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B7 ITALY 2024

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B7 Flash
Reversing the Global Protectionist Drift

Executive summary

The international trade landscape is undergoing considerable paradigm shifts as multiple shocks are impacting global value chains (GVCs). Conflicting interests in security, energy, and digital, and the spillovers of protectionist measures have increased structural uncertainty hampering global trade, highlighting vulnerabilities in GVCs. The concentration of key minerals, raw materials, and components in a few extracting and producing countries has further intensified these vulnerabilities.

Recent events emphasize the conjunction of geopolitics and trade as an intrinsic feature of international relations to the detriment of the World Trade Organization (WTO), which is suffering long standing shortcomings, but remains crucial for businesses, considering the centrality of the Most Favored Nation rule, the National Treatment principle and Trade Facilitation Agreement (TFA) in international trade. Therefore, a sound and comprehensive reform of the Organization remains top priority for businesses.

The challenge is even greater considering the 40 trillion US$ in infrastructure investments required for developing countries to support the green and digital transitions. In this context, Foreign Direct Investments (FDI) will play a critical role, as they provide not only capital, but also technology and know-how.

Despite a decade-long trend of increasing investment flows from developing countries to least developed countries and public intervention in FDI such as the Partnership for Global Infrastructure and Investment (PGII), FDI in developing countries are failing to reach the adequate critical mass, confirming a global trend of FDI slowdown compared to global trade and GDP. FDI flows should keep in high consideration the financial sustainability of projects and the debt capacity of recipient countries.

“Revamping an efficient rule-based multilateral trading system with the WTO at its core, sustaining international foreign investment and strengthening the resilience of Global Value Chains stand as major priorities of the B7 policy recommendations for the benefit of all advanced and developing economies. Building on the Apulia G7 Leaders’ Communiqué of 14 June 2024, the G7 Business is ready to engage proactively with governments, International and Multilateral Organizations and Institutions for G7 initiatives like the Partnership for Global Infrastructure Investment to deploy soon their full potential.

Barbara Cimmino | Vice President for Export and Investment Attraction, Confindustria

“With the aim of safeguarding the competitive potential of businesses and reviving fair and inclusive economic growth, it is imperative that G7 countries collaborate to balance economic security and the free market while promoting regulated multilateral trade that revitalizes foreign direct investments. To achieve this, the G7 must take a leadership role in developing international trade, preserving global value chains, and fostering international cooperation and investments. In 2023, annual global GDP growth dropped below 3% and it is expected to remain under this threshold in 2024 and 2025, along with a 2% contraction in foreign direct investments. Despite this, international trade has continued to grow and is expected to do so in the future, demonstrating extraordinary resilience. It is precisely from this perspective that G7 countries will play a crucial role in increasing the productivity and competitiveness of the business fabric of G7 economies and their trading partners, supporting the ongoing transitions for a more prosperous and equitable international future.

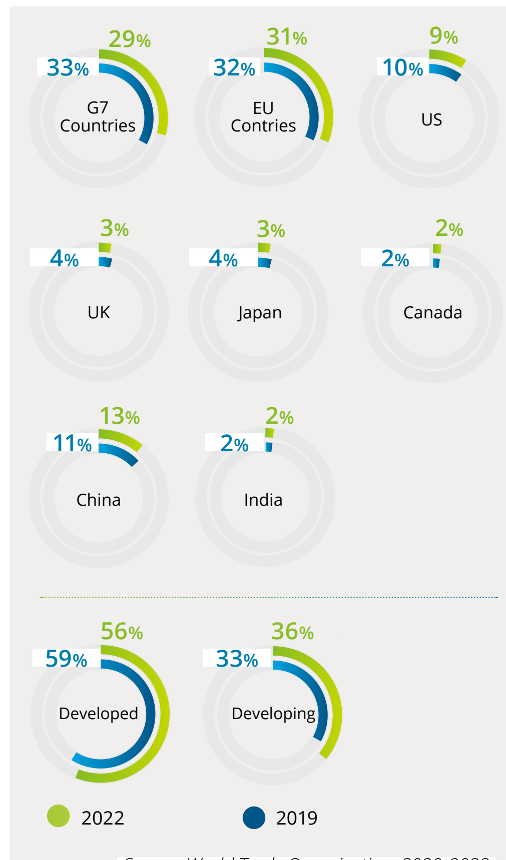
Fabio Pompei | CEO Deloitte

International trade and economic security

Recently, global trade has been affected by a combination of adverse factors: widespread geopolitical tensions, supply and transport bottlenecks, inflationary pressures, the challenges posed by climate change and the energy and digital transitions. Despite these challenges, global trade has displayed remarkable resilience over the past four years: in the fourth quarter of 2023, its volume was up 6.3% compared to the pre-pandemic peak in the third quarter of 2019, and up 19.1% compared to the average level in 2015. World trade volume is projected to grow 2.6% in 2024 and 3.3% in 2025, following a larger-than-expected decline of -1.2% in 2023[1].

