DMCC

THE FUTURE OF TRADE

SNAPSHOT

2024

DECOUPLED AND RECONFIGURED


DMCC

The Future of Trade: Snapshot

INTRODUCTION AND EXECUTIVE SUMMARY

INTRODUCTION: NAVIGATING NEW CHALLENGES AND OPPORTUNITIES

The Future of Trade 2024, DMCC's fifth edition of its biennial flagship report, explores the evolving power dynamics shaping the global trade landscape amidst significant change.

The emergence of new political and economic alliances, increasing geopolitical tensions, and significant industry shifts, such as the "chip war" between the United States and China, the sweeping changes brought about by AI and the drive toward carbon net zero, are redefining the future of trade.

This report delves into how geopolitics, sustainability, technology, and finance are interacting to reshape trade dynamics, reflecting on past predictions and analysing the evolution of trade in the context of ongoing global crises that continue to influence policy and consumer behaviour.

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EXECUTIVE SUMMARY

As we enter a period of profound global change, new challenges and opportunities are emerging that promise to reshape trade for decades. Agility and foresight are critical as businesses and governments navigate a landscape brimming with potential.

THE SIGNIFICANT SHIFTS IN GLOBAL TRADE

Accelerated regionalisation: Influenced by geopolitics, climate concerns, and technology, we are witnessing a significant shift from globalisation to regionalisation. This shift is expected to strengthen as new trade blocs form and countries seek resilience over cost-efficiency in their supply chains.

Restructuring of supply chains: Ongoing political upheavals, economic nationalism, and climate impacts are prompting businesses to reconfigure supply chains, moving towards friendshoring and reducing dependencies, particularly on China.

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Technological and environmental advances: The rapid adoption of AI and a greater focus on sustainability are set to be major drivers of trade, fostering new commodity demands and creating trade hubs centered around digital and environmental goods.

THE DRIVERS OF CHANGE:

Geopolitical events, including elections in key economies, could increase economic nationalism and trade protectionism, affecting global trade policies and economic relations.

The global drive to carbon net zero is shifting the trade landscape. Trade is accelerating in environmental goods and technologies as well as clean and renewable forms of energy to support the energy transition. The landscape is rich in opportunity but risks remain. The EU's carbon border adjustment mechanism is part of a broader move towards integrating environmental goals in trade policies, but which could lead to new tariff barriers and trade protectionism.

Technological innovations, particularly AI, are poised to revolutionise trade practices, enhancing efficiency and inclusivity but also requiring careful navigation around regulatory and data harmonisation issues.

OPPORTUNITIES AND RISKS:

The growing emphasis on regional trading agreements and the restructuring of supply chains present opportunities to forge new trading relationships and enhance economic resilience.

Climate change and the transition towards sustainable technologies offer both challenges and opportunities, as businesses and countries adjust to new consumer preferences and regulatory landscapes.

The digital transformation of trade, through AI and blockchain, offers potential to streamline and secure trade finance and operations but also introduces challenges related to adoption and integration across diverse regulatory environments.

STRATEGIC IMPLICATIONS:

Businesses must stay vigilant and adaptable to leverage new opportunities and mitigate risks arising from rapid economic, technological, and political changes.

Policymakers play a crucial role in creating supportive regulatory frameworks that foster innovation and adapt to the changing needs of global trade, particularly in technology and environmental policy.

ABOUT THE REPORT

The Future of Trade 2024 provides insights from global experts and roundtables, predicting key trends and offering strategic advice for navigating the complexities of the modern trade landscape. With profound transformations underway, understanding these dynamics is essential for businesses and policymakers to make informed decisions that will shape their success in the emerging global trade environment

MAIN FINDINGS

Trade will grow – albeit slowly. All regions will experience export growth over the next two years, with North America, Asia and Africa leading the way.

Regionalisation will accelerate, marked by friendshoring strategies and trade hubs centred around Asia and North America.

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Geopolitical tensions and conflicts will heavily shape supply chain restructuring strategies, leading to a rerouting of trade and potential inflationary pressure.

Digital services will surge, driven by the dawn of generative AI.

Carbon pricing and trading systems will significantly change the nature of trade, favouring lower carbon-intensive producers and sustainable products.

Risks to trade growth include high inflation, elevated interest and the slowdown of the Chinese and European economies.

The widespread adoption of AI will drive greater trade efficiencies.

The battle for supremacy in semiconductors will become more prominent amid the U.S. and China chip war, with knock-on effects across industries and the green transition.

The trade finance gap is likely to remain high or even widen.

Supply chain reconfiguration will allow for the development of new consumer markets and production hubs.

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THE OUTLOOK FOR GLOBAL TRADE

INTRODUCTION

The landscape of global trade is poised for growth, albeit at a gradual pace. After a 1.2% decline in merchandise trade volumes in 2023, the World Trade Organisation (WTO) forecasts a rebound, with growth expected at 2.6% in 2024 and 3.3% in 2025, reflecting similar trends in global GDP projections.

Economic pressures and geopolitical risks

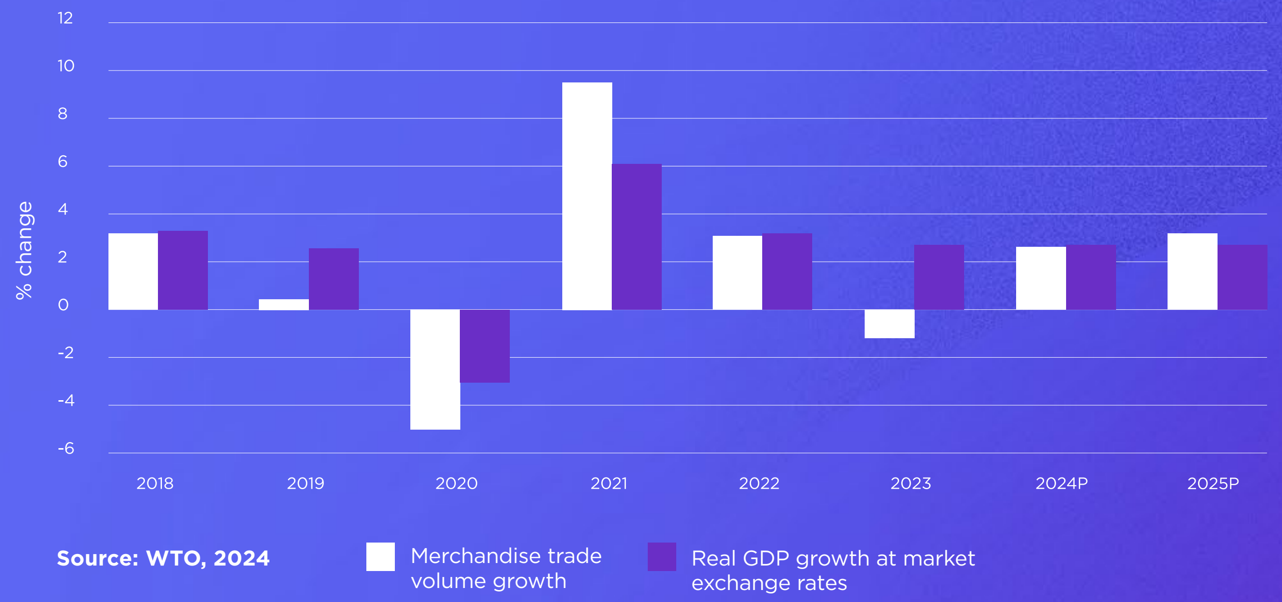
The road to recovery is, however, fraught with challenges:

Economic slowdowns: Significant downturns in major economies like China and Europe are dampening the global trade outlook.

Inflation and geopolitical tensions: High inflation and geopolitical unrest continue to threaten stability, with risks such as sea shipment disruptions and rising protectionism impacting trade dynamics.

FIGURE 1

Merchandise trade volume and GDP growth, 2018-2025



Source: WTO, 2024

Driving forces behind trade resilience

Several factors are set to bolster the resilience of global trade:

Digital transformation: The surge in e-commerce and digital services, catalysed by the COVID-19 pandemic, shows no signs of slowing down. This sector is anticipated to expand further, fueled by the growing young consumer base and increased internet penetration globally.

Technological advancements: The advent of Artificial Intelligence (AI) is set to revolutionise sectors from logistics to trade finance, streamlining operations and enhancing efficiencies.

Sustainability and energy transition: The shift towards renewable energy and sustainable practices is fostering new trade opportunities in green technologies.

