FUNG BUSINESS INTELLIGENCE September 2020

Asia Sourcing Update

Cambodia, Indonesia, the Philippines, Thailand and Vietnam

Southeast Asia | South and West Asia

Highlights: Evaluating sourcing destinations

12-month Sourcing Outlook

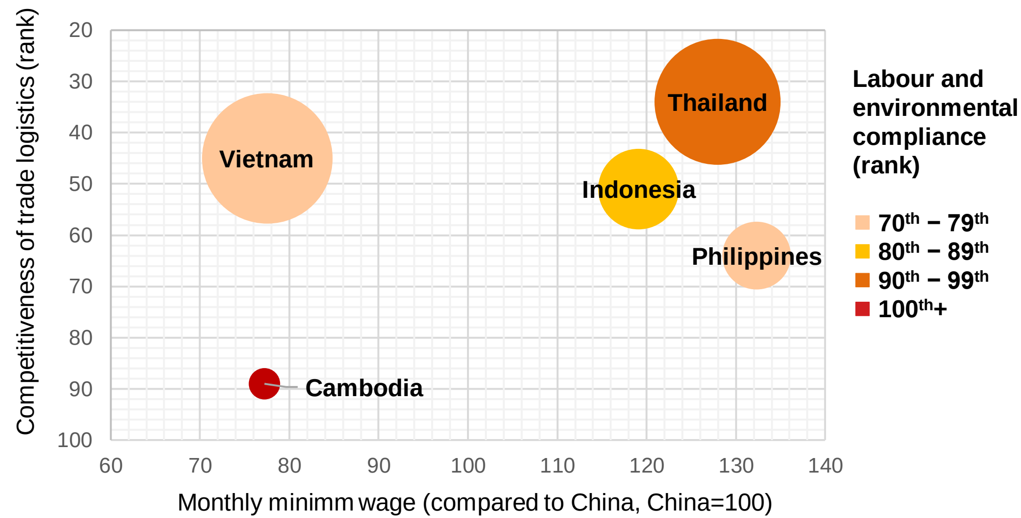
Positive: Cambodia, Vietnam

Neutral: Thailand

Negative: Indonesia, The Philippines

Sourcing destinations: balancing costs, speed, compliance and capacity

(Size of bubbles represents the country's total export value of manufactured goods in 2018)



Source:
Exports of manufactured goods (2018): WTO database;
Minimum wage (as of July 2020): Cambodia (exclusively for the garment and footwear sector), Indonesia (Jakarta), Philippines (National Capital Region), Thailand (Bangkok), Vietnam (Ho Chi Minh City/Hanoi), China (Dongguan), converted to US dollar terms based on exchange rates from Bloomberg;
Competitiveness of trade logistics (rank): measured by the aggregated Logistics Performance Index released by the World Bank;
Labour and environmental compliance (rank): measured by the average ranking of two index components 'environmental-related treaties in force' and 'workers' rights' in the World Economic Forum's 2019 Global Competitiveness Index

Cambodia

Fast facts

CPI (Jun 2020)
+3.2% yoy ▲

Exchange rate (USD: KHR, as of 4 Sep 2020)
4,105 (0.9% depreciation year-to-date)

Merchandise exports (Jun 2020)
+41.0% yoy ▲

Garments
-16.4% yoy ▲

Footwear
-14.2% yoy ▲

Electrical parts
+266.9% yoy ▲

Bicycles
+62.7% yoy ▼

Note: Arrows indicate an improvement (▲) or deterioration (▼) compared to the previous period
Source: National Bank of Cambodia, Bloomberg

12-Month Sourcing Outlook: Positive

In the first half of 2020, US imports from Cambodia shot up by 20.8% yoy to US$2.68 billion, led by woven garments, furniture, lighting products, and plastic goods. EU's imports from Cambodia, however, declined by 15.5% yoy to 1.82 billion euros in the period.

Despite the partial withdrawal of duty-free preferences to the EU market and unprecedented uncertainty amid the COVID-19 pandemic, Cambodia's manufacturing sector, particularly the garment, footwear and travel goods industries, has continued to attract new investment, driven by the country's low labour costs, attractive investment incentives, preferential access to major export markets and the prolonged China–US trade war.