Import demand was weak in 2023 in most regions, especially in Europe but also in North America and Asia. The main exceptions were the Middle East and the Commonwealth of Independent States (CIS) region, where imports surged. World real GDP growth at market exchange rates slowed from 3.1% in 2022 to 2.7% in 2023 but is expected to remain mostly stable over the next two years at 2.6% in 2024 and 2.7% in 2025. The contrast between the steady growth of GDP and the slowdown in merchandise trade volume is also linked to different sectoral dynamics and inflationary pressures, which had a downward effect on consumption of trade-intensive goods.

Percentage of international trade growth by Country[2]

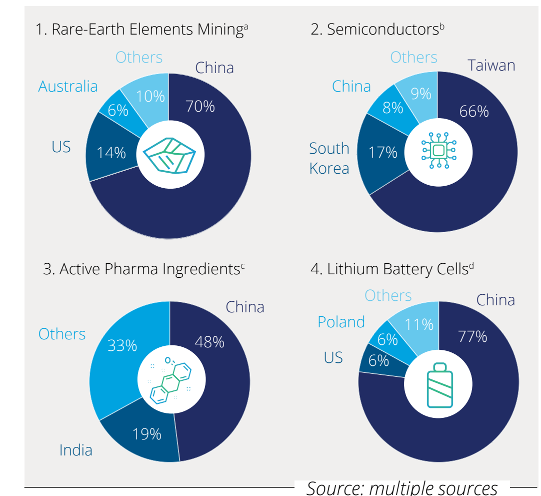


Source: World Trade Organization, 2020-2023

The COVID-19 pandemic and the other aforementioned shocks have highlighted the vulnerabilities in GVCs, the importance of economic resilience, and the persisting market concentration in certain strategic industries, most notably in the rare earth element mining, semiconductors, active pharmaceutical ingredients and batteries industries, with production concentrated in just one or very few countries.

Global production linkages aggravate the impact of localized disruptions in the producing countries, affecting the availability of critical raw materials, goods and technologies worldwide. The relevance of strategic dependencies is reflected in the economic security concerns of the G7 and like-minded countries, setting the challenge of striking a balance between enhancing economic resilience and security through improved GVCs and preserving liberalization and open markets.

Percentage of strategic GVCs with critical exposures[3]



Source: multiple sources

Source: [1] World Trade Organization, 2024 Link | [2] World Trade Organization, 2020-2023 Link | [3] a-United States Geological Survey, 2023 Link, b-Morningstar, 2022 Link, c-Chemical Pharmaceutical Association, 2021 Link, d-BloombergNEF, 2022 Link

Rule of law and competitiveness

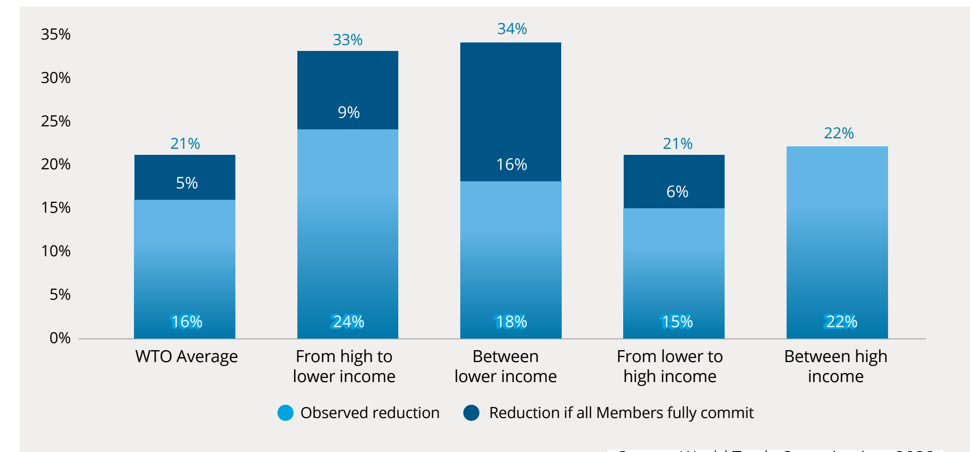
Central to a stable and efficient global trade is a rule-based system and its ability to de-escalate trade disputes. In this context, the WTO is the cornerstone of international trade, and the principles of the GATT, the Most Favored Nation rule and the National Treatment Principle, are still capable to prevent economic discrimination, improve the level playing field and guarantee competitive and free dynamics for both domestic and foreign producers, fostering fair competition in international trade.

