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Navigating the storm: Southeast Asia and the global trade shocks

ANALYSIS

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Key findings

- Southeast Asia's export-oriented economies have so far proven highly resilient to the global trade shocks of punitive US tariffs and China's surging exports.
- The region is capturing shifting global supply chains and leveraging growth-enhancing Chinese imports and capital inflows while nonetheless avoiding excessive dependence.
- Southeast Asia is under pressure but also proving it retains considerable capacity to navigate today's trade and geoeconomic turbulence while continuing to prosper.

Executive summary

Southeast Asia's trade-oriented economies are facing a confluence of global trade shocks. The Trump administration in the United States has imposed punitive tariffs while depressed domestic demand in China has led to a "second China shock" that threatens to crowd out the region's manufacturing industries. Both superpowers are engaged in aggressive mercantilism and Southeast Asia risks being caught in the crossfire.

Yet the region has proven remarkably resilient. Rather than shrinking, exports to the United States have boomed as Southeast Asian goods replace Chinese ones in the American market. Exports to other markets are also growing strongly despite fears that these would be crowded out by cheap Chinese goods deflected from entering the United States. The second China shock has also been mostly growth-enhancing, providing competitive intermediate and capital goods along with substantial investment inflows. Meanwhile, the region finds itself at the centre of global efforts to deepen open rules-based trade in response to US tariffs.

Despite China's growing supply chain role, Southeast Asia remains well diversified, with trade and investment partners geopolitically aligned with the United States collectively outweighing China's role. This provides some space for the region to negotiate with an America focused on reducing its economic dependencies on China and building more diversified supply chains.

Openness and competitiveness have been the keys to Southeast Asia's resilience. The region should double down on this — diversifying partnerships, supporting rules-based trade, and pursuing structural reforms to boost productivity. This would strengthen the region's centrality to global trade, making it more costly for others to decouple or apply geoeconomic pressure, while promoting the industrial upgrading Southeast Asia needs for sustained growth.

Introduction

Southeast Asia is home to some of the world's most trade-oriented economies. Today, however, major global trade shocks are threatening the region's highly successful economic model.

The Trump administration in the United States wants to reshape the global economy through its disruptive America First trade agenda. Southeast Asia (alternatively ASEAN[1]) has been targeted for especially punitive tariffs owing to the region's large and growing trade surplus with the United States. Bilateral negotiations have seen the initially threatened US tariffs reduced but still imposed at a high rate. While the Trump administration's key tariffs could be ruled illegal, it retains other legal avenues to broadly replicate its tariff policies. High US tariffs are not going away.

Meanwhile, depressed domestic demand in China has seen the country's goods exports and trade surplus surge. This has given rise to talk of a second China shock, which threatens to hollow out manufacturing in developing and advanced economies alike, as the original China shock did during the 2000s.[2]

These global trade shocks threaten to interact in deleterious ways. With both superpowers engaged in aggressive mercantilism and the global trade rules substantially weakened, protectionism in the rest of the world risks escalating. Southeast Asia could be a target due to its substantial exports. US tariffs are also deflecting even more Chinese goods to other markets, damaging local industries, and fuelling protectionist sentiment around the world. Finally, Southeast Asia risks being caught in the crossfire of Sino–US geostrategic rivalry as America seeks to disentangle its economy from China's.

Southeast Asia's major trade-oriented economies — Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam — have among the most at stake amid these global trade shocks. Most are developing economies still hoping to capitalise on trade-led growth as the only proven path to rapid economic advancement and eventually high-income status. Various modelling estimates suggest the region will suffer significant economic losses due to the US tariffs.[3] *The Economist* magazine warns that "Southeast Asia is being swamped with Chinese goods".[4] The Trump administration's reciprocal trade deals with Cambodia and Malaysia suggest it may be seeking unrealistically onerous concessions in terms of economic security "alignment" from these countries and the rest of Southeast Asia.

While acknowledging the challenges and uncertainties, this paper offers a more positive assessment. Southeast Asia has so far proven highly resilient to the global trade shocks. This could prove more durable than it appears, and the region could have more room to manoeuvre than is commonly assumed.

Southeast Asia's exports have been growing rapidly. The region's total goods exports were 15% higher in October 2025 than the same time last year, equivalent to roughly $300 billion in additional exports when annualised. Rather than shrinking, exports to the United States have boomed as Southeast Asian goods replace Chinese ones in the US market. Investment inflows remain strong despite elevated uncertainty. Although causing some issues, the new China shock has mostly been good for the region's growth by providing a source of competitive intermediate and capital goods as well as investment. This is in contrast to the original China shock when it primarily competed with the region in basic manufacturing while recycling its trade surplus into US treasuries. Southeast Asian exports to non-US markets are growing robustly despite fears of being crowded out by deflected Chinese goods. The region also finds itself at the centre of global efforts to deepen open rules-based trade in response to US tariffs, rather than the target of further protectionism.

Despite China's growing supply chain role, the evidence shows Southeast Asia remains reasonably well diversified with many other trade and investment partners, mostly geopolitically aligned with the United States, and more than outweighing China's role. This creates some scope for the region to negotiate and engage with an America focused on reducing its economic dependencies on China and building more diversified and fair supply chains.

The future of global trade is still highly uncertain. Southeast Asia has weathered the storm well in no small part because the international context has thus far proven more favourable than originally feared. The Trump administration's initially announced tariffs were ultimately lowered, the world has so far resisted following America into deeper protectionism, and the US and global economies have themselves remained relatively resilient. Yet the international context could quickly become much less favourable.

Nonetheless, the lesson so far is that Southeast Asia is better positioned to navigate the current trade shocks than commonly assumed. The region's competitiveness and openness have been key to that resilience. Southeast Asia should double down on this — diversifying and deepening its partnerships, supporting rules-based trade, and undertaking complementary structural reforms at home to boost its competitiveness and productivity. This would strengthen economic linkages with the rest of the world while dovetailing with the Trump administration's interest in building more diversified and fair supply chains. It would solidify the region's centrality to global trade, making it more costly for others to decouple or apply geoeconomic pressure. And it would promote the industrial upgrading that Southeast Asia needs for resilient economic growth.

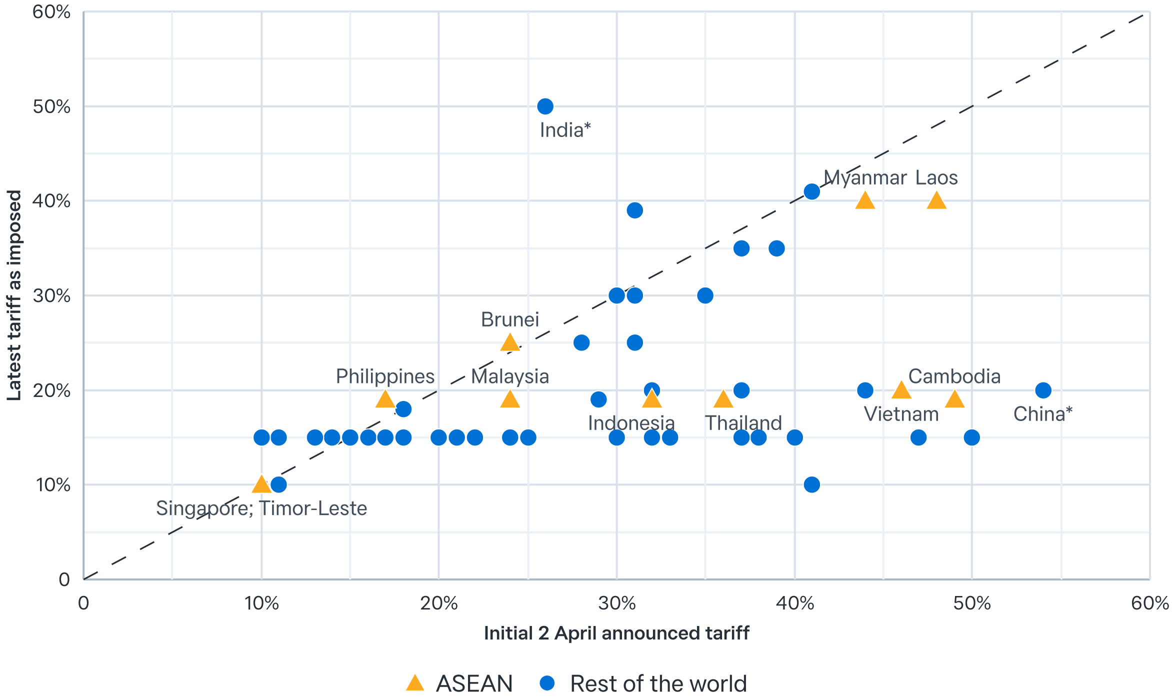
America First, China last, and Southeast Asia in the middle

US President Donald Trump sent shockwaves through the global economy when he unveiled his so-called “reciprocal tariffs” on 2 April 2025. The plan threatened the world with substantially higher tariffs, including a baseline rate of 10% for all countries. Southeast Asian nations were targeted with especially punitive rates. The region’s goods trade surplus with the United States had collectively reached $245 billion in 2024, the third-largest source of the US trade deficit behind only China and the European Union at the time. With the tariffs set using an ill-conceived formula based on the size of a country’s trade surplus with America, many ASEAN economies were targeted for devastatingly high tariffs.[5] Cambodia, Laos, Vietnam, and Myanmar were threatened with tariffs of 44–49%, while Thailand and Indonesia faced tariffs of 36% and 34%. Other major economies including China, the European Union, and Japan were also targeted for stiff tariffs.