Geopolitical and macroeconomic influences

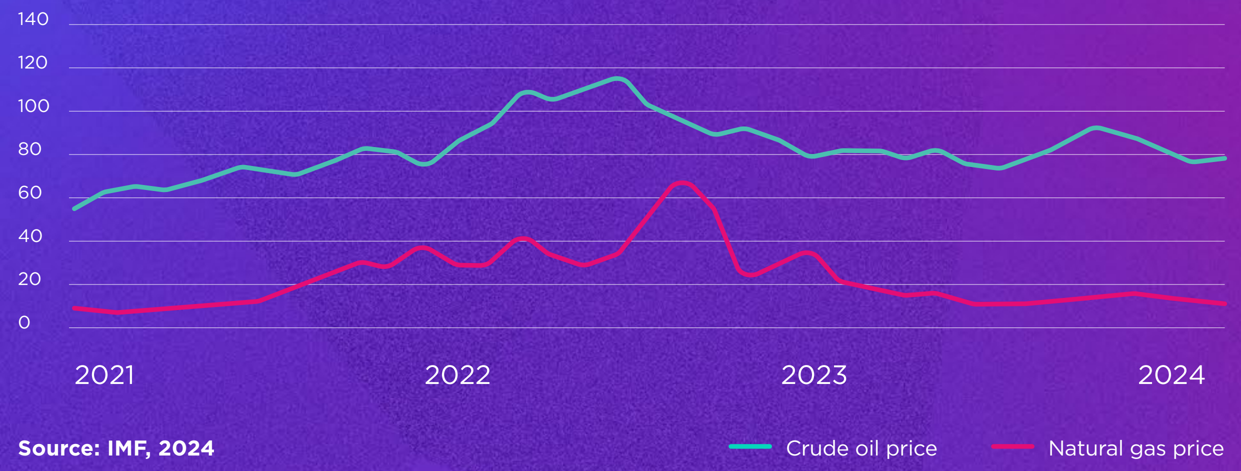
Trade is also being shaped by geopolitical and macroeconomic factors:

Volatility in commodity markets: Recent years have seen significant fluctuations in commodity prices, exacerbated by geopolitical conflicts in Europe and the Middle East, which have disrupted traditional trade patterns, rerouted shipping, and caused spikes in prices for oil, natural gas, grains, and other commodities.

Emerging markets and diversification: Fast-growing emerging markets like Mexico, Vietnam, and India are emerging as significant players, offering alternative manufacturing hubs and reshaping global supply chains.

FIGURE 2

Crude oil and natural gas prices, Jan 2021 - Jan 2024 ($)



Source: IMF, 2024

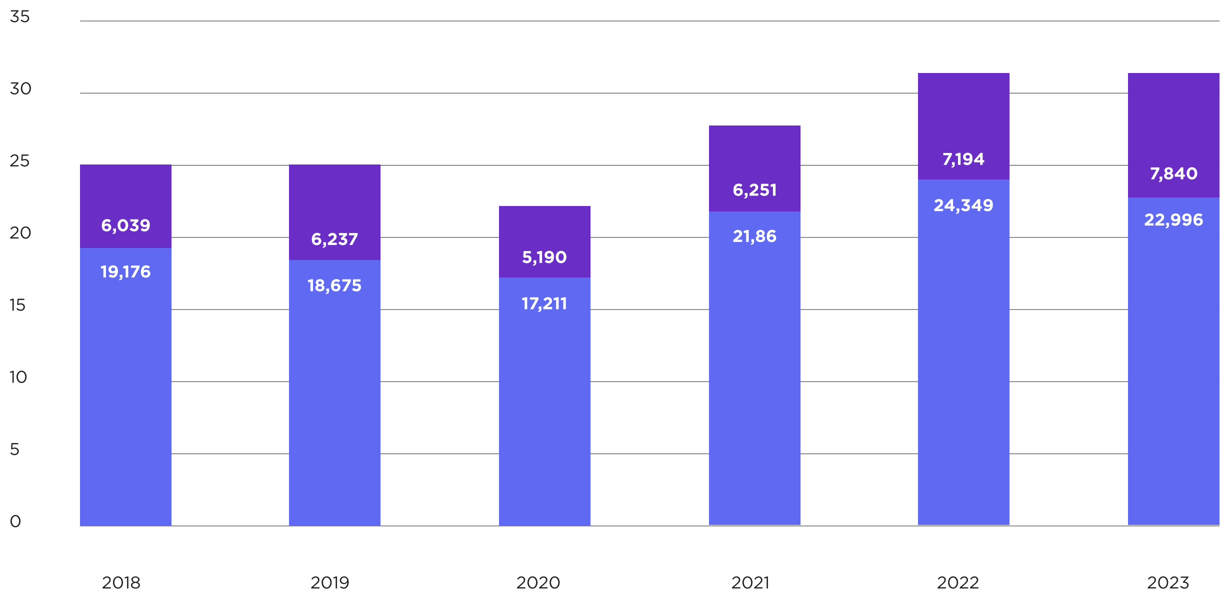
Regional developments

Middle East and Asia: These regions are capitalising on their relatively neutral geopolitical stances and strategic locations to enhance their roles in global trade, particularly in facilitating trade between East and West and within the Global South.

Green and digital growth: The Middle East and Europe, despite facing challenges, are expected to see growth in exports driven by both the green transition and digital services. The latter continues to grow robustly in the Middle East, underpinned by high internet penetration and the expansion of e-commerce.

FIGURE 3

World trade in goods and services, 2018-2023 ($ trillions)



Source: WTO (2024) Goods Commercial Services

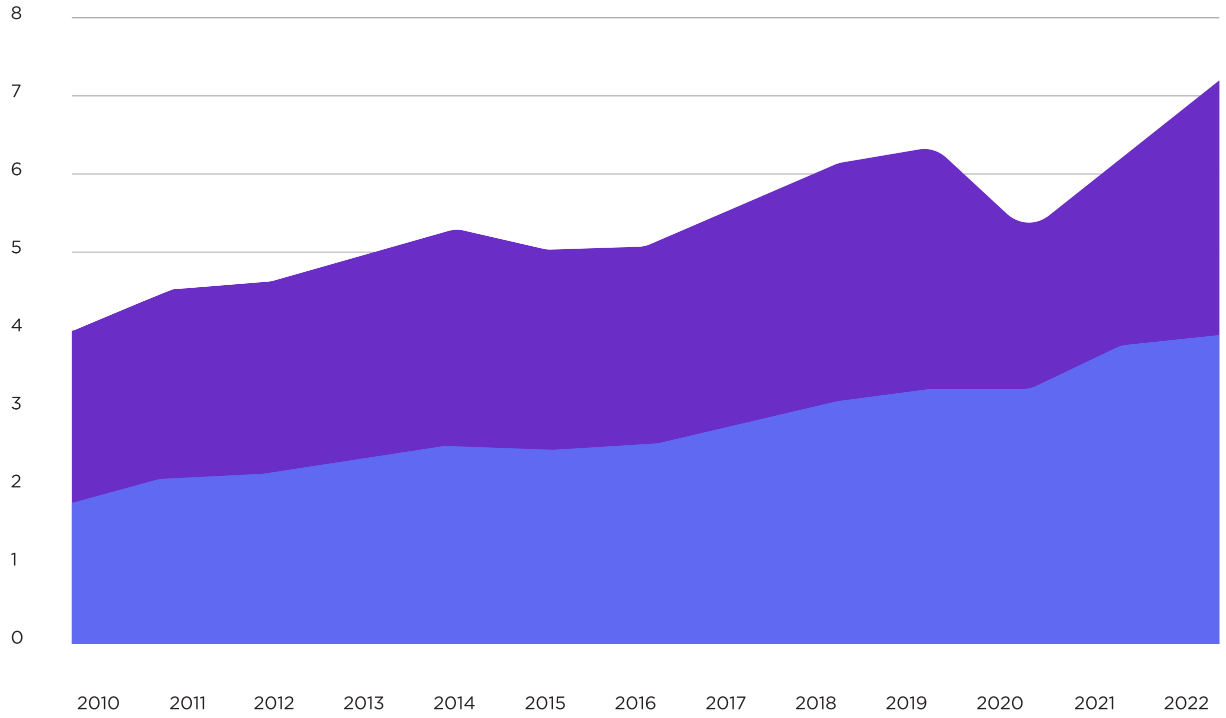
While goods still dominate global trade volumes, services are rapidly catching up. In 2023, the trade in services grew by 9%, outpacing the growth in goods.

Trade volumes: While goods still dominate global trade volumes, services are rapidly catching up. In 2023, the trade in services grew by 9%, outpacing the growth in goods.

Digital and remote services: The shift towards remote and digitally delivered services is likely to continue, enhancing the global reach of sectors such as entertainment, consulting, and tech services.

FIGURE 4

Global exports of services 2010-2022 ($ trillion)



Source: UNCTAD Stats (2023) Digitally delivered service exports Total service exports

Conclusion

As we advance, the landscape of global trade is increasingly influenced by technology and sustainability. The integration of AI and the growth in green technologies are not just trends but are becoming central pillars of trade strategies. These elements, combined with robust geopolitical strategies and economic policies, will dictate the pace and direction of global trade growth in the coming years.

