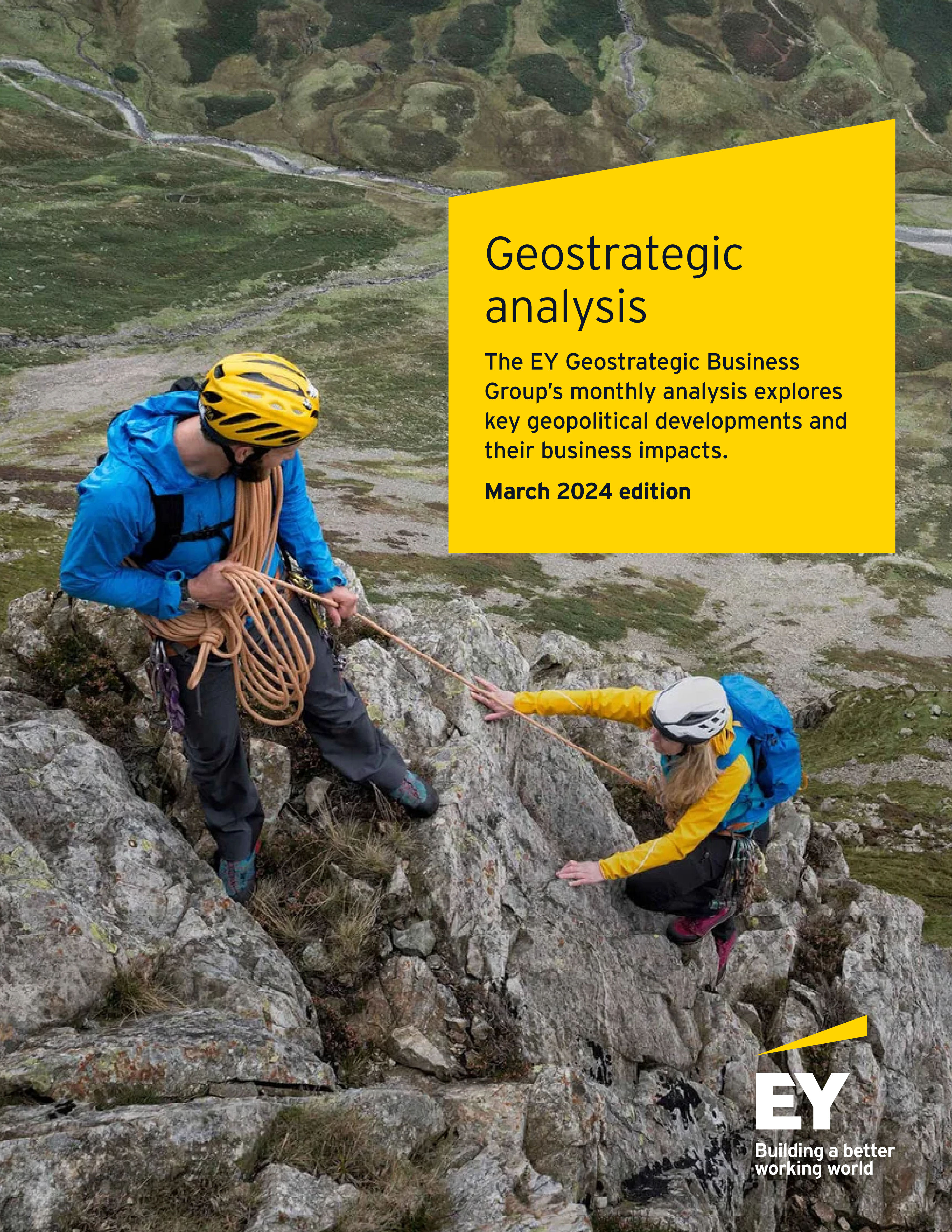


Geostrategic analysis

The EY Geostrategic Business Group's monthly analysis explores key geopolitical developments and their business impacts.

