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Geoeconomics is reshaping supply chains: from complexification to block-building

Allianz Research

The geoeconomic playbook of global trade

Executive summary

Ana Boata
Head of Economic Research
ana.boata@allianz-trade.com

Ano Kuhanathan
Head of Corporate Research
ano.kuhanathan@allianz-trade.com

Lluís Dalmau
Economist for Africa & Middle East
lluis.dalmau@allianz-trade.com

Jasmin Gröschl
Senior Economist for Europe
jasmin.groeschl@allianz.com

Françoise Huang
Senior Economist for Asia Pacific
francoise.huang@allianz-trade.com

Maria Latorre
Sector Advisor, B2B
maria.latorre@allianz-trade.com

Luca Moneta
Senior Economist for Emerging Markets
luca.moneta@allianz-trade.com

Sivagaminathan Sivasubramanian
Data Analyst
sivagaminathan.sivasubramanian@allianz-trade.com

Philippine Renaudie
Research assistant

Garance Talon
Research assistant

- **A renewed but contained trade war could cost global trade growth 0.6pp in 2026, while a full-blown trade war would cost up to 2.4pps.** In his second term as President, Donald Trump is likely to increase tariffs on Chinese and other strategic imports (to 25% for the former and to 5% for the rest of the world, excluding Mexico and Canada), which would decrease global trade by -0.6pp in 2026 as most measures would kick-in from the second half of 2025. China and the EU would bear most of the cost, with USD67bn of exports at risk in 2025-26, especially in automotive manufacturing, transport equipment and metals. Their retaliation measures are likely to hit US pharmaceuticals, automotive, metals, agrifood and machinery. In the event of a full-blown trade war (60% tariffs on China and 10% on the rest of the world, including Mexico and China), the toll would increase to 2.4pps of global trade growth.
- **The outlook for US-China relations remains bleak.** While the US economy was unrivaled from the 1970s to the 2000s, its share of global trade has since fallen from 15% down to below 10% while China's share now stands above 15%. In parallel, China overtook the US to become the world's largest manufacturer in 2009. Although global trade remains strongly intertwined with the US economy, due to the strength of the US consumer and the irreplaceability of the USD, China has emerged as a new superpower in the global economy, banking on its critical role in global manufacturing and its large and rising domestic market. Against this backdrop, confrontations between the two countries range from geopolitical hotspots (Russia, Taiwan, Asia-Pacific more broadly) to trade and tech wars as they are advancing different geoeconomic agendas.
- **American godfathering vs China's "silk" doctrine.** China has been deploying economic statecraft for decades with quite some success. Its "silk" doctrine was trade-centric and industry-centric and it mostly relied on soft power and connective influence – with the exception of the recent tensions around Taiwan, the country did not engage in overt military pressure/action. On the other hand, American "godfathering" rests on four pillars: (i) an unwavering commitment to protect core national interests at all costs (i.e. Donald Trump's "America First" policy, which was quietly maintained by the Biden administration), (ii) securing loyalty within the network of historical allies, (iii) an active economic and military stance against rivals and (iv) expanding American influence and control across new domains (e.g. space, tech, AI etc.).
- **Alignment with the US is costly for the EU, which needs to find its own (green) way in the new geoeconomic order.** While the US and the EU share a common stance on geopolitical issues, their economic interests are not aligned. The EU has not fully committed to establishing a joint trade and investment wall with the US against China, and China continues to acquire EU companies, even as the US has taken a more restrictive approach against Chinese capital. Nevertheless, we see a 79% correlation between the US imposing tariffs on China and the EU imposing tariffs on China one year later, and a 76% correlation between US and EU non-tariff measures actions against China within the same year. These are most costly to the EU: tariffs imposed on China cost the US an equivalent of 4% of its Chinese imports, compared 6.4% per year for the EU. Yet, the EU itself is not safe from US protectionist measures. The ambivalence vis-à-vis China also stems

from internal divisions across the EU. There is a risk that the US and/or China follow a divide-and-conquer strategy by exploiting internal European divisions to seek bilateral deals that would improve their own negotiating positions against the block. There is one way for the EU to navigate through this storm: the bloc, which directed 35% of its subsidies to the transition in 2023, should leverage its green policies as its main economic statecraft tool to both support its industries and achieve its climate goals.

- **Governments' deployment of economic statecraft is making supply chains more complex but opens the way for new trade champions.** Over the past two years, bilateral trade flows between geopolitically close countries have been gradually rising (+2pps to 60% of global trade). While US imports have been breaking away from China, China has been exporting more to its own geopolitically close partners, such as Russia, Singapore, Vietnam, the UAE and Saudi Arabia. Such reconfiguration in global trade flows suggests that trade patterns may be becoming more complex. Our supply-chain complexity index, which takes into account shifts in trade flows, geographic distance, geopolitical alignment and our country risk ratings, shows that supply-chain complexity in 2023 has risen 2x compared to 2017, or 6x compared to the pandemic years. Amid this complexification and the new geoeconomic order, countries are aiming to position themselves as next-generation trade hubs. Looking at efficiency, connectivity and trade potential, we identify 25 next-generation trade hubs in Asia and fast-growing mid-size countries with already established manufacturing or logistics hubs (e.g. Malaysia, Vietnam, Indonesia, the Philippines, the UAE etc.). These 25 economies are expected to grow their share of global exports by +1.6pp over the next five years, reaching USD1,274bn. As these hubs grow to account for up to 21.3% of all global exports by 2029, they will also need to invest USD120bn on port infrastructure alone to maintain their momentum.
- **Picking sides: Asia and Africa are closer to China and the US is losing influence on Latin America.** By looking at the next-generation trade hubs and other major economies' geopolitical, trade and cross-border investment links with the US and China, respectively, we compute geoeconomic distance scores relative to both countries. Our scores range from 0 (very close) to 1 (very distant) and show that China's sphere of influence includes more next-generation trade hubs from the emerging world, while most of the traditional "Global North" countries remain closer to the US. Unsurprisingly, the UK is the closest country to the US, followed by Ireland and the Netherlands, with Canada in 4th place and Mexico only in 28th. Most African and Asian nations are closer to China (on average 0.5 for African nations vs 0.7 distance with the US and 0.4 for Asian nations vs 0.6 distance with the US). After Hong Kong, Canada is the second closest economy to China – managing to remain close to both superpowers. Australia, South Korea and Greece are among the other nations that have managed to maintain the same distance with both the US and China. They are geopolitically closer to the US but retain very strong trade and investment relations with China – a position that could potentially become increasingly uncomfortable and force them to pick a side, should the new geoeconomic order centered on the US-China confrontation deteriorate significantly. Even in an intensified trade war scenario between the US and China (and beyond), business opportunities will continue to remain relatively more elevated in the new trade hubs as China will continue to invest and the US will increase its trade flows with them as they will be relatively more attractive than China.



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US vs. China: a geoeconomic war between two superpowers

Trade war reloaded: What a second Trump term could mean for global trade

Both China and Europe will be in the eye of the storm, with a combined USD67bn of exports at risk in 2025-26.

If the incoming Trump administration initiates a renewed trade war, it would likely involve swift and aggressive measures that would reshape global trade flows and impact numerous economies. Precedents from Trump's first term and current trade policy indicators suggest that the US would likely impose significant tariffs on Chinese imports, targeting industries that are non-critical to US supply chains, while also expanding duties on imports from other countries, especially the EU. An initial tariff increase from 13% to 25% on Chinese non-critical goods would threaten USD34bn of Chinese exports to the US in 2025-26. For other countries, tariffs could rise to 5% on imports, with Canada and Mexico potentially exempted due to the United States-Mexico-Canada Agreement (USMCA). However, the US might increase non-tariff barriers, by imposing stricter border controls for example, to restrict imports from these neighbors. For Europe, we expect the trade losses will amount to USD33bn in 2025-26, equivalent to -0.1pp of annual real GDP growth. The sectors most likely to suffer in Europe include automotive manufacturers, transport equipment and metals – together they account for close to 20% of Europe's exports to the US.

Pharmaceuticals, machinery & equipment, automotive, transport equipment and metals are most at risk.

Looking at European exports to the US by sectors, and focusing on industries whose exports to the US account for more than 2% of their countries' total exports, we find that the pharma sector is particularly exposed, especially in Ireland, Switzerland, Belgium, Denmark and the UK, but we do not expect a trade shock on their products. Machinery & equipment in the UK, Germany and Italy are also quite reliant on the US, as well as the auto and transport equipment sectors, in particular in Germany, UK, France and Italy. Lastly, the metals sectors in the UK and Switzerland also have substantial exports to the US. These

countries and their domestic sectors would suffer most from tariff increases. They are strategic, labor-intensive sectors and are/were pivotal to the economic success of US states that voted strongly for Trump's reelection. The revival of trade war comes in a context of turmoil for the auto industry in Europe and especially in Germany and all three sectors are rated as sensitive risk by Allianz Research.

Retaliation measures could target pharmaceuticals, automotive, metals, agrifood and machinery exports to Europe and China (close to 10% of total US exports).

Oil & gas is the main US export industry to Europe and the second one to China (after Agrifood, see Table 1). In the current backdrop of an ongoing energy crisis in Europe and still expensive crude oil, it is unlikely that either Europe or China would target US oil & gas exports to retaliate against US protectionism. Instead, China is likely to target agrifood products. In the past, China has levied tariffs on US soybeans and other agricultural products and could do so again. Both partners could target machinery & equipment, which accounts for a combined USD41bn of exports for the US. The US metals sector could also be targeted by the EU revoking its exception status to the carbon adjustment mechanism (CBAM), especially as President-elect Trump is unlikely to support the green transition of the US metal sector. China has a long history of state intervention in the steel industry and could target the US both as a retaliation measure and to support its own domestic industry. Lastly, both Europe and China could target the US auto industry. The US-China trade war on electric vehicles is already underway and could escalate, while in the context of Europe's ailing auto industry, the region could implement tariffs on US cars in a defensive move.

