FRAGMENTED GLOBALISATION

The future of global trade by Coface

18 FEBRUARY 2025

FOR TRADE

Editorial

By Jean-Christophe Caffet
Chief Economist

Initiated in the wake of the collapse of the USSR in the early 1990s and accelerated by China's entry into the WTO a decade later, trade globalisation in its contemporary version was based on two promises: one political, the other economic.

The political promise was grounded on the virtues of *le doux commerce* – gentle commerce – extolled by Montesquieu, or *Wandel durch Handel*[1] in its German version two centuries later. Growing trade would help bring countries and people closer together, binding them by shared economic interests. Moreover, a certain "elective affinity" in the Weberian sense between free trade and political freedom inspired hope for a gradual spread of the democratic form to the entire globe. According to some, the combination of political pluralism and open trade would even seal the final victory of liberal democracy over other kinds of political systems.

We now know the political promise will not be kept in two respects. First, the 2020s has seen a rekindling of major geopolitical tensions emanating along the East-West and North-South fault lines. Second, the Chinese example has categorically confirmed that authoritarianism and capitalism are potentially compatible. In short, le *doux commerce* has not prevented wars or the perpetuation of dictatorships. Furthermore, a certain impoverishment of the working and middle classes in advanced countries has undermined the social foundations on which all democracy rests.

"The intensification of trade was supposed to contribute to bring together countries and peoples, linked by common economic interests... We now know that this promise will not be kept."

Jean-Christophe Caffet
Chief Economist

The second promise of globalisation was economic. It argued that the expansion of trade would create a trend of self-sustaining interdependence which, barring a major catastrophe, would prevent us from turning back the clock. Value chains would continue to be designed and deployed on a global scale, constantly adapting to the context but always following the Ricardian logic of comparative advantages. The quest for profitability, the strengthening of multinationals and the gradual widening of large, global trade zones made a return to the past highly unlikely.

This second promise has not been refuted, but it is currently more uncertain. The share of trade in global wealth has stagnated over the past fifteen years, and the first signs of trade flow fragmentation are emerging. This is undeniably the case for energy, with Russia's decoupling from the Western side of globalisation. However, it is also occurring in manufactured goods on back of a growing number of export restrictions and tariff increases. In short, globalisation is not dead, it is changing.

Complex, contradictory and fast-moving, these developments require more than ever impartial analysis based on verified data and facts. Coface's Economic Research Department provides this, working in conjunction with the experts and practitioners who took part in our Country Risk Conference in February. I would like to thank them and the entire team of Coface economists.

1 - Change through trade

Executive Summary

By Olivier Rozenberg,
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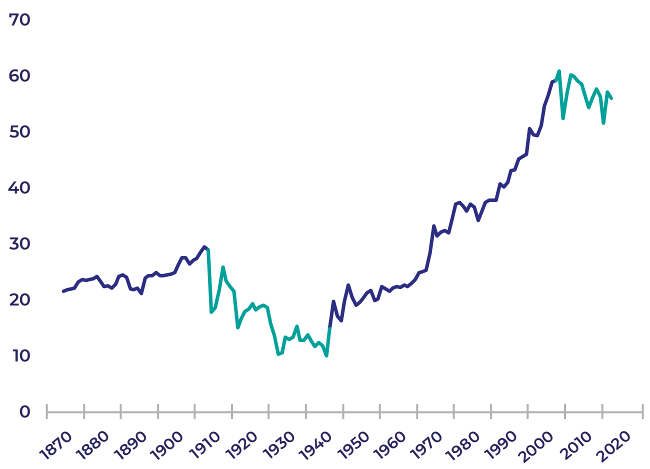
Few charts are as clear as the one showing the share of trade in world GDP over the past 150 years. After almost continuous and relatively regular growth since the immediate post-war period, it fell at the turn of the 2010s due to the Great Financial Crisis and the rebalancing of the Chinese economic model. Since then, **the share of world trade has not grown - nor has it really declined**, as it did between the two world wars.

Share of world trade in GDP *(1875-2022, %)*



Note: exportations et importations in value.
Source: Klasing & Millionis (2014), Penn World Table, World Bank, PIIE, Coface.

The aim of this publication is to examine this state of globalisation by combining the perspectives of geopolitical experts, world economic players and Coface's economic research. To this end, we return to **the Country Risk Conference organised by Coface in Paris on 4 February 2025, which focused on geopolitical fragmentation and its macroeconomic and financial implications.**

The first panel focused on the **current geopolitical dynamics** and, more specifically, on the implications of Donald Trump's election for a second term. Recalling that the deterioration in international relations is a fundamental trend, now reinforced by the increase in tensions within blocks of countries that are in principle aligned, the three experts urged us to keep a cool head: an open conflict between the United States and China, for example, is hardly conceivable in the medium term. Nor can we rule out 'good news' regarding the resolution of certain ongoing conflicts.

But the situation remains extremely fragile and uncertain, with major implications for trade, investment decisions and economic growth. The emergence of two distinct world poles, centred on China and the United States, raises fears of a return to a new Cold War. It opens the door to many unknowns, particularly with regard to the European Union's strategy, India's positioning and a possible rapprochement between Russia and the United States. Divided, Europe seems particularly vulnerable to the double threat posed by Donald Trump's strategic agenda and the commercial aggressiveness of a China relentlessly seeking new markets.

The second panel focused on **the dynamics of fragmentation in the manufacturing, financial and logistics sectors.** The four speakers, experts and/or actors in the global economy, underlined the resilience of certain fundamentals of globalisation to the geopolitical shocks mentioned above. Trade remains at a high level thanks to the support of «connector» countries. Maritime transport had a good year in 2024, despite (or because of) the disruption of the main trade routes (Suez, Panama, etc.). Finally, international financial flows do not seem to have been fundamentally affected (yet?), even if the sanctions regimes make the structuring of certain cases more complex.

Overall, globalisation is holding up, but it seems to be weakened by the proliferation of imbalances. Two of these were of particular concern to the panelists. First, the growing imbalance between China's share of global industrial output and its external markets, which are shrinking as tariffs and trade restrictions are imposed. Second, the wide regulatory gap between Europe, which continues to believe in rules and standards, and the United States, which is firmly committed to unbridled deregulation.

The third part of this publication looks back on the main findings of the work carried out by Coface economists on four major challenges of globalisation. These publications are available on the Group's website. The first study examines the impact of geopolitical tensions on world trade. The second focuses on electric vehicles in Europe - a crucial issue given the EU's commitment to carbon neutrality. The third addresses the issue of industrial overcapacity in China. Finally, the electronics sector is the subject of a special analysis of Sino-American competition.

SUMMARY

Jean-Christophe Caffet

PART 1

Geopolitical fracturing and recomposition

As conflicts escalate or stagnate, revealing the failure of the world's current governance structure, antagonisms are coming to light or have crystallised.

Does Donald Trump's comeback mark a new turning point in the development of international relations?

Three experts compare their views on the fracturing and restructuring of the geopolitical environment, and on the way this issue has penetrated corporate strategies.

Geopolitical fracturing and recomposition

It seems like another case of déjà vu. Donald Trump's second inauguration as President of the United States on 20 January might have sent observers back eight years, but the world has changed profoundly since then. *"First, two major conflicts erupted between Trump 1 and Trump 2: Russia's large-scale invasion of Ukraine in February 2022 and the militarised terrorism of Hamas in October 2023, Israel's reaction to which sparked a recomposition of the Middle East. Then came the acceleration of environmental degradation on one hand, and the spread of technology on the other*", explained Thomas Gomart, director of IFRI, the French Institute for International Relations. While all these events have already begun to reshuffle the geopolitical deck, it is likely that the new Trump administration's decision to establish a transactional approach as the driver of its policy to *"make America great again"* will further damage the existing framework. *"After several decades in a world dominated by the US and in which geopolitical cooperation was the linchpin, we have entered a new era of globalisation that is much more multipolar and volatile"*, added Famke Krumbmüller, EMEIA Leader at EY's Geostrategic Business Group.