March 2024 edition

EY
Building a better working world

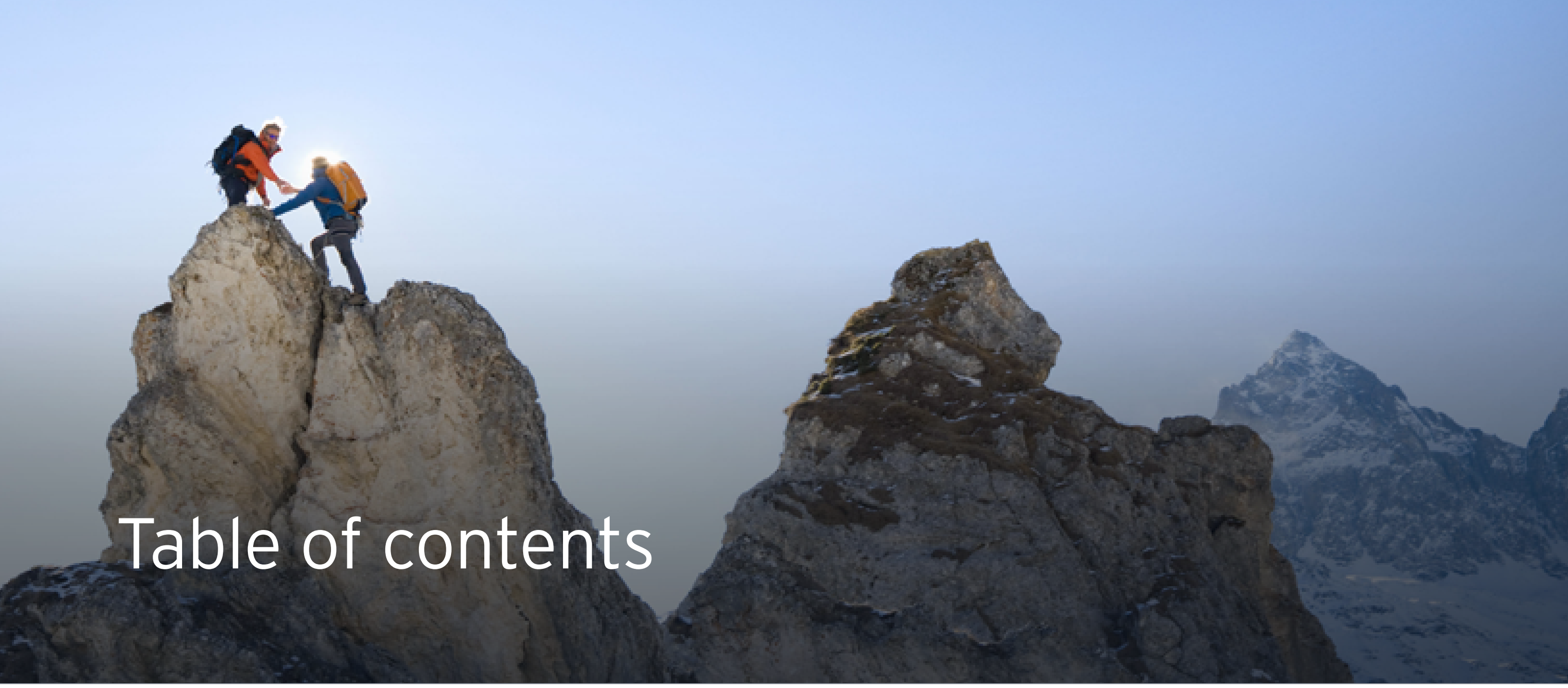


Table of contents

Top development:
Disagreement at the WTO risks further fracturing global trade

Sector in focus:
Financial services: Global interest rates to fall but remain elevated

Other issues we are watching:
European farmer protests, Indonesia's election, Nigeria's foreign exchange reforms

Geostrategic indicator of the month:
Rise of armed conflicts compared to official military spending

EY Geostrategic Business Group (GBG)

Translating geopolitical insights into business strategy

Read more.