Table 1: Top exporting US sectors to countries other than Canada and Mexico in 2023, % of total US exports and in USDbn (above 10bn and above 0.5% of total exports)

Country	Sector	Value (USD bn)	Share of US total exports
EU	Energy - oil & gas	72.2	3.9%
EU	Pharmaceuticals	61.4	3.3%
EU	Machinery & equipment	27.1	1.5%
China	Agrifood - agriculture & farming	22.3	1.2%
China	Energy - oil & gas	19.3	1.0%
Republic of Korea	Energy - oil & gas	17.2	0.9%
EU	Chemicals - plastics & rubber	16	0.9%
China	Pharmaceuticals	15.6	0.8%
EU	Automotive manufacturers	15.5	0.8%
EU	Chemicals - Industrial	14.3	0.8%
China	Machinery & equipment - manufacturing	14.1	0.8%
United Kingdom	Energy - oil & gas	13.4	0.7%
Japan	Energy - oil & gas	11.7	0.6%
Switzerland	Metals - mining, casting & processing	11.3	0.6%
Japan	Pharmaceuticals	11.2	0.6%
EU	Metals - mining, casting & processing	10.9	0.6%
EU	Electronics	10.9	0.6%
United Kingdom	Metals - mining, casting & processing	10.2	0.6%
India	Energy - oil & gas	10.1	0.5%

Sources: UNCTAD, Allianz Research

A renewed but contained trade war could cut global trade growth by -0.6pp, mostly in 2026, but a full-blown trade war would cost -2.4pps. In our baseline scenario, we expect a contained trade war, with measures targeted at China (to 25% from 13% currently) and modest trade tariff hikes (5% for the rest of the world, excluding Mexico and Canada, from currently 2.5%), which would diminish global trade growth by 0.6pp. A full-fledged trade war would be the downside scenario (US tariffs on China hiked to 60% for all critical and non-critical imported goods and to 10% for the rest of the world, including Mexico and Canada), but this looks unlikely as the US would also bear a large cost (up to -1.2pp to US growth coupled with +0.6pp higher inflation). Should this happen, China, Mexico and Canada would be hit the hardest with cumulated export losses totaling to close to USD217bn over 2025-26. We estimate that the shock for global trade growth could amount to a loss of -2.4pps. In any case, most measures and tariff increases in both scenarios would start in Q2 2025 and impact trade growth mostly in 2026.

Table 2: Cumulated 2025-26 direct export losses from increased US import tariffs excluding currency impacts, top 30 most impacted countries

	<i>Contained trade war (USDbn)</i>	<i>Full-fledged trade war (USDbn)</i>
	2025-26	2025-26
China	-34.2	-125.3
Mexico	0	-52.1
Canada	0	-39.2
Germany	-8	-24.5
Japan	-6.8	-24.3
South Korea	-6.1	-20.3
Netherlands	-5	-15.8
Vietnam	-1	-14.8
India	-4.1	-14.2
France	-4.2	-13.4
Ireland	-3.5	-13.3
Thailand	-5.7	-12.5
UK	-2.8	-10.7
Italy	-3.3	-10.5
Malaysia	-4.7	-10.2
Switzerland	-3.4	-9.5
Singapore	-4.7	-9.4
Belgium	-2.6	-8.6
Brazil	-3.5	-8.3
Sweden	-2.4	-7.2
Spain	-2.1	-6.5
Israel	-2.4	-4.9
Denmark	-1.3	-4.8
Colombia	-1.9	-3.9
Chile	-1.9	-3.9
Australia	-1.6	-3.4
South Africa	-1.6	-3.3
Saudi Arabia	-1.3	-3.2
Austria	-1	-3.1
Philippines	-1.1	-2.7

Sources: UNCTAD, Allianz Research

China: reaping the benefits of the “silk” doctrine

China has emerged as a new superpower in the global economy, banking on its critical role in global manufacturing and its large and growing domestic market. China is the world’s largest exporter and a key player in global supply chains. The country’s manufacturing prowess and competitive pricing have made it an indispensable trade partner for both developed and emerging economies. In fact, many economies around the world have critical dependencies on China. For instance, for the US and EU, 45% and 30% of imports from China are critical dependencies, respectively¹. In parallel, the size of China’s domestic market has also attracted global exporters, particularly in sectors such as automotive or luxury goods.

China’s rise stems from its “silk” doctrine. China has been deploying economic statecraft for decades with quite some success. Its “silk” doctrine was trade- and industry-centric and mostly relied on soft power and connective influence. With the exception of the recent tensions around Taiwan, the country did not engage in overt military pressure or action. The country has implemented strong industrial policies to support its manufacturing sectors and managed to transition from low value-added ones (e.g. textile, small electronics) to high value-added ones (e.g. electric vehicles, solar panels, smartphones etc.). Accompanying the trade dependence, China exerts its influence through investment, epitomized by the ambitious Belt and Road Initiative (BRI). Launched in 2013, the BRI exemplifies China’s strategic use of investment to expand its economic and geopolitical influence. The BRI aims to enhance connectivity and cooperation among countries across Asia, Europe and Africa through a network of infrastructure projects, including railways, ports, highways and energy pipelines. By financing and constructing these projects, China has positioned itself as a key driver of economic development in participating countries. This has not only opened new markets for Chinese goods and services but also strengthened China’s geopolitical ties with these nations.

The increasing integration of Chinese technology and telecommunications infrastructure in global markets has become a geopolitical topic. China’s advancements in artificial intelligence, robotics and other high-tech sectors are positioning it at the forefront of the Fourth Industrial Revolution. These technological capabilities not only boost China’s economic prowess but also enhance its strategic leverage. Companies like Huawei and ZTE have become major players in the global technology sector, particularly in the rollout of 5G networks. This has raised concerns about potential security risks and the possibility of Chinese state influence over critical communication infrastructure. Several countries have faced intense pressure from both China and the US over whether to allow Chinese technology in their 5G networks, highlighting the geopolitical ramifications of China’s technological advancements. China’s push for technological self-sufficiency aims to reduce reliance on foreign technology and foster homegrown innovation. This dual approach of exporting technology while simultaneously strengthening its domestic capabilities underscores China’s strategy to dominate future technological landscapes, thereby consolidating its hegemonic effect on the global economy.

China’s rising geoeconomic influence is also evident in its ability to impose its geopolitical goals on third-party countries. The issue of Taiwan is a prime example. China considers Taiwan a breakaway province and has consistently sought to isolate it diplomatically. Through its economic influence, China has been able to pressure several countries into severing official ties with Taiwan and recognizing the “One China” policy (Panama in 2017; Burkina Faso, Dominican Republic and El Salvador in 2018; Kiribati and Solomon Islands in 2019; Nicaragua in 2021). This has been achieved through a combination of trade incentives, investment promises and, in some cases, economic coercion.

1. See our report [“China: keeping the dragon awake”](#)

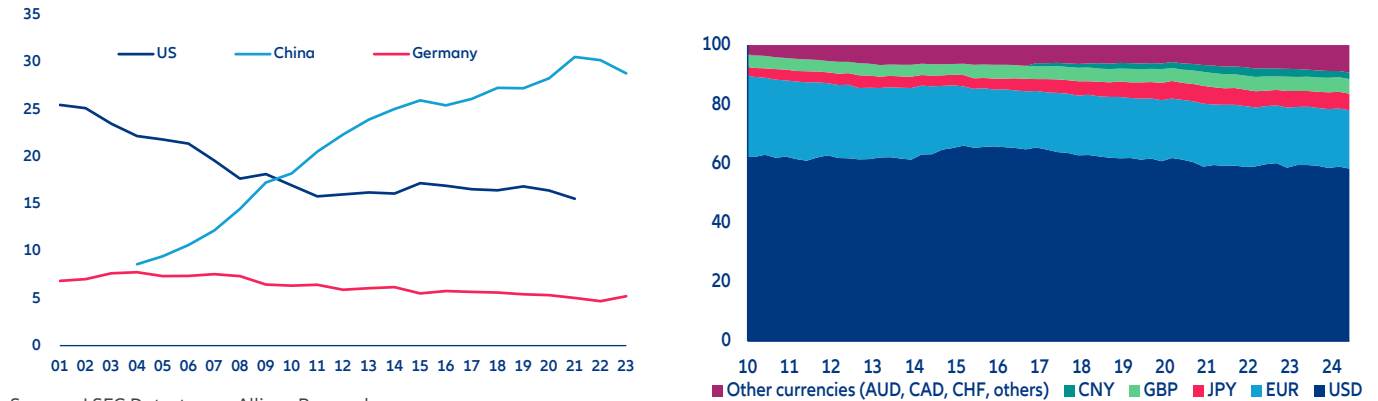
The US's "godfather" approach on a collision course with China's ascent

The US's global economic leadership is contested but its grip remains strong, thanks to the US consumer and the dollar. While the US economy was unrivaled from the 1970s to the 2000s, its share of global trade has since fallen from 15% to below 10% while China's share now stands above 15%. In parallel, China overtook the US to become the world's largest manufacturer in 2009 (see Figure 1, left). Nevertheless, global trade remains highly intertwined with the US economy. Indeed, the US is the largest market in the world: global corporations compete to access the US consumer, positioning US firms and supply chains at the heart of global trade. The biggest ports of the US remain among the busiest and largest in the world, while ports across the world such as Shanghai, Busan or Ho Chi Min are mostly supplying the US economy. The strong consumption and appetite for imported goods in the US has resulted in large trade deficits to the rest of the world and to China. These deficits have been managed by the US through its main tool of power: the dollar. The USD is used in 88% of all global trade transactions, followed by the euro (32%) and the Chinese renminbi (2-3%). Moreover, 59% of central bank reserves are held in USD (see Figure 1, right), though this number has decreased since sanctions were imposed against Russia following the invasion of Ukraine, in favor of gold and the euro (now respectively 13% and 21% of global reserves). More importantly, the US has been able to finance its large (twin) deficits by issuing debt in dollars in the form of Treasury bonds, which are regarded as the global safe asset.

US "godfathering" conflicts with China on geopolitics and economics. American "godfathering" rests on four pillars: (i) an unwavering commitment to protect core national interests at all costs (i.e. Donald Trump's "America First" policy, which was quietly maintained by

the Biden administration), (ii) securing loyalty within the network of historical allies, (iii) an active economic and military stance against rivals and (iv) expanding American influence and control across new domains (e.g. space, tech, AI etc.). US-China relations have progressively and steadily deteriorated over the past decade. The shifting balance of power, compounded by conflicting world views and growing mutual distrust, has brought the world's two largest economies into a state of geoeconomic war. At the heart of the conflict lies Taiwan. Beijing stands by the "One China" policy while Washington sees the nation island as a critical ally in the APAC region to counter China's growing influence. The tensions intensified after the first Trump administration's moves to deepen ties with Taiwan, including arms sales and high-level diplomatic visits. The Biden administration has maintained this course, enhancing military cooperation and reaffirming Washington's commitment to help Taiwan defend itself. The US has also worked to build stronger alliances in the APAC region through the Quad (i.e. US, Japan, India and Australia) and AUKUS (Australia, the UK and the US), aimed at countering Chinese influence. Beijing has responded to these actions with shows of force (i.e. military exercises in the Taiwan Strait etc.). The US-China rivalry has also been shaped by Beijing's close relationship with Russia, especially following the Russian invasion of Ukraine in 2022. While China has not provided direct military support to Russia, it has increased trade with Moscow and refused to condemn the invasion. This growing China-Russia alignment has added another dimension to the strategic rivalry between the two countries. China's political support to Moscow, along with its purchasing of Russian oil and gas, has undermined US and European efforts to isolate and strike Russia's economy.