The first panel of the Country Risk Conference on February 4, 2025

THE US ALONE AGAINST THE REST OF THE WORLD?

Although the experts are not ruling out the possibility that Trump's strategy could have a positive impact in resolving the two major ongoing conflicts, US threats to introduce tariffs and the prevailing desire to coerce the countries concerned into reaching agreements favourable to the US are likely to cause existing alliances to implode. *"In this context, it is interesting to note that there has been a lot of pushback from southern countries – Brazil, India and Turkey, among others – which are beginning to launch investigations or file complaints with the World Trade Organisation, in particular"*, pointed out Andrew Bishop, Senior Partner and Managing Director of Policy Research at Signum Global Advisors. In his view, the world's largest economic power is playing a risky game *"by forcing countries to decide whether they are with the US or against it"*. The expert added that *"by withdrawing and alienating the whole world, the US is paving the way for other countries [to exercise their leadership], especially China"*. Under these circumstances, a new Cold War seems highly plausible and is one of the scenarios envisaged by the EY Geostrategic Business Group. *"We're talking about a world divided into blocs: one dominated by the US, another by China, and a third by some other power"*, said Famke Krumbmüller. It would then be up to the rest of the world to position themselves in one of these blocs. If a third bloc were to emerge, India would be an ideal candidate to lead it. *"The country is growing strongly and will be able to use its demographic dividend over the next two decades in the face of an ageing China"*, said Thomas Gomart.

Andrew Bishop

OPPORTUNITIES FOR CHINA

In the short term, US-China rivalry is nonetheless likely to remain the main driver of the current geopolitical transformation, as is already the case in the field of generative artificial intelligence. On that score, some experts expect the trade war to escalate between the two powers, which could prompt both sides to impose more substantial tariff increases in a few months' time than is the case at present. The US recently announced a further 10% tariff increase

What are the motives behind America's expansionist ambitions?

Canada, the Panama Canal, Greenland... Since his return to power, Donald Trump has repeatedly vowed to take control of several territories. His statements have systematically caused an uproar throughout the international community, but "*they are very much in line with US strategic culture, which is based on the idea of having access to two ocean fronts and maintaining naval superiority*", explained Thomas Gomart, director of the IFRI.

According to the geopolitical expert, the US President's statements "*herald a shift in the strategic game to the North Atlantic*". The plan is based on the expectation of a future increase in the number of Chinese ships passing through this area. As for the Panama Canal, "*the aim is obviously to control the passage between the two coasts*", added Thomas Gomart. Andrew Bishop also believes that the Trump administration's strategy in this area is "*more defensive than truly imperialistic*". Nevertheless, Trump's attitude raises serious concerns about the potential consequences. "*The fact that the guarantor of the post-1945 international order is now talking like Vladimir Putin, and that its President believes that territory can basically be bought or acquired by various means is extremely problematic in that it could create a copy-cat effect*", warned Thomas Gomart.

"The US and China have not yet come to blows. And neither country is under the illusion that a war against the other would be easy to win."

Andrew Bishop,
Senior Partner and Managing Director of Political Research at Signum Global Advisors

which China responded to by hiking its tariffs by 15%. Faced with such a prospect, China would be unable to accept the status quo. *"Even if it does not admit it, China is dealing with a situation of overcapacity and must now export as a matter of urgency"*, explained Thomas Gomart[1]. If it sees the North American market closing, it will have to find new outlets while strengthening ties with its partners.

One must not forget that strategic understanding of China continues to hinge on a lack of information about the country that is partly controlled by the single party governing it. That said, experts agree on China's current priorities, in particular its massive investments in nuclear energy and naval military capacity which are essential to control trade.

A WEAKENED EUROPE

Caught between these two blocs, the European Union is by all accounts in a considerably weakened position for four reasons. First, because its main driving force, the Franco-German duo, is depleted on both the economic and domestic policy fronts. Second, because according to Famke Krumbmüller, the EU historical modus operandi of *"projecting its power around the world through standards and regulations – wielding soft power – simply no longer works"*. Third, because its policies are sometimes insufficiently coordinated. In this respect, Thomas Gomart pointed out that the diametrically opposed choices made by France and Germany have led to vast differences in thinking between the two neighbours. More dependent on Russian gas than the French who have reinstated the nuclear option, the Germans tend to expect more from a hypothetical post-war Ukraine. Last, Europe is adversely affected by decades of underinvestment in defence at a time when the unity required between member states to address these changes is being undermined by the rise of extreme and Eurosceptic parties in an increasing number of countries in the region.

Famke Krumbmüller

Despite these pitfalls, Europe could respond quickly even in the face of Donald Trump's threat to impose new tariffs. Thomas Gomart believes that *"as trade policy is an exclusive competence of the European Union, we can expect some form of common stance in the event of such a scenario"*. That said, there is no doubt that what would become the second major transatlantic stand-off since the war in Iraq in 2003 could harm US-European relations. To the point of upsetting the geographical balance? *"Ideally, we would need a strong Europe that does not need to attach itself to or rely on a partner, but that is not the case"*, said Andrews Bishop. *"Under Plan B, the EU would have to rely on one of the two partners – either the US or China – but I do not think that Europe would necessarily decide to rely on China if the US were to become an enemy. Therefore, we could end up with a catastrophic Plan C, in which Europe finds itself between the two, in a position of weakness."*

With regard to the possibility of a stronger alliance between the EU and China, Thomas Gomart pointed out that a report by the US National Intelligence Council released in 2021 mentions a possible Sino-European rapprochement on ecological grounds. *"We need to keep this in mind"*, he concluded. It is true that China has invested massively in the energy transition, which puts it at odds with Trump's new agenda.

COMPANIES: RETHINKING STRATEGIES

In this changing and uncertain landscape, companies are finding it difficult to know which strategy to adopt. *"Even if they are gradually beginning to take account of this new, volatile geopolitical situation, I have to say they should* have done it sooner and they are too slow", said Famke Krumbmüller, who calls for a more proactive approach.

"Economic power has become central to the notion of power itself, which explains why governments are taking an increasingly interventionist stance in this area."

Famke Krumbmüller,
EMEIA Leader - EY Geostrategic Business Group

1 - See Junyu Tan's survey in Part 3.

Famke Krumbmüller, Thomas Gomart

"Barring nuclear issues, Sino-Russian relations are becoming increasingly unbalanced in favour of the Chinese. This applies not only to the economy but also to the military."

Thomas Gomart,
Director of the IFRI

Europe and Russia: trade relations show no sign of normalising

Three years after it began, is the Russia-Ukraine conflict about to end? Even before his inauguration, Donald Trump repeatedly declared that he wanted to broker a peace agreement between the two countries as soon as possible. Once the war is over, geopolitical experts are convinced that trade relations between Russia and Europe will be permanently altered. "*Just look at what happened in 2014 and the years that followed: although we were not in the situation of a full-scale invasion of Ukraine, the sanctions against Russia remained in place*", said Famke Krumbmüller. European companies need to be aware that there will be no return to the previous situation.

Some observers even believe that the European Union could end up being the big loser. "*Donald Trump's stated goal is to make Russia a "friend" of the US and, in doing so, distance it from China. Further out, he plans to establish a direct link between Washington and Moscow, and bypass Europe*," warned Andrew Bishop.

2 - *https://www.dni.gov/index.php/gt2040-home*

PART 2

From geopolitical fracturing to economic and financial fragmentation

The rise of geostrategic rivalries is affecting a world economy that has also become increasingly fragmented.

Has the growing commercial and financial integration of the last thirty years come to an end?

Should we resign ourselves to a form of regionalisation of trade and a reorientation of flows (goods, capital, etc.)?

Experts and practitioners compare notes in the financial, manufacturing and logistics sectors.