The reciprocal tariffs were, however, quickly paused following the adverse reaction of financial markets and to allow time for negotiations. By early August 2025, a revised schedule of tariffs was introduced, with a combination of bilateral negotiations and unilateral Trump administration decisions lowering the tariffs for most countries (Figure 1). Most Southeast Asian countries achieved substantially reduced, though still high, reciprocal tariff rates. Cambodia, Malaysia, the Philippines, Thailand, and Indonesia all face a tariff of 19%, while for Vietnam it is 20%. However, the Trump administration also plans to impose additional 40% tariffs on any goods deemed to have been “transhipped” (illegally rerouted via third countries to avoid tariffs), a measure aimed squarely at China as the source and Southeast Asia as the conduit. How this will be implemented remains unclear. Meanwhile, Laos and Myanmar still face very high reciprocal tariffs of 40%, though neither is reliant on exports to the United States.[6] Brunei faces tariffs of 25%, while Singapore and Timor-Leste face the baseline 10% rate.

FIGURE 1

Initial vs revised US reciprocal tariffs



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), Fitch Ratings

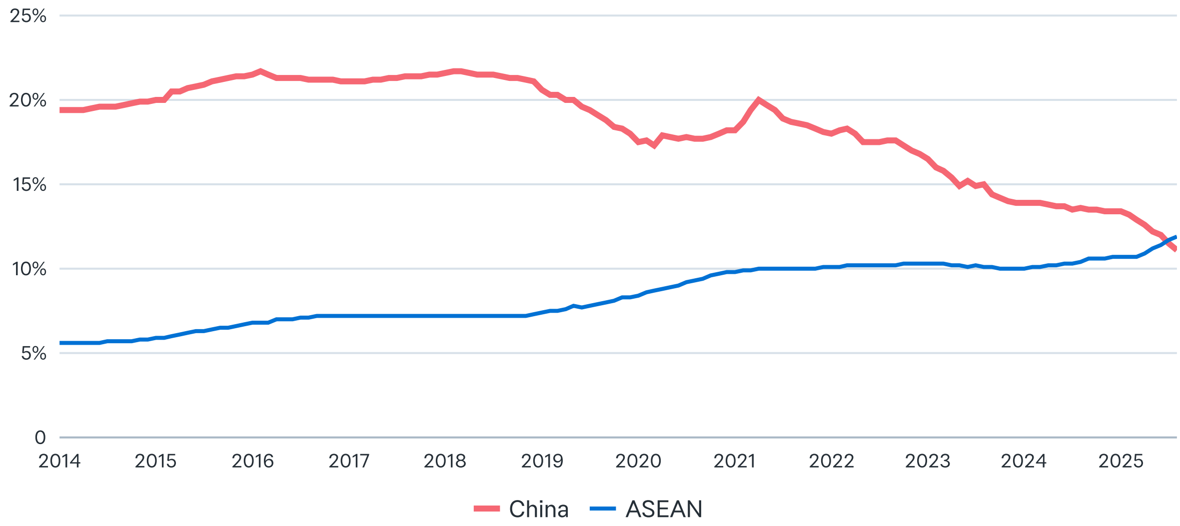
Note: * Inclusive of other tariffs issued under the US International Emergency Economic Powers Act

However, tariff rates are not the only thing that matters. Tariffs result in trade diversion as well as destruction. How tariff rates compare between competing economies is key. China is the region's chief trade competitor, especially in more advanced areas such as electronics, machinery, and automotives that are critical to Southeast Asia's efforts to move up the value chain. And the experience from the tariffs imposed during the first US–China trade war of 2018–19 is that many Southeast Asian economies emerged as winners. That period saw the effective US tariff rate (weighted by trade value) on Chinese imports jump from 3% at the start of 2018 to 19% by the conclusion of the US–China Phase 1 trade agreement in January 2020.[7] This kick-started a substantial shift in US trade away from China as an import source and towards other developing economies, notably Southeast Asia and Mexico (Figure 2). This was reinforced by further targeted China tariffs under the Biden administration, supply chain diversification efforts by multinational firms in response to the Covid-19 pandemic and rising geostrategic tensions, as well as the longer-term trend of rising labour costs in China. Economies of scale meant that higher exports to America also allowed the region to expand its exports to the rest of the world.[8]

FIGURE 2

ASEAN replacing China in the US

% of total, 12 month rolling sum



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data

US–China trade relations over the past year have been tumultuous. Immediately following President Trump's 2 April announcement, tit-for-tat retaliation by each country saw two-way tariffs rise above 100%. China also tightened its chokehold over the global supply of rare earth elements, which are critical to a range of modern manufacturing activities including the defence industry. The situation was viewed as unsustainable, leading to a negotiated pause in May that saw the United States remove all recent tariff increases other than the 10% baseline reciprocal tariffs as well as the 20% tariffs imposed early in the second Trump administration linked to US concerns over illegal fentanyl imports from China. China lowered its retaliatory tariffs to 10% and eased restrictions on rare earth exports. Tensions, however, flared again in October with China introducing a new extra-territorial export control regime for rare earths in response to US export controls and the Trump administration responding with additional 100% tariffs. Subsequent negotiations saw China and the United States pause or withdraw their latest measures, with the Trump administration also reducing its fentanyl tariffs to 10%.

Could President Trump's second trade war again indirectly benefit Southeast Asia? The obvious key difference this time around is that steep tariffs are now also being applied to the region itself. US tariffs on China, however, have risen by more. Reductions in tariffed Chinese exports to America after the first US–China trade war meant the effective US tariff rate on China had fallen to 11% by 2024. By October 2025 however, that figure had jumped again to 31%, with the increase reflecting the maintenance of the 10% baseline reciprocal tariff plus

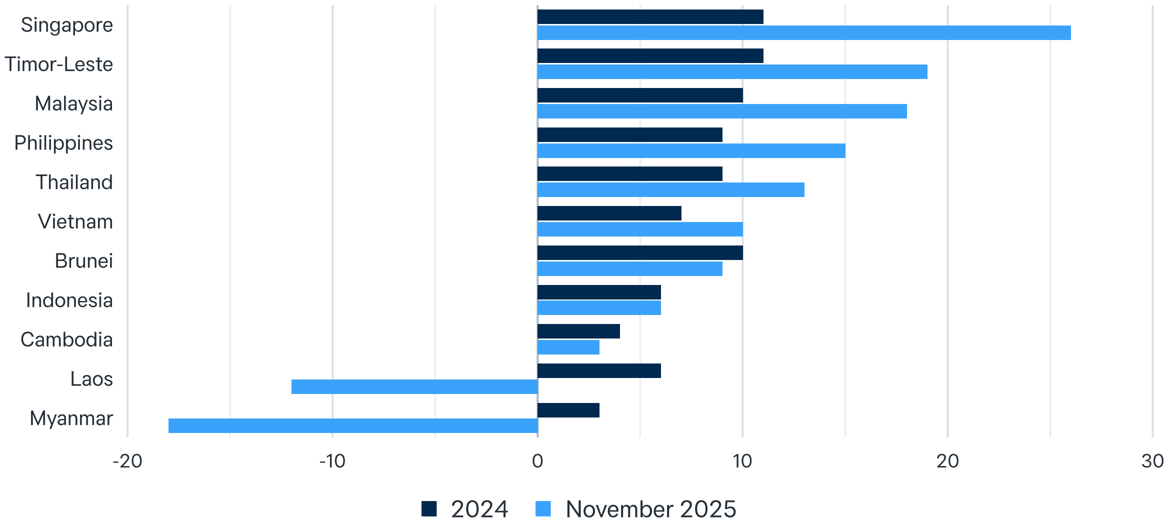
10% “fentanyl” tariffs on all Chinese imports, as well as global sectoral tariffs of 25–50% on steel, aluminium, copper, timber, and automotives.

By contrast, the effective US tariff rate on ASEAN economies has increased by less in most cases. For example, while Malaysia faces a headline reciprocal tariff rate of 19%, its effective US tariff rate is only 11% at present, compared to 0.6% in 2024. Despite facing a similar headline increase in tariffs to China, the effective tariff rate on Malaysia is lower because around half of its exports are electronics products currently exempt from the reciprocal tariffs but captured by the China fentanyl tariffs. Malaysia is also not a major exporter of products attracting even higher US sectoral tariffs. The picture is similar for the Philippines, Singapore, Thailand, and Vietnam. By contrast, others in the region are more affected because most of their exports to the United States (notably textile products) are captured by the reciprocal tariffs. Nonetheless, the major trade-oriented ASEAN economies have seen their effective tariff advantage over China in the US market increase, in some cases substantially (Figure 3).

FIGURE 3

ASEAN’s tariff advantage over China has mostly widened

Effective US tariff rate differential between China and ASEAN



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), Fitch Ratings

Average tariff differentials, however, still understate how important recent US trade policies could be in reshaping trade flows and supply chains to Southeast Asia’s advantage.

For one, Southeast Asia’s tariff advantage over China is especially large in areas critical to industrial upgrading. For example, while Cambodia’s effective tariff advantage over China is presently only 5%, its advantage in machinery and electronics is 46%.[9] The difference is partly due to pre-existing US tariffs on China imposed during the first US–China trade war. However, it is also because numerous electronic products have been exempted from the reciprocal tariffs. Cambodia's machinery and electronics exports are currently minimal but could expand if it can successfully attract supply chains incentivised by the tariffs to move out of China. Focusing on the difference in headline effective tariffs, therefore, understates the potential to capitalise on new and important areas of advantage over China. The picture is similar for others in the region, albeit to a lesser extent, with a tariff advantage over China in machinery and electronics of about 30% for Indonesia, the Philippines, Malaysia, and Thailand. For Vietnam it is 24%.