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TRANSFORMATIVE FORCES OF TRADE

OVERVIEW

Recent years have underscored how swiftly unforeseen crises can reshape global trade, revealing the deep interconnections between structural changes in the world economy and societal shifts. The key transformative forces—increased regionalisation, supply chain restructuring, and the advancement of artificial intelligence (AI)—are poised to significantly alter the trade landscape.

Increasing regionalisation as a response to geopolitics

Geopolitics and macroeconomic risks are driving a shift towards regionalisation, moving away from the long-standing trend of globalisation. The COVID-19 pandemic highlighted vulnerabilities in global supply chains, such as the lack of alternative suppliers and the collapse of just-in-time delivery systems. This shift is further exacerbated by sluggish economic performances of China and Europe, and heightened geopolitical tensions, including conflicts that disrupt trade routes and lead to increased consumer costs.

Significantly, trade agreements like the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), Regional Comprehensive Economic Partnership (RCEP), and African Continental Free Trade Area (AfCFTA) are strengthening regional trade corridors. These agreements reduce trade barriers, harmonise regulations, and enhance economic cooperation, thus fostering regional economic blocs that could redefine global trade dynamics.

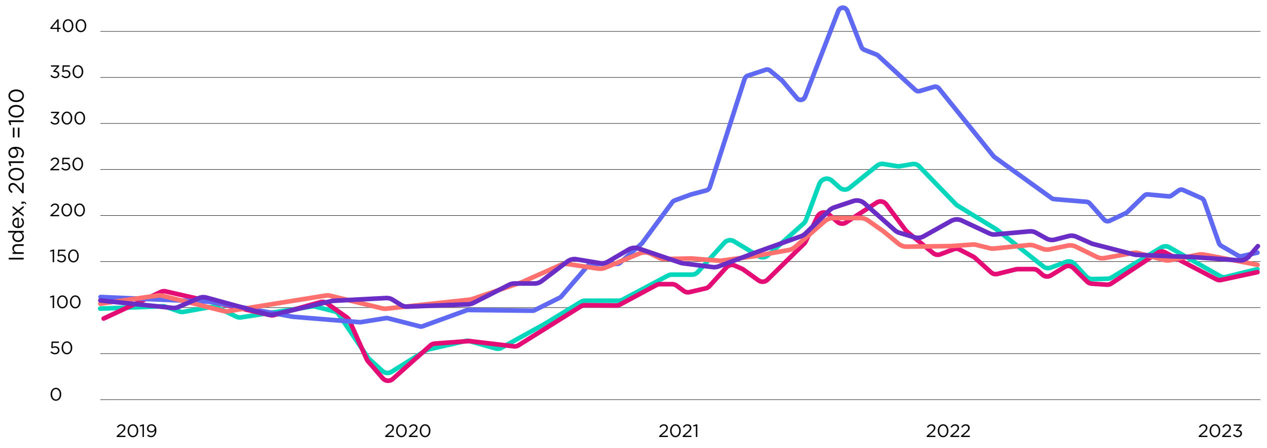
Supply chain reconfiguration due to regionalisation

The move towards regionalisation has prompted companies to prioritise reliability and security over cost in their supply chains. High-profile disruptions such as the COVID-19 pandemic and geopolitical conflicts like Russia's invasion of Ukraine have triggered significant supply chain challenges, particularly in critical commodities like oil, gas, and fertilizers. The ongoing U.S.-China tensions over tariffs and technology exports (notably semiconductors) further complicate global trade, pushing companies to diversify their supply sources to countries less affected by these tensions, such as Vietnam and Mexico.

This environment compels companies to proactively enhance their supply chain resilience, preparing for potential prolonged disruptions by diversifying suppliers and strengthening their logistical frameworks.

FIGURE 5

Global average primary commodity prices, 2019-2023
Index 2019=100 and US$ per million Btu



Source: WTO (2024)

Digital trade expansion and AI integration

Technological advances over the last decade, including automation, robotics, and digitalisation, have already transformed production processes and supply chain management. The expansion of e-commerce and digital trade has been particularly notable, with a significant increase in cross-border online retailing. These sectors have shown remarkable resilience to external shocks, leading to a broader expansion of trade in services and digital goods.

AI stands out as a particularly disruptive technology, surpassing even blockchain in its potential to reshape business operations and global trade. AI enhances supply-side efficiencies, automates decision-making, and powers new solutions in trade finance and customer service. However, the regulatory frameworks necessary to govern AI's integration into global trade remain underdeveloped, posing potential hurdles to realising its full potential.

Conclusion

The forces reshaping global trade are complex and multifaceted, driven by rapid technological advances and shifting geopolitical landscapes. Companies that adapt to these changes by investing in new technologies and diversifying their operations will likely find themselves better positioned in a rapidly evolving global market. The next decade will be critical as these transformative forces become more pronounced, influencing all aspects of global trade from production to consumer engagement.

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DRIVERS AND DYNAMICS OF TRADE RESILIENCE

OVERVIEW

Trade growth is projected to continue in the coming years, albeit at a gradual and uneven pace, demonstrating the inherent resilience of global trade amidst a multitude of destabilising forces. Effective strategies by governments and industries to mitigate risks are crucial for ensuring trade continuity.

Economic challenges impacting global trade

China's economic influence: As the world's second-largest economy and a primary trading partner for numerous countries, China's economic downturn significantly impacts global trade. The crisis in China's property market and the resulting defaults pose substantial challenges to global growth.

Europe's economic stagnation: Europe is grappling with high energy costs and Germany's economic downturn, contributing to a weakened euro and reduced consumer buying power. This slowdown affects global trade by diminishing European demand and investment confidence.

Inflation dynamics

Global inflation trends: Initiated by the COVID-19 economic shock and exacerbated by supply chain disruptions and geopolitical tensions, global inflation surged but is expected to gradually decline from 6.9% in 2023 to 4.6% by 2025. While decreasing inflation may relieve some pressure on producer margins and stabilise prices, high interest rates will likely curb economic growth potential.

Strategic business responses: In response to inflation and its associated challenges, businesses are advised to optimise operational costs and enhance supply chain resilience to mitigate risks related to disruptions and logistics.

Interest rates and financial policies

Persistently high interest rates: Despite a desire to reduce them, key financial institutions like the Bank of England and the U.S. Federal Reserve predict that interest rates will remain elevated to combat ongoing inflation. High borrowing costs dampen investment and consumer spending, complicating global trade dynamics.

Currency strength and trade implications

Dollar appreciation: The strong U.S. dollar, which dominates global trade transactions, makes U.S. exports more expensive and reduces demand. This dynamic affects not only the U.S. but also countries with dollar-pegged currencies or significant dollar reserves. A prolonged strong dollar is expected to continue affecting global trade, especially in emerging markets.

Trade resilience strategies

Diversification and risk management: To combat the vulnerabilities exposed by dollar strength, inflation, and interest rates, businesses and countries should focus on diversifying production hubs and consumer markets, particularly towards rapidly urbanising regions in Asia-Pacific and other emerging economies.

Environmental goods and digital services: The increasing global emphasis on sustainability is boosting the trade in environmental goods, while advancements in technology are expanding the trade in digital services. These sectors present significant growth opportunities but also introduce new risks, such as trade tensions related to technological and environmental products.

Policy and regulatory frameworks

Regionalisation and trade policies: With accelerated regionalisation, governments must prioritise trade liberalisation and facilitation through regional and bilateral agreements. Ambitious regulatory frameworks are also necessary to leverage technology, including AI, in ways that protect consumers without inhibiting innovation.

Conclusion

The section underscores the complexity of the global trade environment, highlighting the interplay between economic downturns, inflation, currency dynamics, and regulatory challenges. It emphasises the importance of strategic diversification, advanced technological integration, and robust policy frameworks to sustain and enhance trade resilience in a fluctuating global market.

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Recommendations for businesses:

1. **Diversify export markets**: Despite slow growth, there are opportunities for export expansion, particularly in North America and emerging markets in Asia-Pacific and Africa. Businesses should adopt diversification strategies for their export markets to capitalise on growth opportunities in these regions.

2. **Reconfigure supply chains against geopolitical shifts**: Rapid reconfiguration of trade flows due to geopolitical tensions presents both challenges and opportunities. Businesses should be prepared to adapt to these changes by building flexible supply chains and exploring new markets and partnerships. Diversification of suppliers and investing in alternative sourcing strategies can also help mitigate supply chain disruptions.

3. **Mitigate macroeconomic risks**: Against a backdrop of global economic uncertainty, businesses should proactively monitor conditions such as economic slowdowns, currency fluctuations, inflation, and taxation. Strategies should be considered to mitigate risks associated with these factors, including cost optimisation.