From geopolitical fracturing to economic and financial fragmentation

Amid a global environment made particularly unstable over the last two years by the Russian invasion of Ukraine, the Hamas attack on Israel and escalating tensions between China and Taiwan (see box), Donald Trump's return to the White House on 20 January 2025 has not taken long to fracture the current geopolitical framework a little more. The Coface Risk Conference brought together key players in the economic world to assess the impact of these developments on trade, finance and global logistics. Their contributions show that while globalisation has in fact been weakened, a generalised contraction is not under way and complex recomposition dynamics are at work.

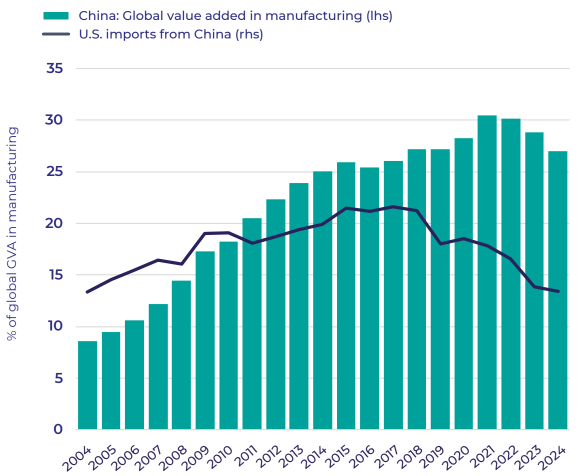
The second panel of the Country Risk Conference on February 4, 2025

A NEW ERA OF GLOBALISATION

Amplified by the initial decisions of the Trump administration, the current geopolitical fracturing movement is undeniably weighing on activity and the configuration of world trade. *"However, in the light of the trade data available to us, we cannot talk of deglobalisation"*, insisted Agatha Kratz, Partner at Rhodium Group, and a view shared by Ramon Fernandez, CFO of CMA CGM, the world's third-largest shipping group. Despite the vast geopolitical and electoral uncertainty that dominated 2024 and the disruptions experienced in certain strategic transit zones[1], trade flows have done better than resist, contrary to forecasts. *"While 85% of world trade passes through oceans, we at CMA CGM have never transported so much cargo since Trump's first term in office, and volumes are continuing to grow,"* pointed out Ramon Fernandez. In 2024, international trade in goods will have grown (by around 6%) twice as fast as world growth (by around 3%), after stagnating in 2023, mainly on back of destocking practices implemented by companies.

In this respect, Agatha Kratz pointed out that "*China's weight in international trade continues to grow*", which is reflected in *"Europe's greater dependence on Chinese imports than five years ago"*. Second, the expert has observed a double fracturing on the economic front. The most visible is the "disintegration" that is gradually taking place between the US and China in terms of investment and trade, which is illustrated, for example, by the significant drop in the share of US imports from China. The figures presented in the graph below confirm that the decline in Chinese exports to the US contrasts with the stability in China's share of world production.

China's share of world manufacturing output and US imports
(%, 2004-2014)



Note: production measured as a share of gross value added
Source: US Census Bureau, World Bank, Macrobond, Coface

Ramon Fernandez and Agatha Kratz

> "Over the last five years, Europe has become more dependent on the Chinese economy."
>
> **Agatha Kratz,**
> Partner, Rhodium Group

In addition to Sino-American tensions, China is withdrawing from the rest of the world. As Agatha Kratz pointed out, the world's second-largest economy is prepared to "*shed its dependence on the outside world*", and is therefore "importing much less". In the financial sector, however, the current geopolitical fracturing is not causing any fragmentation, at least not yet. *"Major companies and financial institutions are continuing to invest and finance themselves all over the world"*, confirmed Anne-Christine Champion, Co-Head of Global Banking and Investor Solutions at Societe Generale.

TRADE WAR: WHAT ARE THE CONSEQUENCES?

Even though the Trump administration took a (temporary?) step backwards with regard to Mexico and Canada a few hours before the Coface Country Risk Conference, the US' decision to impose new customs duties on its main trading partners – starting with China – marked the start of a new trade war, seven years after the one launched by... Donald Trump. Agatha Kratz warned that *"overall, the global economy will lose out. However, a few countries could also benefit, as they did a few years ago."* Hitherto perceived as *"assembly countries"*, a number of so-called "connector" countries such as Mexico and Vietnam have seen their value chains move upmarket and complexity. *"The rest of the ASEAN group (Association of Southeast Asian Nations) has also been favourably impacted"*, added Agatha Kratz. Ramon Fernandez agreed with this observation, noting that *"Asia remains a phenomenal trading area"* and pointing to a massive acceleration in Chinese exports to the economies of South-East Asia and Mexico. *"These countries, in turn, are also exporting more to the US."* Among the advanced economies, the US has bucked the trend, *"having done very well in the field of green products, such as electric batteries and solar panels, in keeping with the Biden administration's priorities"*, added Agatha Kratz.

In addition to the consequences for inflation, world trade growth and the reorganisation of certain supply chains, the US offensive against China in particular could also have knock-on effects. Faced with sluggish domestic consumption, China will have no choice but to find new outlets for its exports, which will not be channelled to the US owing to higher tariffs. Against this backdrop, experts expect some of these goods to be redirected to ASEAN countries, countries of the Global South and the European Union. The prospect is likely to sour relations between the Old Continent and China. Agatha Kratz warned that "*in order to prevent this surge in exports from destroying European industry even further, the Commission will probably be forced to introduce trade protection measures*". But some manufacturers are not shying away from this threat. *"In our kitchen equipment sector, Chinese products already have a strong presence in Europe, so the risk of an influx of imports from China should be put into perspective"*, said Thierry de La Tour d'Artaise, Chairman of Groupe SEB, who believes that innovation is the best salvation measure for companies in advanced economies.

The Taiwanese disaster scenario

An essential cog in the wheel of world trade, Taiwan is a vital link in the global electronics value chain. While the threat of a Chinese invasion has grown stronger over the months, it would be *"potentially the most disruptive event in years to come"*, warned Agatha Kratz. The Rhodium Group consultancy firm estimates that the cost of such a scenario to the global economy could reach or even exceed 3,000 billion dollars[2].

Without going as far as erupting into open conflict between China and Taiwan, which would aggravate Sino-American relations, the offensive led by the world's second-largest economy could take other forms, such as cyber attacks and the rupturing of undersea cables, warned Agatha Kratz. *"Less intense than an invasion, such acts could have extremely large-scale effects on trade, investment and global confidence"*, she concluded.

Anne-Christine Champion and Ramon Fernandez

> "We've never transported so much freight."
>
> **Ramon Fernandez,**
> Group Chief Financial Officer,
> CMA CGM

Anne-Christine Champion

> "The dollar remains an unrivalled currency."
>
> **Anne-Christine Champion,**
> Co-Head of Global Banking
> and Investor Solutions,
> Societe Generale

1 - For example, following the attacks by the Houthis in the Red Sea, the Suez Canal, which handles 30% of the world's container traffic, has been less accessible and more dangerous over the past few months.