Cambodia

	Latest Developments	FBIC's take
Industry Development	Among the 92 projects (excluding those located in special economic zones) approved by the Council for the Development of Cambodia (CDC) in the first five months of 2020, nine were in bag manufacturing and another 25 in the garment industry. In July, CDC issued a final certificate of registration for Mann Long Shoes Co Ltd.'s US$10.3 million footwear factory in Kampong Cham province, while another US$10.3 million investment by Forever Fug Garment Co., Ltd. was approved in August for building a garment factory in Kampong Speu province.	• Despite the suspension of duty-free preferences for selected garment and footwear products and all travel goods to the EU market, investment in Cambodia's garment, footwear and travel goods industry has continued to pour in, showing the strong potential of the industry as a low-cost sourcing alternative.
Trade Agreements	Starting 12 August, partial withdrawal of the duty-free and quota-free preferences granted to Cambodia under the EU's Everything But Arms (EBA) trade scheme took effect. Selected garment and footwear products, all travel goods and sugar from Cambodia are now subject to standard most-favoured-nation (MFN) tariff rates when entering the EU market.	• The move impacts roughly 20% or 1 billion euros of the country's annual exports to the EU, while the other 80% will continue to enjoy duty-free and quota-free preferences. • It will affect some garment and footwear exporters, while impacts on the travel goods industry will be limited as only a small portion of travel goods exports are shipped to the EU market. • If the Cambodian government shows significant progress on human rights, particularly on civil and political rights, the EU Commission may review its decision and reinstate tariff preferences.

Cambodia

	Latest Developments	FBIC's take
Policies & Regulations	A five-year development plan (2020–2025) is in the works for the country's garment, footwear and travel goods sector to improve its competitiveness. The strategy envisages the transformation of the sector into a higher value-added, supportive, diversified and more competitive sector.	• It will become the first ever strategy designed exclusively for the country's garment, footwear and travel goods sector. • It is expected that the five-year roadmap will focus on strengthening human resources and increasing productivity, while at the same time improving working conditions and worker welfare. Industrial investment in higher value-added products and export market diversification will also be promoted.
	The country's new investment law, to replace the previous version effective in 2003, is scheduled to be launched by the end of this year. The new law is designed to solve problems facing existing and potential investors, create a better investment environment and provide incentives to new industries for the long term.	• The launch of the new investment law will be a timely response to the ongoing trend of production relocation amid the China–US trade war and COVID-19 pandemic. • The new investment law is expected to be more attractive to investors, particularly at a time when Cambodia and China are going to sign their free trade agreement (FTA) soon and negotiations on the South Korea–Cambodia FTA just kick-started. Investors are already looking at export opportunities to the Chinese market to benefit through the China–Cambodia FTA.

Indonesia

Fast facts

GDP (Apr–Jun 2020)
-5.3% yoy ▼

Manufacturing PMI (Aug 2020)
50.8 ▲

CPI (Aug 2020)
+1.3% yoy ▼

Merchandise exports (Jun 2020)
+2.1% yoy ▲

Textiles and textile products
-0.1% yoy ▲

Footwear
+47.1% yoy ▲

Sports requisites
+23.3% yoy ▲

Furniture
+70.6% yoy ▲

Exchange rate (USD: IDR, as of 4 Sep 2020)
14,750 (6.0% depreciation year-to-date)

Note: Arrows indicate an improvement (▲) or deterioration (▼) compared to the previous period
Source: Statistics Indonesia, Bank Indonesia, IHS Markit, Bloomberg

12-Month Sourcing Outlook: Slightly negative

Due to the COVID-19 outbreak, Indonesia's exports recorded a 9.9% decrease in July compared to a year ago but jumped 14.33% compared to June, posting positive month-on-month growth for the third consecutive month. Thanks to the recovery of the Chinese economy, Indonesian exports, especially of manufactured goods, show signs of rebound. The country's manufacturing PMI posted 50.8 in August, rising above the neutral 50.0 threshold for the first time since February, signaling an improvement in business conditions of the manufacturing sector.

However, Indonesia is still struggling to contain the spread of the COVID-19. It is the second-worst affected country in Southeast Asia. Lockdown is still ongoing in many sectors and regions, hindering economic activities and dragging on domestic demand. An overall economic contraction is expected in the full year of 2020.

