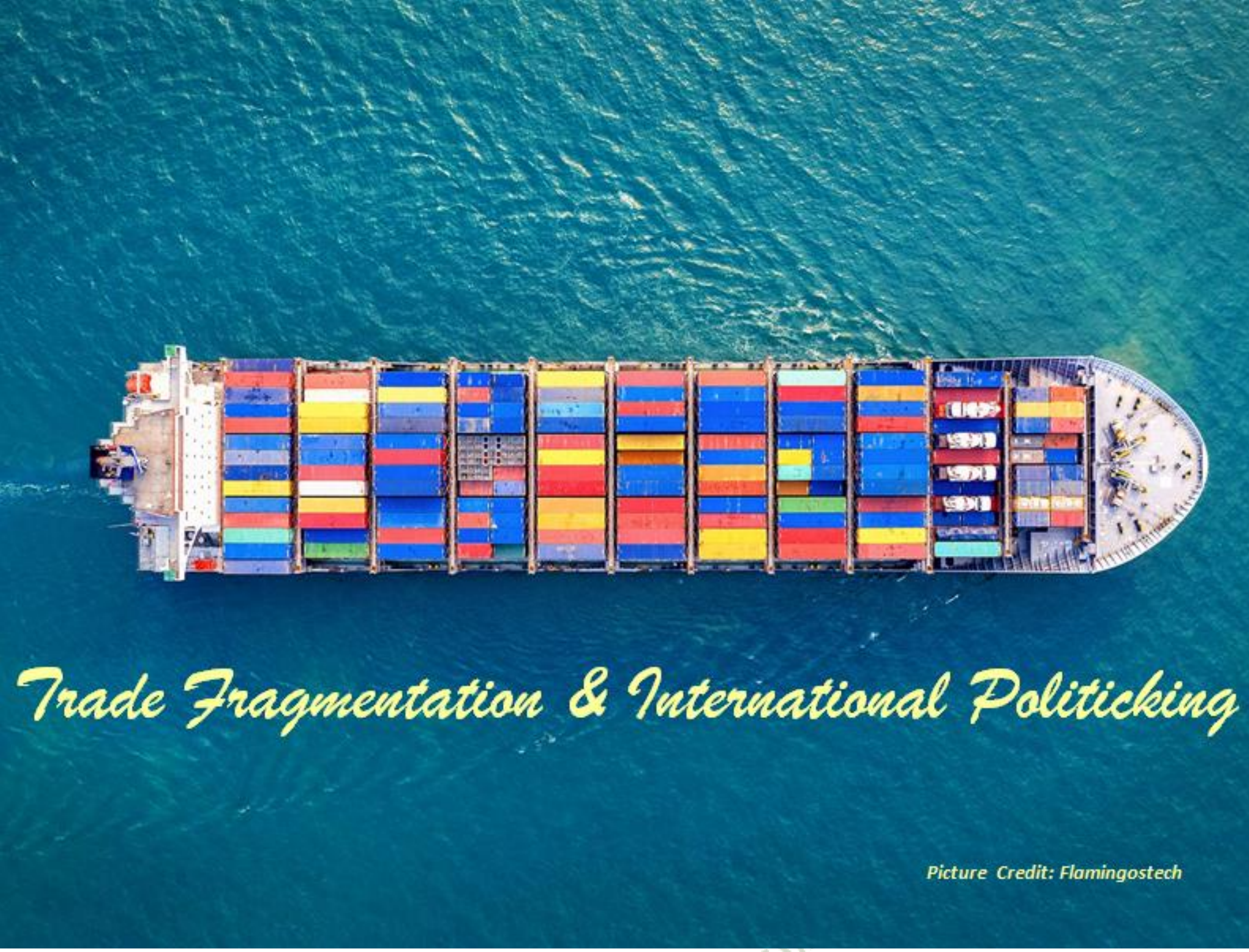

Trade Fragmentation & International Politicking

Picture Credit: Flamingostech

The shift from a uni-polar to a multi polar world has far-reaching implications beyond geopolitics. The paradigm shift in how the world had started conducting its trade, in the era of globalization, has started facing unforeseen hurdles because of emerging power dynamics. Supply chains, once reliable, are now vulnerable to unpredictable international relations. Additionally, traditional shipping routes are increasingly disrupted by piracy and regional conflicts. If the current precarious situation persists, trade fragmentation—the true offspring of globalization—might face severe challenges before it fully matures.