2 - Part of a study conducted in 2023 with the Atlantic Council:
https://www.atlanticcouncil.org/in-depth-research-reports/report/sanctioning-china-in-a-taiwan-crisis-scenarios-and-risks/

Thierry de la Tour d'Artaise

> "In our markets, China is already dominant, particularly through distributors brands that supply products made in China."
>
> **Thierry de La Tour d'Artaise,** Chairman, Groupe SEB

CONTRASTING TRENDS ON THE REGULATORY FRONT

The European Union already confronted the phenomenon of regulatory decoupling with the UK following Brexit. It is now running a similar threat vis-à-vis the US. The risk applies first and foremost to the financial sector, where Donald Trump has vowed large-scale deregulation. *"This poses a problem for European banks and, more broadly, for the European economy insofar as European companies obtain 70% of their financing from the banking market, while their US counterparts obtain 80% from the bond markets,"* pointed out Anne-Christine Champion. This looming competitive disadvantage appears all the more problematic given that European economic players are already subject to restrictions that are not imposed on their competitors, for example in environmental matters. *"In Europe, we have the 'ETS'*[3] *and multiple regulations that take various forms. Even though these are part of a virtuous approach, we are competing with a world where these rules do not exist"*, pointed out Ramon Fernandez. Thierry de La Tour d'Artaise calls on the European and French authorities to reason. *"I'm less afraid of AI (artificial intelligence) than of a CI (Chinese invasion) or of NI (normative inflation). And we in Europe are going to die of normative inflation."*

The need to deal with international sanctions

In addition to the lack of visibility on the geopolitical front, companies with international operations and/or export activities also have to deal with the compliance rules in force, which are becoming increasingly numerous and complex to monitor. *"These include a number of international economic sanction regimes, the spectrum of which has increased significantly since the start of the Russia-Ukraine conflict in February 2022. There are currently 37 such sanctions in force in the European Union, targeting more than 5,000 entities and individuals,»* explained Anne Christine Champion. *"In the US, more than 280,000 people are affected."*

For companies that work with a large number of foreign business partners, monitoring these lists is all the more problematic owing to the constantly changing content. In this context, *"the risk of being sanctioned for non-compliance with these measures is greater"*, warned Anne Christine Champion. The banker cited the recent case of a client in the infrastructure sector whose project was financed to the tune of several billion euros. *"Just as the funds were ready to be drawn by the company, the US placed one of its small Chinese subcontractors under sanctions overnight, forcing all the teams to adapt quickly."*

3 - Greenhouse gas emission allowance trading

PART 3

Globalisation through the lens of Coface economic research

Between political sanctions, economic withdrawal and a disruption of shipping lanes, the major geopolitical blocs are trading less with one another and more within themselves. However, they are continuing to trade, particularly *via* third-party countries.

The European Union has set itself the goal of significantly and rapidly increasing the number of electric vehicles sold in the region – a product for which Chinese manufacturers boast a unique position of strength.

China's industrial apparatus has the capacity to produce more than it currently does in all sectors. In the short term, there is no miracle solution to redress this imbalance, which is a source of geopolitical tension.

Despite growing tensions in the electronics sector, for the time being the US and China remain highly interdependent for most of the sector's products.

By Eve Barré,
Sector Economist

By Marcos Carias,
North America
Economist

Read more **here**

A less global village

World trade in the age of geopolitical fragmentation

In October 2024, Eve Barré and Marcos Carias published a global analysis of developments in world trade. From Ukraine to the Middle East, the resurgence of geopolitical tensions is helping to redraw the map of global trade. There is a clear trend towards trading more with allies and less with rival countries, while the geography of maritime trade is being transformed. However, globalisation is being reorganised rather than dismantled. Connectors provide a buffer between rival great powers. The complementarity of the American and Chinese economies (world champions of consumption and production, respectively) will make decoupling very difficult in the medium term.

Some of the things you will learn

- Since 2022, trade between geopolitical blocs has contracted markedly faster than trade within these blocs.
- Tensions in the Red Sea have more than halved traffic through the Suez Canal.
- Vietnam and Mexico have risen in prominence as trading partners for both the US and China, suggesting they are functioning as trade intermediaries.
- The United States accounts for 29% of global consumption, but only 13% of the production value of tradable goods. China mirrors this, producing 27% of tradable goods and only 13% of global consumption.

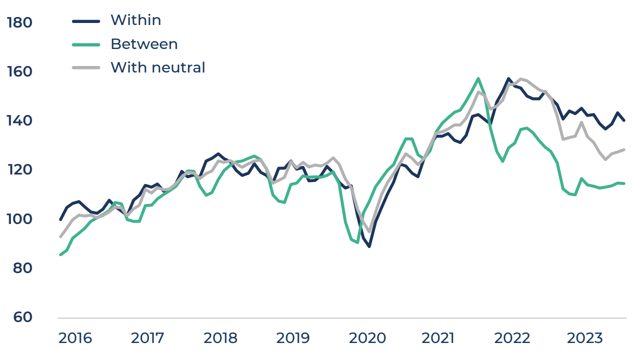
With the re-election of Donald Trump, the system of international trade built over the post-war era has some powerful blows coming its way. Though the size, coverage and timing of incoming tariffs is not fully defined, the President had not waited to take office to threaten 25% blanket tariffs on Mexico and Canada should they fail to do enough to curb migrant and drug flows to the US. **Historically, the US has been the chief sponsor of trade liberalization and is the largest end-market in the world, accounting for roughly a third of global consumption.** Its views on trade matters greatly for the future of global trade. Is globalization about to enter a period of decline?

The backlash against globalization did not begin in November 2024. Arguably, it has been manifesting since the start of the 21st century, with the failure of the WTO Doha round. Brexit showed that even in the ever-expanding European project, integration was not irreversible. The trade war launched under the first Trump administration marked the first ramp-up of tariffs among major economies in the post-war era. The pandemic and the war in Ukraine showed the risks of relying on distant countries for key stages of the production process (be that distance geographical or geopolitical). The conflict in the Middle East has highlighted the potential impact of geopolitics on the logistics of global trade. **And yet, though trade as a share of global GDP has been stagnant since the 2008 financial crisis, it has not quite gone into reverse.**

However, this apparent stability masks the profound changes that are taking place. **Chart 1** plots aggregate trade flows within and between groups of countries that gravitate noticeably towards or away from the Western sphere of influence. If we consider, on one side, a bloc of Western-aligned countries - including most NATO countries and economies such as Australia or the Republic of Korea - and on the other, countries that voted "against" or abstained in response to the first UN motion to condemn Russia's invasion of Ukraine we begin to see a pattern consistent with geopolitical fragmentation. At the core of this trend is **the unraveling of the trade partnership between western countries on one side, and China and Russia on the other.**

However, there is evidence that some of the previous trade between the EU and Russia survives, intermediated through third countries. Since early 2022, several former Soviet republics have experienced a marked increase in demand for goods from the EU, driven by trade in machinery and transport equipment. Similarly, when looking closely at US-China trade, the decoupling narrative gets more nuanced. **Indeed, some of the countries that have gained ground as suppliers for the US are growing as destinations for Chinese exports (Charts 2 and 3)**.

Chart 1 - Global trade value according to geopolitical blocs
(exports and imports, January 2017 = 100)



Source: Trademap, Coface

Chart 2 - Share of US Imports
Percent lost/won since 2017

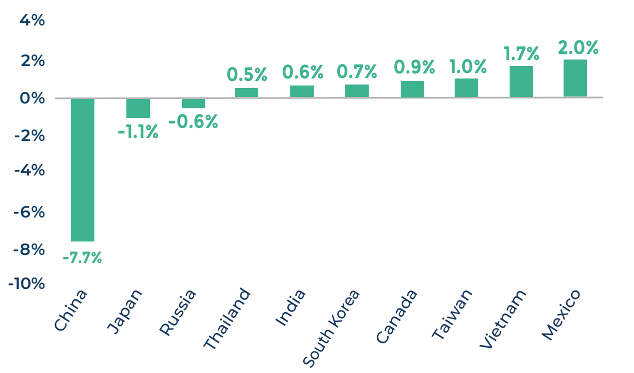
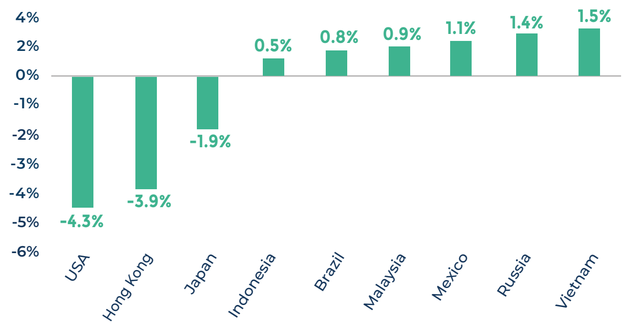


