Swiss Re
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News release

Global supply chain changes pick up pace to yield new opportunities, says *sigma*

- The development of parallel supply chains to de-risk the global flow of intermediate goods/services is a key macroeconomic trend
- COVID-19 has accelerated the trend: the healthcare, technology, consumer staples, textiles and electronic sectors likely at forefront
- Changes will include alternative host markets, mainly in Southeast Asia, and re-shoring of production processes, mainly in the US, euro area and advanced Asia markets
- Over a five-year transition period, the changes will be net positive for the global economy and are anticipated to generate around USD 63 billion in additional global insurance premiums

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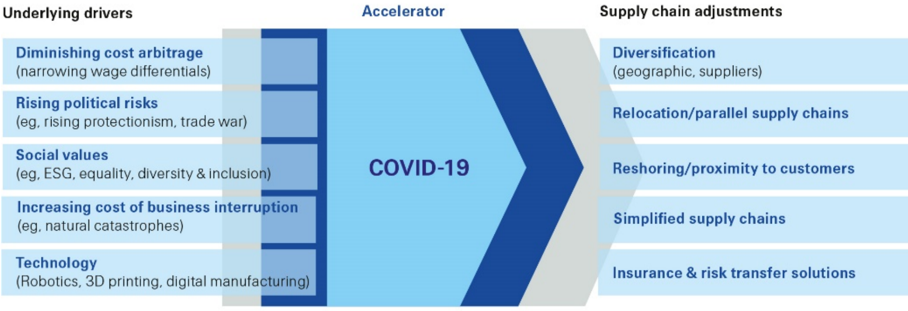
Zurich, 10 September 2020 – Global supply chains are undergoing fundamental and accelerated restructuring, the latest Swiss Re Institute *sigma* study, "De-risking global supply chains: rebalancing to strengthen resilience", says. The disruption to the flow of intermediate goods and services during the COVID-19 lockdowns has made governments and manufacturers ever more aware of the risks inherent in today's increasingly complex, specialised and global production processes. Manufacturers, meanwhile, are speeding up their development of parallel supply chain operations in new host markets alongside existing production bases as a means to diversify and strengthen their operational resilience. Markets in Southeast Asia will be the preferred destinations as new host locations. There will also be some re-shoring of activities back to the US, the euro area and advanced markets in Asia.

"Global supply chain restructuring has become a key macroeconomic trend and the COVID-19 experience has accelerated changes, " Jerome Jean Haegeli, Swiss Re Group Chief Economist, said. "During the pandemic, lockdowns brought international exchange to a near halt, making businesses, and governments increasingly aware of the impacts that disruptions in today's very complex and specialised global supply chains can have."

There had been some tempering of globalisation fervour even before COVID-19 severely curtailed the movement of goods and people. A number of natural catastrophes over the last decade, such as the earthquake and tsunami in Japan in 2011, and widespread flooding in Thailand in the same year, inflicted costly supply chain interruptions across different industries. Rising political risks, such as new tariffs and a looming threat of global trade war, also prompted manufacturers to rethink their globalised production and sourcing strategies.

Figure 1: COVID-19 as the accelerator for global supply chain restructuring



Source: Swiss Re Institute

Parallel supply chains and duplicate sourcing strategies

Supply chain restructuring is also a question of national resilience. For example, the COVID-19 crisis immediately exposed vulnerabilities in the medical manufacturing supply chain. Government responses to the pandemic globally show that in times of crisis, international cooperation can be interrupted as countries prioritise according to their domestic needs, in particular to ensure fail-safe access to vital supplies.

From a business perspective, the driving force for accelerated restructuring of global supply chains is manufacturers seeking to de-risk their operations. In the 20 largest economies, 40–80% of exports are integrated into the global supply chain[1] and, within this, China is the world's largest production hub. Parallel supply chains will form as firms diversify their manufacturing presence across new locations alongside existing operations in China and elsewhere, in an effort to strengthen operational resilience.

Markets in Southeast Asia will likely be the preferred destination as new host locations, given their strong growth potential and competitive labour costs. Vietnam tops the list as an alternative manufacturing location. Countries with similar industry composition to China's export sector and/or free trade agreements with the US, the EU and Japan also stand to gain. In this vein, Mexico and Brazil will benefit as suppliers to the US.

