

Comments on Professor Kimura's Presentation  
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1. I agree with Kimura san that "human life is of utmost importance and that it must be prioritized over other issues," including economic recovery. I think that the epidemiological course of the pandemic will determine the course of the economy. One cannot make a case for dealing with the recession induced by deliberate stilling of the economy via lockdowns in order to contain the spread of Covid-19, or the hit on balance sheets, unless "the pandemic curve is kept within the capacity of healthcare systems." This is the correct sequencing.
2. It is important to correctly identify the nature of the shock--whether demand or supply--because macro policies needed to address them differ. Policies such as lowering interest rates and increasing government spending to stimulate demand, for example, worsen problems of inadequate supply. Meanwhile, policies to deal with insufficient supply, such as relaxing lockdowns and re-opening the economy, or relief from debts and taxes, do not work to restore output growth when aggregate demand is muted or constrained. Therefore, it is important to be able to differentiate demand from supply shocks arising from Covid-19. In the simple AD-AS model, if P rises and Q falls, we know we are dealing with a supply shock, or at least, a situation in which supply shocks dominate. On the other hand, if P and Q both decline, we know that we are dealing with a situation in which the demand shock is dominant, even if there might be an adverse supply shock.
3. The problem is that shocks have varying sectoral effects. During the Covid-19 pandemic, the demand for health products, for example, increased, while the demand for non-essential goods and services like restaurant meals, hotel rooms, etc. largely vanished. But the tools of macro policy--fiscal and monetary policy--are usually not designed to deal with problems at a sectoral level, but rather at an aggregate level. It is difficult to custom-fit monetary policy or government spending and tax policy at a sectoral level.
4. The country effects of this pandemic shock are also uneven across ASEAN. Vietnam is still expected to post positive growth this year while other ASEAN countries that have had less success in controlling the spread of the virus are faring worse, e.g. Philippines, where GDP growth slumped 16.5% YOY in Q2 2020, the lowest in 4 decades. Countries like Singapore, which had initial success at containment of the virus, has also seen a step decline in GDP growth in Q2 2020 after a second wave occurred.

These adverse economic outcomes seem to hold regardless of how connected countries are to International Production Networks (IPNs). The Philippines, for example, is not as connected to IPNs as other countries in the region are yet was more badly hit than countries such as Thailand, which is very much connected to IPNs. It is unclear to what extent the propagation of shocks via IPNs occurs, and evidently, there is no one-size fits all approach based on IPN connections. What seems to be the case, in general, is that a policy of dealing with the health crisis first and ensuring that the health system in a country is capable of managing Covid-19 and succeeding waves is common to countries with good economic outcomes.

5. We do not know how IPNs will be re-configured post- Covid-19. Nor do we know by how much trade volumes will fall. WTO estimates of trade volume declines this year lie in a

very large band--between -13 percent and -34 percent, indicative of great uncertainty. In contrast, Kimura san seems sure that, "once the shock is over, production and trade can return faster and stronger along networks than in other types of activities." Kimura san appears to be too optimistic. What the network configurations will be post- Covid-19 is unknown. If key links are permanently lost, then maybe production and trade in some sectors may not return.

6. If "massive reshoring in Asia" has not been observed, this is likely due to low global demand overall currently and expectations that this state will persist. "Low demand will hurt supply if it persists in the long run." Lack of "animal spirits" will keep output supply low because there is little reason for investors to invest and consumers to consume given low demand amidst heightened uncertainty. The best way to reduce uncertainty and raise confidence is to deal with the health crisis first and get it under control. In terms of macro policy, finding ways to keep the economy afloat in the meantime is key. In Europe, for example, the ECB is employing unconventional policy, including buying corporate bonds in addition to sovereign bonds.
7. The lack of evidence of "massive reshoring in Asia" may also be an indication that the existing patterns of comparative advantage have not yet been disrupted or changed in any significant way by the course of the pandemic or simply because not enough time has elapsed for all the effects to work their way through the economy. Perhaps new areas of comparative advantage have not been revealed by markets yet because of disruptions to the price signaling system and the inability to know whether shocks have temporary or permanent effects. I am unsure why Kimura san would like to "think of how to keep" IPNs as they were pre-Covid-19, as opposed to allowing market participants to find new areas of comparative advantage. Should the emergence of new IPNs be encouraged rather than aiming to merely maintain existing ones and maintain them at any cost?
8. I agree with Kimura san that the "trough of global economic performance is likely to be very deep and prolonged, causing a serious demand shock which may decay the whole economy." But the huge demand shock is already here; it is not impending. In response to a serious demand shock, he says, "At that point macro stimulus will be crucial and we must pay attention to how our production networks could survive."