Chart 3 - Share of China Exports
Percent lost/won since 2017



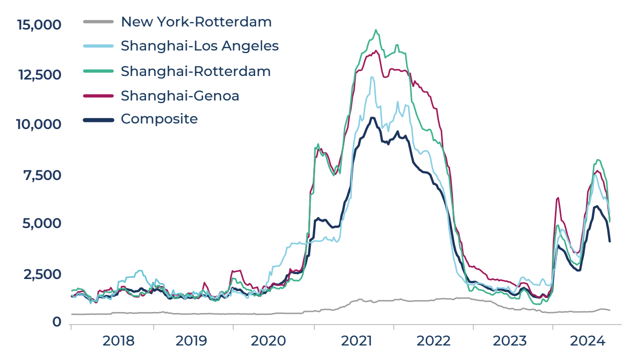
Source: CCS, Macrobond, Coface

The presence of Mexico and Vietnam at the right end of both these charts is worthy of attention. For Vietnam, this role of intermediate step in supply chains linking the US and China is not new, but it appears to have been turbo-charged since the start of the trade war. Similar attributes make Vietnam and Mexico ideal candidates for friendshoring: access to US market, growing manufacturing base and transport infrastructure, competitive cost structure... In sum, when large and strongly integrated economies antagonize and enact measures to decouple trade, the relationship can survive (at least partially), intermediated by third countries that trade with both parties. **Rather than be severed, the supply chain grows an additional link.**

At the same time, geopolitical trade barriers are transforming the physical way in which we trade globally. For instance, the EU's imports bans on Russian crude oil (December 2022) and petroleum products (February 2023) have **markedly boosted cargo traffic along the Northern Sea Route (NSR)**. Prior to these sanctions, the EU was a major export market for Russia, accounting for 46% of its crude oil exports in 2021. In response to the bans, Russia has redirected much of its oil exports to alternative markets, particularly China. These shifting trade patterns gave a boost to the NSR usage, which runs along Russia's Arctic coastline from the Kara Gate Strait to the Bering Strait, as it offers a shorter shipping route between Northern Europe and Asia compared to the traditional Suez Canal passage.

In their more extreme form, war, geopolitical tensions can trade' security. The recent example of attacks on commercial vessels from the Red Sea to the Arabian Sea by Houthi rebels, in solidarity with Hamas, is striking.. This has forced carriers to avoid to transit the Suez Canal, which traditionally handles 12% of global trade and 30% of container traffic. The number of ships going through the chokepoint plummeted by more 60% in the last quarter of 2024 compared to the same period in 2022. Instead, carriers opted for the Cape of Good Hope. In 2024, the Drewry World Container Index, which measures weekly ocean freight rates for 40-foot containers across seven major maritime lanes, was 2.4 times higher than the preceding year (**Chart 4).**

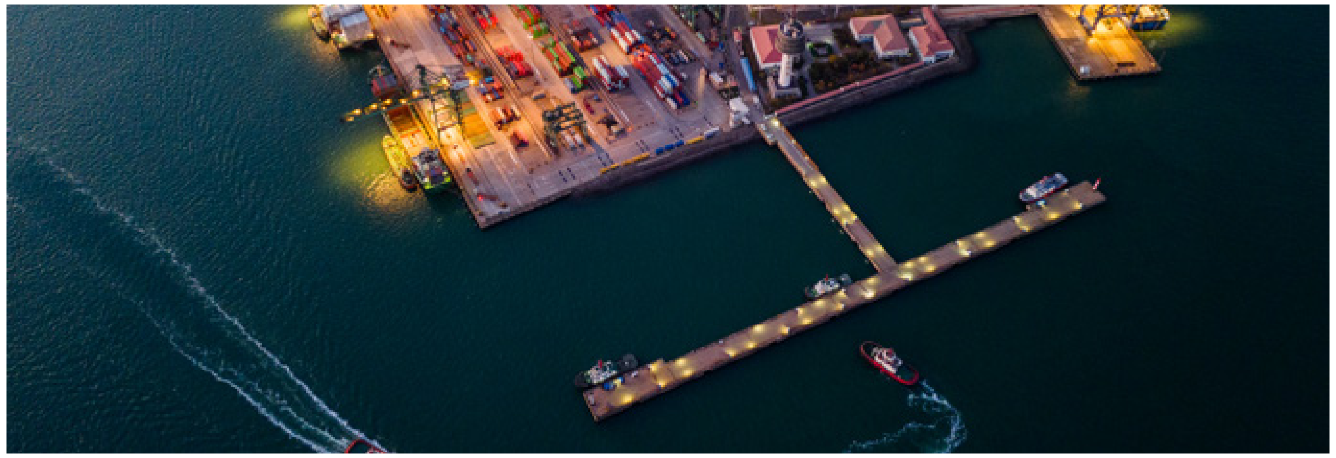
Chart 4 - Drewy World Container Index
(USD per 40 ft container)



Source: Drewry Shipping Consultants Ldt, Macrobond, Coface

But, despite higher sea fret rates, volume reached record-high levels in 2024. Meanwhile, **rail trade, which typically plays a secondary role, has stepped up** and acted as a valuable release valve. The expansion of international rail trade has been facilitated by the development of several cross-border railway connections over the past decades, primarily driven by China's Belt and Road Initiative.

The resilience and adaptability of international trade stand out in light of the increasing frequency and intensity of geopolitical shocks. Despite these disruptions, global trade continues at significant levels, a testament to the emergence of connector countries and the agility of global merchandise transport systems. **This suggests that the integrated global economy remains too profitable for market participants to permit a disorderly breakdown, even as international relations strain.**



By Simon Lacoume,
Sector Economist

Read more **here**

Electric vehicles

Competition between China and Europe in an age of mobility transition

In October 2024, Simon Lacoume, Coface economist and automotive specialist, analysed China's penetration of the European electric vehicle market with the help of Lucile Bembaron, Christiane von Berg and Grzegorz Sielewicz. Their focus highlights the fact that it will be difficult for European industry alone to meet the target of zero sales of internal combustion engine vehicles in the European Union by 2035. China is making its mark in this sector, thanks to the high level of vertical integration of its manufacturers and generous support from the public authorities. It is so far advanced that the EU's tariffs are unlikely to be enough - unless they are substantially increased. In addition, Chinese carmakers, driven by the sluggishness of the domestic market, are renewing their strategies for penetrating Europe, notably through direct investment and the establishment of assembly plants.

Some of the things you will learn

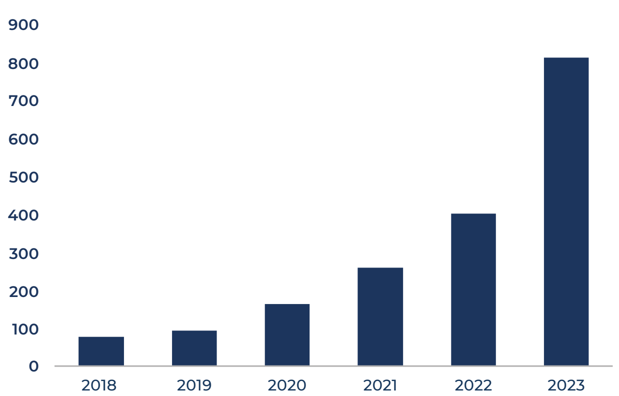
- In 2024, Volkswagen and Stellantis account for 40% of new registrations in the European market.
- In 2024, global sales of electric vehicles surged by 25%.
- Beijing targets domestic production of 16 million electric vehicles.
- If the price of Chinese electric vehicles were to become unattractive in the European market, tariffs of the order of 50% would be necessary.

In June 2022, the European Parliament voted to ban the sale of new internal combustion engine (ICE) vehicles within the European Union (EU) from 2035. The objective is to achieve carbon neutrality by 2050 by drastically reducing emissions across several sectors, including transport. The latter contributes 60% of the greenhouse gas (GHG) emissions in Europe. This deadline poses significant risks to the automotive industry on the Old Continent, particularly to European car manufacturers.

