of CAREC exports by far.

Currently most of the CAREC countries have substantial trade deficits vis-à-vis Asia (Chart 13). Trade deficits with the PRC are a major part of this (Chart 14). Restrictive import policies are not a solution, in the end they lead to stagnation and poverty. Developing exports is key.

In 2019, the PRC broke the 10,000 USD GDP per capita ceiling. The PRC's middle-class is developing fast. As a result, imports shift towards more sophisticated, high quality, specialized intermediary and consumer goods. This trend is already apparent. Among the fastest growing imports by the PRC during the last decade are such goods as cosmetics, specific foods and apparel, and pharmaceuticals. Other Asian countries also develop their middle-class.

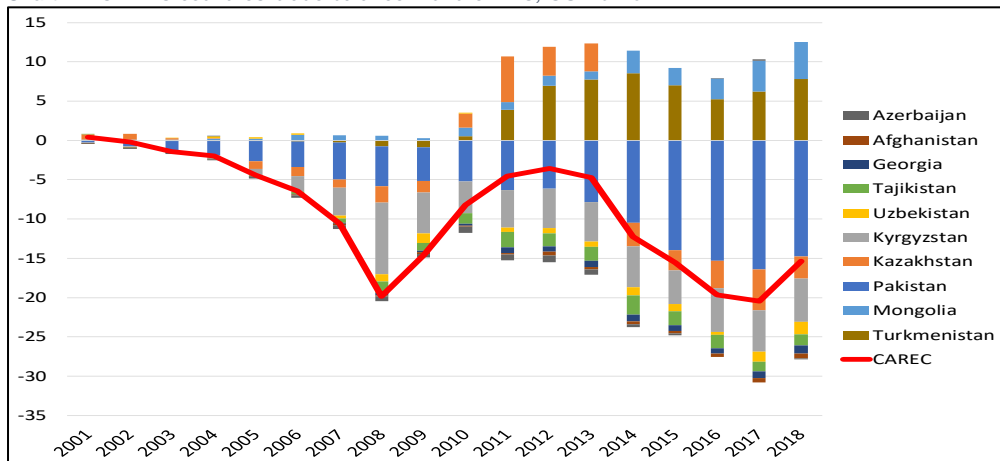
While trade wars and nationalism, including the one re-enforced by the Covid-19, might cause difficulties for advancing the Asian economic cluster in the short to medium term, they accelerate its creation in the longer run by triggering policies that enable Asia, and especially the PRC, to become technologically and economically more self-sufficient.

Chart 13: CAREC countries' trade balance with Asia, USD billion



Source: TradeMap, author's calculations

Chart 14: CAREC countries' trade balance with the PRC, USD billion



Source: TradeMap, author's calculations

To be a successful part of the Asian economic cluster, CAREC countries have to upgrade their export performance. They have to foster new technologies which allow to do this. This is more important in a time when innovation forges ahead globally and when climate change and other ecological concerns might reduce demand for CAREC's current major export products. Such conclusion does not result from the Covid-19 lessons, it is rooted in much deeper developments. However, the Covid-19 epidemic once again confirms it.