4. **Invest in digital transformation and innovation**: Against a tide of technological advancement, the dawn of AI stands to revolutionise trading systems. Companies that invest in understanding AI and how to build use cases stand to benefit. Those that do not run the risk of losing out to competition.

Recommendations for governments:

1. **Build new trade relationships**: Governments should make trade promotion a core policy objective and foster trade partnerships beyond traditional markets. Encouraging exports to regions with strong growth potential can help build new consumer bases, mitigate the impact of slow global trade growth and enhance resilience against economic fluctuations.

2. **Invest in digital infrastructure and innovation**: Recognising the growth potential of digital services trade, governments should prioritise investments in digital infrastructure and innovation ecosystems. Supporting the development of AI technologies and digital trade platforms can unlock new opportunities for economic growth and competitiveness.

3. **Strengthen industry supply chain security**: Given the intensifying competition between regions and the strategic importance of commodities and minerals, governments should prioritise measures to strengthen supply chain security. This may include diversifying sourcing locations, promoting domestic production of critical goods, and enhancing collaboration with international partners to ensure reliable access to essential resources.

4. **Facilitate regional integration and cooperation**: Geopolitical tensions are driving a shift towards greater regionalisation in trade flows. Governments should actively promote regional integration and cooperation initiatives to capitalise on emerging opportunities and mitigate risks associated with geopolitical instability. Creating frameworks for cross-border trade facilitation and harmonising regulatory standards can foster economic resilience and sustainable development.

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THE GEOPOLITICS OF TRADE

New alliances, new trade routes

The past few decades of secure international trade environments have shifted dramatically to a scenario fraught with geopolitical and macroeconomic uncertainties. This shift is significantly impacting global trade dynamics, making resilience and adaptability key traits for businesses and governments alike. The Future of Trade survey of over 100 business leaders highlighted geopolitical tensions, particularly between China and the United States, as the foremost challenge to trade growth, with a significant impact also from rising nationalism and onshoring trends. These factors are influencing trade policies increasingly driven by ideology and economic security rather than pure economic efficiency.

Supply chain restructuring for security and trade resilience

The push towards friendshoring and nearshoring is reshaping global supply chains, aiming to mitigate disruptions and bolster trade resilience. This strategy is crucial in sectors reliant on critical materials, where alternatives are limited, thus making them vulnerable to geopolitical shifts. The restructuring is also influenced by a realignment of geo-economic strategies post-COVID-19, focusing on reducing dependency on contentious geopolitical players.

Regionalisation redrawing trade architecture

The transformation into a multipolar trade world continues as anticipated, with regions like North America, Europe, and a China-centric Asia diversifying their trade partners. This shift is creating new regional trade dynamics and opportunities, especially for rising middle powers and non-aligned countries. The increasing regionalisation is supported by multilateral agreements like RCEP, CPTPP, and USMCA, which are aimed at reducing tariffs and fostering regional trade connections.

Geopolitical tensions and economic nationalism driving uncertainty

With numerous global elections scheduled for 2024, there's a potential rise in protectionist policies, especially in the United States, where political outcomes could significantly influence global trade policies. Economic nationalism is increasing globally, necessitating businesses to adapt swiftly to changing regulations and trade barriers.

Conflicts and tensions fueling trade instability

Ongoing geopolitical conflicts, such as those in Europe and the Middle East and the sustained tensions between the United States and China, are reshaping economic landscapes and causing major disruptions in vital global supply routes. These tensions are expected to escalate the risk of supply chain dislocations and alter global trade volumes, necessitating robust risk management strategies.

Emerging production hubs and the decline of China's dominance

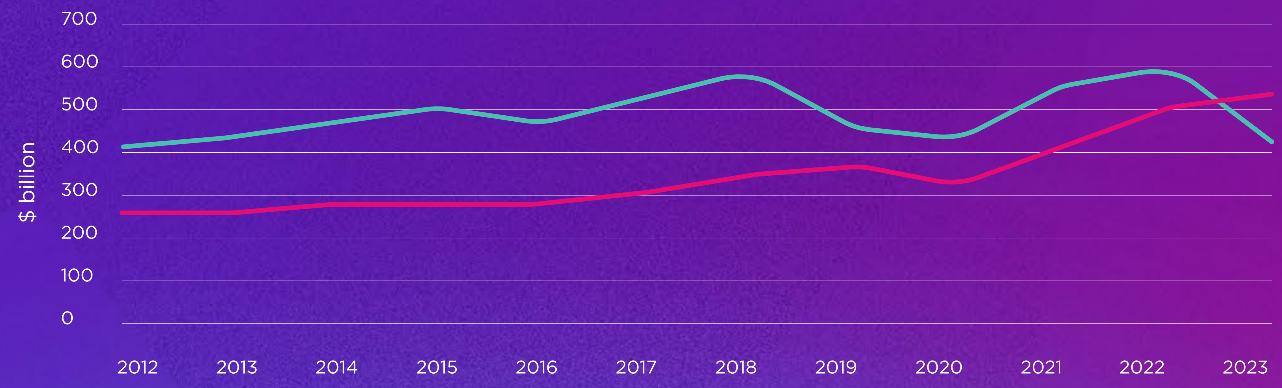
In response to geopolitical shifts, particularly U.S.-China tensions, new production hubs are emerging as alternatives to China. This shift is partly due to strategic decoupling efforts like the U.S. Inflation Reduction Act and the CHIPS Act. Countries like Vietnam, Thailand, South Korea, and Mexico are becoming significant players in diversifying global supply chains away from China, providing new opportunities and challenges in global trade.

Technology and climate as new battlegrounds

The United States is actively seeking to limit China's influence in high-tech sectors by bolstering domestic capabilities in sectors like battery technology, biotechnology, semiconductors, and clean energy. These efforts are reshaping trade relationships and creating new competitive dynamics in the global trade arena.

FIGURE 6

US total goods imports ($bn) 2012-2023



Source: UN Comtrade Database (2024)

US imports from China
US imports from Mexico

Conclusion

The current geopolitical landscape of trade is characterised by significant shifts towards regionalisation, supply chain restructuring, and the emergence of new trade battlegrounds influenced by technological and environmental factors. Companies and governments must navigate these changes strategically to maintain stability and growth in the global economy. The ongoing geopolitical tensions, notably between the United States and China, coupled with regional conflicts, pose continuous challenges and opportunities for reshaping global trade practices and partnerships.

Recommendations for businesses:

1. **Elevate geopolitical risk awareness**: Geopolitical risk should be a top-level concern, addressed by both the board and executive committee. Regular scenario planning sessions, involving key decision-makers, are essential to anticipate potential geopolitical developments and their implications for business operations. This proactive approach enables businesses to develop contingency plans and mitigate risks effectively.

2. **Monitor economic security policies to maintain operational resilience**: Economic security considerations are increasingly shaping domestic government policies. Businesses should stay vigilant and continuously monitor potential shifts in government policies, and their impacts on business operations. Analyse the potential consequences of policy changes, both intended and unintended, to adapt strategies accordingly and maintain operational resilience.

3. **Communicate supply chain risks to key stakeholders**: Proactively engage with authorities and other critical stakeholders to communicate the risks facing supply chains. By fostering open dialogue and sharing insights, businesses can contribute to informed decision-making on trade policy and negotiations.

4. **Prepare for regulatory changes**: Businesses should anticipate an increasingly protectionist regulatory environment and be prepared to adapt accordingly. This may involve restructuring operations, establishing new legal entities, or relocating business activities to align with evolving regulations.

5. **Regularly assess supply chain vulnerabilities**: Continuously review supply chains to identify vulnerabilities and assess potential disruption risks from regional shocks. Conducting regular risk assessments allows businesses to proactively address weak points in their supply chains and implement mitigation strategies to minimise the impact of unforeseen events.

6. **Develop regional expertise and local intelligence**: As supply chains are restructured in response to geopolitical shifts, understanding diverse national laws, regulations, data restrictions, and trade barriers becomes increasingly important. Businesses should invest in resources and capabilities that facilitate effective risk management, such as developing regional expertise and local knowledge.

Recommendations for governments:

1. **Develop trade diversification strategies to mitigate geopolitical risk**: By diversifying trade partners and markets, governments can reduce dependence on volatile regions and enhance economic resilience. Trade policymakers should prioritise strategic trade diversification initiatives to adapt to the rerouting of trade driven by geopolitical tensions. This includes fostering partnerships with fast-growing emerging markets like Mexico, Vietnam, and other ASEAN members.