On the one hand, **the European automotive market is still predominantly dominated by internal combustion engine (ICE) vehicles, which account for about half of sales in 2024**. In addition, hybrid (HEV) and plug-in hybrid vehicles (PHEV), which have experienced significant sales growth in Europe, represent 38% of sales in 2024. Only battery electric vehicles (BEVs) will be allowed for sale starting in 2035, but currently, more than 85% of car sales do not comply with this regulation. Furthermore, BEVs ranked only third (by powertrain) with 13.5% of total sales in the past year. **Achieving the EU's goal of 100% BEV sales would require an annual growth rate of 14% for BEV sales starting from this year—well above the -5% achieved in 2024 compared to the previous year.**

On the other hand, several Chinese automotive companies—both manufacturers and suppliers—have acquired considerable expertise, particularly technological, in the electric vehicle (EV) segment. Widely supported by Beijing[1] **(chart 1)**, Chinese battery and electric vehicle manufacturers have developed a robust value chain since the 2000s, spanning from the mining sector (upstream) to the final manufacturing of EVs (downstream). China is a major global player in the extraction and supply of essential raw materials, owning numerous mining assets abroad and producing, for example, around 60% of the world's refined lithium supply.

Chart 1 - Chinese subsidies to CATL *(USD, millions)*



Sources: Center for Strategic and International studies (CSIS), Coface

The establishment of an extensive vertical value chain—integrating extraction, refining, and manufacturing—along with financial backing of the Chinese central government, has allowed the rise of a leading Chinese electric vehicle sector. Chinese manufacturers have developed a wide range of products, improved production capacities, and invested heavily in research and development. In response to intense domestic competition and a price war within the Chinese market, manufacturers have progressively lowered their production costs, and consequently, their selling prices. **EVs sold in China are therefore two to three times cheaper than those sold in export markets.**

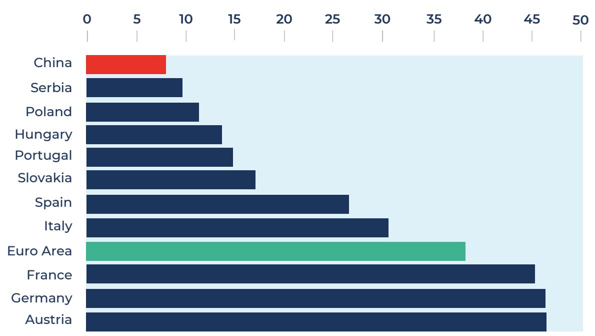
From a European perspective, there is an evident risk of domestic manufacturers being outpaced by Chinese competitors, who

1 - The Chinese government has actively supported the mining sector through policies such as the 'Made in China 2025' initiative, which includes significant funding for mining technologies and materials processing.

are better positioned to meet the 2035 deadline. This challenge is being addressed by the European Commission, which is implementing tariff surcharges to narrow the price gap.

If Europe wants to maintain a leading automotive industry on its soil, it must establish sufficiently competitive electric vehicle production capabilities to rival Chinese competitors. However, **the main issue lies in the substantial difference in production costs between Europe and China (chart 2)**. The introduction of tariff surcharges aims to reduce the gap between the EU and China. These new trade barriers, which could be strengthened over time, appear to be part of a **"reverse offshoring"** industrial strategy. This strategy was adopted by the United States in the 1980s in response to fierce competition from Japanese manufacturers. By combining import quotas with a monetary system rebalancing in favor of the U.S. dollar, Washington encouraged Japanese manufacturers to establish factories on U.S. soil to access the American market. Thus, ten years after the signing of the Plaza Accords[2], Japanese vehicle imports to the U.S. had decreased by 55%, replaced by Japanese car production based in the U.S. **(chart 3).**

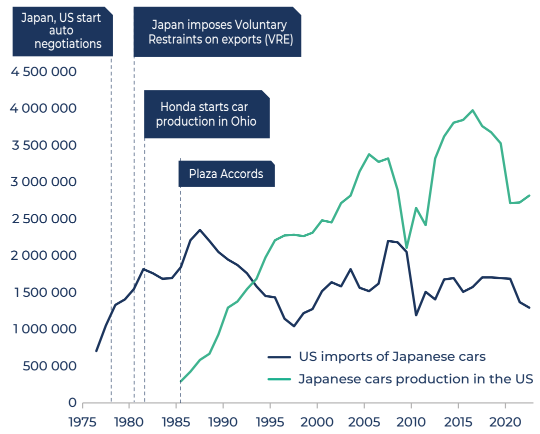
Chart 2 - Hourly Labor costs in industry in 2023 *(in EUR)*



Source: European Automobile Manufacturers' Association (ACEA), Macrobond, Coface

Theoretically, this model could appeal to European policymakers. However, European negotiating margins currently appear quite limited. In the U.S.-Japan case, Washington had a position of strength over Tokyo since 1945. Furthermore, in 1980, the American market accounted for 45% of Japan's total car exports. Moreover, the tariffs imposed by the EU do not close the price gap between European and Chinese EVs. For example, the Chinese firm BYD shows price differences of around 80% to 100% between its models sold in China and those sold in Europe. **To truly bridge the price gap between the Chinese and European markets, surcharges in the range of 45% to 55% would be required.**

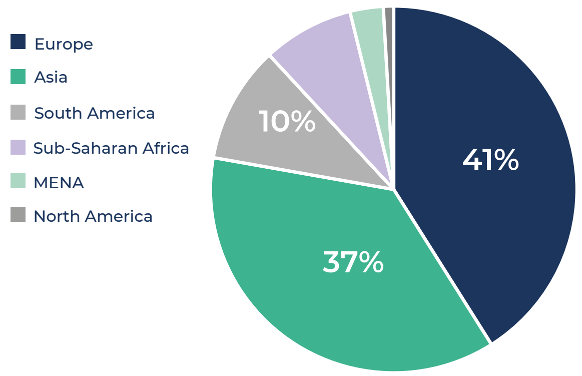
Chart 3 - Timeline of Japan-US passengers car trade *(by millions of vehicles)*



Source: Japanese Automotive Manufacturers Association, Coface

The European market will remain a significant target for Chinese car manufacturers in the medium term, who are seeking alternatives due to the slowdown in the domestic market and are increasing their investments in different regions of the world **(chart 4)**. To limit customs measures against them, Chinese manufacturers could opt for a hybrid solution. This would involve **assembling vehicles from kits produced in China**[3]. This is the case with the partnership between Stellantis and the Chinese company Leapmotor, which will assemble its T03 electric model in Poland.

Chart 4 - China investment by region in auto industry in 2023



Sources: Trademaps, Coface

2- On September 22, 1985, finance ministers from the US, Japan, Germany, France and the UK agreed to coordinate efforts to depreciate the US dollar.
3- CKD (Complete Knock Down) ou SKD (Semi Knock Down).

By Junyu Tan,
North Asia
Economist

*Read more **here***

Made in China

How China can deal with its industrial overcapacity

On 7 November, Junyu Tan, economist for North Asia at Coface, published an analysis of industrial overcapacity in China. The focus explains that China has the capacity to produce more than it does, that this is not new, but that this time it applies to a wide range of sectors. Each solution to this imbalance has its drawbacks: boosting domestic markets, but Chinese consumers lack confidence; improving quality, but it is already high; exporting, but tariffs are increasing... and not only in the US. These difficulties call for greater Chinese investment worldwide.

Some of the things you will learn

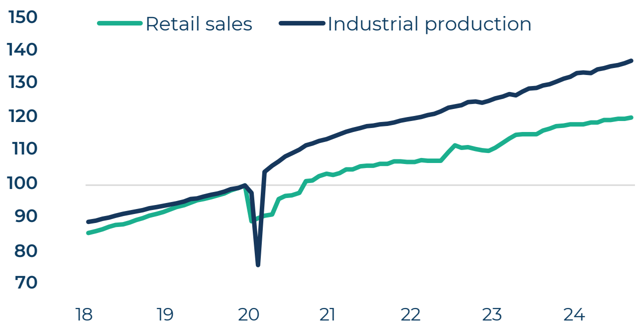
- China's idle production capacity in new energy vehicles and lithium batteries is enough to double current exports.
- One thousand barriers of local protectionism within China were removed in 2023.
- Emerging markets with close trade ties to China are also considering raising trade barriers against China: Thailand, South Korea, Indonesia...
- Saudi Arabia is the second largest destination for Chinese investment.