In addition to the tariff differential, there is also an important risk differential. This is difficult to incorporate into the standard economic models used to assess the impact of tariffs but could be crucially important in reshaping US–Asia supply chains. While US trade policy towards all countries is highly uncertain, that is especially so with regard to China. This will likely have a major bearing on trade and investment decisions by multinational firms, which have been pursuing a China+1 diversification strategy for some time.[10] In 2025, actual or threatened US tariffs on China have twice reached more than 100%, a level seen as effectually a trade embargo.[11] The current de-escalation is also widely seen as only a temporary and fragile truce as each side seeks to build its economic resilience.[12] For instance, the United States is currently readying its ability to impose further trade measures by initiating a new investigation into China's (non)compliance with the Phase 1 US–China trade agreement.[13] A recent survey of US importers suggests that ASEAN is the preferred manufacturing base among firms making supply chain realignments in response to US tariffs.[14]

Southeast Asia’s exports have boomed, but can it last?

Southeast Asia is already replacing Chinese goods in the United States, with the region’s exports to America booming despite the tariffs. ASEAN’s goods exports to the United States were around 23% higher in September 2025 compared to the same time in 2024, equivalent to roughly $70 billion in additional exports when annualised. Notably, all the major trade-oriented ASEAN economies have seen faster growth in exports to the United States than normal. Vietnam and Thailand have led the way, with US-bound exports surging by about 30% compared to last year.

Can this last? A common assumption is that much of the apparent boom in Southeast Asia’s exports to the United States has merely reflected the temporary effects of frontloading by US importers to get ahead of impending tariffs. However, the evidence does not align neatly with this story. Substantial frontloading was evident only in the first quarter of 2025, prior to the 2 April “Liberation Day” announcement, and primarily for imports from Europe.[15] There is much less evidence of frontloading for Southeast Asia, whose US-bound exports have been persistently strong this year (Figure 4). This could partly be explained by the delay in imposing reciprocal tariffs above the baseline rate between April and August. However, there are only limited signs of this in terms of total US imports, which collapsed after April, especially for consumer goods.

A more convincing explanation is the role of ASEAN in replacing goods previously being imported from China. China’s exports to the United States have fallen by almost 30% (Figure 4). Looking at exports from ASEAN and other economies that compete in similar export categories, there is little visible sign of frontloading (Figure 5). Instead, exports from these countries to the United States have on aggregate declined, entirely due to reduced US imports from China and only partially made up for by increased imports from others, principally ASEAN. Importantly, while the collapse in China’s exports occurred almost immediately in April when US tariffs on China temporarily reached more than 100%, there has been no recovery since — suggesting the deterioration in US–China relations could have already created long-lasting effects as firms read the writing on the wall.

FIGURE 4

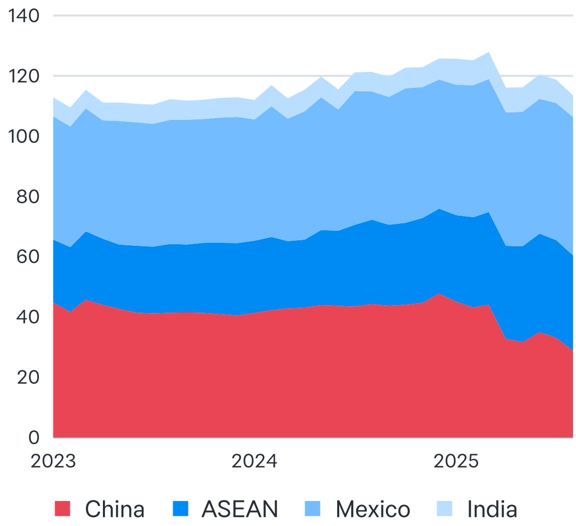
ASEAN exports to US surge as China's collapse

Goods exports to US, indexed (Dec 2024 = 100)

FIGURE 5

Frontloaded or replaced exports to the US?

Goods exports to US, US$ billions



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data

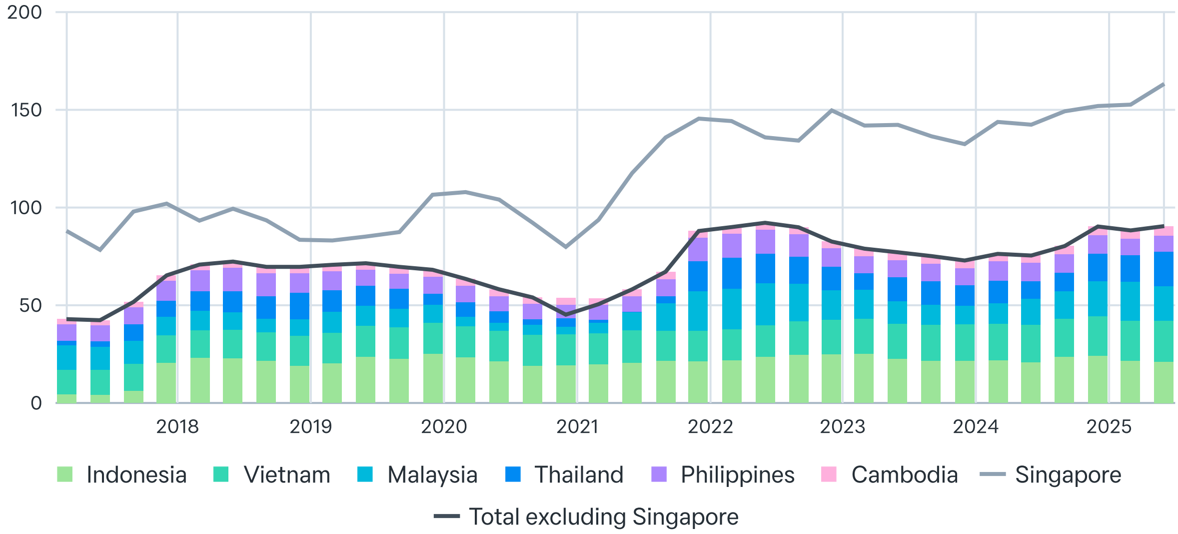
All this suggests that the strength of Southeast Asia's exports to the United States could prove relatively durable. To be sure, there are reasons to suspect ASEAN's exports to the United States could soften somewhat going forward. For one, the immediate benefit of replacing China in the US market has likely already substantially played out. Higher reciprocal tariffs of 19–20% for major ASEAN economies were also only imposed in August and the effects could bite harder in coming months as firms and consumers adjust. It is also possible that total US import demand could weaken more substantially if US firms begin to pass on greater price increases to consumers or if there is a sharp economic downturn. For now, the US economy remains unexpectedly resilient, driven by a boom in AI-related investment and equity prices, the latter supporting consumer spending through the wealth effect. In its latest forecasts, the International Monetary Fund projects the US economy to grow by 2.1% in 2026, slightly faster than in 2025.

Southeast Asia's exports to America might soften over the coming year but will have nonetheless moved to a much higher new base, due to their role in replacing Chinese imports. Over time, new investment responding to differences in tariffs and risk between the region and China should see new export capacity come online, greater economies of scale, and increased exports. Despite the region itself facing high uncertainty, it is notable that foreign direct investment inflows have to date been generally undeterred (Figure 6). Exports to the rest of the world also continue to grow strongly (discussed later). Most importantly, there is the opportunity for industrial upgrading over time if countries are also able to deepen their participation and move up the value chain, especially if governments also respond with complementary reforms (also discussed later).[16] Traditional economic models struggle to capture these impact channels and could therefore prove limited in fully understanding the actual and potential impact of the tariffs.

FIGURE 6

Foreign direct investment inflows to ASEAN remain at peak levels

Rolling 4 quarter sum, US$ billions



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data

The second China shock and Southeast Asia

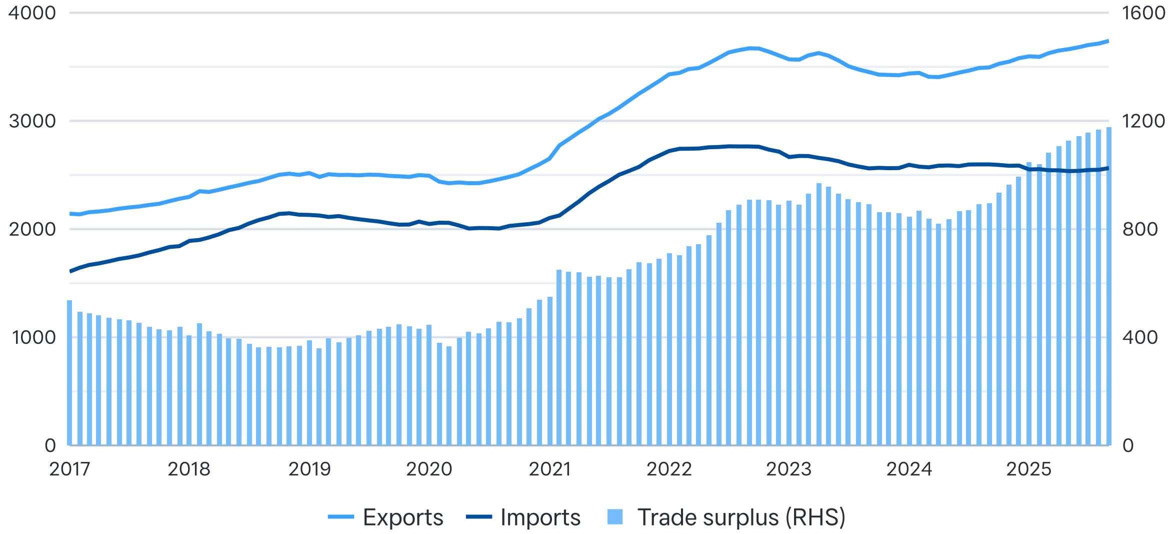
The impact of US tariffs has been especially complicated by China's simultaneously surging exports and trade surplus. This has been dubbed the second China shock. China's goods exports have jumped by around $1.2 trillion since 2019, before the Covid-19 pandemic. But China's imports have only increased by $500 billion. As a result, China's goods trade surplus now totals almost $1.2 trillion (Figure 7). The fear is that this second China shock could lead to a hollowing out of manufacturing bases in developing and advanced economies alike.