1 Top development

Disagreement at the WTO risks further fracturing global trade

What happened

On 26–29 February, trade ministers from 164 states and territories attended the WTO's Thirteenth Ministerial Conference (MC13), agreeing modest outcomes on duty-free electronic transmissions and improvements in the treatment of least developed countries. An agreement among 71 WTO members to facilitate services trade by implementing more predictability and transparency in domestic services regulations entered into force.[1]

Significant fault lines prevented more substantial progress on the global trade agenda. Most notably, major disagreements persist on how to reform the 30-year-old organization, including how to improve countries' existing commitments to submit regular information to the WTO on their trade measures, how to restore a functioning dispute settlement system and how new rules can be integrated when agreed by only a sub-section of the membership.

MC13 was held amid concerns about the global trading system, following a 96% spike[2] in trade policy interventions deemed "harmful" by Global Trade Alert and an estimated 5% contraction[3] in global trade in 2023.

What's next

Delegations will return to Geneva later in March to try to chart a way forward on the ambitious list of tasks in the MC13 Ministerial Declaration.[4] These efforts will be challenging due to long-standing divisions that are complicated by political positioning for domestic audiences around elections in many major trading powers in 2024. Delegations nevertheless feel a sense of urgency to make progress on their agenda, as businesses currently rely on international trade rules that were negotiated before the advent of the internet.

The US-led coalition will continue to provide security to ships transiting WTO reform and the re-establishment of a functioning dispute settlement system will be a focus for many delegations — with 2024 set as the goal for the latter. These efforts are seen as necessary to maintain the WTO as a core pillar for the functioning of the global economy. Indeed, there are ongoing concerns about the outlook for global trade due to geopolitical tensions and the rise in protectionist measures. The IMF finds that trade flows are shifting as countries build new regional and "friendly" trade groupings — particularly in strategic sectors.[5]

Resuming negotiations among the 90 WTO members involved in the Joint Initiative on E-Commerce will also be a priority. The Joint Initiative aims to codify new obligations on facilitating electronic transactions and digital trade, strengthening consumer protection and improving cross-border telecommunications. The withdrawal of US support from several ambitious digital trade and data flow provisions is likely to weigh on the next negotiating round in mid-March.

There will likely be a renewed push for members to ratify the WTO's 2022 Agreement on Fisheries Subsidies to eliminate harmful fisheries subsidies contributing to the collapse in global fish stocks so that it can take effect (109 members are required to ratify; only 62 have done so).[6] At MC13, negotiations failed to deliver an agreement to extend this to subsidies that have contributed to fishing fleet overcapacity.

Recent WTO negotiations on agriculture have focused on tackling export restrictions on food; agricultural production and trade in net food importing developing countries and least developed countries (LDCs); and domestic support to the agricultural sector. The WTO was unable to address these issues at MC13, and international agreement on these issues will continue to be difficult due to domestic political considerations in many markets.

Business impact

Major sectors affected include technology, agribusiness, life sciences.

The failure to reinstate a fully functioning dispute settlement mechanism will perpetuate risks for companies that engage in cross-border trade. With the appeals process frozen, protectionist trade measures can persist, elevating costs and restricting market access for companies.

Technology companies and others that rely on cross-border data flows will continue to enjoy tariff-free trade as the E-Commerce Moratorium was extended again for two years.[7] Although WTO members have reaffirmed their commitment to not imposing tariffs on data crossing their borders, the issue is likely to be raised again in 2026.

The waiver on Trade Related Aspects of Intellectual Property Rights (TRIPS) related to COVID-19 vaccines was not expanded to also include therapeutics and diagnostics. This decision leaves in place intellectual property rights protections for such projects, which may encourage more life sciences companies to invest in innovative products.

Given the concerns about illegal, unreported and unregulated fishing, opportunities may expand in sustainable aquaculture. But the lack of agreement to minimize agricultural export restrictions means that global disruptions across the food value chain will likely persist, requiring market participants from farmers to grocers to re-evaluate their supply networks and diversify where possible.

