Geopolitics, Trade and Foreign Relations

Agbiz Conference

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6 June 2024

Introduction

The world we live in is marked by rising geopolitical tensions, which hamper international trade. South Africa is a trade-dependent economy, and agriculture is an export-oriented sector. Data compiled by Agbiz early this year showed that total agricultural exports reached a new record of US$13,2 billion in 2023, up 3% from the previous year.

An open global economy is essential for South Africa's long-term growth and prosperity. The agricultural sector cannot do without an open global economy. The sector's continued growth requires predictable global supply chains and deepening global interdependence.

The fractures we witness today are not good for global stability; they are bad for our economy. Weak supply chains pose a risk to input prices and supplies of critical implements and inputs. There are other difficulties facing the global economy I intend to discuss today. The point is not to dwell on problems but to determine the best course of action in preparing for the storms that lie ahead. Now, turning to the subject of geopolitics and supply chain risks.

Geopolitics and Supply Chain Risks

Although we are undoubtedly post-pandemic, we are clearly not post-crisis. The world has faced multiple risks since the end of the COVID-19 pandemic. The escalation of the war in Ukraine in February 2022 has triggered new incidents of geopolitical friction that

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have spilled over into trade. Sanctions against Russia and tensions between the US and China over trade and technology have worsened. The Trans-Atlantic Alliance has a renewed focus on dealing with what the West calls “China’s overcapacity” problem.

Many are concerned that the new geopolitical challenges will affect long-term growth. Recent figures from the IMF and WTO reports show that global growth has picked up, and international trade is steadily rising. However, disturbing trends have emerged that weakens global supply chains and compounds global uncertainty. These trends are tied to geopolitics, friendshoring, and new global regulations targeting imported products.

What are the features of this new trend?

i) We have seen that geopolitical risks have spiked since 2022, when the war in Ukraine started, with trade and investment flows increasingly following geopolitical alignments (“friendshoring”). Trade and FDI flows between blocs that are not geopolitically aligned have declined by roughly 12 to 20 per cent.

ii) A recent IMF report shows that new trade restrictions have increased sharply and more than tripled since 2019. This delecerates and and fragments supply chains.

iii) The use of industrial policies by advanced industrial economies is becoming frequent. Just last year, there were 2500 incidents of industrial policy measures used mainly by developed economies and China.

- These measures distort investment flows and competition. Many developing countries, including ours, cannot compete fiscally in an environment of subsidies-driven industrial policies.

iv) Furthermore, financial sanctions are rising and imposed on trade and investment relations, reinforcing proxies of what could become a new Cold War.

- The changing geopolitical landscape poses a challenge for our foreign and economic relations and choice of partners. We are entering a dispensation of neat binaries, where the mantra – are you for us or against us – could become a core feature of foreign policies of major powers.

v) "Today's fragmentation", the IMF points out, "is not significantly different from the initial years of the Cold War". However, trade fragmentation is costlier today than it was during that period. At the start of the Cold War, goods trade to GDP stood at 16%; today, this is at 45%, which means that the risk of global fracture could have far-reaching implications than during the Cold War. Geoeconomic fragmentation, as the IMF World Economic Outlook notes, "could reduce portfolio and foreign direct investment, slow the pace of innovation and technology adoption, and constrain the flow of commodities across the fragmented blocs, resulting in large output losses and commodity price volatility".

vi) There is, however, another interesting development that is emerging and linked to geopolitics. This is about a new group of countries called *connector* countries, which serve as conduits for trade flows between geopolitically fragmented blocs, essentially between the US and China. These *connector* countries, including Mexico and Vietnam, have cushioned the decoupling of China and the US. They serve as a glue against deeper global fragmentation. Since they are not geopolitically aligned, they are reaping dividends for their non-aligned positioning. Their unspoken mantra must be to *make no enemies and multiply friendships*.

Lessons from these trends

What all of this means is that we are not yet experiencing deglobalisation. The bigger lesson is that it pays to be non-aligned and have an open trade and investment regime.