Yet, as we show in this section, for Southeast Asia there are important differences between the first and second China shocks. Whereas the first China shock saw it crowd out others in low-skill manufacturing while recycling its trade surplus into US treasury bonds, the second China shock has seen the country become a direct source of growth-enhancing intermediate inputs and capital goods while channelling the proceeds of its trade surplus into substantial new investments in the region.

FIGURE 7

The 'second China shock'

Merchandise trade, rolling 12 month sum, US$ billions



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data

In the 2000s, China's accession to the World Trade Organization and rise as a manufacturing powerhouse were associated with deindustrialisation in much of the rest of the world. In the United States, studies linked increased Chinese imports to geographically concentrated job losses mostly in low-end manufacturing such as garments, toys, and furniture.[17] Meanwhile, developing economies faced "premature deindustrialisation", with China's rise as a manufacturer combined with increasing automation crowding out these countries from the export-led manufacturing historically seen as vital to achieving rapid and sustained growth.[18]

Prior to the Covid-19 pandemic, many thought that rising labour costs, a maturing economy, and the reluctance of the rest of the world to absorb ever more Chinese imports would eventually see China become less reliant on export manufacturing. However, recent developments have defied such predictions. The end of China's property boom and the after-effects of the Covid-19 pandemic have left China with persistently weak domestic demand. Instead of stimulating consumption, China's policymakers have doubled down on manufacturing as part of efforts to engineer an export-led recovery but also as the key means of achieving technological advancement. China's exports to developing countries have especially surged, with Southeast Asia a key destination. The region's goods trade deficit with China has widened considerably post-Covid to more than $180 billion in 2024, compared to $100 billion before.

The United States and other rich countries fear this new China shock will see a hollowing out of their advanced manufacturing industries and create unwanted dependencies on China in high-end technologies, especially those related to clean energy.[19] For developing economies, the concern is surging low-priced Chinese imports leading to factory closures and job losses as well as dashed hopes of China finally ceding ground in manufacturing to others.

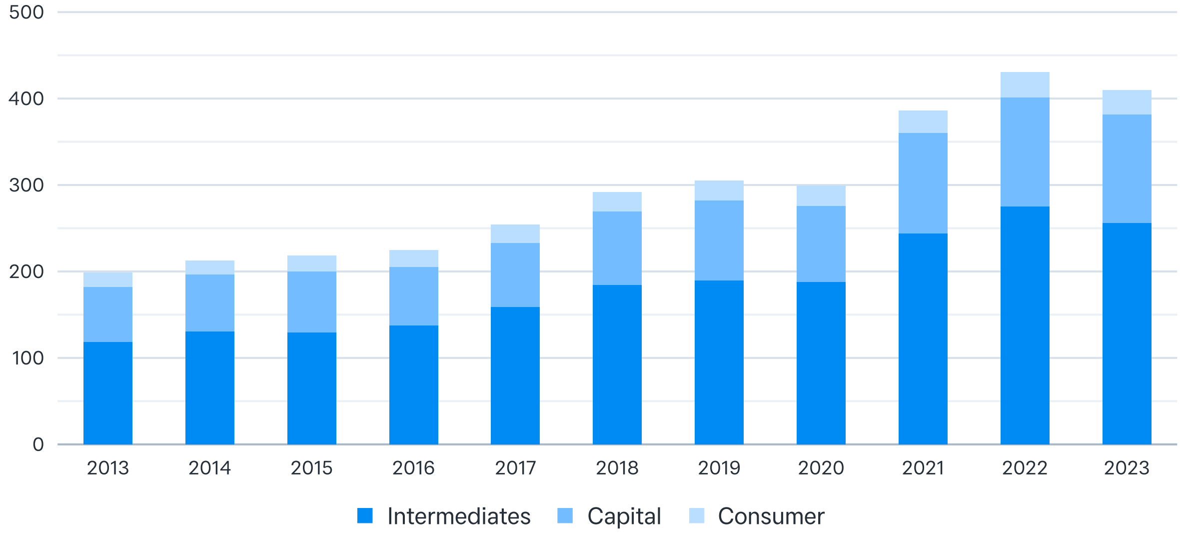
However, the evidence in Southeast Asia is mostly at odds with this worrisome narrative. Though contributing to some problems, the second China shock has primarily been growth enhancing for ASEAN.

Looking at the composition of what ASEAN imports from China reveals that China is mostly acting as a source of competitive inputs and capital goods (Figure 8). Sixty per cent of imports from China, and most of the increase in recent years, has been for intermediate inputs (parts and components) that mostly feed into and enable the region's own booming exports. Capital goods (e.g. machinery and equipment) used for investment make up roughly a further 30% of imports from China and have also expanded significantly in recent years. China now provides more than 40% of the capital goods imported by ASEAN, displacing Japan, South Korea, and Western Europe to become far and away the region's largest source of capital goods. In total, more than 90% of Chinese imports are used to support the region's own production and growth. By contrast, imports of Chinese consumer goods, which often compete more directly with local producers, remain at just 7% of imports from China.

FIGURE 8

ASEAN imports from China are mostly pro-growth

Imports by broad economic category, US$ billions



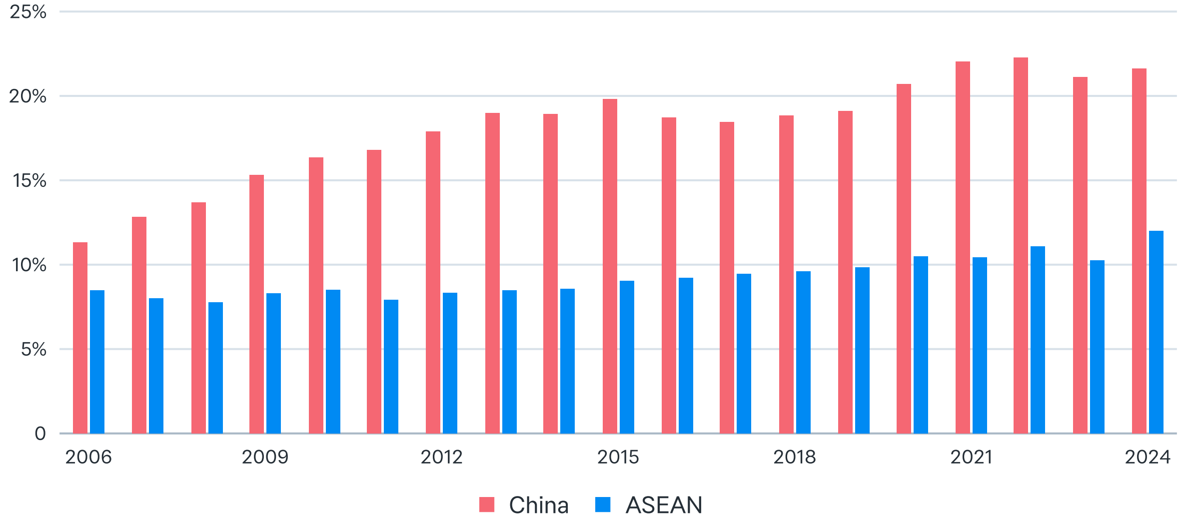
Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), UN COMTRADE

That the new China shock has mostly been pro-growth for the region can also be seen at a more granular level by examining key global value chain (GVC) industries — textile products, electronics, machinery, and automotives. These industries are among the most important for economic development due to the scope for international integration and the productivity benefits that come from it.[20] Southeast Asia's share of global exports in key GVC industries has risen alongside China's (Figure 9). Indeed, the region's performance has been even better than China's in recent years. Southeast Asia's gross GVC exports have increased by 73% since 2017 compared to 54% for China. Vietnam is the stellar performer, but other Southeast Asian economies have also done relatively well. Crucially, the region's strong GVC export performance is more than just the assembly of Chinese-made parts and components, with most of the value coming from production in Southeast Asian nations themselves (discussed later).