2. **Consider financial support for critical import supply chain resilience**: Recognising the changing dynamics of supply chain strategies, governments should incentivise businesses to boost resilience and economic security. This may involve providing financial incentives, tax breaks, or subsidies to encourage investment in local manufacturing capabilities, diversification of suppliers, and adoption of resilient supply chain practices.

3. **Build partnerships with the UAE and other global trade facilitators**: Countries like the UAE and ASEAN member states are poised to benefit from their geopolitical neutrality and diverse trade relationships. Governments should foster partnerships and trade agreements with these powers to facilitate increased trade flows and investment opportunities. By leveraging their strategic geographic locations and trade-friendly policies, they can serve as key hubs for regional trade and economic integration.

4. **Support efforts to reform the WTO**: The World Trade Organisation fulfils a critical role in the global trade landscape. Governments must actively engage with reform efforts to address the existential challenges facing the WTO and ensure its relevance and effectiveness in the future. Most urgently, this includes finding solutions to the dispute resolution mechanism impasse.

THE DAWN OF AI AND THE TRANSFORMATION OF GLOBAL TRADE

OVERVIEW

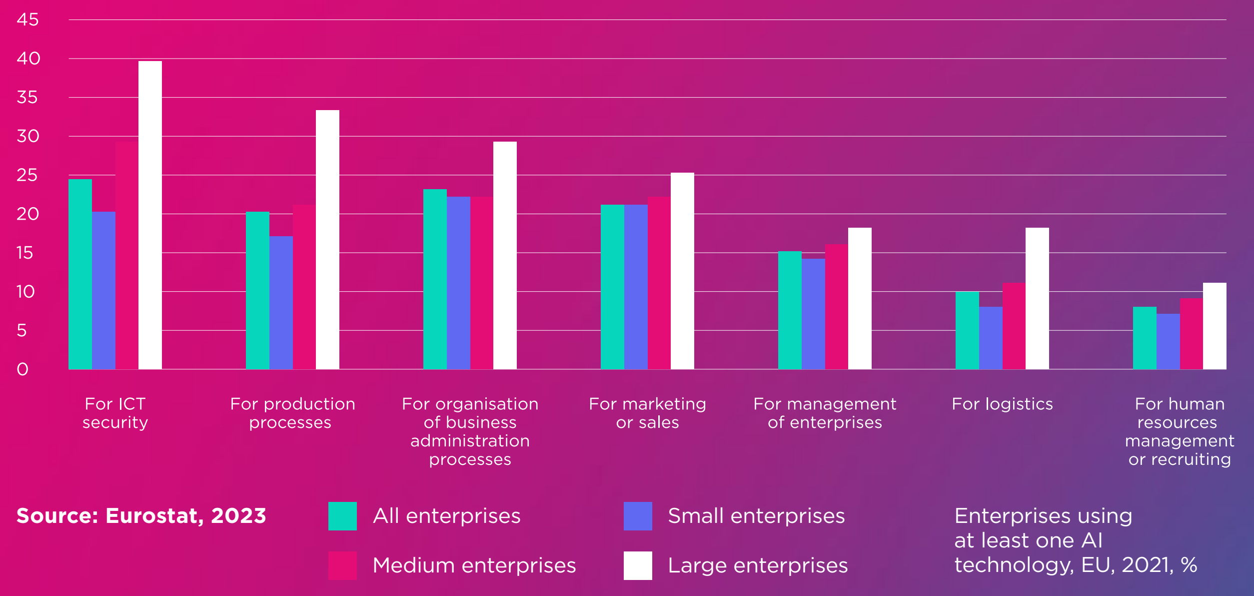
Artificial Intelligence (AI) is poised to dramatically transform global trade by enhancing efficiencies, reducing costs, and overcoming geographical barriers. This chapter delves into AI's impact, focusing on its integration in various sectors, the pivotal role of semiconductor chips, the evolution of cryptocurrencies, Central Bank Digital Currencies (CBDCs), and the potential of blockchain technology to revolutionise e-commerce and supply chain management.

Artificial Intelligence: A New Frontier in Trade

AI's integration into trade is becoming increasingly profound, forecast to add $15 trillion to the global economy by 2030. AI technologies, particularly generative AI like ChatGPT, are advancing capabilities across highly tradeable sectors such as IT services, transport equipment, and electronics, which dominate AI-related patent filings. AI enhances supply chain management through improved forecasting and inventory management, boosts trade finance security, and optimises market analysis, profoundly impacting global trade operations.

FIGURE 7

Enterprises using AI software and systems by type of purpose and economic activity, EU, 2021, percentage of enterprises using at least one AI technology



Source: Eurostat, 2023

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Challenges to AI implementation

Despite its potential, AI's global adoption faces hurdles including the need for standardised regulations and the high costs associated with deploying AI technologies. These challenges could slow AI adoption, particularly in less developed regions, potentially exacerbating global trade inequalities.

Semiconductor industry: The battle for technological leadership

Semiconductors remain crucial for AI and the broader digital economy, yet face geopolitical tensions, notably the U.S.-China tech rivalry. The United States has intensified efforts to maintain semiconductor supremacy through significant subsidies and stringent export controls, which directly impact China's technological advancements. This tug-of-war over semiconductors underscores the strategic importance of these components in global trade and national security.

Cryptocurrencies and blockchain: Enhancing digital trade

Cryptocurrencies and CBDCs are reshaping financial transactions in global trade by offering faster and more secure payment methods. However, the volatile nature of cryptocurrencies and security concerns pose significant barriers to their widespread adoption in trade finance.

Blockchain's untapped potential

Despite its potential, AI's global adoption faces hurdles including the need for standardised regulations and the high costs associated with deploying AI technologies. These challenges could slow AI adoption, particularly in less developed regions, potentially exacerbating global trade inequalities.

Digital trade agreements: Shaping the future of e-commerce

Digital trade agreements are becoming increasingly critical in managing cross-border data flows and establishing common legal frameworks for digital trade. These agreements, such as the CPTPP and RCEP, include digital chapters that facilitate e-commerce by standardising customs procedures and enhancing electronic transaction security.

Conclusion

AI and digital technologies are set to redefine global trade by breaking down traditional barriers and fostering new efficiencies. However, the full realisation of these technologies' potential in trade depends on overcoming regulatory challenges and ensuring broad and inclusive adoption across all regions. As digital trade agreements evolve, they must address the complexities of data governance and digital commerce to fully harness the benefits of these transformative technologies.

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Recommendations for businesses:

1. **Embrace comprehensive digital transformation**: Businesses should continue to embrace digital transformation, incorporating advanced technologies such as AI into their operations. This entails not only adopting these technologies but also fostering a culture of innovation and digital literacy across the organisation.

2. **Invest in R&D and pilot programmes**: Digital transformation may require additional investment in research and development or multiple pilot programmes to identify the best use cases for new technologies or combinations thereof. Investing in experimentation and iterative testing allows businesses to refine their digital strategies and maximise the value derived from emerging technologies. Those that do this stand to gain a significant competitive advantage on those that do not.

3. **Engage proactively on technology regulation**: Businesses should actively engage with regulators and policymakers, especially in the early stages of regulatory framework development for emerging technologies. Given the widening gap between digital development and related regulation, businesses must participate in shaping regulatory frameworks to ensure they are conducive to innovation while addressing societal concerns and risks.

4. **Advocate for common standards and harmonisation**: Making the case for more efficient markets and increased economic growth can help persuade policymakers to adopt standardised approaches, particularly benefiting digital SMEs engaged in trade. Businesses should advocate for common and harmonised standards across geographies to reduce costs and complexity associated with fragmented legislative frameworks.

5. **Leverage data analytics for business insights**: Businesses should use data analytics provided by new technologies to gain actionable insights into market trends, consumer behaviour, and supply chain operations. By leveraging advanced analytics tools, businesses can make informed decisions, optimise operations, and identify opportunities for growth and efficiency improvements.

6. **Invest in e-commerce capabilities**: E-commerce offers opportunities for businesses to reach new markets, engage with customers more effectively, and streamline transaction processes, thereby enhancing competitiveness and agility in the digital economy. Businesses should invest in e-commerce capabilities to expand sales channels and optimise inventory and logistics operations.

7. **Monitor and push for blockchain progress**: Despite not fully realising its promise, there remain huge potential benefits of blockchain technology. Businesses should continue to observe progress in regulation and technological development and advocate for advancements in standards to facilitate widespread adoption of blockchain for secure, transparent, and efficient transactions.

Recommendations for governments:

1. **Foster AI adoption and regulation**: Governments should prioritise policies that encourage the adoption and responsible use of AI. This includes investing in AI research and development, supporting AI education and workforce training programmes and establishing regulatory frameworks to ensure ethical AI deployment. By fostering innovation and addressing concerns related to privacy, bias, and accountability, governments can unlock the transformative potential of AI in driving operational efficiencies, enhancing customer engagement, and facilitating trade.