An additional contribution of the WTO is the TFA introduced in 2017, which streamlines customs procedures, reducing delays, and builds trust among international trade operators, resulting in an average reduction of trade costs around 16%. This reduction in costs is particularly beneficial to developing countries, enabling them to participate more extensively in global trade.

Considering the above, the ongoing stalemate of the WTO's Appellate Body looks particularly critical. This has led to delays in resolving trade disputes, affecting the overall efficiency and reliability of the WTO's dispute settlement process. Furthermore, permanent regulation is needed for the e-commerce custom duties on electronic transmissions, currently requiring yearly moratorium renewals.

Failure to renew the e-commerce moratorium would have a high impact on the digital economy, particularly hitting developing countries. Moving forward, the challenge will lie in supporting the WTO, including through rules-based multilateral agreements, to ensure that the global trading system remains functioning and capable of meeting future targets.

***Percentage of trade and border cost reduction of TFA implementation*[4]**



Source: World Trade Organization, 2023

Source: [4] World Trade Organization, 2023 Link

Foreign direct investments

In 2023, global FDI decreased by 2%, to 1.3 trillion US$. Excluding wild swings in financial flows through a small number of European conduit economies, global FDI flows were over 10% lower compared to 2022. FDI are increasingly under scrutiny, with four additional countries that implemented FDI screening measures in 2023, and several more expected to follow in 2024. Countries that conduct FDI screening now account for over half of global FDI flows and three quarters of FDI stock.

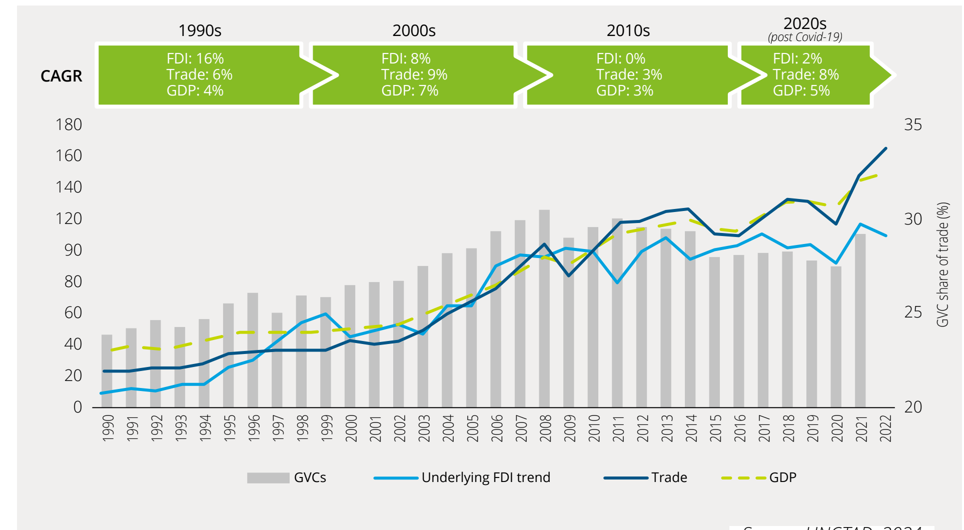
Despite an estimated 40 trillion US$ in infrastructure investments required for developing countries by 2035 to support the green and digital transitions, the global environment for international investment remains challenging in 2024[5]. Weakening growth prospects, trade and geopolitical tensions, industrial policies and supply chain diversification are reshaping FDI patterns, leading some Multinational Enterprises (MNEs) to adopt a cautious approach to international expansion.

Since 2019, the geographical distribution of manufacturing projects of the top 100 non-financial MNEs, notably in strategic sectors, has shifted towards locations closer to major markets in Europe and the United States. West Asia, North Africa and Central America are emerging as strategic locations for manufacturing MNEs.

The long-term trend in cross-border investment shows that a slowdown in global FDI[6] already started around 2010 and that FDI no longer keep pace with global trade and GDP. Trade within GVCs has also slowed, confirming the close link between FDI and GVCs.

The comparison between trends in GDP and trade underscores the distinctive nature of the early "slowbalisation" of cross-border investment. GVC participation, defined as the steps of GVCs taking place in international contexts, shows a similar pattern to FDI. This suggests a connection between the decline in FDI and the slowdown in GVC trade, emphasizing the importance of GVCs in shaping international trade and investment.