With Comoros and Timor-Leste joining the WTO at MC13, companies operating in or with these economies are likely to have expanded growth opportunities in the years ahead. The WTO estimates that new members' economies expand by about 30% in the first five years of membership.[8]

For more information, contact George Riddell and Courtney Rickert McCaffrey

Additional reading: Top 10 geopolitical developments for 2024

1. MC13 ends with decisions on dispute reform, development; commitment to continue ongoing talks (wto.org) https://www.wto.org/english/news_e/news24_e/mc13_01mar24_e.htm
2. Global dynamics (globaltradealert.org) https://www.globaltradealert.org/global_dynamics/day-to_0216
3. Global Trade Update, December 2023 (unctad.org) https://unctad.org/system/files/official-document/ditcinf2023d3.pdf
4. Draft Abu Dhabi Ministerial Declaration (wto.org) https://docs.wto.org/dol2fe/Pages/SS/directdoc.aspx?filename=q:/WT/MIN24/W12R1.pdf&Open=True
5. Global Economy Approaches Soft Landing, but Risks Remain (imf.org) https://www.imf.org/en/Blogs/Articles/2024/01/30/global-economy-approaches-soft-landing-but-risks-remain
6. WTO | Members submitting acceptance of Agreement on Fisheries Subsidies https://www.wto.org/english/tratop_e/rulesneg_e/fish_e/fish_acceptances_e.htm
7. Work Programme on Electronic Commerce (wto.org) https://docs.wto.org/dol2fe/Pages/SS/directdoc.aspx?filename=q:/WT/MIN24/W26R1.pdf&Open=True
8. WTO | WTO accession and growth: Tang and Wei Redux https://www.wto.org/english/res_e/reser_e/ersd202101_e.htm#:~:text=We%20find%20that%20WTO%20accession,beyond%20the%20first%20five%20years.

2

Sector in focus: Energy and resources

Sector in focus: Financial services. Global interest rates to fall but remain elevated

What happened

The global inflation surge of 2021–22 was induced by fiscally stimulated demand and constrained supply conditions in the post-pandemic period, along with the effects of the war in Ukraine on commodity and food prices.

Central banks reacted to high inflation by implementing the fastest monetary policy tightening cycle in decades, pushing up short- and long-term borrowing costs.[9]

What's next

With inflation falling quickly and generally moving back toward central banks' inflation targets, the tightening cycle appears largely over. Some emerging markets have already begun cutting rates and more policymakers in emerging and advanced economies are considering carefully easing monetary policy.[10]

But upside risks to inflation from still-elevated wage growth, potential supply shocks and geopolitical risks — including the recent increase in shipping costs — will translate into a gradual easing cycle with interest rates expected to remain well above pre-pandemic levels.

The US Federal Reserve[11], European Central Bank[12], Bank of England[13], Reserve Bank of Australia[14], South African Reserve Bank[15] and other central banks are maintaining restrictive monetary policy stances. So although rate cuts are on the horizon, they may not begin until the second or third quarter of 2024. The stance of many central bankers was summed up by Michelle Bullock, Governor of the Reserve Bank of Australia, "we are not yet where we need to be."[16]

Business impact

Banks benefitted from higher interest rate margins during the tightening cycle. But higher interest rates have also reduced loan demand and led to deteriorating asset quality — especially in the commercial real estate segment — which has kept downward pressure on banking sector revenues.

Higher bank funding costs and deposit volatility will continue to pressure small and midsized banking institutions, but policy rate cuts should gradually alleviate these pressures.[17] Still, with global debt maturities expected to rise from nearly US$2t in 2024 to a peak of US$2.8t in 2026, exposure to over-valued debt represents a risk for lending institutions globally.[18] Many banks will likely have to mark their loans and bond holdings to market in the coming months.

Several sectors that were most exposed to the higher cost of capital environment — including residential investment, commercial real estate, and small business lending — have faced reduced growth prospects, but lower policy rates may offer refinancing opportunities in the coming months.[19] Monetary easing will likely provide a boost to global manufacturing activity as well.