Figure 1: Share of global manufacturing value-added (%), left) and Distribution of global FX reserves (%), right)

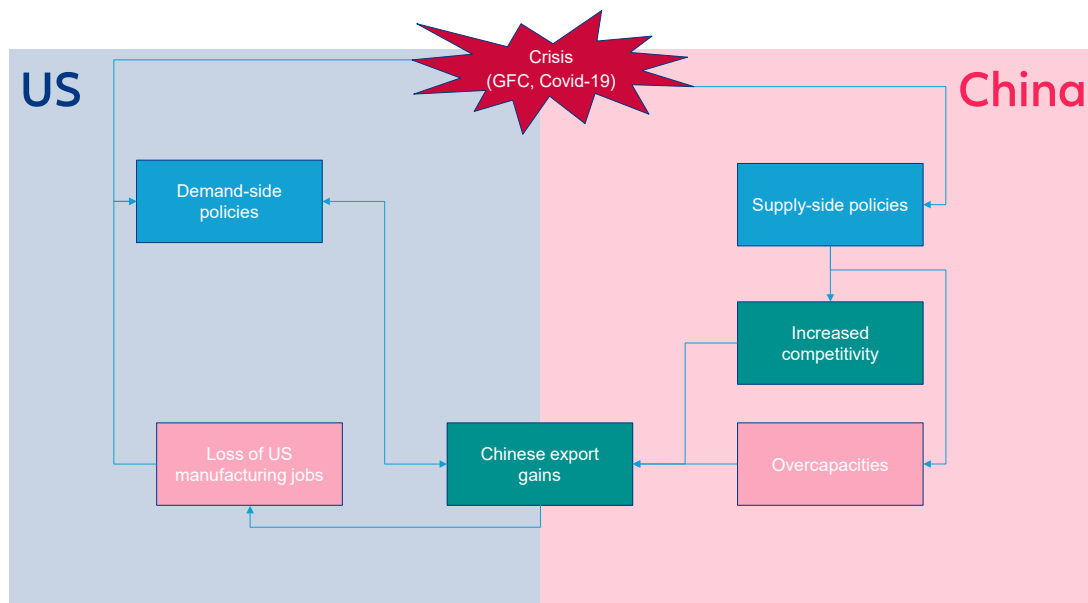


Sources: LSEG Datastream, Allianz Research

The trade war has become a protracted conflict that finds its sources in diverging domestic policies and results from strong US economic statecraft. Economic tensions between the US and China turned into a full-scale trade war in 2018 under the Trump administration, which sought to address China’s alleged unfair trade practices (e.g. non-respect of intellectual property rights, state subsidies etc.). The US imposed tariffs on billions of dollars’ worth of Chinese goods and China retaliated in kind. Despite several rounds of negotiations, the trade war has not yet been resolved. In 2023, tariffs remained on approximately USD360bn worth of Chinese goods and Beijing continues to apply duties on USD110bn worth of US imports. The US-China trade war has had substantial economic impacts on both countries: According to the

Peterson Institute for International Economics, US tariffs on Chinese imports have cost American companies and consumers USD53bn per year. The root of the conflict can be found in diverging domestic policies between the US and China. While China has been focused on industrial and other supply-side policies over the last couple of decades, the US, especially when responding to crises, has been using demand-side policies. As US consumers had more dollars to spend, Chinese manufacturers were able to offer cheaper and more competitive goods, and damage further US manufacturing industries (see Figure 2). Tariffs and the ongoing trade war may be an attempt at breaking the loop and defending the core national interest on jobs and sovereignty.

Figure 2: Illustration of US & China policies



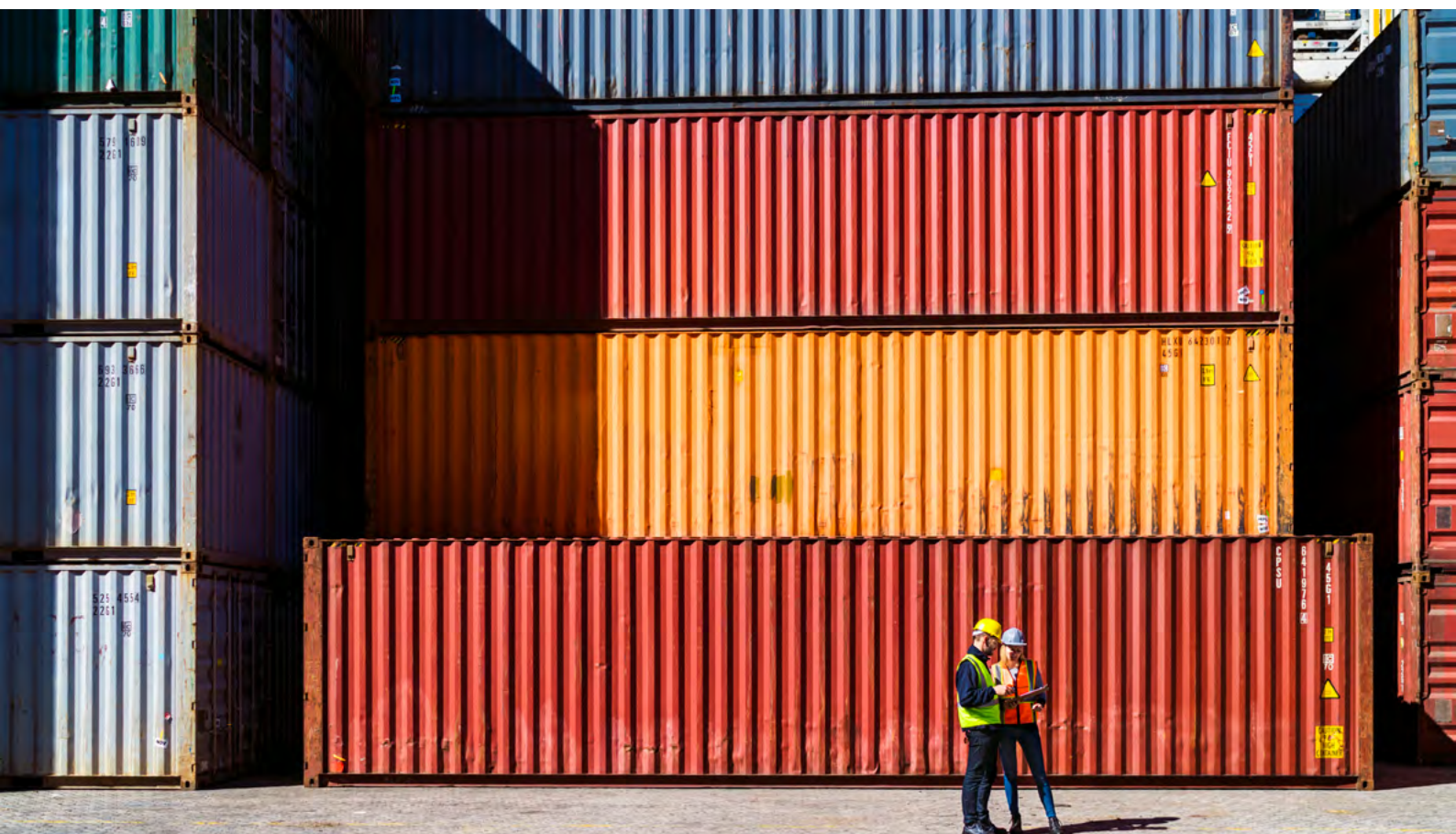
Source: Allianz Trade

The trade war is increasingly becoming a tech war. While the trade war initially focused on reducing the US trade deficit with China and re-industrialising the country, it has since turned into a confrontation aimed at curbing China's rise in tech and expanding US influence in emerging technologies (e.g. AI, robotics etc.). This shift in focus became particularly clear under the Biden administration as the US was increasingly concerned about China's ambitions to dominate cutting-edge technologies such as AI, quantum computing or 5G networks. Furthermore, Washington views China's advances as both an economic threat and also a national security risk, particularly in sectors like semiconductors, which are critical for both civilian and military applications. Consequently, the US has deployed strong economic statecraft by enacting a series of measures aimed at restricting China's access to key technologies. In 2020, the US imposed export controls on semiconductors and chip-making equipment, particularly those manufactured by American companies. In 2023, the Biden administration expanded these restrictions, placing new limits on the sale of advanced chips to Chinese firms and especially on Huawei. More recently, the US reached an agreement with allies such as the Netherlands, Japan and South Korea to curb certain exports to China in order to cut the country off from the global semiconductor

supply chain. The US has also been trying to set up strong supply-side policies of its own: it incentivized semiconductor manufacturing at home through the CHIPS Act and many companies have begun building capacities in the US. The impact of these measures is yet to be assessed and although they might not prevent the rise of China in the tech industry, they are likely to slow it down.

With Donald Trump winning the US Presidential election, the outlook for US-China relations remains bleak.