FDI, trade and GDP trend, indexed 2010=100



Source: UNCTAD, 2024

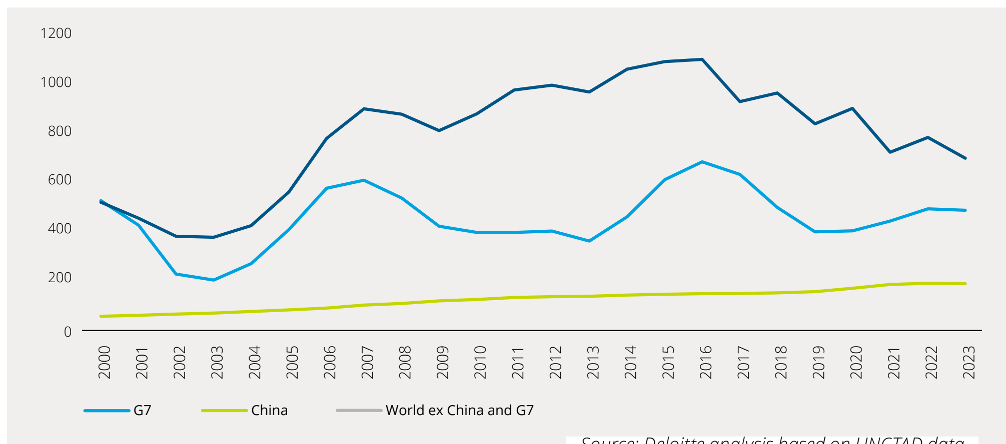
Source: [5] UNCTAD, 2024 Link | [6] UNCTAD, 2024 Link

Foreign direct investments

The regional rebalancing of global FDI has been significantly influenced by the declining share of China as a recipient country, specifically for 2023. FDI inflows to developing economies, which have been robust over the past few years, declined by 7% in 2023. FDI to developed economies, net of conduits, fell by 15%, affected mainly by corporate financial reconfigurations – driven in part by moves to introduce a global minimum tax for large MNEs – and by a sharp drop in the value of cross-border M&As. In recent years, G7 countries have experienced better dynamics despite the weak growth of FDI worldwide, especially compared to China's.

FDI flows from public institutions play a crucial role, as projects financed through these entities are typically high in value and impact. In particular, the World Bank, the International Monetary Fund and the Paris Club have historically been the most relevant providers of FDI to developing countries. In the last decade China's Belt and Road Initiative has played an increasingly large role in this space. In 2022, the G7 announced the PGII, pledging to invest 600 billion US$ by 2027.

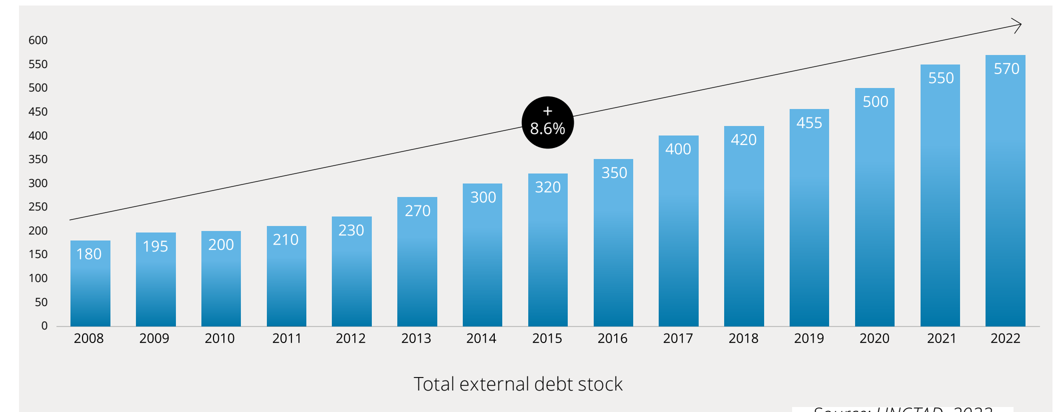
FDI inflows, (Billions of dollars, three-term moving average)[7]



Source: Deloitte analysis based on UNCTAD data

However, the role of such investors has developed from investors to full-fledged creditors. This trend poses new challenges, as it increases the financial burden on recipient countries. Since the beginning of the 2010s, least developed countries have started to be increasingly indebted towards external creditors, signaling a critical issue that needs to be addressed. Moving forward, the challenge will lie in balancing the need to guarantee adequate investment flows for the green and digital transitions while making sure investments and debt profiles remain sustainable.

External debt stock of least developed countries[8]



Source: UNCTAD, 2023

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Source:[7] Deloitte analysis based on UNCTAD data| [8] UNCTAD, 2023 Link