For more information, contact Gregory Daco, Marek Rozkrut, Angelika Goliger, Cherelle Murphy and Maciej Stefański

Additional reading: How financial firms can prepare for the 2024 regulatory landscape

9. Global Monetary Policy Tracker | Council on Foreign Relations (cfr.org) https://www.cfr.org/global/global-monetary-policy-tracker/p37726
10. World Economic Outlook Update, January 2024: Moderating Inflation and Steady Growth Open Path to Soft Landing (imf.org) https://www.imf.org/en/Publications/WEO/Issues/2024/01/30/world-economic-outlook-update-january-2024
11. Federal Reserve Board — Federal Reserve issues FOMC statement https://www.federalreserve.gov/newsevents/pressreleases/monetary20240131a.htm
12. Monetary policy decisions (europa.eu) https://www.ecb.europa.eu/press/pr/date/2023/html/ecb.mp231214~9846e62f62.en.html
13. Monetary policy | Bank of England https://www.bankofengland.co.uk/monetary-policy
14. Monetary Policy Decisions | RBA https://www.rba.gov.au/monetary-policy/int-rate-decisions/2024/
15. Statement of the Monetary Policy Committee January 2024.pdf (resbank.co.za) https://www.resbank.co.za/content/dam/sarb/publications/statements/monetary-policy-statements/2024/january/Statement%20of%20the%20Monetary%20Policy%20Committee%20January%202024.pdf
16. Opening Statement to the House of Representatives Standing Committee on Economics | Speeches | RBA https://www.rba.gov.au/speeches/2024/sp-gov-2024-0 2-09.html
17. Minutes of the Federal Open Market Committee, January 30–31, 2024 (federalreserve.gov) https://www.federalreserve.gov/monetarypolicy/fomcminutes20240131.htm
18. Credit Trends: Global Refinancing: Maturity Wall Looms Higher For Speculative-Grade Debt | S&P Global Ratings (spglobal.com) https://www.spglobal.com/ratings/en/research/articles/240205-credit-trends-global-refinancing-maturity-wall-looms-higher-for-speculative-grade-debt-12991317
19. US Commercial Real Estate Remains a Risk Despite Investor Hopes for Soft Landing (imf.org) https://www.imf.org/en/Blogs/Articles/2024/01/17/us-commercial-real-estate-remains-a-risk-despite-investor-hopes-for-soft-landing

Other issues we are watching

Softening of EU green regulations, Indonesia's election, Nigeria's foreign exchange reforms

European farmer protests lead to a softening of EU green regulations

Farmers across Europe have been protesting against high energy prices, cheap agricultural imports and the EU's environmental legislation, leading the European Commission to backtrack on measures to reduce emissions and bind agricultural subsidies to sustainable practices such as limiting the usage of arable land and halving the use of pesticides.[20] Nationalist parties are capitalizing on farmers' anti-green frustrations and are expected to secure more seats in the European Parliament elections in June.

Business impact: Road blockages and other logistical disruptions will likely persist in the months leading up to the European Parliament elections, as farmer protests intensify and potentially spread to more countries. Such protests may fuel anti-green tensions in other sectors with similar concerns, such as automotives. More broadly, the rise of anti-green, nationalist parties in the new European Parliament may weaken consensus on the EU's current environmental agenda. In the short-term, the easing of environmental rules will mean farmers benefit from lower compliance costs and continued access to subsidies. It will also lead to heightened uncertainty about the timing, content and implementation of green agriculture policies, including sustainability requirements, carbon taxes, water management and biodiversity initiatives.

For more information, contact Famke Krumbmüller

Indonesia's election portends policy continuity and state control

Preliminary quick count results done by survey agencies indicate that the current Minister of Defense of Indonesia Prabowo Subianto won a majority of votes in Indonesia's presidential election.[21] If these results are confirmed, Prabowo will take office in October 2024. However, results indicate his party won less than a majority in the legislature, so governing will require the formation of a coalition. This more complex political landscape could constrain the government's ability to implement any major policy shifts in the near to medium term. Foreign policy is expected to continue to focus on attracting foreign investment across the geopolitical landscape.

Business impact: Prabowo is likely to expand the state's role in Indonesia's economy with investments in mining, manufacturing and agriculture to achieve greater food security. In addition, a Prabowo government is likely to continue support for domestic metals processing and existing nickel export controls in pursuit of higher value-added export-oriented growth. Companies should monitor future policy decisions that may indicate greater favoring of domestic firms and develop mitigation plans should concerns materialize about the possible weakening of labor and other institutional standards.