2. **Ensure semiconductor supply chain resilience**: Recognising the critical importance of semiconductors in global trade and industry, governments should implement measures to safeguard semiconductor supply chains. This includes fostering collaboration between industry stakeholders, investing in domestic semiconductor manufacturing capabilities, and diversifying semiconductor sourcing to mitigate supply chain shocks. Proactive measures to address potential shortages will help maintain trade continuity and support economic resilience.

3. **Promote adoption of emerging technologies**: Governments should promote the adoption of emerging technologies such as IoT, 5G, cloud computing, additive manufacturing and quantum computing, through supportive policies and incentives. This includes investing in infrastructure development, fostering public-private partnerships, and providing financial incentives for technology adoption. By leveraging these technologies, businesses can realise efficiencies, cost savings, and enhanced fraud protection, thereby driving positive impacts on international trade.

4. **Address blockchain adoption barriers**: Governments should address regulatory barriers hindering the adoption of blockchain technology. This may involve updating existing regulations to accommodate blockchain applications, providing legal clarity on blockchain-based transactions, and promoting interoperability standards. Additionally, enhancing security measures and fraud protection in regulation can increase blockchain adoption by improving trust and reliability in digital transactions.

5. **Harmonise global regulation and data flows**: Governments should prioritise efforts to harmonise global regulation and data flows across technologies to facilitate international trade. This includes negotiating digital chapters in trade agreements to establish common standards and rules for cross-border data flows, privacy protection, and intellectual property rights. By promoting regulatory coherence and interoperability, governments can reduce barriers to technology adoption, foster innovation, and promote inclusive and sustainable economic growth on a global scale.

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SUSTAINABILITY AND THE FUTURE OF TRADE

INTRODUCTION

At COP28 in Dubai, December 2023, the urgency of transitioning from fossil fuels was a central focus. This chapter examines the relationship between international trade and climate change, in particular how trade can facilitate the spread of renewable energy and green technologies essential for achieving net-zero targets.

Sustainability trends influencing global trade

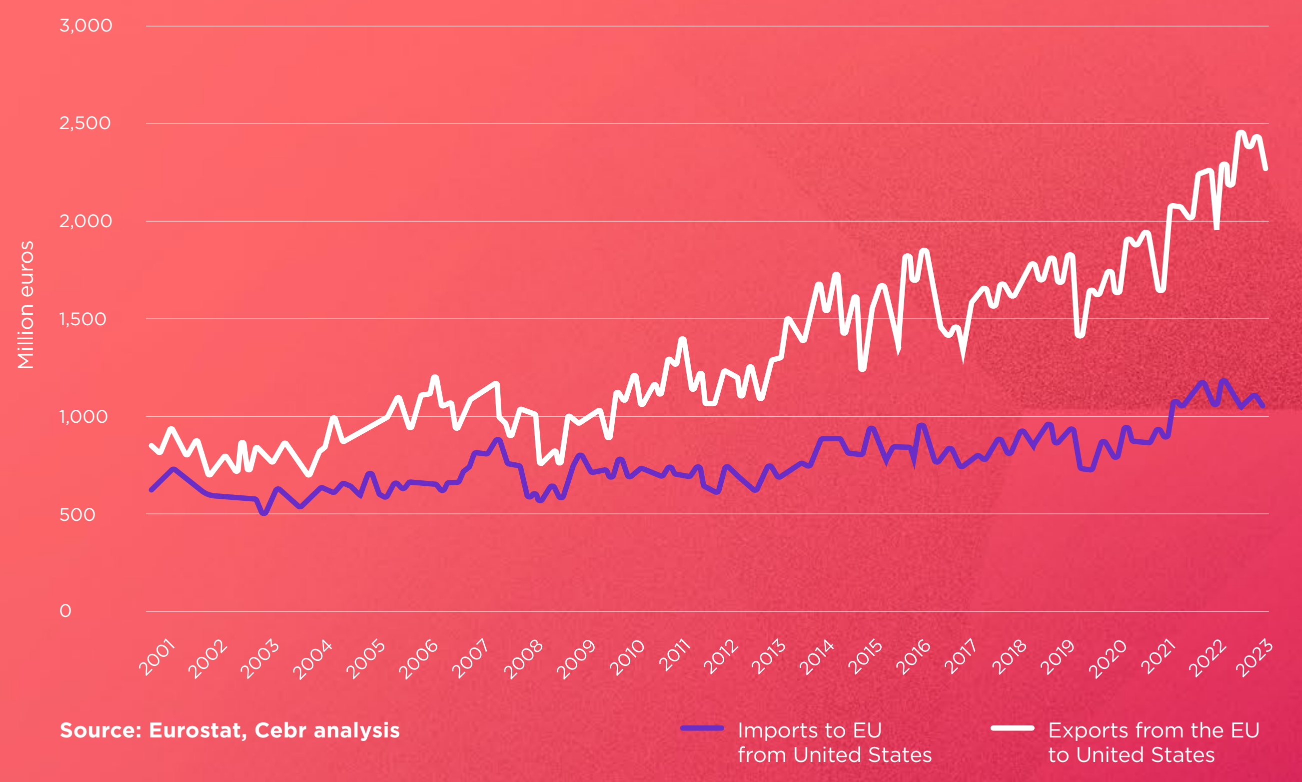
Carbon markets:
The development of carbon pricing and emissions trading systems is shifting trade patterns by incentivising the search for greener production methods. This change is driving companies to adapt by seeking environmentally friendly producers.

Increased trade in renewable energy:
As global energy policies pivot towards sustainability, there is a significant increase in the trade of renewable energy technologies. Countries that can provide reliable sources of energy supply, both traditional and renewable, as well as the critical raw materials needed for the manufacturing of environmental goods and technologies, stand to gain a competitive advantage in this landscape.

As global energy policies pivot towards sustainability, there is a significant increase in the trade of renewable energy technologies.

FIGURE 8

EU/USA trade in environmentally sound technologies



Source: Eurostat, Cebr analysis

Shifting Government Priorities:
Climate considerations are increasingly influencing foreign policy decisions, leading to a greater focus on sustainable trade practices and the resilience of energy supplies.

How climate policy is reshaping trade

Global agreements:
COP28's commitment to a fossil fuel transition underscores the growing linkage between trade policies and climate goals. This alignment is expected to drive significant changes in global consumption patterns and trade flows, particularly in energy.

Renewable energy demand:
The global shift toward renewable energy is not only altering traditional energy trade but is also fostering new trade corridors for countries with high renewable capacity.

Supply chain greening:
Businesses are increasingly focusing on reducing their environmental impact by integrating sustainability into their supply chains. This shift is part of broader efforts to meet environmental, social, and governance (ESG) criteria, which are becoming critical in global trade operations.