China has long accustomed to an investment-driven growth model, which is central to its stellar economic growth over the past three decades. But it also makes the economy susceptible to supply-demand imbalances, leading to recurring episodes of industrial overcapacity. These can be traced back to the 1990s, when accelerated market reforms led to a glut of labor-intensive manufactured goods. A more recent episode occurred in 2014-2016, when the massive investment-led stimulus that followed the global financial crisis triggered an oversupply of construction materials.

While this playbook is not new, the imbalances have become evident again since the COVID-19 outbreak (Chart 1), largely due to a production-driven stimulus approach aimed at reducing social interaction. Meanwhile, to pick up the slack from the shrinking housing market, the government has also proactively cultivated new growth drivers such as advanced manufacturing and green technology through state support.

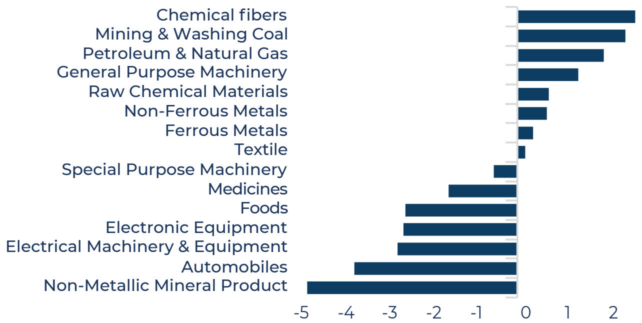
While the situation is not yet as severe as in 2016, overcapacity is prevalent in more sectors and faces more global pushbacks this time. It is no longer confined to specific sectors (labor-intensive consumer goods such as such as textile and home appliances in late 1990s, and construction materials such as steel and aluminum in the 2010s). **This time, it has spread across traditional and emerging sectors.** We see idle capacity most evident in consumer goods (food, medicine), construction non-metallic minerals (cement, glass), and machinery and transportation equipment (automobiles) **(Chart 2)**. Our estimates show there is enough excess capacity in China to potentially double the exports of new energy vehicles and lithium batteries **(Chart 3)**. But amid the global race of green transition, China's production surplus in clean technology products has also made this round of overcapacity a focal topic globally and triggered more retaliations from trading **partners.**

Chart 1 - China: Economic activities recovery
Index, Dec 2019 = 100, seasonally adjusted



Source: China NBS, Coface

Chart 2 - Changes in capacity utilization rate
3Q-24 minus historical average, trailing 4Q



Source: China NBS, Coface

The most obvious solution to absorb excess production capacity is to expand domestic demand. Amid the ongoing supply-demand imbalance, recent policy focuses have shifted more towards subsidizing goods and facility consumption rather than construction. Meanwhile, efforts to stabilize the housing market have been made to curb the drag on household wealth given the substantial role of real estate in household assets. The ongoing buyback program for social housing supply is also the right move to disincentive the "saving for housing" motive, while access to affordable public housing can reduce rental burdens to unleash more spending power. **But with consumer confidence near historic lows, the economy cannot just rely on demand-side recovery and endure chronic overcapacity.** Because this will amplify deflationary pressures, affect corporate profits and hinder business expansion.

Government measures have also been taken to regulate capacity expansion through industrial upgrading. To this end, higher quality requirements have been imposed on the production of lithium-ion batteries, solar energy and cement clinker. These measures should help facilitate the orderly exit of excess capacity but are unlikely to be replicated across a wide range of industries. This is because **doing so will harm short-term economic growth and would also be less technically feasible for advanced technology products with already high standards.**

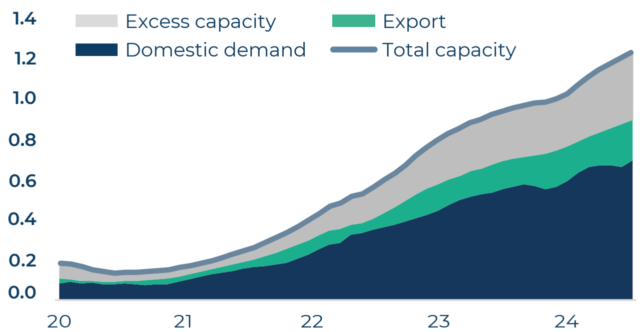
Historically, the shortfall in domestic demand has been compensated by external demand through exports. But now, Chinese exporters must navigate a more complex global trade environment as free trade is longer the hype it used to be. Trade barriers are already rising as developed economies aim to reduce their dependence on Chinese goods, likely even more so during a second Trump presidency. Against this backdrop, China's Belt and Road Initiative (BRI), a central component of Xi's "Major Country Diplomacy", can be instrumental in securing market access to the emerging world. But **trade barriers erected by emerging economies have not abated either, as policymakers face pressure to protect domestic jobs and manufacturers.**

The increased trade frictions may in turn facilitate more outbound investment by China to bypass such barriers. In our view, this is the most feasible solution because overseas production bolsters intermediate goods exports but avoids trade frictions by bringing in jobs and technologies. **Overtime, the industrialization in host countries could generate demand to absorb the excess capacity while helping to build new trade blocks for China with potentially less trade barriers.**

Some actions in this direction are already underway. Balance of payments statistics show that China has experienced a persistent outflow of direct investment since the second half of 2022, signaling a shift in China's role from a net importer of capital to an exporter. ASEAN[1] remains the main destination for Chinese investment in 2022-2023, while Hungary is the main beneficiary in Europe, receiving 4.5% of Chinese FDI **(Chart 4)**. Nevertheless, Chinese investment is coming under increasing scrutiny from governments in developed countries, not least for reasons of national security. In Europe, although scrutiny has intensified, some countries such as Hungary, Poland and Italy continue to welcome such investment, particularly in the electric vehicle sector.

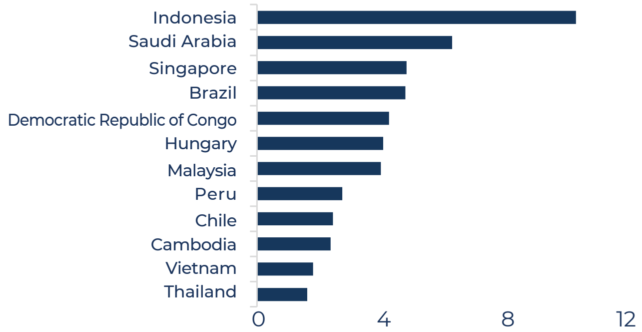
Domestically, there may be greater pressure to make up for job losses from increased outbound investment. This is especially true at a time of rising youth unemployment and weaker economic growth. To address this, the Chinese government has been working to further open up service industries (Internet, education, culture, telecommunications, health care), which tend to employ more workers and create more jobs. But there are uncertainties about its effectiveness, as investors still need to be assured of a more transparent and stable policy environment.

Chart 3 - New energy vehicles *(Million unit, 12m rolling average)*



Source: GAC, Coface

Chart 4 - Chinese outbound FDI *(USD bn, 2022-2023)*



Source: The American Enterprise Institute, Coface

1 - The Association of Southeast Asian Nations is made of Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam.