FIGURE 9

ASEAN global value chain role rising alongside China

Share of world global value chain exports



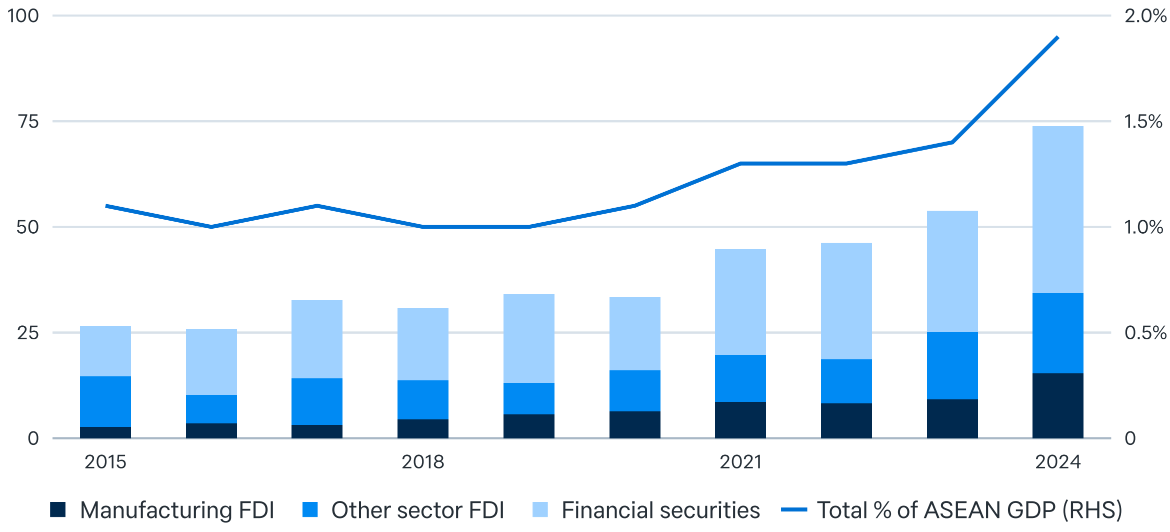
Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), UN COMTRADE

Rising Chinese investment into the region has also been an important growth-enhancing element of the second China shock for Southeast Asia. Basic accounting requires that China's total trade surplus (technically, its current account surplus) with the world must be matched by corresponding net capital outflows to other countries. This need not directly align with its trade surplus with individual countries. However, in Southeast Asia's case, a widening China trade deficit is being accompanied by substantial Chinese investment inflows (Figure 10). This is a key difference compared to the first China shock, when China's trade surplus was primarily channelled into US treasury bonds. The available data show that China's direct and portfolio investment flows to Southeast Asia reached almost $75 billion or 2% of the region's GDP in 2024. China also provides substantial development loans to the region, which in 2023 amounted to an estimated $5 billion.[21]

FIGURE 10

Chinese investment inflows to ASEAN

Annual investment, US$ billions



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data

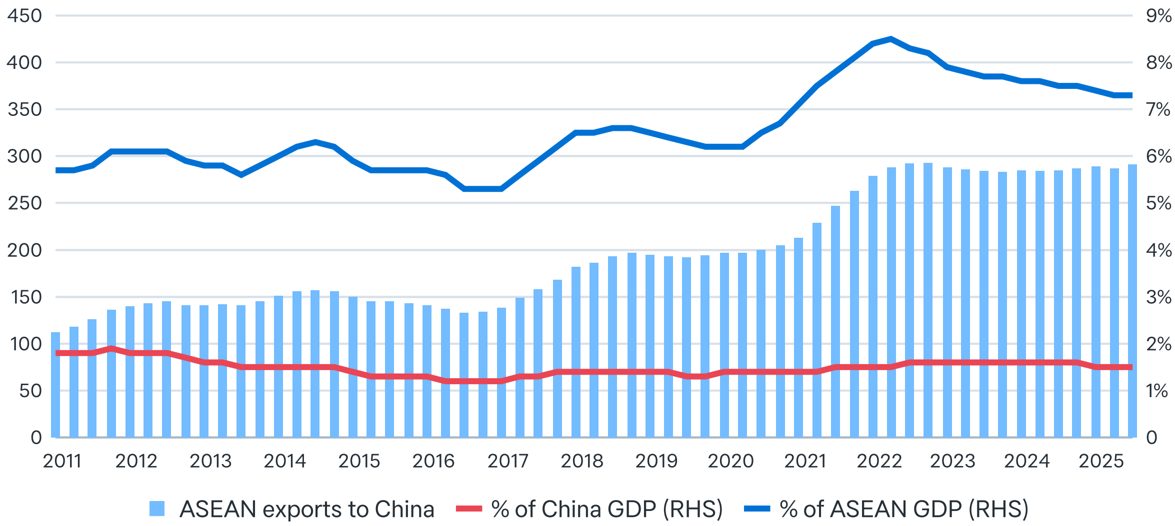
Although the second China shock has been mostly pro-growth for the region, there are some important caveats.

First, weak domestic demand in China and a policy focus on self-sufficiency mean Southeast Asia's goods exports to the country are stagnating, albeit at a high level (Figure 11). Exports to China jumped sharply higher during 2022 to about $290 billion but have flatlined since. The upshot is that exports to China have become considerably more important to Southeast Asia's economy post-Covid but are now also a persistent drag on economic growth. On China's side, imports from Southeast Asia have remained steady at about 1.5% of China's nominal GDP. However, falling prices in China means this likely masks the degree to which economic growth in China has decoupled from its imports from the region. China's economy has been growing in real terms by about 5% in recent years using official figures. Yet China's imports from Southeast Asia are flat in nominal terms and likely declining in real terms.

FIGURE 11

ASEAN exports to China stagnating but at a high level

Goods exports, rolling 12 month sum, US$ billions



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data

A second important caveat to the pro-growth story is that increased imports of cheap Chinese consumer goods are contributing to acute pockets of economic pain. Though a small portion of overall trade, China's consumer goods often compete directly with domestic producers in low-skill industries for basic consumer products. In Indonesia, the textile association reports 60 factories closed between 2022 and 2024 at the cost of some 250,000 jobs. In Thailand, the government reports 2,000 factories were shuttered in 2023. Competition from cheap Chinese imports is mostly blamed as the cause. Indonesia and Vietnam have each banned certain Chinese e-commerce firms, a key conduit for cheap Chinese consumer imports, from operating in their countries.[22]

Imports of Chinese consumer goods have indeed increased sharply in most of the region (Figure 12). Excluding Singapore and Malaysia, which have bucked the trend, imports of Chinese consumer goods by Southeast Asian nations increased by almost 70% between 2017 and 2023. The increase was sharpest in Cambodia, where Chinese consumer imports rose by 128%. Exacerbating the problem, the region's local producers are not only losing out in their home markets but also in exporting to each other. Since 2017, the share of ASEAN consumer goods imports sourced from within the region itself has fallen steadily as Chinese imports have increased (Figure 13). Malaysia, Thailand, and Indonesia have seen their share of intra-ASEAN consumer exports drop sharply. Vietnam and Singapore though have managed to increase their share substantially.

FIGURE 12

A jump in imported Chinese consumer goods

USD billions

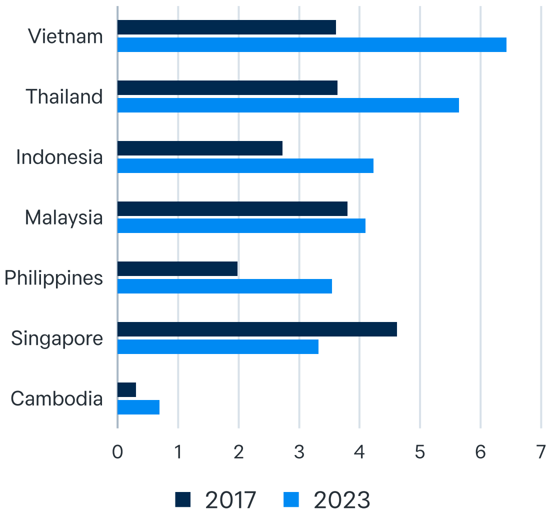
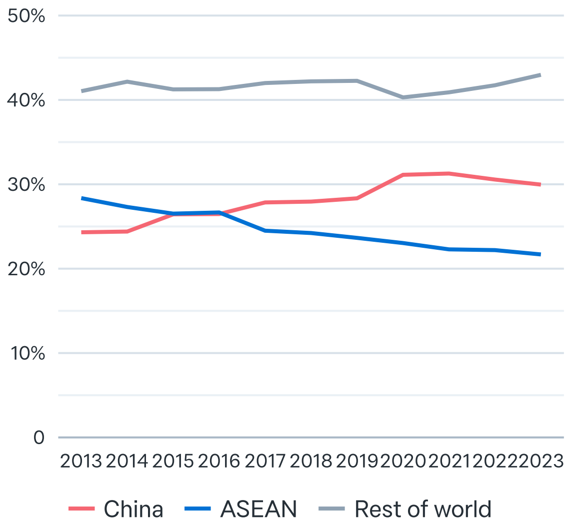


FIGURE 13

Intra-ASEAN consumer goods displaced

% of ASEAN consumer goods imports



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), UN COMTRADE

Trade deflection and global protectionism

There are several important ways in which US tariffs and the new China shock risk interacting negatively for Southeast Asia. High US tariffs are deflecting Chinese goods from the United States to other markets, threatening to cause even more economic dislocation for import-competing local industries but also potentially crowding out Southeast Asia's exports in other international export markets. Meanwhile, the combination of aggressive mercantilism by both the United States and China could also prompt the rest of the world down a more protectionist path that would prove especially damaging for trade-driven ASEAN economies.