Indonesia

	Latest Developments	FBIC's take
Macroeconomic Trends	Indonesia's exports reached US$13.73 billion in July, a 9.9% decrease compared to a year ago. However, exports in July jumped 14.33% compared to June, posting positive month-on-month growth for the third consecutive month, a positive sign that the economy is en route to recovery. Exports of manufactured goods, which contributed over 80% of total exports, reached US$11.28 billion in July, a year-on-year decrease of 1.91% but a 17.0% jump compared to the previous month.	• China's recovery from the COVID-19 crisis is one of the main drivers of the rebound in Indonesia's exports. Indonesia's exports to China grew by 11.8% yoy in the first seven months of the year. China is Indonesia's second largest export destination, accounting for 18% of the nation's total non-oil and gas exports. • Demand from other major destinations has also started to recover: Indonesia's exports to ASEAN and the US, the nation's first and third most important export destinations, grew by 15.9% mom and 17.1% mom in July.
	Indonesia's GDP contracted by 5.3% yoy in the second quarter, the first time since 1999 that the economy saw a negative quarterly growth, as lockdown measures to curb the COVID-19 pandemic dealt a blow to the nation's economy. Compared to the first quarter, the economy shrank by 4.2%.	• The economic contraction was driven by a 5.5% yoy contraction in household consumption, which accounts for about 60% of GDP, as well as a 9% contraction in investment, which represents more than a third of GDP. • With gradual reopening of the economy and recovery of global demand, the Indonesian economy is likely to improve in the second half of 2020, resulting in a slight contraction in the full year. The World Bank, the International Monetary Fund and the Asian Development Bank forecast the Indonesian economy to contract by 0%, 0.3% and 1% respectively in the full year of 2020.
Labour Issue	The Indonesian parliament is aiming at completing deliberation on the controversial Omnibus Bill on Job Creation by end-September for the President's endorsement amid widespread protests against the bill. As of mid-August, the parliament had finished deliberating 75% of the bill.	• The Omnibus Bill, which aims to cut red tape by revising 79 prevailing laws and more than 1,200 articles ranging from labour and mining regulations to business license and environmental laws, is one of President Joko Widodo's initiatives to improve the nation's Ease of Doing Business ranking and attract investment. • The business community in Indonesia largely welcomes the business-friendly Omnibus Bill. • Labour unions, on the other hand, strongly oppose the bill because it includes reforms that may undermine labour rights, such as the abolition of city minimum wage and the elimination of severance pay. In response to public concerns, the parliament agreed with 18 labour unions on 21 August to remove certain amendments regarding fixed-term employment agreements, wages, severance pay, employment relations, layoffs, dispute settlements and social security.

The Philippines

Fast facts

GDP (Apr–Jun 2020)
-16.5% yoy ▼

Manufacturing PMI (Aug 2020)
47.3 ▼

CPI (Aug 2020)
+2.4% yoy ▼

Merchandise exports (Jun 2020)
-13.3% yoy ▲

Woodcrafts and furniture
-0.3% yoy ▲

Garments
-20.5% yoy ▲

Travel goods and handbags
-52.4% yoy ▲

Exchange rate (USD: PHP, as of 4 Sep 2020)
48.615 (4.2% appreciation year-to-date)

Note: Arrows indicate an improvement (▲) or deterioration (▼) compared to the previous period
Source: Philippine Statistics Authority, IHS Markit, Bloomberg

12-Month Sourcing Outlook: Negative

The worsening COVID-19 situation in the Philippines, which is now the worst hit by the pandemic in Southeast Asia, has continued to dent manufacturing activities and business operations. Metro Manila and surrounding areas were reverted to modified enhanced community quarantine from 4 August to 18 August. Besides, the recent strengthening of the Philippine peso could further erode the price competitiveness of the country's exports amid sluggish external demand.

Production capacity in the garment industry has been reduced to just 40% in the third quarter of the year due to a lack of orders and over 30% of the garment workers in the country could be placed on furlough until the end of the year, according to the Confederation of Wearable Exporters of the Philippines.

The Philippines

	Latest Developments	FBIC's take
Macroeconomic Trends	The Philippine economy shrank by 16.5% yoy in the second quarter, the deepest contraction in a data series started in 1981. Household consumption fell by 15.5% yoy and exports declined by 37.0% yoy in the second quarter, while government expenditure rose by 22.1% yoy.	• The economic recession was mainly attributed to the country's tough and prolonged lockdown to curb the spread of COVID-19. • Household consumption, accounting for over 70% of the country's GDP, was weighed on by record-high unemployment and a drastic drop of remittances by overseas Filipino workers. • It is expected that the Philippine economy will still take time to heal, as uncertainty is heightened surrounding the country's effectiveness in containing COVID-19. Confirmed cases in the Philippines rose exponentially after lockdown measures were eased in June, making the country the worst hit by COVID-19 in Southeast Asia.
	The Philippine peso closed at 48.56 against the US dollar on 19 August, the strongest position in more than three years, according to spot exchange rates provided by Bloomberg. It represented a year-to-date appreciation of 4.3% against the greenback, outperforming other major Asian currencies.	• High foreign reserves and a strong balance-of-payment (BOP) position, resulting from slower imports and lower outward payments, have contributed to the peso's resilience at an unprecedented time of crisis. • A strong peso, however, could erode the price competitiveness of the country's exports amid sluggish external demand and lower the value of dollar remittances by overseas Filipino workers, a key driver for domestic consumption and investment.
Infrastructure	During the first half of this year, the Duterte Administration approved a total of 12 new special economic zones (ecozones) worth 6.4 billion pesos (US$130 million). These new ecozones, comprising of nine IT centers, two manufacturing zones, and one IT park, will provide tax holidays and other fiscal incentives to eligible investors located in these areas.	• The establishment of ecozones is expected to become drivers for the Philippines' economic recovery, and to help create jobs for the locals and complete the supply needs in the area. • The acceleration of ecozone construction is also part of the government's efforts to decentralize economic and business activities from traditional economic centres. The Administrative Order No.18 issued last year imposes a moratorium on building new ecozones in Metro Manila, where the bulk of existing ones operate, and promotes the development of ecozones in the countryside.