For more information, contact Adam L Barbina

Nigeria's foreign exchange reforms will have diverse business impacts

The Central Bank of Nigeria (CBN) is advancing toward a flexible exchange rate system, evidenced by recent policy adjustments such as the elimination of spreads on foreign exchange transactions.[22] This shift, spearheaded by CBN Governor Oluyemi Cardoso, is part of a set of market-oriented economic reforms.[23] The considerable autonomy granted to Cardoso in shaping CBN policies signals that these reforms are being implemented without political interference, with the latest move being a significant 400bps increase in the policy rate. Nevertheless, the durability of these reforms rests on the ability to effectively counter inflationary pressures amid fluctuating exchange rates. Protests about higher food and fuel prices have heightened political pressure on the government, which reacted by releasing 42,000 metric tons of food amid speculation about the introduction of price controls.[24]

Business impact: The evolution of Nigeria's foreign exchange policy will exert varying impacts across sectors and business functions. Businesses that primarily focus on exports such as fertilizers stand to gain from a more competitive exchange rate, bolstering their global competitiveness.[25] Conversely, businesses that rely on imports such as machinery and boilers may encounter heightened costs due to currency devaluation and the new set of foreign exchange rules.[26] The petroleum products industry will be affected by both dynamics. Enterprises with substantial foreign exchange exposure should manage risks and adapt strategies such as flexible pricing and hedging mechanisms to navigate the dynamic economic landscape.

For more information, contact Angelika Goliger and Hulisani Muloiwa

20. Commission allows derogation from certain agricultural rules (europa.eu) https://ec.europa.eu/commission/presscorner/detail/en/ip_24_582
21. Prabowo on track to succeed Jokowi - Politics - The Jakarta Post https://www.thejakartapost.com/indonesia/2024/02/15/prabowo-wins.html
22. Central Bank of Nigeria – Financial Markets Department (cbn.gov.ng) https://www.cbn.gov.ng/Out/2024/FMD/FMD%20circular.pdf
23. Turning the Corner, time to move from reforms to results (worldbank.org) https://www.worldbank.org/en/news/press-release/2023/12/13/turning-the-corner-time-to-move-from-reforms-to-results
24. https://allafrica.com/stories/202402240004.html
25. Nigeria Exports By Category (tradingeconomics.com) https://tradingeconomics.com/nigeria/exports-by-category
26. Nigeria Imports (tradingeconomics.com) https://tradingeconomics.com/nigeria/imports

Geostrategic indicator of the month

Rise of armed conflicts compared to official military spending

The indicator

In recent years there has been a dramatic rise in the level of violence and the number of armed conflicts around the world.[27] At the same time, however, the level of official military spending has remained relatively flat as a share of GDP. This seeming contradiction may be explained by the trend of geopolitical power becoming more fragmented and smaller actors seeking to change the status quo, both within their own country and in their broader region. This trend is likely to continue as long as the multipolar global order of fragmented and dispersed geopolitical power persist.