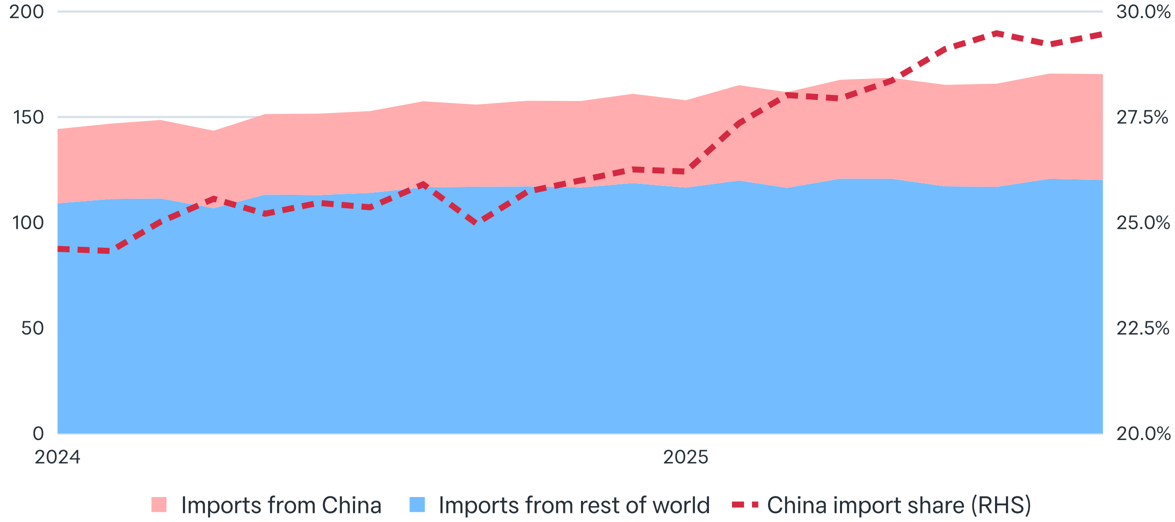
Southeast Asia has certainly seen a flood of deflected Chinese imports since the Trump administration's tariffs on China were introduced. Imports of Chinese goods were around 30% higher in September 2025 than the same time the previous year — a surge in Chinese imports equivalent to almost $150 billion when annualised.

However, deflected Chinese goods seem less to be displacing local producers of consumer goods and more to be displacing other import sources, especially for intermediate goods. Southeast Asia's total imports in September 2025 were 15% higher than the previous year, much less than the increase in Chinese imports but largely in line with the region's export growth of about 17%. Much of the increase in Chinese imports this year has, therefore, likely been for intermediate inputs used in Southeast Asia's own rising exports while crowding out other sources of intermediate imports, including from within the region (Figure 14).

FIGURE 14

Deflected Chinese goods crowding out other ASEAN import sources

Monthly ASEAN imports, US$ billions



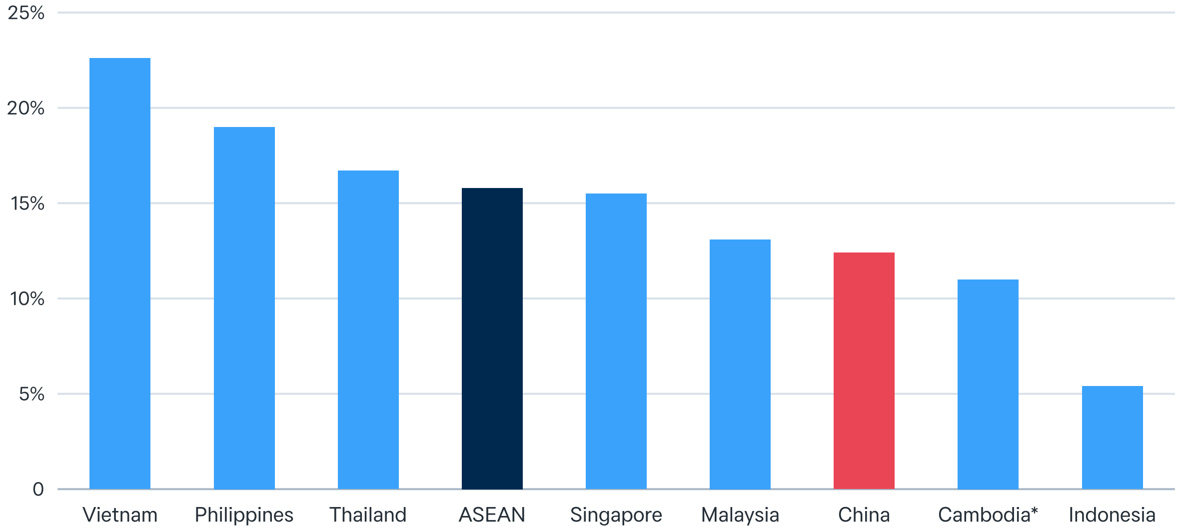
Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data

Meanwhile, there is little evidence that Southeast Asia is being meaningfully crowded out in non-US markets by Chinese goods deflected by US tariffs. ASEAN exports to non-US markets were up by about 16% in September 2025 compared to the year before, versus 12% for China's exports (Figure 15). Most major ASEAN economies have seen faster growth to non-US markets than China, with only Indonesia lagging substantially.

FIGURE 15

ASEAN global exports not crowded out by deflected Chinese goods

Year-on-year % change in exports to non-US markets, September 2025



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), CEIC Data Note: *Cambodia data is for July 2025

Southeast Asia's exports have performed strongly in part because of the region's competitiveness, including the leveraging of competitive Chinese intermediate inputs. However, it is also because global trade has been surprisingly resilient despite the Trump administration's protectionism. Global trade remains higher than last year, has reached a new peak (outside of the pandemic period) of close to $4 trillion per month, and is still expected by most major forecasters to grow over the coming years despite the tariffs.[23]

Underpinning resilient global trade has been the lack of a protectionist response from the rest of the world to US tariffs. Retaliation against the United States by other governments has been minimal aside from that by China. Moreover, Southeast Asia has found itself at the centre of global efforts to keep markets open and promote rules-based trade.

The European Union has concluded a new free trade deal with Mexico, Mercosur, and Indonesia. It is exploring enhanced cooperation with Malaysia, the Philippines, and Thailand as well as members of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) as a bloc. The CPTPP already includes Singapore, Malaysia, Vietnam, and Brunei as members. Indonesia and the Philippines have applied for membership and Cambodia is considering doing so. The China–ASEAN free trade agreement has been upgraded, while several economies (Hong Kong, Sri Lanka, Chile, and Bangladesh) are seeking to join the ASEAN-centred Regional Comprehensive Economic Partnership (RCEP).[24] Malaysia, the Philippines, and others have recently joined the Multi-Party Interim Appeal Arbitration Arrangement, a work-around to settle trade disputes established after the United States effectively disabled the World Trade Organization's mechanism. Singapore and Malaysia have joined with 14 other countries in the Future of Investment and Trade (FIT) partnership as an informal platform for addressing emerging issues and strengthening rules-based trade.

Supply chain diversification or a backdoor for Chinese exports?

The gross trade flows suggest Southeast Asia is playing a helpful role in diversifying international supply chains away from China, particularly for exports to the United States. However, China's growing role as a source of imports and investment suggests a different story — that Southeast Asian supply chains are becoming increasingly dominated by China.

This is of particular concern for the Trump administration, which sees Southeast Asia serving as a backdoor for indirect Chinese exports to the United States to circumvent its tariffs.[25] This includes pure tariff evasion through the illicit transhipment of Chinese goods via third countries as well as the heavy use of Chinese parts and components in the region's exports to America with little value added besides final assembly. Many analysts point to the high correlation between Southeast Asia's booming exports to the United States and its surging imports from China as the key evidence.[26] This pattern was seen after Trump's first-term tariffs on China in 2018–19 and has accelerated again with his second-term tariffs.

In response, the Trump administration has stated it will impose additional 40% tariffs on goods deemed to have been transhipped from third countries (i.e. China).[27] Recent reciprocal trade deals with Cambodia and Malaysia have also included a focus on ensuring third countries, again principally China, and their nationals are unable to benefit from lower tariffs or otherwise use these economies as a base for exports in ways deemed detrimental to the United States.[28] This includes provisions on combatting transhipment, the potential of the United States establishing specific rules of origin, the ability of the United States to request countries adopt similar measures to its own in restricting imports from a third country, countries regulating unfair practices by companies from third countries operating in their jurisdictions, and a requirement to cooperate with the United States on the security implications of inbound investments.

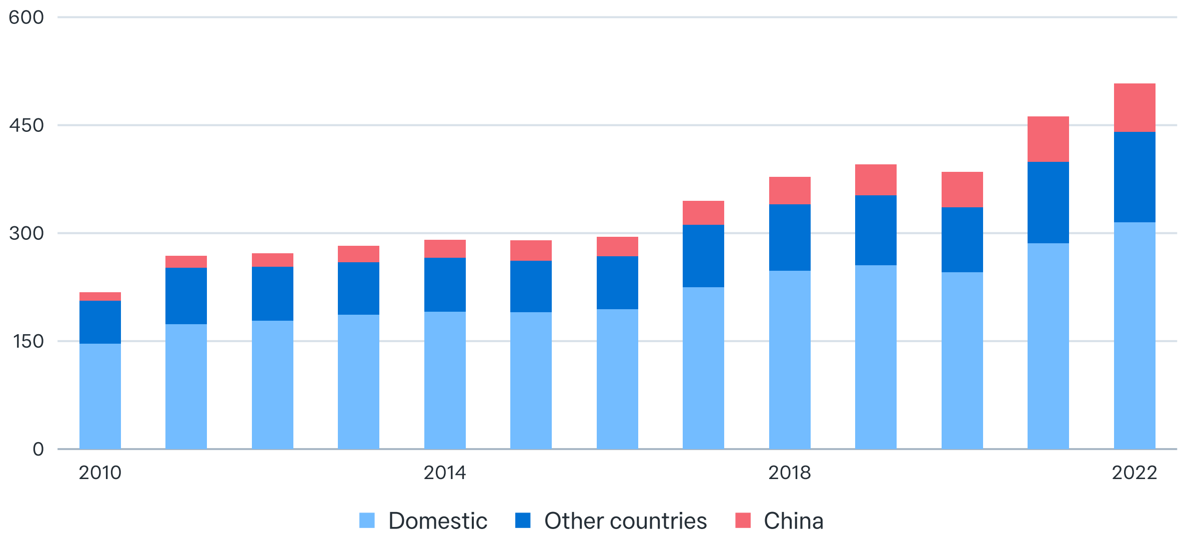
It is unclear if and how measures of this kind will be implemented in practice. A heavy-handed approach towards restricting China's involvement in Southeast Asian economies would either have devastating economic consequences for the region if it complied or cause a rupture with the United States if they did not and potentially a return to devastatingly higher US tariffs. A nuanced and evidence-based understanding of China's supply chain role is crucial to reaching a workable solution. Notably, Southeast Asian governments share some of the concerns of the Trump administration. Most worry that their economies are not gaining sufficiently from participating in global supply chains and that they risk getting trapped in low value-added activities. Meanwhile, participating in the illegal transhipment of Chinese goods provides virtually no economic benefit to countries but contributes to trade tensions with the United States.