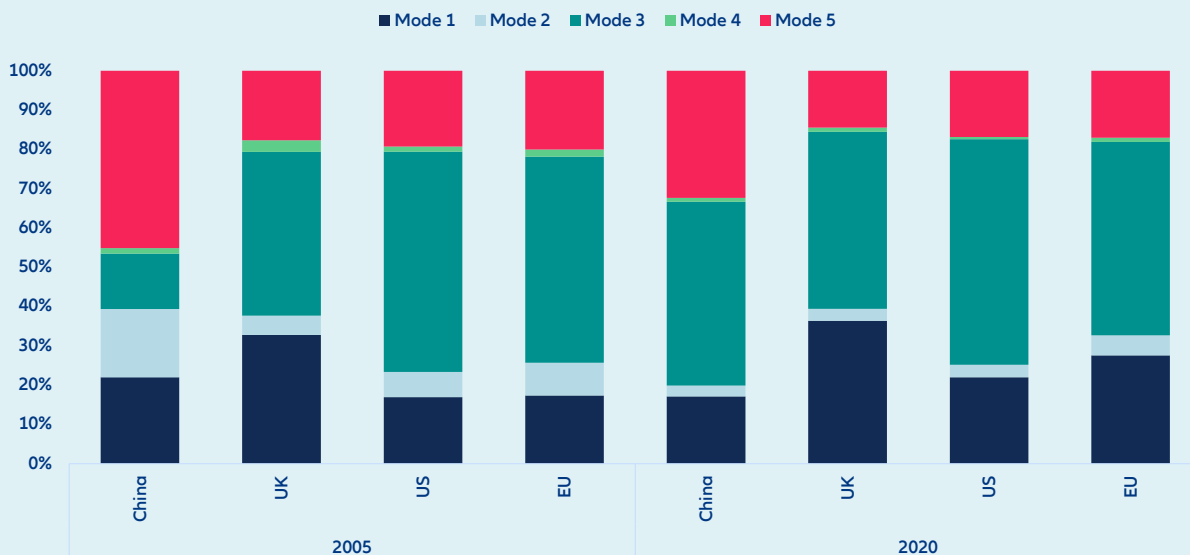
Trump views China as the US's first strategic competitor and is unlikely to make significant efforts to warm up relations. He has consistently emphasized a hardline stance and a continuation of the policies of his first term, including increasing tariffs on Chinese imports, and his confrontational approach leaves little room for diplomatic improvement. He will also most likely follow Biden's efforts to reduce reliance on Chinese supply chains and limit China's access to advanced technologies, especially in semiconductors and artificial intelligence.



The next trade battlegrounds are services and cross-border data flows

Global goods trade peaked around the financial crisis in 2008 and has been gradually declining since, while services trade is becoming increasingly important in a more fractionalized world. The share of global manufacturing for G7 countries fell from 66% in 1999 to 37% in 2020. In contrast, six emerging economies – China, India, South Korea, Indonesia, Thailand and Brazil – saw their manufacturing share rise from 10% to 38% during the same period, with the rest of the world remaining stable at about a quarter. Since 2005, the nature of trade has shifted significantly; services have become increasingly important with now 63% of global trade compared to 37% for goods. But the kind of services provided matter in a more fractionalized world. Mode 3 services, where companies establish a physical presence abroad, are particularly crucial while mode 5 services such as engineering, banking, software and logistics enhance firms' export capabilities and intensity. Between 2019 and 2022, cross-border supply services grew by +39%, while commercial presence increased by +9%. However, consumption abroad decreased by -12% and the physical presence of individuals fell by -60%. Looking ahead, there is substantial potential in new technologies and associated services embedded in goods. However, countries have varied their focus on different service types (Figure 3). For instance, China emphasizes commercial presence to circumvent protectionist measures while the UK and US lean towards cross-border supply alongside slight increases in commercial presence. Meanwhile, EU countries have generally expanded cross-border supplies at the expense of other service types.

Figure 3: Services exports by mode of supply, share of total services exports 2005, 2012 and 2020

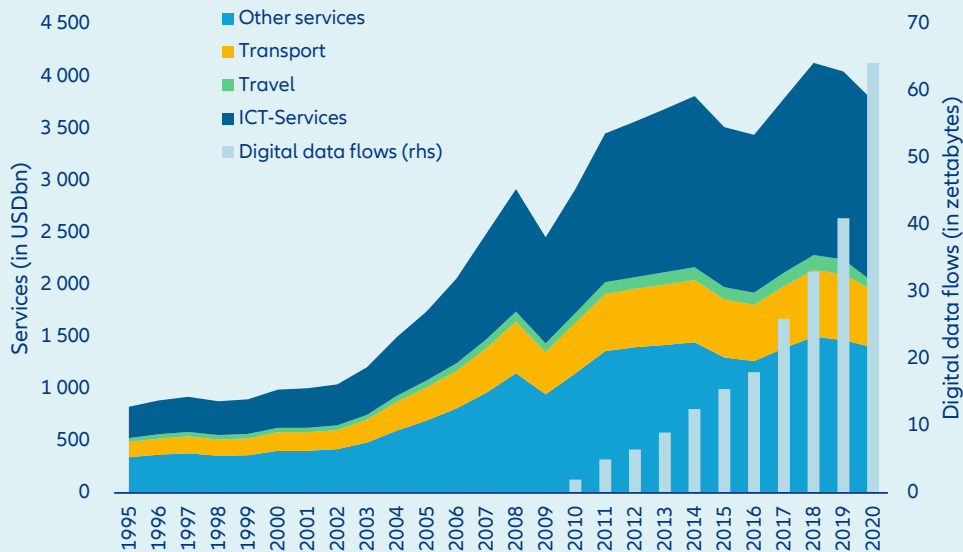


Notes: Mode 1 is cross-border supply, mode 2 is consumption abroad, mode 3 is commercial presence, mode 4 is presence of natural persons as defined by GATS services. Mode 5 are covered by GATT rules and are services incorporated in manufacturing goods.

Sources: WTO TiSMoS, OECD TiVa

The next trade war frontline might emerge in soft tech and data. The digital transformation of the global economy is fostering closer connections among countries and individuals, enabling modern conveniences like international travel, online shopping and secure cross-border payments through seamless data flow. But that could also be a problem in a geo-politicized world. While manufacturing exports and foreign direct investment (FDI) have slowed, information and communication technologies (ICT)-enabled services have flourished since the 2008 financial crisis. Emerging economies are experiencing significant export growth, especially in intermediate soft tech services such as ICT. World services exports rose from 4% of GDP in 1980 to 7% in 2019, with total trade in services increasing from 16% to 24% over the same period. Notably, FDI has shifted towards services. Cross-border greenfield projects might be used to circumvent trade protectionism. In 2023, a series of investments in battery and EV plants across Europe pushed Chinese greenfield investment to EUR5.3bn, up +48% on 2022. Worldwide, greenfield investments increased from an average of 66% between 2004 and 2007 to 81% from 2020 to 2023, while FDI in manufacturing dropped from 26% to just 13%. The US and Europe are already debating on how to condition greenfield investments from China and the tools they could use. In addition, cross-border data flows are increasingly vital, with global trade in data-driven services – like computing, telecommunications and finance – now making up nearly half of all service trade (Figure 4). Between 2003 and 2013, cross-border data volumes doubled, followed by an additional +9% increase from 2013 to 2018. The total amount of data stored on the internet is projected to surge from 33 zettabytes in 2018 to an astonishing 175 zettabytes by 2025, with nearly half residing in the cloud.

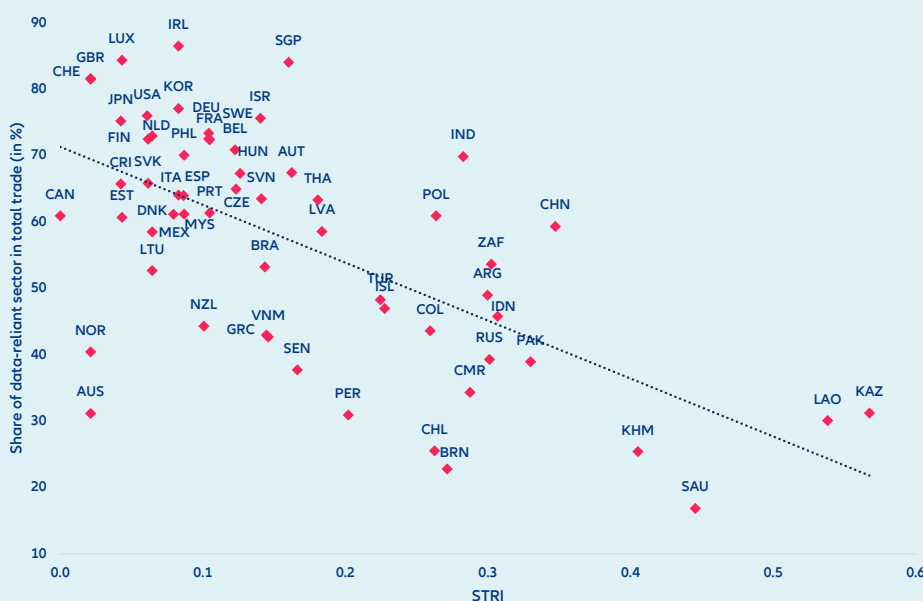
Figure 4: Cross-border trade in services and digital data flows, in USDbn and in zettabytes



Sources: LSEG Datastream, Allianz Trade

Cross-border data flows benefit not only the services industry but also many manufacturing sectors. Access to and sharing of data across borders can generate social and economic benefits amounting to 2.5% of GDP. In 2020, data-reliant sectors represented 6.8% of GDP in the EU27, 2.9% in the US and 5.9% in China, with manufacturing representing a third in the EU27, a quarter in the US and half of data-reliant sectors in China. But many countries have introduced restrictions or regulations on cross-border data flows. Countries that impose stricter regulations on services trade tend to have a lower share of data-reliant sectors in their total trade (Figure 5). The EU and US, for instance, limit data exports to China due to concerns over individual rights and national security. While the US primarily cites national security for outbound data flow restrictions, the EU emphasizes data privacy. In contrast, China merges both rationales in its own protectionist approach, setting the stage for a potentially major geoeconomic conflict. We calculate that implementing a 5% export tax on cross-border data exports could generate significant revenue on the fiscal side – for instance, USD0.8bn per year for the EU27 – but would also raise trade costs. As limiting data flows can hinder innovation, elevate costs for businesses and consumers and ultimately stifle economic growth, we calculate that taxing data-reliant sector exports could result in a GDP loss of -0.1% for the EU27. In this context, rising digital fragmentation could result in countries missing out on current opportunities and jeopardize future prosperity.

Figure 5: Data-reliant sectors and their shares of total trade (in %) to the services trade restrictiveness index (STRI)



Sources: OECD TiVA, OECD STRI, Allianz Research. Notes: The sector shares are as reported in OECD TiVA VA exports for the year 2020. Data-reliant sectors are identified through the OECD grading of sectors based on digital intensity according to Calvino, F. et al. (2018), "A taxonomy of digital intensive sectors", OECD Science, Technology and Industry Working Papers, No. 2018/14, based on: ICT investment, software investment, ICT intermediate goods, ICT intermediate services, robot use, online sales and ICT specialists and apply a filter to remove sectors that are rarely traded internationally. Sectors are considered data-reliant if they are in the top quartile for at least two of the seven criteria or in the top two quartiles for at least four criteria. Data-reliant sectors include wholesale and retail, other business sector services, financial and insurance activities, transport equipment, chemicals and pharmaceuticals, coal and petroleum, IT and other information services, machinery and equipment, furniture, telecommunications, media, computer & electronics, electrical equipment, paper and printing.