To understand trade fragmentation and its impact on global power dynamics, it is important first to know what it exactly means. Trade fragmentation refers to the process where different components of a finished product are manufactured in various parts of the world and then assembled in a separate location. This approach is driven by several factors, including the availability of technology, access to inexpensive natural resources, and cheap labour, with the primary goal being to reduce the per unit cost of the product.

A well-known example is Boeing, whose airplane parts are produced globally but assembled in Seattle, USA. Businesses prefer sourcing parts from politically friendly countries, as this facilitates smoother operations and reduces *complications. This preference is not limited to manufacturing; the services sector also expands internationally by establishing branches in other countries. In the food industry, companies like Coca-Cola, Pepsi, and KFC are prominent examples. In these cases, while ingredients are sourced locally, the technology used remains American, ensuring that a KFC chicken wing or a Coca-Cola bottle tastes the same in New York as it does in Lagos.*

In the era of online businesses, Amazon, Wal-Mart, and eBay stand out as prime examples of trade fragmentation, where products sourced globally can be delivered to any postal address. Globalization and technology have undoubtedly made the world a more convenient place to live.

However, the situation has changed drastically in the past three years. With Russia's invasion of Ukraine and the severe economic sanctions imposed on Russia, many prominent Western brands across diverse industries, including automobiles, food retail chains, and pharmaceuticals, had to cease their operations in Russia abruptly. Even before the Russia-Ukraine conflict, COVID-19 had serious repercussions on global supply chains. China considered the world's manufacturing powerhouse faced increasing scrutiny from the West for its actions during the COVID-19 pandemic.

But now disruption has reached epic proportions with the United States under the Trump administration declaring high tariff rates to prevent foreign goods and services swamping the country. At the core of this planned disruption is to ensure that all goods consumed in the USA should be manufactured locally so that the country regains its premiere manufacturing base stature which no doubt post globalisation has been hijacked by countries like China, Canada, Mexico and many other Asian countries.

This discussion delves into the new dynamics of trade fragmentation, exploring whether this unique phenomenon can withstand the uncertainties of the mid-21st century. The paper focuses on contemporary geopolitics, particularly with the emergence of three spheres of influence driven by the US, Russia and China. It examines how this geopolitical landscape impacts trade fragmentation and what the future might hold in this context.

While the world is witnessing the resurgence of power blocs, it is important to note that a significant number of nations are not fully aligned with either major bloc as these superpowers might desire. It is this group of unaligned nations that will play a crucial role in shaping the future of trade fragmentation.

Trade Fragmentation & State of the World

While the G7 countries and the European Union were broadly categorized as allies in the global power dynamics, that existed so far; Donald Trump in his second stint as the president of the United States has chosen to upset the apple cart. His disruptive policies are targeted to ensure that the US allies who usually benefit from one sided trade deficits, be made to pay for the largesse that they have enjoyed so far. He has ordered tariffs to be charged for all imports made from Europe and Canada. This has not only send the US allies into a top spin, but also other American trade partners suddenly find themselves at the receiving end of Trump’s ire.

And the most affected is China. At the time of writing this article Trump has imposed a massive 145% tariff on the goods imported from China, with the latter promising reprisals for US goods being imported into China. Unfortunately the Chinese import very less, in fact US exports into China form a very small percentage of the goods exported by China to the US.

While the regular US trade partners seem to be confused at the sudden imposition of the tariff regime; the rest of the world are rushing to secure bilateral trade agreements (BTA) amongst themselves and the US.

The role of the Asian Tigers and some other nations in shaping the future of trade fragmentation is crucial.
Over the years, several developing countries have established impressive manufacturing bases that produce high-quality products. These countries include India, Vietnam, Thailand, Indonesia, Bangladesh, the Philippines, Cambodia and Malaysia in Asia; Mexico, Brazil and Ecuador in the Latin Americas, and some others in Africa. Many of them engage in contract manufacturing, wherein they are hired by some of the world's largest brands to manufacture entire products or components. The primary allure of these brands is the low cost of labour available in these countries.

Understandably, these countries strive to maintain good relationships with the nations that host these renowned brands, as their economic progress becomes increasingly tied to the demands of these large businesses. Globalisation has been witness to these countries being subjected to overexploitation of labour and natural resources, including non-renewable energy sources by some of the best known consumer brands in the world.