Read more **here**

By Aurélien Duthoit,
Senior Sector
Economist

Tech War

US-China rivalry for electronics out to 2035

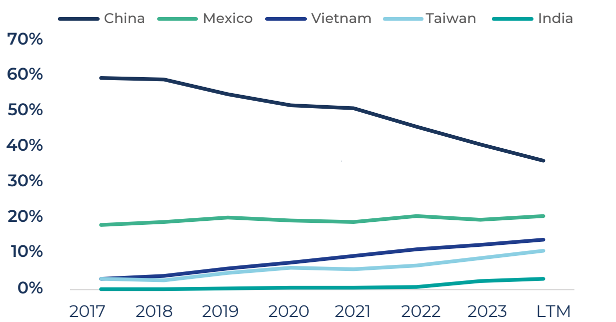
On 19 November 2024, Aurélien Duthoit, Coface's senior economist specialised in information and communication technologies, published an analysis of the Sino-American rivalry in the electronics sector. The focus notes that China has lost a lot since the United States introduced import restrictions in 2017. However, the volume of trade between the two countries remains significant. What's more, US companies command more than half of the sector's global profits, while heavily relying on China for manufacturing. At a global level, the future of the sector depends as much on future technological breakthroughs as on geopolitical tensions. In one scenario, two parallel economic systems would compete head-on.

Some of the things you will learn

- Between 2017 and 2024, China's market share in US electronic device imports fell from 59% to 36%, costing China nearly USD 150 billion in lost exports.
- Despite growing restrictions on US technology exports to China, close to 30% of US semiconductor manufacturing machinery exports still go to the latter.
- US companies have captured 54% of the profits generated by the global electronics industry over the past decade vs. a mere 7% for their Chinese competitors.
- Until the 1990s, Japan controlled half the semiconductor markets, but the development of personal computers and later smartphones completely reshuffled the cards.

The US-China tech war has intensified dramatically since 2017, employing a full spectrum of measures from tariffs and export controls to restrictions on market access in a race for technological dominance that is reshaping the global electronics landscape. **While our calculations indicate a substantial shift in US imports away from China that has cost the latter close to USD150 billion in lost exports since 2017 (Chart 1), they also suggest that underlying, mutual interdependence remains deeply rooted in the very structure of the industry:** 29% of US semiconductor manufacturing machinery exports flow to China, and US electronics imports from Mexico, Taiwan and Vietnam incorporate a great deal of Chinese value-added.

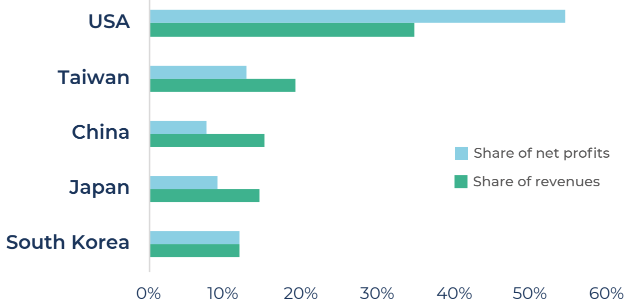
Chart 1 - US imports of electronic devices by country of origin *(in %)*



Sources: USITC, Coface

If the ties connecting the US and Chinese electronics industries have proven more resilient than what headline bilateral trade figures might suggest, it is largely because **the US administration's long-term drive to cut ties with China contradicts the short-term interests of corporate America and the world's most dominant electronics companies.** We estimate that over the last decade US companies alone accounted for 54% of global electronics profits, a share that balloons to 88% when including their Japanese, South Korean, and Taiwanese peers **(Chart 2)**. Meanwhile, despite surging sales and remarkable technological progress, Chinese companies only secured 7% of global industry profits and are still lagging far behind leaders in the all-strategic semiconductor segment **(Chart 3)**. A major supplier of critical inputs, an unmatched manufacturing hub and one of the world's largest consumer markets for electronics, China resembles more a condition for, rather than a threat to, the profitability of dominant US electronics companies.

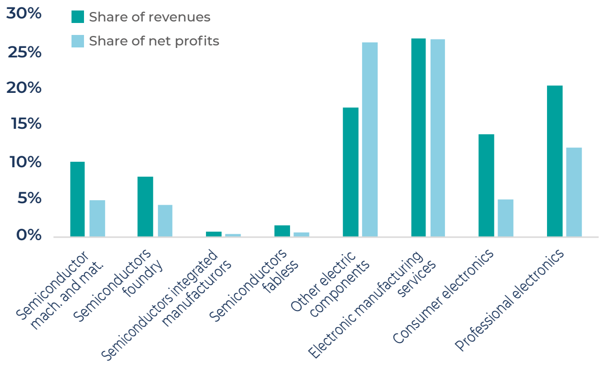
Chart 2 - Share of listed electronics companies in sales and profits by headquarter location in 2014-2023 *(in %)*



Sources: LSEG Eikon, Coface

However, the assumption that current patterns are going to continue during the coming years is at complete odds with the **deep resolve of the US and China to maintain or acquire technological leadership and reduce dependencies**, often by using trade as a weapon. Such a belief also discounts the **possibility of a major industry shake-up** triggered by radical innovation – a feature of the electronics industry. Home to more than 50% of global semiconductor production in the 1980s, Japan's dominance was undermined by the rise of personal computing and the US's strategic interventions to limit Japanese exports. Similarly, the smartphone revolution in the 2000s reshaped the industry, displacing leaders like Nokia and Motorola while elevating new players like Apple, Samsung, and TSMC. These shifts highlight the potential for unforeseen disruptions to redefine competitive dynamics and geographic leadership.

Chart 3 - Share of listed Chinese companies in global sales and profits by segment, 2014-2023 average *(in %)*



Sources: LSEG Eikon, Coface

To explore how an acceleration in US-China rivalry and potential disruptive innovation might transform the industry value chain, we have identified the four scenarios: presented in **Chart 4**.

Chart 4 - Changes in the innovation and trade environment and their possible outcomes over the next decade

Source: Coface

Depending on the scenario, the countries dominating the electronics industry will need to employ a mix of coping, adaptation and transformative strategies to keep their competitive edge in the intensifying tech race. Governments, particularly in the US and allied countries, are adopting strategic measures to bolster domestic capabilities, tie technology and trade alliances and reduce reliance on China. The US CHIPS and Science Act, which allocates USD 52 billion to semiconductor manufacturing and research, exemplifies such efforts. At the same time, China has accelerated its push for technological self-sufficiency, as evidenced by its doubling of semiconductor manufacturing machinery imports since 2017. **These investments reflect both countries' recognition of the strategic importance of electronics to national security and economic leadership**. Emerging manufacturing hubs such as Vietnam and Mexico are well-positioned to benefit from trade fragmentation. For Europe, the challenges are particularly acute. The region lacks the centralized strategic momentum of the US and China and has yet to specialize in any specific part of the value chain. To maintain competitiveness, Europe must strengthen its innovation ecosystems, invest in strategic capabilities, and deepen cooperation with allied countries.

To assess the vulnerability to shocks of the various segments making up the electronics industry, we have developed a comprehensive risk scorecard measuring growth, innovation, profitability, capital intensity, leverage, etc. over a five-year period that captures a complete business cycle (2018-2023). Our analysis reveals that **upstream segments like semiconductors and components were found to be structurally less vulnerable.** These segments benefit from high profit margins, driven by value-added products and oligopolistic markets. However, their weaknesses include high capital intensity, which increases fixed costs, and long cash cycles, resulting from complex supply chains. Conversely, **consumer and professional electronics segments scored higher in risk due** to their exposure to competitive pressures, mature markets, and dependency on semiconductor companies with significant market power. These segments face moderate growth and are particularly impacted by competition from Chinese firms.

In this increasingly polarised landscape, electronics companies will have to navigate **heightened risks of supply chain disruptions, foreign market access restrictions, geopolitical compliance pressures, standards divergence and investment constraints**, all of which will play a part in exacerbating volatility in an already cyclical industry and adding a significant cost burden. Companies would be well-advised to pursue proactive supply chain diversification, devise contingency plans, empower regional subsidiaries with greater decision-making autonomy and flexibility, and reinforce risk management and compliance functions to enhance resilience and responsiveness within increasingly complex and localised trade environments.

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