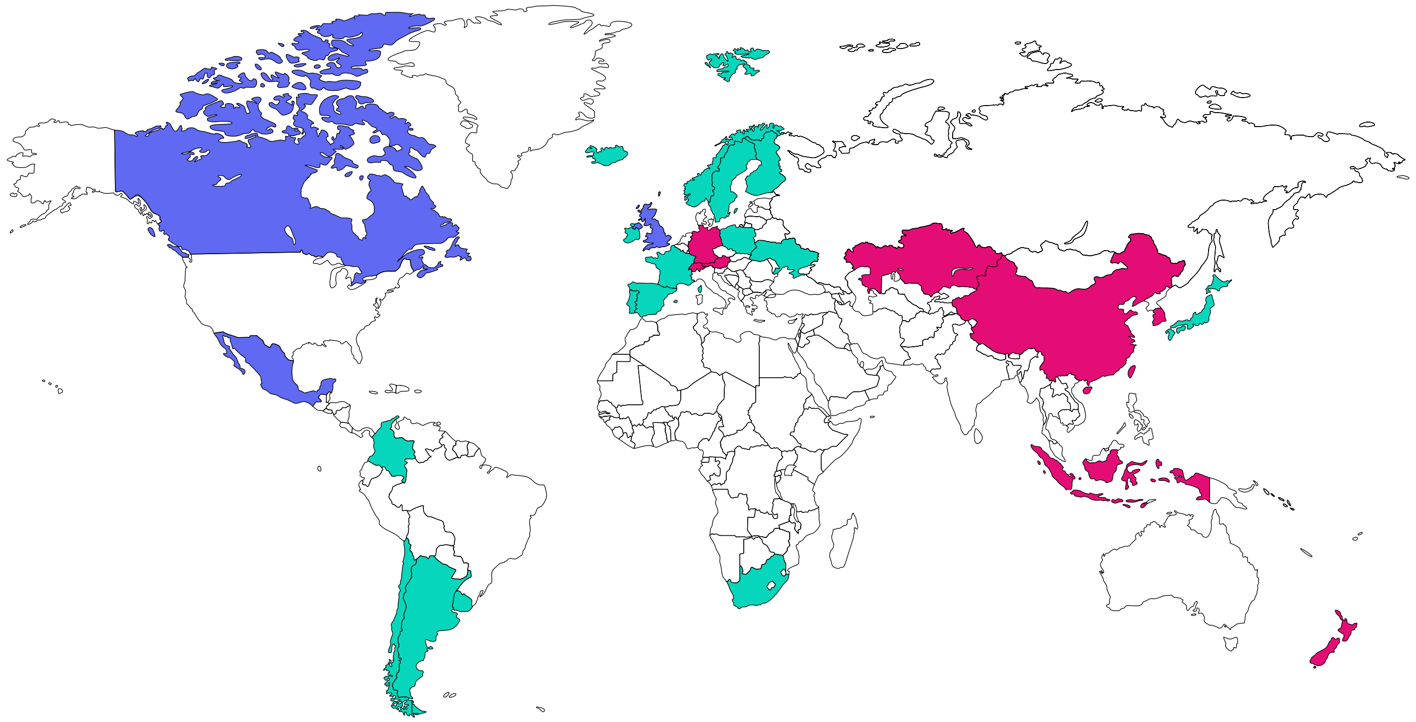
Carbon pricing and its impact on trade

Mechanisms for emission reduction: Carbon pricing mechanisms, such as taxes and emission trading systems (ETS), are becoming widespread. These policies are essential for encouraging businesses to invest in cleaner technologies and practices. However the varying levels of scope and ambition between governments mean that some regions will move faster than others, potentially leading to a patchwork of carbon regulations around the world and new trade barriers for business.

European Union's Carbon Border Adjustment Mechanism (CBAM): Set to be implemented in 2026, CBAM aims to level the playing field by charging importers for the carbon emissions associated with goods produced outside the EU. This mechanism is designed to prevent carbon leakage and promote global emissions reductions.

FIGURE 9

Countries that have implemented carbon pricing systems



Source: World Bank (2023b)

The role of carbon trading systems

Mandatory and voluntary systems: Various countries have adopted carbon trading systems to meet their climate targets. These systems encourage businesses to reduce emissions by allowing them to trade carbon credits.

Challenges and opportunities: While carbon trading has the potential to significantly reduce emissions, it also introduces complexities in compliance and market stability. Businesses must navigate these challenges while leveraging the opportunities for innovation in green technologies.

Trade, sustainability, and technology: An interdependent relationship

Trade as a catalyst for sustainability: Trade policies can accelerate the adoption of sustainable technologies and practices. By facilitating the global exchange of goods, services, and technologies, trade can help reduce the carbon footprint of production processes and foster economic resilience against climate impacts.

Technological advancements: Digital and green technologies are set to play a pivotal role in the sustainable transformation of trade. Innovations in these areas will be crucial for improving efficiency, reducing emissions, and enhancing the sustainability of global supply chains.

Conclusion

Trade is set to be a critical tool in the global response to climate change. By promoting the exchange of renewable technologies and sustainable practices, trade can help achieve environmental goals while supporting economic growth. However, this will require concerted efforts to align trade policies with climate objectives, ensuring that trade contributes positively to a sustainable future.

Recommendations for businesses:

1. **Prioritise sustainability at the board level**. Companies that fail to prioritise sustainability risk being at a significant competitive disadvantage in the long term. Businesses should elevate sustainability to the top of the board agenda and integrate ESG considerations into strategic decision-making to ensure alignment with overall objectives.

2. **Review and optimise supply chains**. Implementing sustainable sourcing practices not only reduces environmental impact but also contributes to long-term profitability by mitigating risks associated with resource scarcity and regulatory compliance. Businesses should conduct a comprehensive review of supply chains to identify opportunities for sustainability improvements and seek out suppliers and vendors that align with sustainability goals.

3. **Mitigate climate-related supply chain risks.** Businesses should proactively plan for supply chain disruptions resulting from climate-related events and other shocks, assess climate risks to key supply chain nodes and operations, and implement risk mitigation strategies such as securing property and casualty insurance coverage tailored to climate-related risks. Businesses should regularly review and update climate risk assessments to adapt to changing environmental conditions and ensure business continuity.

4. **Engage in voluntary carbon markets**. Participating in voluntary carbon markets allows businesses to proactively manage their carbon footprint, demonstrate environmental stewardship, and position themselves for compliance with future carbon and sustainable business regulations. Businesses should increase engagement in voluntary carbon markets as part of preparations for regulatory changes and the wider adoption of mandatory carbon trading schemes. As part of this they should also collaborate with industry partners and carbon market stakeholders to explore opportunities for carbon offsetting and emissions reduction initiatives.

5. **Invest in regulatory expertise and data collection**. To stay informed about emerging sustainability regulations and standards at national and international levels, businesses should invest in expertise capable of providing timely information on fast-changing regulatory landscapes, evolving emissions reporting requirements, and potential tariffs arising from carbon border adjustment mechanisms. Businesses should enhance data collection capabilities to track and report emissions data, enabling informed decision-making and strategic planning.

Recommendations for governments:

1. **Invest in green infrastructure and technology**. Governments should prioritise investment in green infrastructure and technology to support the transition to net-zero. This includes funding renewable energy projects, upgrading transportation networks and supporting research and development of green technologies. By investing in green initiatives, governments can create opportunities for trade and stimulate demand for green finance initiatives, driving sustainable economic growth.

2. **Harmonise regional carbon pricing mechanisms**. Whilst carbon pricing and trading systems can incentivise emissions reductions and facilitate the transition to a low-carbon economy, the patchwork of different regimes between Europe, North America, Australia, China and Asia-Pacific will result in a fragmented environment that will increase the risk of trade barriers. Governments should prioritise compatibility and harmonisation between different systems to avoid trade complexities and costs. By creating a unified approach to carbon pricing, governments can enhance market efficiency and promote fair competition while addressing climate concerns.

3. **Promote sustainable supply chains**. Governments should enact policies to encourage companies to green their supply chains and reduce their carbon footprint. This includes incentives for adopting sustainable practices, such as tax breaks or subsidies for investments in renewable energy and energy-efficient technologies. Additionally, governments can leverage trade agreements to include environmental provisions that promote sustainable production and trade practices, ensuring that companies prioritise environmental sustainability in their operations.

4. **Facilitate technology transfer and dissemination**. Governments should leverage trade agreements and partnerships to facilitate the transfer and dissemination of green technologies essential for renewable energy production. This includes promoting collaboration on research and development, reducing trade barriers for clean energy products, and providing financial assistance for technology transfer initiatives. By enabling the global dissemination of green technologies, governments can accelerate the transition to a low-carbon economy and address climate change on a global scale.

5. **Enhance climate resilience and regional cooperation**. Governments should prioritise efforts to enhance climate resilience and regional cooperation to mitigate the impacts of extreme weather events and promote sustainable development. This includes investing in climate adaptation measures, such as infrastructure upgrades and disaster preparedness initiatives, and fostering regional partnerships for knowledge sharing and resource pooling. By building climate-resilient economies and fostering regional cooperation, governments can promote stability, prosperity, and sustainability in the face of climate change challenges.

GLOBAL TRADE AND FINANCE GAPS

INTRODUCTION

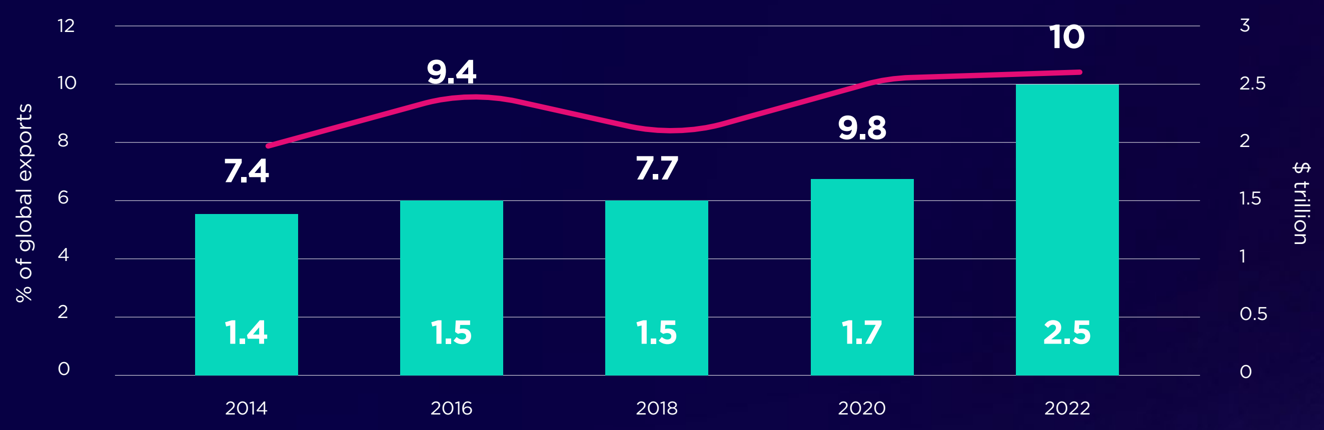
Trade finance, crucial for facilitating global trade, is experiencing a widening gap, reaching $2.5 trillion in 2022. This chapter explores the factors contributing to this growing finance gap and potential solutions to bridge it.