Alignment with the US is costly for the EU

Forging alliances: The EU and a US-led protectionist agenda

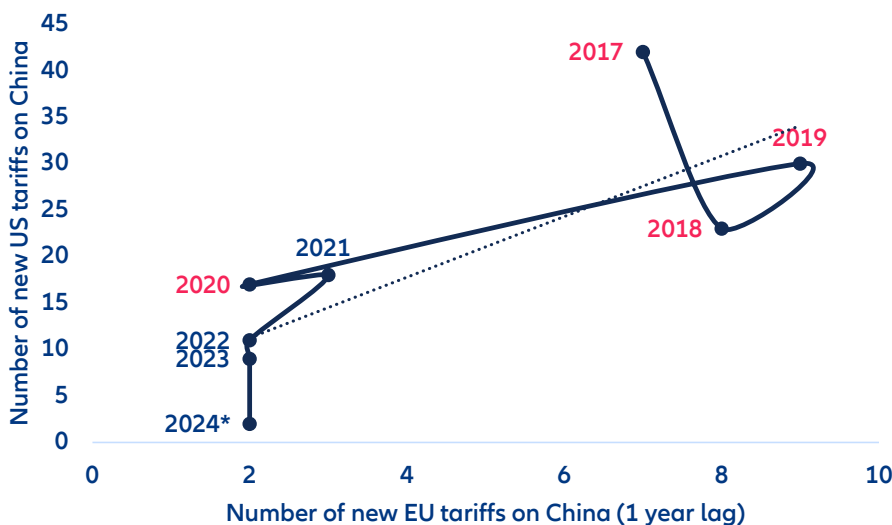
While the US and the EU share a common stance on geopolitical issues, their views on geoeconomics remain distinct. Despite evident differences between member states, EU trade policy seems to have been subject to the US hegemonic effect recently, with the ban of Huawei’s 5G infrastructure or the imposition of tariffs on Chinese EVs. But this is only part of the story as the EU is also following its own agenda in terms of industrial policy, the green transition (i.e. through the Carbon Border Adjustment Mechanism (CBAM)) and digitalization (through the Digital Single Markets Act and the Digital Markets Act). This will potentially hurt trade flows in the meantime.

In recent years, both the US and the EU have experienced significant trade deficits with China, yet they have also begun to fortify their protectionist measures against it. Currently, the EU maintains a stronger trade connection with China, which accounts for 15% of its total trade compared to 12% for the US. Notably, green trade related to China constitutes 15% of the EU’s total trade in green products, while for the US this figure stands at only 10%. The US’s aggressive push towards trade protectionism against China has manifested not only through tariffs and open trade disputes but also through more subtle mechanisms such as non-tariff barriers

(NTMS) and restrictions on foreign direct investment (FDI). The question remains: will the US succeed in persuading allies like the EU, Canada or Turkey to adopt similar measures, such as tariffs on electric vehicles (EVs)?

While the EU seeks to align with the US for security reasons, it has not fully committed to establishing a joint tariff wall. Although it has joined the US in a tariff dispute over EVs and is discussing a potential agreement on aluminum and steel – proposing 10% tariffs on aluminum and 25% on steel for non-market economies – historical data reveals an intriguing trend. There is a remarkable 41% correlation between the timing of EU tariffs on China and those imposed by the US in the same year. This correlation increases to 79% when considering a one-year lag for EU tariffs (Figure 6). However, it is essential to recognize that the EU remains significantly more dependent on trade with China than the US. Following a US-led protectionist agenda could result in collateral trade damage for Europe. Additionally, since the EU27 is not a monolithic entity but rather a collection of individual countries with diverse perspectives, it is unlikely that they will fully align with US protectionist policies.

Figure 6: New tariffs implemented by the US and the EU against China, 2016 – 2024*



Notes: 2024* is not the full year, but the cut-off date for NTMs is end of September 2024. In red the years of the first Trump presidency and trade war.

Sources: GTA, Allianz Research.

The tariffs imposed on China have resulted in significant costs for both the US (USD0.9bn annually) and the EU (USD1.6bn annually). Initially, the measures taken at the onset of the US-China trade dispute appeared to be less targeted, affecting products from solar panels to washing machines. However, the US has since shifted towards more targeted actions against specific Chinese imports. For the US, the highest costs from tariffs are associated with textiles (0.44%), plastics and rubbers (0.43%) and foodstuffs (0.42%) (Figure 7, left). In contrast, the EU's most affected categories include foodstuffs (1.02%), animal products (0.95%) and chemicals (0.74%) (Figure 7, right). These differences can be attributed to varying trade structures and tariff frameworks between the two blocs. In terms of agricultural imports, the EU imported USD5.5bn worth of products from China in 2023, imposing an average applied tariff of 11.3%. The US, on the other hand, imported only USD3.7bn in agricultural goods, with a significantly lower average applied tariff of 3.3%. The

disparity is less pronounced in manufacturing. The EU imported Chinese products valued at USD549.9bn with an average applied tariff of 4.2%, while the US imported USD444.3bn worth of goods subject to an average applied tariff of 3.5%. These figures highlight the differing geoeconomic interests between the US and EU, as well as the influence of national interests within individual EU member states regarding trade policies. A recent example illustrating this divergence is the EU's decision to impose substantial tariffs – up to 35.3% – on EVs manufactured in China. This move followed a divided vote among EU countries, where 10 nations supported the tariffs, five opposed them and 12 abstained from voting altogether.

Figure 7: Costs of tariffs against China for the US (top) and EU (bottom), in % of imports from China

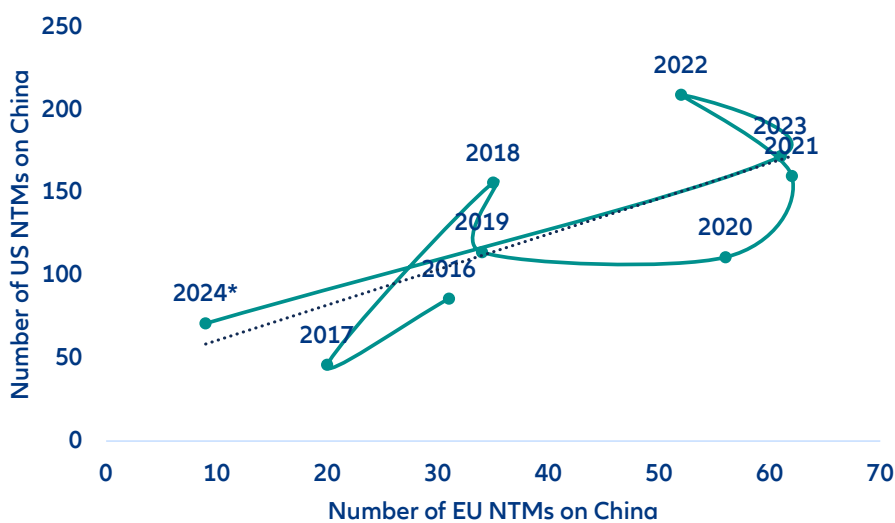


Sources: WITS Trains, UNComtrade, Allianz Research. Notes: Calculations are based on tariff schedules from 2022 and import data from 2023

When it comes to NTMs, the US significantly outpaces the EU in its efforts to shield its market from Chinese competition. In 2022, the US reached a peak of 209 new NTMs, while the EU introduced only 52 new measures during the same period (Figure 8). Between 2016 and 2018, the US saw an impressive +81% increase in NTMs targeting China, followed by an additional +10% rise over the past five years. In contrast, the EU saw a modest +13% increase in NTMs during the earlier period, though this surged by +74% in the last five years. Does this trend indicate that the EU is following the US lead in constructing

a protectionist barrier? To some extent: there is a notable correlation of 76% between US and EU NTM actions. However, when it comes to investment controls, the US has taken a more restrictive approach due to national security concerns, effectively closing its doors to certain investments. Meanwhile, China continues to pursue acquisitions of EU companies. As China leverages FDI to advance its technological capabilities, the EU has emerged as a highly attractive destination for Chinese investments abroad.

Figure 8: Number of new NTMs by the US and the EU against China, 2016-2024*



Notes: 2024* is not the full year, but the cutoff date for NTMs is end of September 2024.

Sources: GTA, Allianz Research

The EU braces for potential trade tensions post US elections

Despite aligned geopolitical positions, the EU itself is not immune to US trade restrictions. In 2018, the Trump administration imposed tariffs on EU steel and aluminum, catching the Europe Commission off guard. At the time, the EU retaliated only partly, hoping to de-escalate the fight. This time, a task force that aims at preparing for the consequences of the US elections has been set up at the level of the Secretariat-General of the European Commission. This means that the European Commission intends to retaliate if the new Trump administration imposes further tariffs after the elections.

Unresolved issues and potential new targets. Steel remains an ongoing issue as the EU extended a pause on its duties last December for 15 months, meaning that, there will be a reckoning within weeks of Donald Trump

taking office. Additionally, European leaders, officials and businesses are particularly worried about the ongoing debates in the US on the German car industry as the US is the largest importer of German cars after China.

In the event of increasing tensions on trade with the US, the EU is hoping for a negotiated solution as Europeans and Americans have the common objective to prevent China's industrial surpluses and subsidy policies from impacting their own industries. A way out of this potential trade war would therefore revolve around closer cooperation between the EU and the US on China. This will, however, depend on the European Commission's ability to stifle dissension between member states, which have diverging interests, agendas and views towards China.

The EU trying to walk its own (green) path, with or without a united front

The EU balancing act between the US and China will ultimately be difficult as further geopolitical alignment with the US might come with a substantial economic cost for several member states.

Germany, for example, has historically been opposed to implementing protectionist measures on China and represents a more neutral view on China in the European Council. The stakes are high for the largest EU economy as China remained its largest trading partner in 2023 with exports amounting to nearly EUR100bn. To put that into perspective, this is nearly double the combined exports to China of France, the UK and Italy. Additionally, major German companies like Daimler, Volkswagen, BMW and Siemens have established significant production facilities in China, which contribute substantially to their profits. Apart from Germany, several Central and Eastern European countries are also developing strong economic ties with China. China now invests more in this region than in Western Europe, and Hungary in particular receives 44% of all Chinese FDI in the EU (mostly along the electrical vehicle supply chain). Countries in Central and Eastern EU are thus likely to follow Germany with a more neutral stance on China.