It is clear to me that the world will not be what it was pre-pandemic and pre-war. Geoeconomic contestations and friendshoring in the patterns of trade and investment flows will continue to be major factors shaping global economic relations for the foreseeable future.

Global leaders must think seriously about boosting global supply chain resilience. As a global commercial player, South Africa's agricultural sector must make rational calculations about how it navigates the difficult geopolitical terrain. Before offering my thoughts on how we might go about this, I'd like to highlight yet more raging storms ahead.

Industrial Policies and New Regulations

As I have noted earlier, advanced industrial economies have ratcheted up the use of industrial policy measures to boost their competitiveness in green sectors, especially in the face of China's rising competitiveness.

The EU has its New Green Deal, which is linked to its climate law and aims to create an environment that attracts green investments within the EU. The EU provides state aid, grants and relaxed competition regulations to direct investment flows into the green sectors, while using "green" protectionist measures to discipline imports of carbon-embedded products. Some of these regulations are in the form of carbon border adjustment measures and deforestation regulations, and will affect both the agricultural and industrial sectors.

On the investment side, the EU has recently adopted a Corporate Sustainability Due Diligence Directive (CSDD), which makes it obligatory for the EU companies and their subsidiaries to account for environmental and human rights risks in third countries across their supply chains.

For its part, the US has the Inflation Reduction Act, which provides a combination of subsidies, tax breaks and local content requirements to build new industrial capabilities in the green sectors. The trend towards sustainable and green agriculture will likely gather pace with new protectionism becoming common place.

Quite clearly, the Western world is becoming increasingly inward-looking as part of derisking supply chains from countries deemed geopolitically unfriendly. We want to avoid being caught in the crossfire.

What do all these developments mean for us in South Africa?

First, these developments are restructuring global economic relations in profound ways, with protectionism advancing along the intersections of geopolitics, trade, and environment. This challenges industries and firms to rethink their supply chain management, including contracts in the long term.

Second, it makes it all the more important that government and business work together to respond to the changing global realities. This is particularly essential for the agricultural sector whose fortunes are tied to an open global economy, conducive international trade environment, and predictable global supply chains.

Third, we must do all we can to defend and grow our export markets. As the recent figures by Agbiz show, South Africa enjoys a trade surplus of US$1.4 billion on the back of a buoyant sector in Quarter 1, where we registered $3.1 billion in exports. The lead regions and countries beyond the African continent (which absorbs 42% of our exports) are Europe at 22%, Asia and the Middle East combined at 19%, and the Americas at 6%. Reversal is not an option. Complacency is not a strategy. We need to be more proactive than be at the mercy of the vicissitudes of geopolitics.

Fourth, we must be more deliberate about defining the future directions of our trade through aggressive opening of non-traditional markets, especially in Asia and the Middle East. This becomes urgent given the new EU regulations, which will hit our exports hard, from agriculture to manufacturing.

Fifth, we must build on the Agriculture and Agroprocessing Master Plan (AAMP) to navigate the treacherous waters of geopolitics. Two years ago, when we concluded the master plan, we constructed a good framework for dealing with domestic structural challenges, including those related to transformation and inclusion, and we defined the policy outlines for supporting the sector's growth and competitiveness. We must act with urgency while building capabilities and coordinating efforts to open new markets for the sector's long-term growth and prosperity.

Conclusion

In conclusion, we must not forget that there are opportunities in a crisis. Where we are today reminds me of a fable told by the business thinker, John Kotter, in his book titled, *Our Iceberg is Melting*.

In short, this was a story of a colony of penguins who took for granted the permanence of their home until signs of melting started to appear. They realised that all along they had a false sense of security and that change – sometimes disruptive change – is a part of life. They needed to make quick arrangements to find a new abode that would last for generations.

South Africa still commands respect internationally, but we should not take this for granted. There is much we can accomplish when we work collaboratively as part of South Africa Inc. The geopolitical realities we face today also present an opportunity for us to pivot into new directions. We must direct our efforts towards accelerating innovation at home, uncovering new sources of vitality in sustainable agriculture, and finding new export markets abroad.

Thank You