The healthcare, technology, consumer staples, textiles, and electronic sectors will be at the forefront of supply chain restructuring, which will also include some re-shoring of production activities back to advanced markets. New technologies such as robotics can simplify and shorten supply chains. For example, advances in industrial 3D printers can handle rapid prototyping and small-scale orders without sacrificing on quality. This allows for easier product

[1] A common measure of integration into global supply chains is the Global Value Chain participation index, which summarises the domestic value added in foreign export (forward participation) and foreign value added in domestic export (backward participation). The value goes from 0 to 100. The higher the value, the higher the country's participation (ie, trade in intermediate products is more prevalent in total trade).

differentiation and manufacturing that is closer to the customer. The US, euro area and markets in advanced Asia will benefit most from re-shoring.

Assuming a five-year transition period for these changes to take effect, Swiss Re Institute estimates that gross domestic product (GDP) growth in the alternative host markets for production processes will be boosted by 0.7% annually. In the re-shore markets, growth will increase by 0.2% annually.

Table 1: Winners of relocation and reshoring

	Relocation to	Reshoring
1	Vietnam	US
2	Cambodia	Germany
3	Malaysia	France
4	Thailand	Italy
5	Philippines	UK
6	Taiwan	Japan
7	India	South Korea
8	Czech Republic	Canada
9	Indonesia	Taiwan
10	Hungary	

Note: Relocation countries are ranked by relative attractiveness; see Table 2 "Production relocation scorecard" in the *sigma* report. Reshoring countries are ranked by 2018 volumes of intermediate goods imports.

Source: Swiss Re Institute

Global and China growth impacts

The *sigma* study estimates the changes to global supply chains will generate combined export and investment value of close to USD 1 trillion in the alternative production locations over the five-year transition period. Global growth will gain by an estimated aggregate 0.2% each year in that period. In China, the government will likely enact additional fiscal stimulus to boost demand at home to compensate for the loss of some production activities to alternative markets, and to further the desired transition from an export-oriented to a domestic demand-led growth strategy.

Swiss Re Institute forecasts that after a slump in the first quarter due to lockdown, GDP growth in China will recover strongly. Full-year real growth is forecast to remain in positive territory at 2.7% in 2020, and to rebound to 7% next year. In contrast, growth in the US and euro area is expected to remain in negative territory this year, given the later easing of lockdown measures in these markets. The post COVID-19 recovery is forecast to push growth back up to 4.2% in the US and to 4.8% in the euro area in 2021.

Insurance to facilitate stronger supply chain resilience

Supply chain restructuring will have important implications for insurers, by generating new demand for risk protection covers and providing new opportunities for the industry to underpin global economic resilience. Insurance plays a key role in supply chain risk management. Supply chain, contingent business interruption and non-physical damage covers can compensate for losses resulting from incidents at suppliers.

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"For insurers seeking to cover business disruption exposures, the more transparency there is on supply chain flows, the more insurable the risk becomes," Gianfranco Lot, Head of Globals Reinsurance at Swiss Re, says. "To this end, the industry is extending its digital technology capabilities, to better process and understand all the structured and unstructured data out there. The idea behind the Swiss Re Digital Market Center is to develop large-scale tools to predict and manage exposures, to facilitate the development of innovative risk protection solutions."

The *sigma* report estimates the overall income effect from the higher growth created by supply chain restructuring will generate additional global premium volumes of around USD 63 billion cumulatively during the five-year transition period. This includes a one-time boost of USD 1.2 billion arising out of new demand for engineering covers during the construction phase of manufacturing facilities and associated infrastructure, and USD 9 billion for commercial insurance in the operational phase of the new facilities.

Notes to editors

Swiss Re
The Swiss Re Group is one of the world's leading providers of reinsurance, insurance and other forms of insurance-based risk transfer, working to make the world more resilient. It anticipates and manages risk – from natural catastrophes to climate change, from ageing populations to cybercrime. The aim of the Swiss Re Group is to enable society to thrive and progress, creating new opportunities and solutions for its clients. Headquartered in Zurich, Switzerland, where it was founded in 1863, the Swiss Re Group operates through a network of around 80 offices globally. It is organised into three Business Units, each with a distinct strategy and set of objectives contributing to the Group's overall mission.

How to order this *sigma* study:
The English version of the *sigma* 6/2020, "De-risking global supply chains: rebalancing to strengthen resilience", is available in electronic format. You can download it here:
https://www.swissre.com/institute/research/sigma-research/sigma-2020-06.html