The risk is that the US and/or China follow a divide-and-conquer strategy against the EU by exploiting internal European divisions to seek bilateral deals that would improve their own negotiating positions against the block. This would lead to increasing tensions between EU member states, which are already quite divided on some trade issues, such as the Mercosur agreement. The risk is that this would ultimately lead to a fragmentation and complexification of trade policy in the EU.

In the meantime, the EU aims to be ahead of the global curve in terms of its climate actions and green transition efforts, but must be cautious not to use these initiatives as protectionist tools. To achieve a 55% reduction in greenhouse gas emissions by 2030 and become the first climate-neutral continent by 2050, Europe needs to raise carbon emission prices. As a leader in climate policy, the EU has introduced mechanisms like the CBAM, which targets trade and aims to protect emission-intensive

industries at home. While costly for some trade partners, CBAM should incentivize global carbon-pricing policies, with the US and China already committing to step up their climate actions. To prevent trade conflicts and foster global climate cooperation, the EU should strengthen its ambitions while remaining open to negotiating the CBAM's implementation details and exemptions. This will help ensure that the CBAM serves as a catalyst for global climate efforts rather than a form of green protectionism. The EU is also ramping up its green industrial policy to accelerate the green transition in response to the US IRA. REPowerEU allocates over EUR250bn to support one-stop shops for approvals, tax incentives and workforce reskilling. The InvestEU Fund offers guarantees for sustainable infrastructure and R&D investments, with EUR11.4bn available from 2024 to 2027. In 2023, the EU implemented 49% of its industrial policies with climate ambitions, directing nearly 35% of total subsidies toward the green transformation in 2023, compared to 14% in the US. Green subsidies for the EU27 increased from EUR13.4bn in 2022 to EUR42.8bn in 2023. While carbon pricing and targeted industrial policies are crucial to maintain competitiveness for EU companies, Europe must remain cautious to avoid provoking retaliatory actions from key trade partners or using these measures for targeted protectionism.

Geoeconomics is reshaping supply chains: from complexification to block-building

Geopolitics is already complexifying trade flows

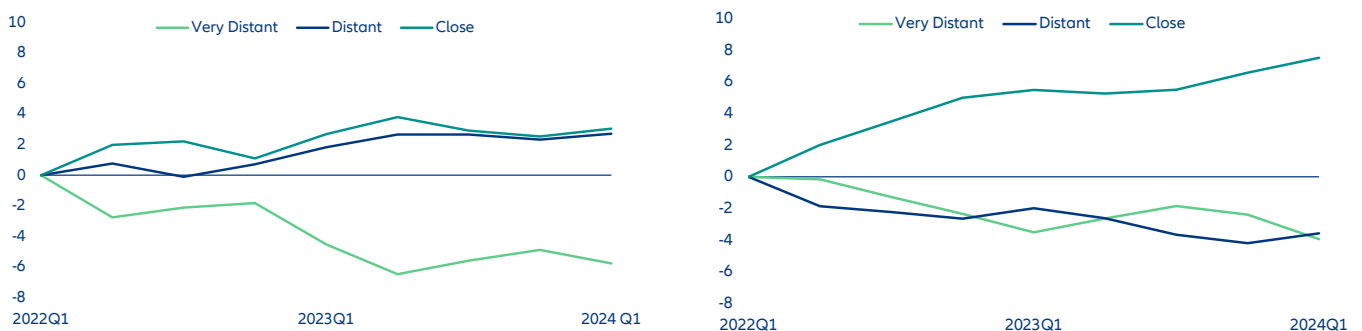
Geopolitically distant and very distant countries have been trading less and less with each other since 2022.

Based on votes at the United Nations' sessions, academics² have calculated distances between country pairs, which we then categorize into three groups: geopolitically close countries, geopolitically distant countries and geopolitically very distant countries. We then look into how global trade is distributed across these three groups. In Q1 2022, bilateral trade flows between geopolitically close countries represented 58% of global trade. The share rose to 60% two years later. Symmetrically, the share of global trade occurring between geopolitically distant countries declined by -1pp over these two years (35% to 34%), as did the share for geopolitically very distant countries (7% to 6%). Most of these changes are explained by trade flows between the US and China (geopolitically very distant), the EU and Russia (geopolitically distant), the US and the EU (geopolitically close), China and Russia (geopolitically close) and China and a few Southeast Asian countries (geopolitically close).

US imports are breaking away from geopolitically very distant partners (China) but are not necessarily being

replaced by purely friendly dependences. Drilling down at the country level, we find that Chinese exports follow the global pattern. Out of total Chinese exports, the share going to geopolitically close countries has risen by nearly 8pps since the beginning of 2022 (see Figure 9, right), driven by Russia, Singapore, Vietnam, the UAE and Saudi Arabia. The share of Chinese exports headed to geopolitically distant and very distant countries, respectively, declined by nearly 4pps. The former was driven by exports to the EU, Japan, South Korea and Canada, and the latter was unsurprisingly mostly led by exports to the US. Focusing on the US, it is interesting to note that while the share of US imports coming from geopolitically very distant countries declined (-6pps), it increased similarly for both distant (+3pps) and close (+3pps) countries (see Figure 9, left). Notably, the US is importing less from China and more from both friendly partners such as the EU and Canada and also geopolitically distant partners such as Mexico, South Korea and Japan.

Figure 9: Change in distribution of US imports (left) and Chinese exports (right), with respect to Q1 2022, in pp



Sources: Bailey et al. (2017), UNCTAD, Allianz Research

2. Bailey, Michael A., Anton Strezhnev, and Erik Voeten. 2017. Estimating dynamic state preferences from United Nations voting data.

This reconfiguration in global trade flows suggests that trade patterns are complexifying. Our proprietary measure shows that supply-chain complexity in 2023 was 2x that of 2017 or more than 6x that of the pandemic years. Our proprietary supply-chain complexity index takes into account how trade flows are redistributing, as well as specificities of each bilateral trade flow: the geographical distance between the two trading partners, the geopolitical distance between the two trading partners and risks related to each of the trading partner (their infrastructure connectivity and quality, vulnerability to climate change, growth potential and openness, etc.). We find that supply-chain complexity may have started to rise before the pandemic, before declining significantly over 2020-2022. A possible reason is that in the context of lockdowns and supply-chain shortages, companies were prioritizing being able to source goods, rather than worrying about where they came from. But as sudden-stop concerns receded and

geopolitical worries took over, supply-chain diversification initiatives seem to have come back into focus. As a result, our proprietary measure shows that supply-chain complexity in 2023 was 2x that of 2017, or more than 6x that of the pandemic years. Supply-chain diversification is likely more about rerouting and longer trading routes, rather than substituting or reshoring.

Next-generation trade hubs still try to play the competitiveness game

Amidst the new geoeconomic order and the clash between the US and China, third-party countries are positioning themselves to reap the benefits of a more fragmented trading and financial system. This fragmentation has led to a more complex trade and financial network, where the old rules of good quality infrastructure now interact with energy independence or banking system health. In this context, we assess all emerging markets around three pillars – efficiency, connectivity and trade potential – to identify which ones are likely to play a bigger role in the complexified trading and financial system (see appendix for more details on our methodology).

Our result shows three clear trends. First, the Asian continent will remain central even in a fragmented trading system. Second, fast-growing mid-size countries with already established manufacturing or logistics hubs are going to be the pillars enabling trade throughout the globe. The markets on top of our next-generation trade

hubs ranking are mostly located in Southeast Asia, at the intersection of Asia and Europe, and those in the Western Hemisphere also connect the US market to Asia. Finally, our next-generation trade hubs are forecasted to continue growing in importance. In the next five years, they are projected to increase their share of global exports by +1.6%, 19.7% to 21.3%, reaching USD1,274bn by 2029.

Table 3: Next-generation trade hubs ranking

		Connectivity	Efficiency	Trade potential
UAE	1	1	17	10
Malaysia	2	4	1	6
Vietnam	3	9	16	1
Türkiye	4	10	7	4
Indonesia	5	23	13	2
Romania	6	6	14	5
Hungary	7	5	18	3
Chile	8	8	2	14
Peru	9	19	5	7
Poland	10	7	9	11
Philippines	11	21	8	8
Bangladesh	12	22	11	9
Colombia	13	11	6	18
India	14	24	4	15
Saudi Arabia	16	3	19	13
Thailand	17	15	10	19
Mexico	18	13	21	12
Kazakhstan	19	14	22	17
Brazil	19	16	3	21
Morocco	20	17	23	16
Algeria	21	20	24	20
Argentina	22	12	20	22
South Africa	23	18	12	25
Nigeria	24	25	15	24
Qatar	25	2	25	23

Sources: Source: Allianz Research

Southeast Asia's strong growth potential could be further unlocked by better-performing infrastructure.

Malaysia and Vietnam rank #2 and #3 in our assessment of next-generation trade hubs, exhibiting high scores in efficiency and trade potential, but their score is structurally different. Malaysia's score is driven by both the strongest result in efficiency across the 25 next-generation trade hubs, as well as solid scores in its connectivity and trade potential. As a wealthier and larger economy, Malaysia is much better equipped with its infrastructure to access global supply chains, while providing higher end manufacturing products to the global economy than its neighbor. Vietnam scores decently in its capital and financial sector openness, yet it loses out in the connectivity and efficiency pillars. Vietnam's logistics performance has room to improve,

displaying the investment gap in the infrastructure space, especially in railways and internet connectivity. On top of this, Vietnam's banking system health is among the worst performers globally, reflecting recent concerns in the sector. The other well-performing Southeast Asian nations, including Indonesia (#5), the Philippines (#11) and Thailand (#17), show strong scores in trade potential, enhanced by strong forecasted growth, and solid results in their efficiency indicators. Similarly to Vietnam though, Indonesia, the Philippines and Thailand all perform well below average in their connectivity scores, exposing the investment gap in infrastructure throughout the Southeast Asia region, except for Malaysia.

To tap the growth opportunities, governments will have to invest heavily in upgrading port infrastructure.

