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Malaysia will realise supply chain potential with further investment

South-east Asia, and particularly Malaysia, cannot expect to see a wide-scale divergence of supply chains coming its way unless there are improvements in production technology and capacity, and regional integration, according to HSBC.

The comments follow widespread commentary about supply chains shifting to South-east Asia because of the region's growing economies and consumer markets, especially with trade tensions and rising production costs affecting other markets. Despite the speculation, there has been little evidence of a wide-scale shift occurring to date.

"The changes in global trade are causing businesses to re-visit their supply chain investment and capacity strategies, but we have yet to see this convert into wide-scale shifts to South-east Asia, South Asia or other parts of the world," said Andrew Sill, Country Head of Commercial Banking, HSBC Malaysia.

Rather than see a wide-scale shift to ASEAN, due to trade tensions, multinationals are diverging in their supply chain strategies with a mixture of localisation, offshoring and re-shoring activities emerging.

Recent examples include:

- The world's largest furniture retailer IKEA has invested RM908 million to set up a regional distribution and supply chain centre to serve the ASEAN market, in Malaysia.¹
- US-based Honeywell International Inc has chosen Kuala Lumpur as its ASEAN headquarters as part of its bid to expand its reach in the region. The headquarters is expected to further attract and develop the best talent to drive its broad software-industrial offerings across the region.²
- Firms, like Tesla³, see China's production reliability, technological sophistication, and ease of business as unparalleled and are moving more of their production to the mainland.
- With China moving up the technological curve, its lower-value production is shifting to lower-cost markets. For example: Guizhou Tyres – based in China – has expanded plans for its previously announced tyre plant in Vietnam increasing the budget investment to nearly \$500 million.⁴

¹ <https://www.theedgemarkets.com/article/ikea-set-rm908m-regional-hub-malaysia>

² <https://themalaysianreserve.com/2017/10/03/honeywell-establishes-asean-hq-kl/>

³ <https://www.bloomberg.com/news/articles/2019-01-07/elon-musk-in-china-to-break-ground-for-tesla-s-china-factory>

⁴ <https://www.tyremanmagazine.com/latest-news/posts/2019/february/guizhou-tyres-invests-500-million-in-new-tyre-site-in-vietnam/>

- Elsewhere, there are instances of western companies, such as Intel, Whirlpool and Caterpillar⁵ re-shoring to be closer to home markets and higher-end technology.
- Across Europe, firms like British manufacturer, Dyson⁶, are forging ahead with South-east Asian investment to cater for the local consumer market whilst retaining existing production facilities for exports elsewhere.

“Shifts in supply chains have been a multi-year phenomenon due to structural changes in production technology, labour costs and emerging consumer markets. Over the past decade, ASEAN has been perceived as a strong production option for multinationals given its role within existing supply chains, growing consumer base, and strong trade and investment ties⁷,” continued Andrew.

“Businesses from China, Europe and the US want to see South-east Asia, and Malaysia, further position itself as a viable alternative for lower-end production. For example, leveraging on initiatives like the ‘Belt and Road’ that are accelerating the region’s production capacity. However, to convert its much-touted supply chain potential, South-east Asia needs to build more visibility and credibility amongst international firms, particularly in their ability to handle and deliver production orders.”

The hot buttons that will matter for both large and small firms include how ASEAN can deliver competitive production costs, and how technology and innovation are being introduced to improve productivity. It will also come down to the relationship factor and whether businesses feel confident that orders will be serviced on time and on budget.

At a government level, this will require educating international firms about the regulatory frameworks, tax incentives, and free trade zones, along with demonstrating the improvements in ports and rail and other transport infrastructure.

It will also require ASEAN governments to demonstrate a pathway to longer-term initiatives to remove the non-tariff barriers around the flow of goods across ASEAN, the development of skilled labour; and the protection of IP, cybersecurity, and movement of commercial data across borders.

Areas of specific focus to improve intra-ASEAN trade flow include:

- Improvement in ASEAN’s transport infrastructure including roads, rail and ports
- Policies that raise the level of technological adoption
- Increasing skilled labour and the flow of skilled labour
- Increase the minimum threshold for goods that would require a Certificate of Origin
- Establishing automation of customs clearance across all ASEAN member states
- Introduce simplified and expedited clearances for low-value shipments
- Introduce electronic system for the payment of cross-border duties and taxes
- Harmonising of goods standards across sectors amongst ASEAN members to avoid country-specific standards.⁸
- Policies that encourage the cross-border sharing of commercial data

⁵ <https://www.usatoday.com/story/money/business/2018/06/28/manufacturers-bringing-most-jobs-back-to-america/36438051/>

⁶ <https://asia.nikkei.com/Business/Business-trends/Dyson-s-HQ-move-boosts-Singapore-ambitions-to-be-Asian-hub>

⁷ <https://www.about.hsbc.com.sg/news-and-media/are-asean-corporates-downplaying-the-trade-tension-risk>

⁸ EU-ASEAN Business Advisory Council’s Trade Facilitation paper 2018
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- Link up each of the ASEAN countries' payment systems to make payments convenient, affordable, fast, seamless and secure⁹.

Reducing supply chain barriers of this nature could increase South-east Asia's gross domestic product by 9.3 per cent and exports by 12.1 per cent, according to the World Economic Forum.¹⁰

"While trade relations between Malaysia and the world's major economies, like China, have generally been positive and steadily growing, there is a lot of ground still to cover within ASEAN's backyard to further improve the intra-regional flow of trade and investment. Agility and responsiveness to these challenges by ASEAN governments and corporates will determine whether the region's supply chain potential can be realised amongst international firms who are re-examining their options," concluded Andrew.

Ends/more

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Note to editors:

ASEAN trade and investment

- ASEAN is the US's fourth largest trading partner, nearly 4,700 American companies are in the region, and it's the top destination for US foreign direct investment in Asia¹¹. A recent American Chamber of Commerce report finding that 80 per cent of US firms, that are already in South-east Asia, are looking to increase investment in South-east Asia over the next five years¹².
- The EU is ASEAN's 2nd largest trading partner and largest source of FDI¹³
- China continues to be ASEAN's largest trading partner (15% of its total trade) and ASEAN is China's third largest trading partner¹⁴ Chinese FDI into ASEAN was US\$8.2 billion in 2015 -4th largest.¹⁵

About HSBC Malaysia

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⁹ <https://www.straitstimes.com/opinion/why-asean-should-push-for-seamless-payment-across-borders>

¹⁰ WEF (2013): "Enabling Trade, Valuing Growth Opportunities"

¹¹ <https://www.pacificcouncil.org/newsroom/examining-state-us-asean-relations>

¹² <https://www.uschamber.com/press-release/rising-demand-and-economic-growth-outlook-drive-continued-us-business-optimism-asean>

¹³ EU-ASEAN Business Advisory Council "Business Investment study" 2018

¹⁴ Source: State Council Information Office of China

¹⁵ ASEAN/MOFCOM joint media statement

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