Will macro stimulus work in cases where the pre-Covid-19 business models are no longer viable post-Covid-19? IF companies were to go bankrupt temporarily because a lockdown prevented consumers from being able to consume the products or services they normally provide, or supply disruptions constrained production, then govt can help these businesses stay afloat to at least meet payroll and certain costs (moratorium on repayments to creditors, landlords, taxes etc.) during the crisis, and expect that when the economy re-opens, demand will return.

On the other hand, if certain businesses are no longer going to be viable in the post-covid-19 world, governments should not infuse money to indefinitely prop them up lest they end up with zombie firms. Some supply chains will be permanently disrupted (as we have seen even from the US-China trade war) and some firms in these chains may be gone permanently. More importantly, government must provide public goods and structure incentives in a way that encourages businesses to look for new areas of comparative advantage in the post- covid-19 world. For example, government could invest in better internet facilities, a wider broadband, that will help not only businesses,

but also help deliver education to a wider audience. In this, I agree with Kimura san's emphasis on the importance of the acceleration of ICT introduction.

9. The services sector makes tradeable goods more competitive-BPOs, for example. If protectionist policies in the US induce US firms to re-shore previously outsourced services, the goods those US firms produce will likely be more expensive and shift comparative advantage to the production of goods to other countries that take the US' place in the use of outsourced BPO services. This is an example of how IPNs might change due to a shock such as Covid-19.
10. On the China "decoupling" issue, I am likewise unsure to what extent countries will want to consciously decouple or if they can even unconsciously decouple. In a study of the effects of the US-China trade war on the Philippines, for example, we were surprised to find that the country was already extremely dependent on China, both a source of imports and as a destination of exports, pre-trade war. Although the trade war massively reduces trade volume according to our model, the patterns of trade for the Philippines, at least, remain the same. The Philippines also has not seen any reshoring of industries to it from China, with the exception of online gambling.
11. On Emergency Responses under macroeconomic policy, Kimura san recommends the following: "Stabilize exchange rates and prevent a collapse of asset markets." However, during the period when countries are still grappling to control the pandemic and perhaps even for some time after, unconventional monetary policy may be needed, possibly monetizing govt debt for govt to finance its increased Covid-19-related expenditures at a time when tax revenues have collapsed. These actions will naturally exert depreciation pressures on the domestic currency. But this is not the time to stabilize the exchange rate (i.e., prevent large currency depreciation), nor worry about supporting asset markets, at the expense of spending to contain the pandemic.
12. Kimura san's suggestion is to "Keep IPNs and related industries alive with social distancing." While governments certainly want to keep their economies going, much depends on the ability to contain the disease. I also think that it may be too much to ask govts to keep all IPNs and related industries alive. Some of these IPNs will naturally be disrupted permanently and/or may not be viable in the post-covid-19 world because comparative advantage may shift to some other product or service or method of production. Hence, some of these IPNs should not be kept afloat by govt.

It seems that during this pandemic, the focus of many governments has been to ensure that the food supply chain and other essential sectors in the domestic economy remain functioning. Ensuring the survival of IPNs is not the main priority of governments now because external demand has collapsed and is likely to be down for a long time and also because it is unclear how IPNs will be reconfigured. With even more limited resources, governments have had to prioritize spending and focus on social protection and the delivery of essential goods and services.

13. There is no mention of international policy coordination under Macroeconomic Policy during the Emergency Response phase. This appears only under Exit Policies and Policies under the New Normal. What is the scope for and importance of a regional response during the crisis itself? It seems that if there is any incentive to try and resolve a seemingly insurmountable challenge that is common to countries in the region, it would be at the height of the crisis, not when the crisis is over. Even trying to stabilize

exchange rates in the Emergency Response phase (or any phase, if that is the aim) entails cooperation and rules to prevent beggar-thy-neighbor kinds of policies.

14. On the role of ASEAN, it is difficult to generalize about ASEAN being a “model for recovery” given the heterogeneity in country experiences and outcomes. Perhaps ASEAN and other countries can learn from the good experiences of countries like Vietnam in containing the pandemic and being able to sustain economic growth. I agree with Kimura san on ASEAN and Asian countries, in general, being firm believers and advocates of free trade, being beneficiaries of the gains from trade. But I do not think that this necessarily means preserving the pre-Covid-19 IPNs. Ways to increase aggregate demand and attract investment to the region need to be formulated, as supply chains will not automatically come to the region any more than they did in the aftermath of the US-China trade war which is still ongoing.