More than 80% of all global trade volume and 70% of its value is transported via maritime routes. In Southeast Asia, infrastructure investment is expected to soar, with port infrastructure being a top priority during the next decade. Indonesia is expected to invest USD20bn, Vietnam between USD10bn and USD15bn, Malaysia up to USD8bn and the Philippines a much smaller quantity of around USD300mn. Meanwhile, oil-rich nations, including the UAE and Saudi Arabia, have announced investments above USD20bn for building new ports or upgrading existing ones, with the Abu Dhabi's Khalifa Port among the largest global ports. We estimate that the total amount of port investment in our next-generation trade hubs will equal USD120bn between 2025 and 2030.

Contrary to Southeast Asian countries, the strength of the connectivity indicator plays a crucial role in the presence of Middle Eastern and European countries at the top of the next-generation trade hubs ranking. Quality infrastructure in ports, airport, railways and internet connectivity have enhanced these countries' role in global trade.

The UAE (#1 in our ranking) is the world's fourth largest re-exporter hub and hosts Jebel Ali port, the 10th busiest port in the world. It has positioned itself as a trade hub connecting Asia, the Middle East region, Africa and to a lower extent Europe, thanks to its port and air infrastructure. Railways remain the worst performer of the UAE's connectivity pillars and they are the focus of one of the main infrastructure investment projects under the UAE's development plans. Similarly, Saudi Arabia (#16), and Qatar (#25) are also highly ranked, thanks to their strength in their connectivity, enabled by the investments in physical infrastructure, given their economic positioning towards hydrocarbon exports, while performing much below average on their efficiency pillar. European nations such as Romania (#6) and Hungary (#7) also perform very well in their connectivity scores, showing their strength in infrastructure and their connectivity to global supply chains, given their closeness to developed European markets. However, while they also score strongly on their trade potential, they lag behind in their efficiency scores.

In contrast, countries such as Peru (#9), Bangladesh (#12), Colombia (#13), or India (#14) show solid scores in their trade potential and efficiency pillars but poor performance in their connectivity scores. Unlike Middle Eastern countries, their competitive advantage relies on their efficiency in logistics, energy sustainability or their export growth or capital formation scores, rather than their physical infrastructure. India, Bangladesh, Peru and Colombia are growing their manufacturing capacity by sourcing from their respective regions, becoming regional manufacturing and trade hubs, while being well connected to the rest of the global trading system, acting as the gateway for their regional markets.

Finally, Türkiye (#4) and Poland (#10) are strong performers in our ranking, thanks to strong overall scores. Türkiye in particular ranks in the top 10 of all three pillars, together with Malaysia. This result demonstrates their more balanced economies with efficient labor forces, well-connected infrastructure, and still-high levels of trade and investment growth.

Choosing sides: block-building with the next generation trade hubs and beyond

In the new US-China geoeconomic order, standard competitiveness indicators are not sufficient anymore to assess countries' roles in the global trade network.

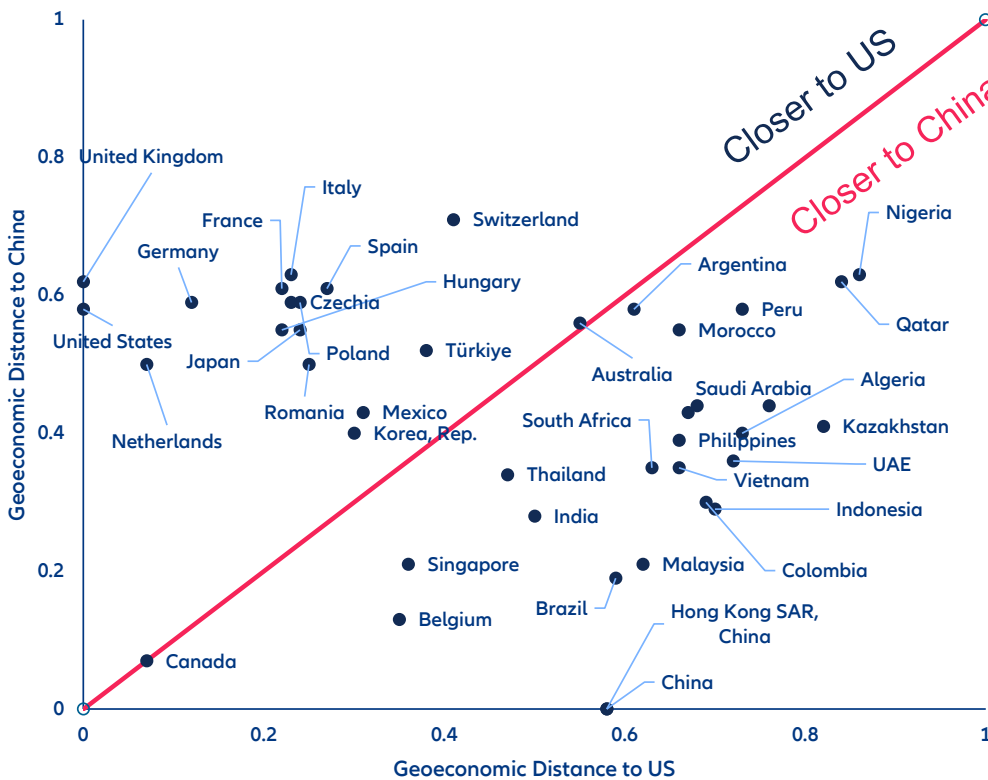
We position the next-generation trade hubs and other major economies on a scatter plot (see Figure 10), with the distance to the two hegemonies depending on how much their export structure is complementary to the import structure of the US and China, respectively, how much foreign direct investment they receive from the US and China, respectively, and how distant they are geopolitically-speaking from the US and China, respectively

Next-generation trade hubs are more frequently in China's sphere of influence, while most of the traditional "Global North" countries remain close to the US. Our analysis shows that, as things stand, the bloc centered on the US is composed of comparatively larger players in global trade, while the bloc centered on China includes

more next-generation trade hubs from the emerging world. Some countries are also not clearly in one or the other, such as Australia, Canada, South Korea or Greece. These countries are geopolitically closer to the US but retain very strong trade and investment relations with China. It is also interesting to note that our assessment puts Vietnam closer to China than it is to the US, suggesting that even though US-Vietnam relations are warming up on all fronts, this next-generation trade hub remains more dependent on China for now.

Next-generation trade hubs are likely to represent strong business opportunities going forward. These new trade hubs will continue to remain relatively attractive for investors and firms as China will continue to invest and the US will increase its trade flows with them as they will be comparatively more attractive than China from both a cost and geopolitical risk perspectives.

Figure 10: Scatter of countries, with relative distance to the US and China based on geopolitical distance, trade complementarity and foreign direct investment sorted by distance to China



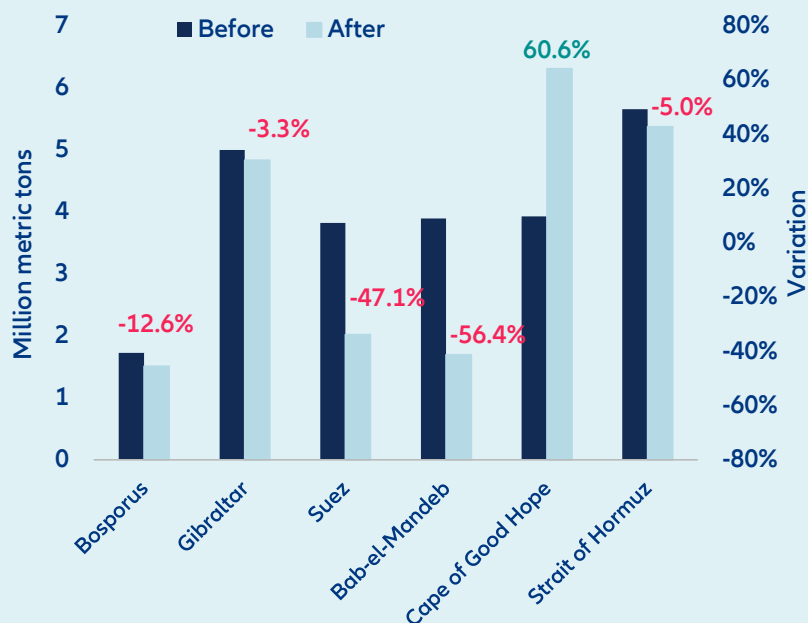
Notes: Only countries with at least 1% weight in global trade as well as those that are emerging trade hubs are shown in this table. Emerging trade hubs are highlighted in bold.

Source: Allianz Research

Geopolitics redrawing the map and reshuffling the shipping sector: The Mediterranean's waning role in a fragmented global trade landscape

One year after the resurgence of hostilities in the Middle East and the initial attacks on containerships in the Red Sea, cargo volumes through the Mediterranean access points of Suez, Gibraltar and the Bosphorus have decreased by -21% compared to the pre-conflict period. The Houthi attacks on commercial ships in the Red Sea since late 2023 have triggered disruptions in the shipping industry, altering routes and shipping freight rates. Specifically, the Suez Canal has seen a significant decline in traded volume, which has nearly halved by -47% (Figure 11). Even if some freight has been rerouted via rail, road or even air, there has been no corresponding increase in volumes through other nearby choke points. But, as expected, cargo volumes passing by the Cape of Good Hope have almost doubled, increasing by approximately 2.4mn tons per day, a 55% increase in the last reported 12 months compared to the preceding 12-month period, while the Strait of Gibraltar has experienced a -3% decrease. In fact, the role of the Mediterranean has been waning throughout. In the last 12 months, 1.4bn metric tons of goods have been rerouted, which represent a loss of over 30% of total traded goods through the Mediterranean key sea passages in a regular year.

Figure 11: Average volume of goods passing through selected chokepoints before and after the threats of the Houthis in the Red Sea (07 November 2023)

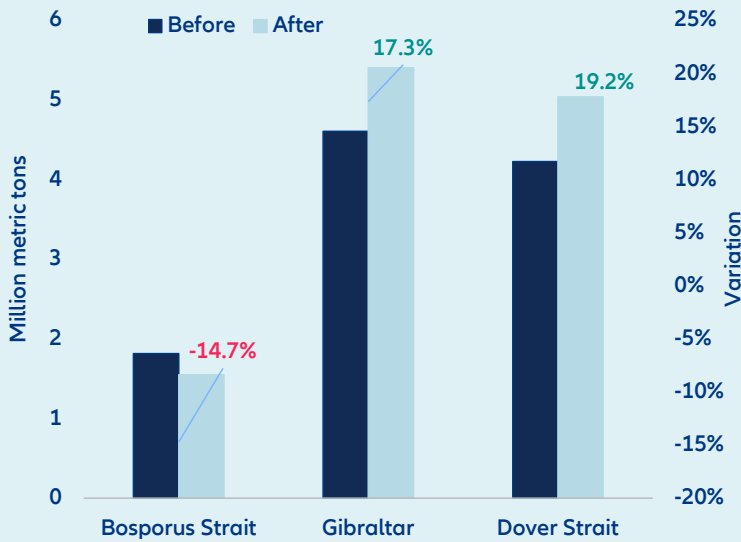


Sources: IMF Port Watch (as of end of October), Allianz Research.