Thailand

Fast facts

GDP (Apr–Jun 2020)
-12.2% yoy ▼

Manufacturing PMI (Aug 2020)
49.7 ▲

CPI (Aug 2020)
-0.5% yoy ▲

Merchandise exports (Jul 2020)
-11.4% yoy ▲

Textiles and apparel
-22.9% yoy ▼

Furniture
-11.7% yoy ▲

Footwear
+13.9% yoy ▲

Exchange rate (USD: THB, as of 4 Sep 2020)
31.392 (5.4% depreciation year-to-date)

Note: Arrows indicate an improvement (▲) or deterioration (▼) compared to the previous period
Source: National Economic and Social Development Council, Ministry of Commerce, Bank of Thailand, IHS Markit, Bloomberg

12-Month Sourcing Outlook: Neutral

Even though Thailand has emerged as one of the successful countries in containing the COVID-19 pandemic, impacts of the crisis have continued to weigh on the manufacturing sector, with output, new orders and exports all dropping at marked rates in recent months.

The impacts on specific manufacturing industries are mixed. For example, capacity utilization rates of textiles, wearing apparel and leather and leather product industries in July were still substantially below pre-COVID-19 levels, according to the Office of the Industrial Economics.

However, some sectors, such as computers, electronics, and electrical appliance, have proven their resilience against the crisis. These sectors are potentially among the biggest winners from the fallout of the China–US trade war, thanks to the well-developed infrastructure, skilled workforce, strong manufacturing capabilities and favourable investment policies in Thailand.

Thailand

	Latest Developments	FBIC's take
Macroeconomic Trends	The Thai economy shrank by 12.2% yoy in the April–June quarter, the worst contraction since the Asian Financial Crisis in 1998. Following a revised contraction of 2.0% in the first quarter, Thailand's GDP shrank by 6.9% yoy in the first half of this year.	• The COVID-19 pandemic has dealt a heavy blow to the Thai economy, which has relied heavily on exports and tourism. • The situation was compounded by the strengthening of the Thai baht in the second quarter, which appreciated by around 7% against the US dollar in the period. • The recent revamp of the government's economic team, which saw six of its ministers resign and replaced, including the finance minister and the deputy prime minister in charge of the economy, has brought fresh uncertainty to implementation of the country's largest-ever stimulus package and the country's economic recovery.
	Total value of investment applications received by the Thailand Board of Investment (BOI) dropped by 17% to 158.9 billion baht in the first half of the year, while the total number of investment applications filed rose by 7% to 754 projects.	• The lower average investment value of projects reflects the uncertainty facing investors amid the unprecedented COVID-19 crisis. • Sectors that received the highest value of investment pledges were electrical appliances and electronics, agriculture and food processing, automotive industry, medical industry and petrochemical industry. • In particular, the number of investment applications for medical projects filed with the BOI almost tripled in the six-month period, thanks to the incentives announced by the BOI in April to boost investment in the manufacturing of medical equipment and supplies amid the pandemic.
Politics & Geopolitics	For more than a month, there have been almost daily student-led anti-government rallies across the country, particularly at school and university campuses. On 16 August, over 10,000 protesters joined the demonstration led by the Free People group in Bangkok, the largest political gathering in Thailand since the military coup in 2014. Protesters reaffirmed their "three core demands". Some protesters even called for the reform of the monarchy.	• As the protests held so far are relatively peaceful and on a small scale (compared with previous anti-government demonstrations which had hundreds of thousands of protesters), business activities in the country have not been impacted. • We see an escalation of the situation as unlikely for the time being, due to limited social class representation among protesters, deeply entrenched support for the monarchy in the country and government's restrained response to protesters. The incumbent government has also initiated the constitutional amendment process recently, which is likely part of the concessions offered to cool down the protests.