Despite these challenges, developing countries often welcome large businesses to establish manufacturing bases. The immediate benefits are significant, including employment opportunities for thousands of citizens and the development of a robust manufacturing ecosystem, which enhances the overall quality of production in these countries. However with the new Trump dictates, most of these economically fragile countries like Bangladesh and Sri Lanka face severe complications ahead. (For information the Trump administration has imposed 37% & 44% tariffs respectively for these two countries). For one they stand to lose their manufacturing bases leading to large scale unemployment and consequently increase in poverty. Secondly their poor citizenry does not have the resources to buy the high value goods from the US to meet their needs.

Looking at the high tariffs proposed on goods and services being imported from poor economies like Bangladesh and Sri Lanka, from the US perspective this can be a double edged sword. United States may benefit from having the manufacturing bases back, but at the same time they may not be able to sell their excess products to the third world countries because of their prohibitive costs.

The concentration of major business conglomerates in the USA and Western Europe had shifted geopolitical influence in their favour. Globalization had fostered favourable trade relations with developing countries that host their manufacturing bases.

For example, despite a decade-long war with the United States, Vietnam is now considered a friendly nation towards the USA.

But the situation seems to be extremely fluid presently as the US settles for a new tariff regime. The primary objective of the Trump administration is to ensure that manufacturing bases are reopened in the US so that Americans are able to secure more jobs in the country. Earlier as pointed out globalization has helped shifting expensive manufacturing bases in the US to other economies with cheaper manufacturing costs.

This shift was particularly evident in China, Taiwan, Vietnam, South Korea, India, Mexico and Canada. But with the new trade order being forced by the US, there is churn in the way the big brands are working. Back of the envelop calculations are being done by the executives in these companies working out, which countries will provide a cheaper manufacturing base, and also how much tariff is being charged by the US on goods produced in that country. Thus an automobile component produced in China which attracts 145% tariff in the US should shift base to India which is attracting only 26% tariff.

The unique position enjoyed by China so far

If any country has reaped the most benefits from globalisation and trade fragmentation, it is likely China. At the turn of the century, China implemented policies to provide government assistance in establishing manufacturing units that met international quality standards. This strategy enabled the country to secure numerous manufacturing contracts from some of the world's largest brands. Subsidized power and a range of other government-supported incentives acted as magnets, attracting major businesses to set up their manufacturing operations in China. Not only did Western companies find China attractive, but businesses from Japan, Taiwan, and India also followed suit.

The fact that most supply chains run through China carries significant geopolitical implications. Many countries had raised security concerns regarding electronic products manufactured in China. So far the Chinese have played this game skilfully. After securing the manufacturing rights of major global businesses from 2014 onwards, China has gradually begun to exhibit its imperialistic ambitions. It has not only vocalized its long-standing desire to annex Taiwan but also laid claim to vast areas of the South China Sea, including numerous islands that fall within the exclusive economic zones of the Philippines, Brunei, Indonesia, Malaysia, Vietnam, Japan, South Korea, and, of course, Taiwan. The situation is highly complex, as many of these countries depend heavily on Chinese manufacturing lines for their brands. For instance, Sony and Samsung, from Japan and South Korea respectively, have significant production units in China.

It seems China wants to not only achieve its territorial ambitions but also retain manufacturing rights from businesses across countries. But the recent actions by US are sharply pruning China's ambitions.

Trump's anti China directives

The consequences of the US imposing a 145% tariff on Chinese goods once they touch the US ports are far reaching. As on 2023 approximately 15% of Chinese worldwide export of goods was exported to the US. This amounted to more than $ 502 billion. Loosing such a huge lucrative trade partner can be very punishing for the Chinese. They are left with no alternative but to look for other countries which can absorb this loss of revenue. But no country other than the ones in European Union has the funds to import goods worth $ 502 billion.

This is forcing the Chinese to revamp their policies not only trade but also the way they conduct their geopolitics. All of a sudden they find that in these uncertain times it may not be wise to push ahead with their imperialistic ambitions. ***Clearly at one stroke of pen Trump has gone for the Chinese jugular***.

Future of Trade Fragmentation in the era of new power equations

In spite of the present disruptions the future of fragmentation in international trade still looks promising, although it will be confined to more limited geographical areas. Unlike in the past when China dominated global manufacturing, emerging geopolitical pressures are creating opportunities for other developing countries. What China loses, others stand to gain. In the aftermath of COVID-19, many countries had made concerted efforts to establish alternative supply chains that bypass China. As a result, nations like India, Vietnam, Mexico, the Philippines, and several other South Asian countries are becoming significant beneficiaries of these shifting geopolitical dynamics. Without doubt this shift is also aligning these and other developing nations more closely with Western countries.