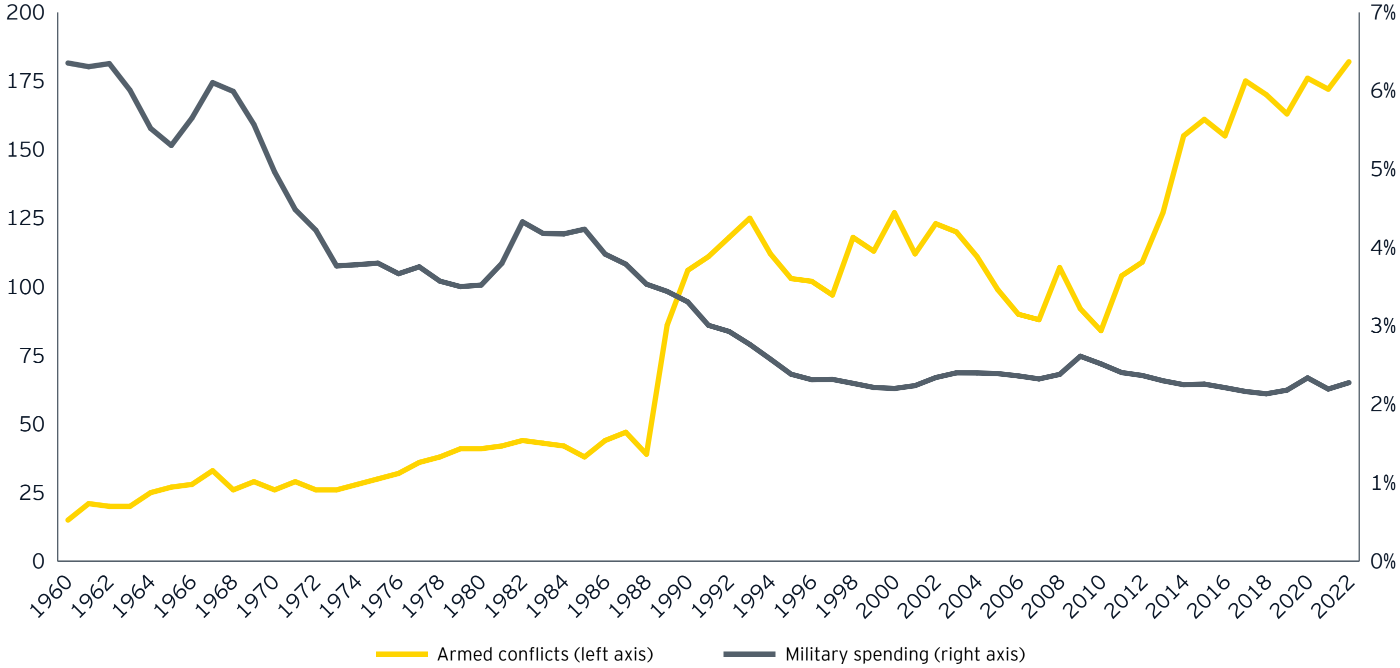
Business impact

Conflict in locations in which companies may have operations raises a large number of challenges. These include the safety of employees and broader global workforce issues and damage to physical facilities. Armed conflicts can also disrupt companies' operations and supply chain, either directly or indirectly. Companies also have to think through the reputational risks of operating in conflict zones.

Additional reading: Top 10 geopolitical developments for 2024

Armed conflicts have risen dramatically, even as official military spending remains flat

Armed conflicts (total) and military expenditure (% of GDP)



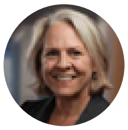
Sources: UCDP/PRIO Armed Conflict Dataset[28] and World Bank World Development Indicators[29].

27. A New Era of Conflict and Violence | United Nations https://www.un.org/en/un75/new-era-conflict-and-violence
28. UCDP/PRIO Armed Conflict Dataset https://ucdp.uu.se/downloads/index.html#armedconflict
29. World Bank World Development Indicators https://data.worldbank.org/indicator/MS.MIL.XPND.GD.ZS

Contacts

Oliver Jones
London
oliver.jones@uk.ey.com

Angelika Goliger
Johannesburg
angelika.s.goliger@za.ey.com

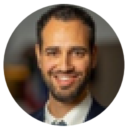


Mary Karol Cline
Washington DC
mary.k.cline@ey.com

Courtney Rickert McCaffrey
Washington DC
courtney.r.mccaffrey@ey.com

Adam Barbina
New York
adam.l.barbina@parthenon.ey.com

Ari B. Saks Gonzalez
Mexico City
ari.b.saks.gonzalez@mx.ey.com



Ben-Ari Boukai
Washington DC
ben-ari.boukai@parthenon.ey.com

Jay Young
Dallas
jay.young1@parthenon.
ey.com

Famke Krumbmüller
Paris
famke.krumbmuller@
parthenon.ey.com

David Kirsch
Houston
david.e.kirsch@ey.com

Nobuko Kobayashi
Tokyo
nobuko.kobayashi@
parthenon.ey.com

Alessandro Faini
Paris
alessandro.faini@
parthenon.ey.com

EY | Building a better working world

EY exists to build a better working world, helping create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EYG no. 002825-24Gbl

2403-4489116
ED None

ey.com