How the COVID-19 will redefine the Global Supply Chains

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Abstract

The spread of the COVID-19, that began in December 2019, reveals the increasingly fragility of the international trade in the globalization era. The current crisis combines both a global health pandemic and the fragility of our economies built up over the last 30 years. International organizations have warned that the COVID-19 will have negative impacts on the global economy. The recent report of the United Nations Conference on Trade and Development (UNCTAD, 2020) noted that there are clear indications that things will get much worse for developing economies before they get better.

Key words: COVID-19, Global supply chain, Economic crisis

Cómo el COVID-19 redefinirá las cadenas de suministro globales

Resumen

La difusión del COVID-19, que comenzó en diciembre de 2019, revela la creciente fragilidad del comercio internacional en la era de la globalización. La crisis actual combina una pandemia mundial de salud y la fragilidad de nuestras economías acumuladas en los últimos 30 años. Las organizaciones internacionales han advertido que el COVID-19 tendrá impactos negativos en la economía global. El reciente informe de la Conferencia de las Naciones Unidas sobre Comercio y Desarrollo (UNCTAD, 2020) señaló que hay indicaciones claras de que las cosas empeorarán mucho más para las economías en desarrollo antes de que mejoren.

Palabras claves: COVID-19, Cadenas de suministro globales, Crisis económica.

1 Development

The spread of the COVID-19, that began in December 2019, reveals the increasingly fragility of the international trade in the globalization era. The current crisis combines both a global health pandemic and the fragility of our economies built up over the last 30 years. International organizations have warned that the COVID-19 will have negative impacts on the global economy. The recent report of the United Nations Conference on Trade and Development (UNCTAD, 2020) noted that there are clear indications that things will get much worse for developing economies before they get better.

In the same vein, in the analysis on trade forecast report, the World Trade Organization report (WTO, 2020) observed that the world trade is expected to fall by between 13% and 32% in 2020 as the COVID-19 pandemic disrupts normal economic activity and life around the world, and the negative impact of this crisis will be greater in some industries in particular. For example, the projection of the Gross Domestic Product (GDP) growth rate for Latin America and Caribbean in 2020 will be -5.3%. In case of Mexico, the GDP rate will decrease by -6.5% (ECLAC, 2020).

In this regard, this paper examines the consequences of the coronavirus on the international trade and the economic damage to the economy as a whole, analyzing the added domestic value as the key determinant in the Global Supply Chains (GSCs). We will examine both orthodox and heterodox theories concerning the international trade in this coronavirus crisis.

As the virus keeps spreading rapidly, governments all over the world have decided to switch off almost all economic activities, travel restrictions and bans globally. Despite all these measures, many people have been infected by this virus. Many indicators show that the economic impact and consequences of COVID-19 will be worse than the Great Financial Crisis in 2008. Based on the U.S. Bureau Labor of Statistic (BLS, 2020), during the last month, the civilian unemployment rate reached 4.4%, more than 22 million people in the United States of America of the workforce is without a job. What is more, the crisis has erased trillions of dollars from the global market and imperiled the future of millions of small businesses around the world (Wall Street Journal, 2020).

What happens over a long period of time is that, GSCs have increasingly gained importance in linking developing countries to international markets (UNCTAD, 2020). Due of its highest domestic value added, China has become *the most favored nation* of this hyper globalized world. Over the past three decades, mainstream policies have changed the core of the economic development and much attention was given to the elasticity of export and import to prices. It is important to note that one of the effects of the neoliberal era was the shift from the Import Substitution Model to the Export Led-Growth, under which the international trade would be the principal vector of economic growth. However, this proposal has created a systematic tendency by reducing the responses of state capacity of developing countries to respond effectively to the scale of this pandemic crisis. The origins of the mainstream macroeconomics approach are rooted in the classical economics. The synthesis of the Ricardian theory "free market" or neoliberal rules in which the comparative advantages play a central role under the GSCs concept.

The complementary strategies of multilateralism, embraced by the Foreign Direct Investment (FDI), have raised pressures to the state governments as the only option for the necessary condition of growth. According to David Ricardo (interpreted by Rehim Kılıç: 2002):

> If a country or individual is relatively more efficient in the production of a good than another country or individual, then we say that she has comparative advantage in production of that good […] Since countries have limited resources and level of technology, they tend to produce goods or services in which they have a comparative advantage. Comparative advantage (from now on CA) implies an opportunity cost associated with the production of one good compared to another. That is why countries tend to specialize in production of certain products. This notion is called international division of labor.

The COVID-19 brings to the forefront two important questions that lie at the heart of the modern macrodynamic: first, whether the cross border supply chains, the aggregate demand and the aggregate supply interreact through the price analysis will continue to prevail the international market, or, second, some government policy interventions to support strategic industries that allow more economic growth and less negative impacts in the economy as a whole. But who can undertake this mission?

Answering this question in the multilateralism era is more complicated than it might have been fifty years ago. Basically, this is because the mainstream economics theory treats the government intervention policies as an afterthought of the private-sector-based free market economy. The classical and neoclassical approach perspective analyzed the free market as an ordered social structure and the profit maximization mechanism is "self-organized". Orthodox theorists are agreed with the idea that financial liberalization, the opening market based on the comparative advantage without any government intervention encourage economic growth in developed and developing countries.

In my view, the concept of *sovereignty risk* is the key for a deeper understanding of the complex hyper globalization world dynamics. Under this current pandemic crisis, the production decisions should deviate from the typical equation of cost minimization and prioritize some strategic sectors that government considers crucial in order to reduce dependence from abroad, thus, the need for macroeconomic approach that considers the relevance of the sovereignty risk under the open economy analysis.

In this regard, the heterodox macroeconomic policies provide a detailed foundation for understanding the international trade crisis under which, the GSCs are limited to provided enough specific products that can satisfy the aggregate demand of the international market. Thus, governments have the responsibility to produce sufficient public benefits and mitigate negative effects in this coronavirus crisis. The heterodox macroeconomics theory responds to this question. Particularly, Grabel's current research focuses on the *sovereignty risk* (Grabel, 2009). He pointed out that:

> Sovereignty risk refers to the danger that a government will face constraints on its ability to pursue independent economic and social policies once it confronts a financial crisis. The constraint on policy autonomy can be introduced for numerous reasons […]. Although sovereignty risk stems from the structural position of developing economies in the world economy, this does not imply that this risk is unmanageable. Measures that constrain currency, flight, fragility and contagion risk render financial crisis less likely (or reduce its severity should it occur), and thereby buttress policy sovereignty vis-à-vis speculators and external actors.

What is the most interesting about the Grable's contribution is that he underlined the crucial role of government to protect the national policy space and mitigate both the intensity of the external and path dependence. In this current health crisis, and under the economic uncertainty where the future is unknown, having a dependence China-only Supply Chains is very risky; the state must be responsible to guarantee some strategic economic policies to ensure the production process of specific goods and services in order to reduce the Global Supply Chains reliance on China. In addition, attention was given to the Keynesian fundamental uncertainty (1936) over which, state should establish not only policies, but also institutional structure to meet a macroeconomic foundation of stability and social public needs.

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