The growing trade finance gap

Current State: Trade finance is essential for 80 to 90 percent of world trade, yet there is a significant shortfall in available funding. The gap has expanded by 47 percent since 2020, influenced by macroeconomic stresses, geopolitical tensions, and stringent regulatory compliance.

FIGURE 10

Global Trade Finance Gap



Source: ADB (2023). Their analysis draws on WTO data.

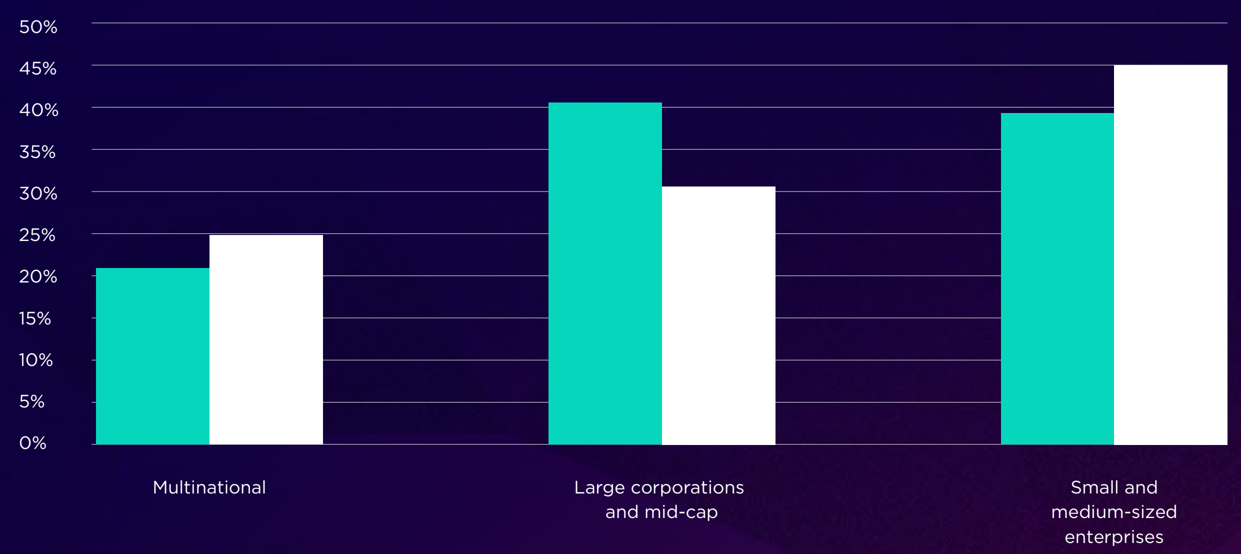
Solutions to the global trade finance gap

Multi-faceted approach: Addressing the trade finance gap requires a collaborative effort from governments, export credit agencies, banks, and non-traditional financial institutions. Solutions include enhancing government support, using digital technologies to streamline processes, and embracing alternative financing methods.

Digital and fintech solutions: Digital technologies and fintech offer promising avenues to reduce the trade finance gap by improving access to finance, particularly for SMEs and businesses in high-risk markets. These technologies can streamline trade finance processes, reduce costs, and expand access to credit.

FIGURE 11

Trade Finance Application and Rejection 2022 (%)



Source: ADB (2023)

Alternative financing solutions

Non-traditional finance: Various initiatives aim to narrow the trade finance gap by mitigating risks and reducing the barriers to accessing finance. These include:

- **Multilateral development banks (MDBs)**: These institutions provide guarantees to reduce the perceived risks associated with lending to exporters in developing countries.
- **Export credit agencies (ECAs)**: ECAs offer loans, insurance, and guarantees to protect exporters from non-payment risks and facilitate longer repayment terms.
- **Microfinancing**: This provides small loans to individuals and small businesses that lack access to traditional bank loans, helping them to engage in trade.

Emerging challenges and opportunities: While these solutions are impactful, they are not sufficient to completely close the trade finance gap. The complexity of the global trade system, varying risk perceptions, and the need for a cohesive regulatory framework continue to pose challenges.

Conclusion

The trade finance gap represents a significant challenge to global economic growth and the effective functioning of international trade systems. Closing this gap requires a comprehensive approach that includes governmental support, innovative financing solutions, and the strategic use of technology to streamline and democratise access to finance. Addressing this issue is crucial for enabling more equitable participation in global trade, especially for SMEs and developing economies.

Recommendations for businesses:

1. **Increase data collection to boost attractiveness and ESG ratings**. Businesses should prioritise the collection of comprehensive data on their activities and outcomes. This includes data on environmental, social, and governance (ESG) factors, which are increasingly important for investors and financiers. By collecting rich data, businesses can enhance transparency, demonstrate their commitment to sustainability, and improve their ESG ratings. This, in turn, can support financing requests by providing investors with the information they need to make informed decisions about allocating capital.

2. **Engage with non-traditional finance sources**. Businesses, particularly SMEs, should explore alternative sources of funding beyond traditional bank loans. This includes venture capital, private equity, crowdfunding, and impact investing. SMEs can increase awareness of these alternative funding options to diversify their financing sources and access capital more efficiently. Larger businesses can collaborate with development banks on blended finance initiatives, where public and private funds are combined to support projects in emerging markets. By participating in blended finance initiatives, businesses can benefit from de-risked lending and access new markets and opportunities.

3. **Collaborate with governments on investment protection**. Businesses should seek opportunities to collaborate with governments of consumer markets to promote investment protection. This includes identifying areas of mutual benefit, such as highly demanded products that require additional financing to export. By working with governments to create a supportive investment climate, businesses can mitigate risks and enhance market access, leading to increased trade and investment opportunities.

4. **Consider fintech options to drive finance efficiency**. Businesses should consider adopting fintech solutions in their operations to streamline time-intensive administrative processes, reduce costs, and increase efficiency. This includes implementing digital payment systems, automated accounting software, and blockchain-based supply chain management solutions. By leveraging fintech, businesses can optimise their operations, improve cash flow management, and free up resources for strategic investments and growth initiatives.

5. **Regularly review risk ratings and data collection**. Banks should regularly review risk ratings and collect more data on underrepresented markets, particularly in emerging economies. By improving data collection and analysis, financial institutions can better assess creditworthiness and manage risks associated with lending to businesses in diverse markets. This includes leveraging technology and data analytics to identify emerging trends, mitigate risks, and support responsible lending practices.

Recommendations for governments:

1. **Prioritise all policy and non-policy measures to address the trade finance gap**. Given the scale of the global trade finance gap, governments should treat this as a growing emergency requiring innovative solutions. This can be a blend of policy and non-policy options, including collaborating with international financial institutions and multilateral development banks to increase the availability of trade finance instruments and support mechanisms, and implementing regulatory reforms to reduce barriers to trade finance and promoting greater transparency and information sharing in trade finance processes to reduce perceived risks and increase access to finance for SMEs.

2. **Mitigate macroeconomic factors to reduce lending pressure**. Governments should implement measures to stabilise macroeconomic conditions, such as reducing inflation and maintaining accommodative monetary policies, to alleviate pressure on banks and encourage trade finance issuance. In addition, governments should provide targeted support to SMEs through fiscal stimulus packages and credit guarantee schemes and foster economic diversification and resilience to reduce dependency on traditional banking channels for trade finance, including promoting alternative financing mechanisms and facilitating access to capital markets.

3. **Leverage digital technologies for fintech adoption**. Governments should invest in digital infrastructure and regulatory frameworks to support the adoption of fintech solutions in trade finance, including AI, blockchain, and digital platforms. This can facilitate partnerships between financial institutions, technology companies, and government agencies to develop and deploy innovative fintech solutions tailored to the needs of SMEs and trade finance providers.

4. **Scale up non-traditional finance methods**. Governments should expand the availability of non-traditional finance mechanisms, such as export credit, blended finance, and microfinance, to address the trade finance gap on a larger scale. Priority should be given to partnerships with international organisations and donor agencies to mobilise additional funding for non-traditional finance initiatives, supporting their implementation in developing countries, as well as promoting awareness and capacity-building initiatives to increase SMEs' understanding and access to non-traditional finance options for trade expansion and growth.

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