Increased geopolitical tensions are indeed redesigning logistics, the viability of trade and related facilities onshore across the Mediterranean basin. The conflict between Russia and Ukraine – which began in February 2022 – has contributed to reduced transits (-14.7%) through the Bosphorus Strait, a vital maritime corridor connecting the Black Sea and the Mediterranean. Yet, in parallel, this loss has been more than compensated by increased ship transits through the Gibraltar Strait (+17.3%) and the English Channel (+19.2%), particularly with liquefied natural gas and oil cargoes replacing reduced pipeline flows from Russia. Importantly, reduced trade in the Black Sea has led to significant investment in land infrastructure to avoid bottlenecks and allow goods to reach destination markets before they perish, as in the case of grains.

Detour ahead: the environmental toll of taking the long route. New shipping routes are having a negative impact on the planet. The rerouting of containerships around the southern tip of Africa, bypassing the Suez Canal, significantly increases transportation times and distances. For instance, for a containership going from Asia to Europe, detouring through the Cape of Good Hope can more than double the journey duration if compared to the conventional shorter voyage of crossing the Red Sea. Because of the extended travel time, vessels need more marine fuel to navigate, which directly leads to higher CO₂ emissions from burning oil. This route shift not only raises operational costs (including fuel, manpower and ship leasing) but also exacerbates the already negative environmental impact of the shipping sector. This is especially worrying because the Houthis' threats have already lasted a year and there is still little visibility as to when the conflict will end.

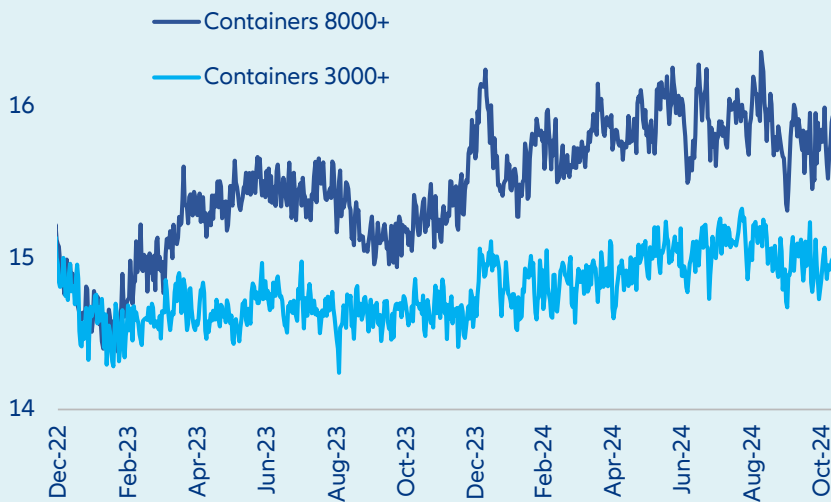
Figure 12: Average volume of goods passing through selected chokepoints before and after the invasion of Ukraine (24 February 2022)



Sources: IMF Port Watch (as of end of October), Allianz Research

Going faster, polluting harder: the high-speed shipping conundrum. In response to longer shipping routes, many shipping companies have been increasing the speed of their vessels to improve their delivery schedules, overcome congestion delays and meet customer demand (Figure 13). However, this strategy comes with significant environmental costs as the faster a vessel travels, the more fuel it consumes per unit of distance. According to Sea Intelligence, a +1% speed increase usually produces a +2.2% increase in fuel consumption and therefore in carbon emissions. Figure 13 shows that the average speed of large containerships has already surpassed 16 knots this year, from 14.5 knots at the beginning of 2023 (+10%), which translates into an increase of around +22% in CO₂ emissions (*ceteris paribus*). If we add the longer distances of today’s trade routes, the total carbon emission increase is likely around +50% because of geopolitics. This intensified fuel consumption directly contradicts the sector’s greening goals, and the shipping industry is already under pressure to reduce its carbon footprint in line with global climate targets. By accelerating speeds, shipping companies are inadvertently making it harder to meet the emissions reduction targets set by international initiatives like the International Maritime Organization’s carbon intensity standards and the broader goals of the Paris Agreement.

Figure 13: Daily average speed of containerships (knots), by vessel size



Sources: Workspace LSEG, Allianz Research

Appendix

Methodology for our next-generation trade hubs index

We assess all emerging markets around three pillars, **efficiency, connectivity and trade potential**, to identify which countries will play a bigger role in the complexified trading and financial system.

Looking at **efficiency**, we identify which emerging markets are more competitive to operate in, combining labor productivity, logistics performance, banking health and energy security and sustainability. Through this 360° lens, we look at competitiveness in a wider perspective. While labor productivity allows us to identify emerging markets that continue to offer lower relative labor costs, essential for any trade hub, assessing it next to logistics performance and energy security, we can understand better how a country's costs go beyond labor. Our logistics performance indicator derived from the World Bank looks at several characteristics of trade-related infrastructure and processes. It assesses the quality of trade and transport infrastructure as well as logistics services, the timeliness of shipments and ability to arrange high quality ones, but also the efficiency of tracking and tracing services, and customs and border management. Regarding energy security and sustainability, we consider energy use per GDP, renewable electricity output or water stress. This helps us understand the impact of global energy price volatility and the energy independence of a country, while also considering energy sustainability, which we believe will remain a crucial aspect of market and business decisions going forward. Finally, banking health is evaluated by examining the Financial Soundness Indicators of the International Monetary Fund to understand how a country's capital markets provide liquidity and solvency to the financial system. Nations in South and Southeast Asia and Latin America overperform under the efficiency pillar. Malaysia, India, Chile and Brazil rank among the top performers.

Connectivity is essential for any trade hub. Our methodology considers a country's infrastructure quality by looking at all major transportation methods, as well as access to the internet, to get a clear picture. We assess port connectivity by looking at container port traffic, the railway system quality by assessing goods transported by railways and air transportation by looking at air freight. Countries in the Middle East and Eastern Europe already well plugged into existing global supply chains and with well-developed infrastructure capacity overperform in this pillar. The UAE, Saudi Arabia, Hungary or Romania are among the top ranked.

The first two pillars, efficiency and connectivity, allow us to understand already established trade hubs that will remain relevant in the future. To enable us to look beyond already established hubs, our index also accounts for **trade potential**. We consider trade freedom by assessing the tariffs and non-tariff barriers that a country has in place. Furthermore, we look at the potential of trade growth a country has by considering our trade forecasts for the upcoming two years. On top of trade, our trade hub trade potential pillar considers investment and financial freedom. By examining current investments, both private and public, we can gauge how each country is investing in itself for future opportunities. The Chinn-Ito capital openness indicator measures the degree of a country's financial openness and its integration into the global financial system. It is on this pillar that future trade hubs emerge on top of the ranking next to already established hubs that will continue to be top players in global trade, such as Vietnam, Indonesia, Hungary, or Turkey.

Finally, to ensure relevance to global economic dynamics, our index includes only those countries with a projected nominal GDP exceeding USD120bn in 2024. This threshold accounts for economic size, allowing the index to focus on nations with substantial economic influence.



Our
team

Chief Economist
Allianz SE



Ludovic Subran
ludovic.subran@allianz.com

Head of Economic Research
Allianz Trade



Ana Boata
ana.boata@allianz-trade.com

Head of Insurance, Wealth & ESG Research
Allianz SE



Arne Holzhausen
arne.holzhausen@allianz.com

Macroeconomic Research



Lluis Dalmau
Economist for Africa &
Middle East
lluis.dalmau@allianz-trade.com



Maxime Darmet Cucchiarini
Senior Economist for UK, US & France
maxime.darmet@allianz-trade.com



Jasmin Gröschl
Senior Economist for Europe
jasmin.groschl@allianz.com



Françoise Huang
Senior Economist for Asia Pacific
francoise.huang@allianz-trade.com



Maddalena Martini
Senior Economist for Italy, Spain,
Greece & Benelux
maddalena.martini@allianz.com



Luca Moneta
Senior Economist for Emerging
Markets
luca.moneta@allianz-trade.com

Corporate Research



Ano Kuanathan
Head of Corporate Research
ano.kuanathan@allianz-trade.com



Maria Latorre
Sector Advisor, B2B
maria.latorre@allianz-trade.com



Maxime Lemerle
Lead Advisor, Insolvency Research
maxime.lemerle@allianz-trade.com



Sivagaminathan Sivasubramanian
Data Analyst
Sivagaminathan.Sivasubramanian@allianz-trade.com

Capital Markets Research



Jordi Basco Carrera
Lead Investment Strategist
jordi.basco_carrera@allianz.com



Bjoern Griesbach
Senior Investment Strategist &
Eurozone Economist
bjoern.griesbach@allianz.com



Yao Lu
Investment Strategist
yao.lu@allianz.com

Insurance, Wealth and ESG Research



Michaela Grimm
Senior Economist,
Demography & Social Protection
michaela.grimm@allianz.com



Patrick Hoffmann
Economist, ESG & AI
patrick.hoffmann@allianz.com



Hazem Krichene
Senior Economist, Climate
hazem.krichene@allianz.com



Patricia Pelayo-Romero
Senior Economist, Insurance & ESG
patricia.pelayo-romero@allianz.com



Kathrin Stoffel
Economist, Insurance & Wealth
kathrin.stoffel@allianz.com



Markus Zimmer
Senior Economist, ESG
markus.zimmer@allianz.com

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Director of Publications

Ludovic Subran, Chief Economist
Allianz Research
Phone +49 89 3800 7859

Allianz Group Economic Research

https://www.allianz.com/en/economic_research
<http://www.allianz-trade.com/economic-research>
Königinstraße 28 | 80802 Munich | Germany
allianz.research@allianz.com


 @allianz

 allianz

Allianz Trade Economic Research

<http://www.allianz-trade.com/economic-research>
1 Place des Saisons | 92048 Paris-La-Défense Cedex | France
research@allianz-trade.com

 @allianz-trade

 allianz-trade

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