Does China dominate the region's export supply chains? Data on trade in value-added can provide useful evidence on the underlying production contribution of different countries to the value contained in a country's exports. Decomposing Southeast Asia's goods exports by the underlying source of value-added shows that China's importance in the region's supply chains is indeed growing but remains modest. In 2010, value created in China accounted for just 3% of the region's exports. By 2022, this figure had grown to 7%. The figure is larger, however, in key GVC sectors (textiles, electronics, machinery, and automotives), having risen from 6% in 2010 to 13% in 2022 (Figure 16). China's share is highest at 29% and 18% for GVC exports from Cambodia and Vietnam, the two countries most reliant on Chinese imports. Nonetheless, the evidence clearly does not support a view that Southeast Asia's export supply chains are dominated by China. Nor does it show that these countries are failing to benefit from their participation in international supply chains, with domestic production accounting for about two-thirds of the value contained in the region's exports.

FIGURE 16

China's growing but still small role in Southeast Asia's global value chain exports

ASEAN global value chain exports by value-added source, US$ billions



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), OECD Trade in Value Added Database

What about China's role in Southeast Asia's exports to America specifically? The technical limitations of the data mean it is not possible to decompose the sources of value-addition contained in a country's exports to individual destinations. We therefore create our own (upper) estimates based on changes in trade flows since 2017, assuming that any increase in China's role in the region's exports beyond the pre-existing trend has been driven entirely by increased indirect exports to the United States in response to the 2018–19 tariffs.[29]

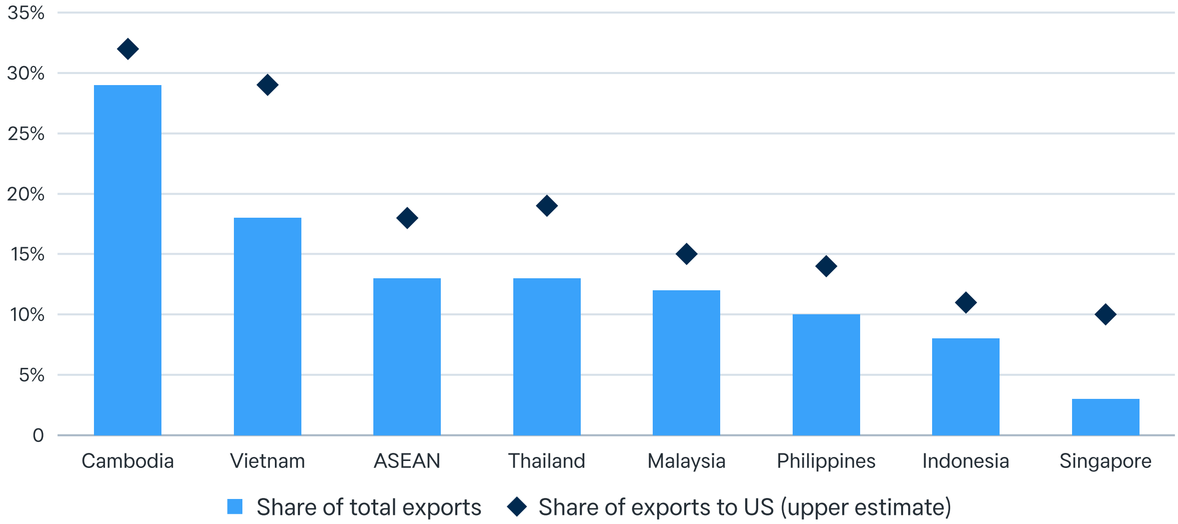
Figure 17 shows our estimates for Southeast Asia as a whole and for individual major ASEAN economies for GVC sectors, where China's presence is most significant. Our estimates suggest that China's role in the region's exports to the United States has indeed risen substantially and is now much larger than for its GVC exports more generally. Nonetheless, the picture remains qualitatively the same. China accounts for a higher share at 18% of total GVC exports for the region. But the vast majority of the value embedded in the region's US-bound GVC exports is still coming from a combination of domestic value-addition by Southeast Asian countries themselves and other supply chain partners besides China. This remains true even in Cambodia where China's role is most substantial.

Our estimates cannot distinguish between indirect Chinese exports to the United States in the form of illicit transhipment or the legitimate export of parts and components to third countries. However, our estimates are consistent with other detailed studies of transhipment since the first US–China trade war. For instance, a study of Vietnam finds that transhipment accounts for less than 10% of the overall increase in exports to the United States.[30]

FIGURE 17

China's larger but still limited role in ASEAN global value chain exports to US

China's value-added share of ASEAN gross global value chain exports



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), OECD Trade in Value Added Database

There is also little evidence of excessive Chinese dominance of the region's supply chains when looking at individual GVC sectors (Figure 18). For GVC exports to the United States specifically, China's supply chain presence is higher but still limited. The one exception is the automotives sector in Cambodia, where China's value-added share is estimated at 81%. These exports are, however, worth just $8 million.

FIGURE 18

China's value-added share in ASEAN global value chain exports by destination

	TEXTILES		ELECTRONICS		MACHINERY		TRANSPORT	
	World	US*	World	US*	World	US*	World	US*
Vietnam	20%	19%	17%	24%	17%	28%	16%	18%
Thailand	12%	19%	13%	15%	12%	24%	12%	36%
Cambodia	29%	32%	19%	26%	24%	35%	23%	81%
Singapore	12%	*NA*	3%	1%	4%	5%	3%	4%
Malaysia	11%	26%	12%	15%	12%	17%	9%	26%
Philippines	6%	6%	11%	16%	9%	9%	9%	16%
Indonesia	8%	9%	8%	13%	6%	13%	7%	24%

Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), OECD Trade in Value Added database   Note: *estimated

China's role in Southeast Asia's exports is undoubtedly much higher for some specific products. For instance, there is evidence that indirect Chinese exports via third countries are higher when it comes to strategic sectors.[31] China also notably dominates clean energy supply chains and the United States under both the Biden and Trump administrations has imposed high penalty duties on solar cells and panels exported by Vietnam, Cambodia, Malaysia, and Thailand based on findings that Chinese firms had circumvented US anti-dumping and anti-subsidy duties via factories and partners in these countries.[32] Trade investigations have now begun into Indonesia and Laos.[33] Nonetheless, it remains that the vast majority of the value contained in Southeast Asia's total exports to the United States — more than 80% by our estimate — reflects production by non-China sources.

Trends in greenfield manufacturing investment mirror this picture of China's still limited role and suggest that the shift in supply chains away from China could increase over time. Southeast Asia has seen a surge in new manufacturing investment since the first US–China trade war, with investment jumping 90% from $40 billion a year in 2010–2017 to $75 billion a year in 2023 and 2024. There is much attention to how the shifting of supply chains has been accompanied by rising Chinese manufacturing investment into ASEAN, which has indeed more than tripled to $19 billion in recent years. Focusing on China, however, overlooks that there has been an even larger surge in investment from America and its key partners (Figure 19).

Investment from Advanced Asia (Japan, South Korea, and Taiwan) has long outstripped that from China and has surged further to $26 billion a year recently. Investment from the United States has tripled. Along with increased investment from Western Europe, the United States and geopolitically aligned countries have been investing almost $50 billion a year into ASEAN manufacturing, far outstripping China at $19 billion (Figure 20). Only in Cambodia does China outweigh investment from the United States and its partners. Importantly, the pattern of the United States and geopolitically aligned countries collectively investing more than China also holds if one focuses only on GVC sectors.