Vietnam

Fast facts

GDP (Apr–Jun 2020)
+0.4% yoy ▼

Manufacturing PMI (Aug 2020)
45.7 ▼

CPI (Aug 2020)
+3.2% yoy ▼

Merchandise exports (Jul 2020)
+8.5% yoy ▲

Textiles and garments
-7.7% yoy ▲

Toys and sports goods
+82.3% yoy ▲

Wood and wooden products
+29.6% yoy ▲

Footwear
-15.7% yoy ▼

Exchange rate (USD: VND, as of 4 Sep 2020)
23,169 (0.02% appreciation year-to-date)

Note: Arrows indicate an improvement (▲) or deterioration (▼) compared to the previous period
Source: General Statistics Office of Vietnam, General Department of Vietnam Customs, IHS Markit, Bloomberg

12-Month Sourcing Outlook: Positive

Though textile and garment exports dropped 12.1% yoy in the first seven months of this year, Vietnam saw its shares in the US and EU textile and garment import markets increase steadily. As one of the countries successfully contained the COVID-19 outbreak, Vietnam did not suspend production in the first half of 2020. Currently, Vietnam is the world’s second largest textile and garment exporter after China.

Plus, the EU–Vietnam FTA entered into force on 1 August 2020. In particular, tariffs on approximately 77% of textile and apparel exports (by value) will be eliminated over the next five years.

Also, Vietnam is seen as the top alternative for companies seeking to reduce dependence of their supply chain on China. There are more FDI inflows and opportunities for further industrial upgrading, making the outlook of the country one of the brightest in the region. A gradual rebound in textile and garment sourcing from Vietnam is expected when global demand recovers.

Vietnam

	Latest Developments	FBIC's take
Macroeconomic Trends	Vietnam's industrial production index (IIP) rose by a modest 2.6% yoy in the first seven months of 2020, much lower than the growth rate of 9.4% yoy recorded in the same period last year. The manufacturing sector was the main driver of the growth during the seven-month period, with a year-on-year increase of 4.2%.	• Vietnam's IIP in June and July registered year-on-year growth of 7.2% and 1.1% respectively, after booking year-on-year declines in April and May, indicating a gradual rebound in industrial output. • The recovery, however, is highly uneven among industries. Several key industries saw output declines in the first seven months, including apparel (-4.6% yoy), leather and related products (-4.2% yoy), wood and wood products (-3.4% yoy), and motor vehicles (-15.4% yoy). Pharmaceuticals, on the other hand, grew by 27.1% yoy while paper products and computers and electronics recorded year-on-year growth of 8.2% and 8.1% respectively.
Industry Development	15 Japanese firms are expected to shift their manufacturing plants from China to Vietnam with subsidies from the Japanese government under a scheme aimed at reducing Japan's reliance on China and increasing supply chain resilience. Most of the 15 firms relocating to Vietnam manufacture medical equipment while the rest produce semiconductors, phone components, air conditioners or power modules.	• Among the 87 firms participating in the scheme, 57 will relocate to Japan, 15 will head to Vietnam, while another 15 will shift to other Southeast Asian countries, according to the list unveiled by the Japanese Ministry of Economy, Trade and Industry. • The shift of manufacturing from China has already been ongoing as companies seek alternatives amid China–US trade tensions and rising production cost in China. The COVID-19 pandemic has further accelerated relocation and reconfiguration of global value chains.
Trade Agreements	The EU–Vietnam free trade agreement (EVFTA) entered into force on 1 August. Under the agreement, tariffs on 99% of all goods traded between Vietnam and the EU will be eliminated over the next ten years. Touted as "the most ambitious and comprehensive agreement that the EU has ever concluded with a middle-income country", the EVFTA also covers domestic policies such as labour rights, environmental rules and competition policy, in addition to eliminating trade barriers.	• Several key export items from Vietnam to the EU enjoy tariff reduction under the EVFTA. Most notably, tariffs on approximately 77% of textile and apparel exports (by value) will be eliminated over the next five years, while the remaining 23% is set to enjoy tariff reduction after seven years. • The EVFTA also enables Vietnamese textile enterprises to import high-quality machinery and textile fabrics tariff-free from the EU. • However, Vietnamese enterprises may not meet the EVFTA's rules of origin requirements due to their high dependence on imported materials. To reap full benefits from the EVFTA, Vietnam needs to improve its domestic backward linkages.

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