FIGURE 19

Surging manufacturing foreign direct investment to ASEAN, by source

Annual average, US$ billions

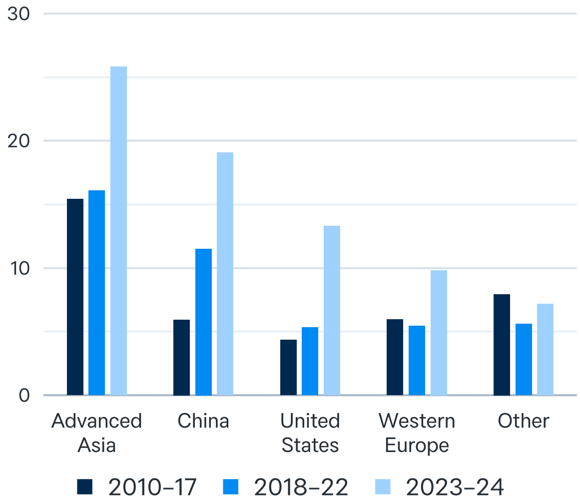
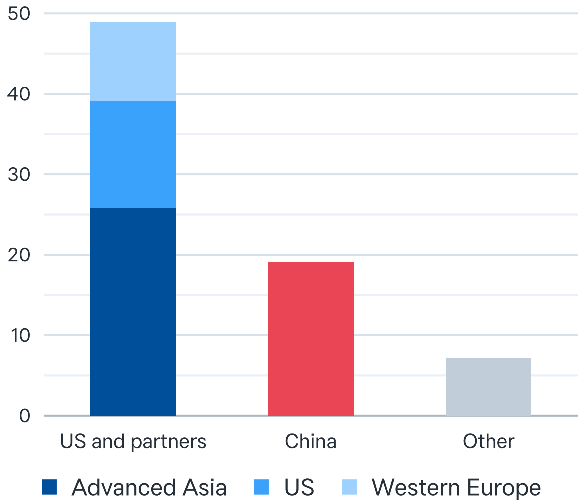


FIGURE 20

US and partners dominate manufacturing foreign direct investment into ASEAN

2023–24 annual average, US$ billions



Source: Lowy Institute (Rajah, Albayrak, and Walker, 2025), fDi Markets

Higher investment will expand future manufacturing capacity in Southeast Asia, increase domestic value-addition, and likely increase the supply chain role of the United States and its partners who are collectively making far greater new investments in manufacturing in the region than China. For Southeast Asia, this can provide an important foundation for future growth and industrial upgrading through new industrial clusters and trade networks as well as the diffusion of knowledge and technology.[34] For the United States, this would help to expand and deepen supply chain diversification away from China over time without needing to resort to punitive rules of origin. This could provide an important foundation for constructive and mutually beneficial engagement between Southeast Asia and the United States.

Realising this will, however, depend on policies in both the United States and Southeast Asia. On the US end, the key will be maintaining less punitive tariffs and other restrictions on the region as compared to those on China and developing an approach that reflects how Southeast Asia's supply chains are presently structured, what is realistic to achieve over time, and focuses on growing non-China participation rather than simply restricting China's involvement. For Southeast Asia, the key is adopting complementary policies to attract more foreign investment and supply chain participation from partners other than China and accelerate domestic industrial upgrading. The core policy agenda is well known, including further liberalising trade and investment, deepening and expanding participation in rules-based and multilateral agreements, reforming state-owned enterprises, improving regulatory standards, strengthening the domestic business environment, and making effective investments in institutions, infrastructure, and people.[35]

Where next for America First?

The future of US trade policy remains highly uncertain. The Trump administration's key tariffs issued under the International Emergency Economic Powers Act (IEEPA), which includes the reciprocal tariffs as well as the fentanyl tariffs on China, could be ruled illegal by the US Supreme Court.[36] Yet even this may offer little relief as many believe the Trump administration could likely replicate its existing tariff policies through other, more legally robust, methods.[37]

Another source of uncertainty is potential US sectoral tariffs under Section 232 of the Trade Expansion Act. These are premised (at least notionally) on national security grounds. Sectoral tariffs of 25–50% have already been imposed on steel and aluminium, copper, wood, furniture, and automotives. President Trump has also threatened tariffs of 100% on semi-conductors and pharmaceuticals, though with carve-outs for firms that invest in the United States.[38] Investigations that could result in tariffs are also underway for critical minerals, commercial aircraft and jet engines, polysilicon, drones, wind turbines, robotics and industrial machinery, medical equipment, clothing, and consumables. Other sectoral tariffs might also be introduced.

How consequential these sectoral tariffs might prove for Southeast Asia is difficult to gauge and will depend on tariff rates, scope of coverage, and any exemptions. The implications could, for instance, be substantial if all products containing semi-conductors were tariffed as it would cover a swathe of electronic goods. This would, however, also impose very high costs for US consumers, firms, and its economy more generally and therefore seems unlikely to happen.

Leaving aside such extreme scenarios, the implications of future sectoral tariffs could be relatively contained for Southeast Asia. Although some countries are major exporters of goods subject to Section 232 investigations (e.g. Malaysian and Singaporean semi-conductor exports), only a portion of these goods are sent to the United States. By our estimate, exports to the United States of goods facing potential sectoral tariffs account for roughly 4% of ASEAN's total exports, with Malaysia and the Philippines the most exposed, but with still only 6% of exports at risk. However, exports of these products to the United States have been growing relatively fast, so tariffs could still be felt sharply.

Ultimately, the evolution of the Trump administration's policies specifically towards Southeast Asia and how this relates to China will likely prove the most consequential for the region. Recently completed reciprocal trade deals with Cambodia and Malaysia offer important indications. Though not lowering the reciprocal tariffs of 19%, the deals say the United States will not raise these tariffs further while also introducing some new exemptions for both countries. The agreements also provide for both countries to grant the United States preferential market access while making substantial import purchases from America. Malaysia committed to invest $70 billion in the United States over ten years.

However, the most interesting element in both deals relates to their substantial provisions for "alignment" on economic security. In addition to seeking to limit the role of third countries (i.e. China) within the Cambodian and Malaysian economies, the deals envisage them adopting similar measures to the United States when it imposes trade restrictions, export controls, or other national security-based economic actions against a third country. The deals also include so-called "poison pill" clauses that seemingly give the United States a say over the ability of the two countries to enter into other trade and digital agreements with other countries.[39]

Although Cambodia and Malaysia have signed onto these agreements, they and most other Southeast Asian governments have repeatedly made clear that they have no interest in explicitly aligning with either the United States or China.[40] China has already warned both countries over the deals.[41] How aggressively the Trump administration will seek to enforce alignment on economic security is uncertain. The Cambodian deal explicitly incorporates greater flexibility to reflect Cambodia's own sovereign interests whereas the Malaysia agreement generally has stronger language. Nonetheless, Malaysia's trade minister has said that the deal only amounts to a commitment to consult, maintaining that "if it's not in our interest to follow the US we won't".[42] Demonstrating specific pushback, both Malaysia and Indonesia continue to resist US pressure for them to remove export restrictions on raw critical minerals despite this being included in agreements with the United States.[43] Reports indicate Indonesia is also currently pushing back on the inclusion of "poison pill" and other coercive clauses during ongoing negotiations.

Putting aside the risk of extreme US economic security demands, Southeast Asia could potentially work with the Trump administration on the related but more mutually beneficial objective of building more diversified and fair supply chains. The Trump administration has signed critical mineral cooperation deals with Malaysia and Thailand. Both the Cambodian and Malaysian deals include reference to cooperation on critical minerals and other strategic US investments, including America potentially providing investment financing via its Export–Import Bank and Development Finance Corporation.

Both the Malaysia and Thailand deals (as well as framework deals with Vietnam and Thailand) also contain provisions covering numerous trade and investment policies. Much of this pertains to removing barriers specifically related to US imports and investment as well as agreeing not to impose measures that go against US tech interests.[44] However, there is also a considerable focus on undertaking reforms that would benefit trade and investment with all countries. This includes strengthening rules and enforcement for intellectual property, labour rights, and environmental protection. It also covers improving regulatory practices, digitising trade facilitation, and ensuring state-owned enterprises operate on a primarily commercial basis.

Southeast Asian nations will have little enthusiasm for undertaking difficult reforms simply to appease the Trump administration. However, much of this agenda dovetails with the kind of policies countries should be implementing anyway to help attract shifting supply chains and greater investment, and achieve the industrial upgrading needed to underpin continued rapid growth.[45] Indeed, a wider reform agenda focused on enhancing openness and competitiveness would strengthen the region's economic resilience by helping to diversify trade and investment relationships and solidify its centrality to global trade, thereby making it even more difficult and costly for the United States or others to decouple or apply geoeconomic pressure.

Conclusion

Southeast Asia's competitiveness and, somewhat paradoxically, openness have been central to its economic resilience to the global trade shocks. Even within the region, while all the major trade-driven economies have proven resilient in broadly the same ways we have outlined, those that are relatively more open and competitive have fared best. For instance, Vietnam is experiencing some of the strongest increases in exports to both the United States and the rest of the world. Indonesia, by contrast, has seen much less export growth while still experiencing the substantial economic dislocation of local industries by surging imports of cheap Chinese consumer goods. Cambodia has done well on openness and exports, but its lower competitiveness has left it much more reliant on China for supply chain inputs and investment than others.

The future of global trade remains highly uncertain. But Southeast Asia is much better placed to navigate this than widely assumed. The region's openness and competitiveness has allowed it to capture greater market share in the United States, leverage useful Chinese imports and investment, compete effectively with China in global markets, attract more international partners, and deepen its international integration while largely avoiding excessive dependence. This gives the region more options amid the trade and geoeconomic turbulence of the current moment. It also provides more scope to negotiate with an America that wants to reduce its economic dependencies on China and build more diversified and fair supply chains. Even now, openness is serving the region well.

Note: All currency quoted is in US dollars.

Notes

1 ASEAN refers to the Association of Southeast Asian Nations. In this paper, it refers to the region generally, and specifically the seven economies of focus — Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam. These economies also represent the vast majority of trade and investment in the region as well as having more up-to-date and comprehensive data available.

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