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T20 Policy Brief

Task Force 04

TRADE AND INVESTMENT FOR SUSTAINABLE AND INCLUSIVE GROWTH

Rising Blocs in Trade and Industrial Policy. Is Economic Security the Future?

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Abstract

In a world torn apart by geopolitical tensions, policymakers are facing multiple crises, leading to what economists have labelled as a new “global dis-order.” Simultaneously, the resurgence of industrial policy signals a return to state intervention in the economy. Although the emphasis has shifted to de-risking rather than decoupling, the United States and the European Union are actively seeking to reduce their dependencies on China in key sectors. This approach will have economic and geopolitical implications, potentially fostering increased trade among politically aligned trading blocs.

Understanding this new landscape is imperative as economic, geopolitical, and climate challenges converge, leading to unprecedented tensions. By examining the impact of neo-protectionist policies on global trade, the objective of this policy brief is to design ad-hoc recommendations for navigating the current challenges in Global Value Chains (GVCs). The policy brief presents the tools used by governments to implement industrial policies, highlighting how “economic security” sometimes can provide cover for protectionist policies. The brief discusses the interplay between trade and industrial investments, focusing on the chips and clean tech industry. It also offers actionable recommendations for calibrating economic security tools to prevent the race into economic weapons that could undermine the GVCs efficiency.

Given the redistribution of global economic power, the G20 is in a unique position to take a proactive role in shaping the outcome so as to safeguard global stability, development, and environmental goals. This brief envisions a future marked by increasing trade, technology and industrial exchanges among like-minded countries, with the Global South that is set to play a key role. Notwithstanding, an agreed agreement on a set of agreed rules for international trade and economic relations is pressing to de-escalate tensions and ensure the smooth functioning of international markets.

Keywords: Economic Security, Minilateralism, G7, Industrial Policies, Global South



Diagnosis of the issue

In a world rife with geopolitical tensions, policymakers grapple with many crises, giving rise to what economists dub a new "global dis-order."¹ Concurrently, industrial policy is resurging, signaling a return to state intervention in the economy. While some argue for "de-risking" over "decoupling," notable powers like the United States and the European Union are actively promoting policies aimed at reducing dependencies on China in pivotal sectors. This shift carries significant economic and geopolitical implications, fostering trade within politically aligned trading blocs.

Understanding this evolving landscape is crucial as economic, geopolitical, and climate challenges converge, leading to unprecedented tensions. This policy brief aims to explore the impact of neo-protectionist policies on global trade and design tailored recommendations for navigating the current challenges within GVCs. By scrutinizing the tools governments employ to implement industrial policies, this brief highlights the emergence of protectionist attitudes under the guise of "economic security." It delves into the intricate interplay between trade and industrial investments, focusing on chips and clean tech sectors. Over the past few years increased geopolitical tensions and intensified competition have overlapped and fed into domestic pressure to enact industrial policy aimed at enabling and capturing growth from the energy transition. Although national and economic security concerns have in many cases been warranted, they have also fed into protectionist trends that are increasingly visible in some countries' trade policies.

¹ [El-Erian, Mohamed A. "The Growing Risk of Global Disorder," Project Syndicate, December 14, 2023.](#)

Furthermore, the study offers actionable insights for calibrating economic security tools to avert a race toward economic weaponization, which could undermine the efficiency of GVCs. Given the redistribution of global economic power, envisioning a future characterized by increased trade, technology, and industrial exchanges among like-minded countries is imperative, with the Global South poised to play a pivotal role. However, establishing a consensus on a set of rules for international trade and economic relations is essential to de-escalate tensions and ensure the smooth functioning of international markets.

The rise of economic security tools reflects a reality where countries increasingly seek to safeguard critical economic sectors and advanced technologies. The tools of economic security are different and growing in number and scope, such as export controls (e.g. semiconductors, graphite and germanium), investment screening, industrial policy (e.g. I.R.A.), trade defense tools (e.g. EV anti subsidy investigation in the EU), but also long-term indigenization policies (Made in China 2025 as the leading example). Even though they help address national security concerns, such tools' widespread and uncoordinated use could disrupt international markets and weaponize interdependencies, potentially reducing global economic output over the long term. Moreover, economic security measures could impede advancements in cutting-edge technologies crucial for the green transition, complicating efforts to achieve global climate targets.

These economic security tools inevitably strain trade relations among countries, eroding global trust and undermining a rules-based, open, sustainable, and transparent multilateral trading system. Such measures must adopt a non-discriminatory, country-agnostic approach, yet recent trends indicate a propensity for country-specific measures, especially in the context of US-China economic tensions.

The global response to the current disorder has led to a crisis within the multilateral institutions established post-Bretton Woods. The proliferation of minilateral groupings, characterized by uniform political positions, challenges the existing order and risks impairing global economic efficiency. These groupings can be either diplomatic initiatives (such as the US-India-ROK trilateral technology dialogue) or established regional economic agreements. However, the rise of minilateralism, resulting from a global multilateral system that is often no longer effective, could represent a suboptimal yet practical and adaptive framework. This framework aligns well with the ongoing reconfiguration of global trade dynamics, where geopolitical alignment is increasingly regarded as a key factor to consider.

As the most prominent institution convening both G7 countries and emerging economies from the Global South, the G20 emerges as a potential arena for reconciling minilateralism and addressing the major externalities of the economic security approach. Indeed, it is crucial to balance economic security with the emergence of new tools, while maintaining a relatively open global economic system. This approach helps preserve at least some critical pillars of a rules-based, sustainable, and transparent multilateral trading system, and addresses some of the main risks recalled for instance by the 2023 G20 Trade and Investment Ministerial Meeting in Jaipur, India.

Recommendations

Given the presented diagnosis of the issue, this brief aims to address the following outcomes:

1. Reduce the cost of economic security

- a. How to achieve a green transition and technological development while promoting domestic industry: strike a balance between economic security and economic efficiency.
- b. Set a level playing field, a minimum set of internationally agreed rules and a general framework for economic security tools at the G20 level.
- c. Promote international tools to avoid economic coercion, in particular for vulnerable countries.

2. Make the economic security tools work within the broader international trade agreements. In particular, reducing the costs of economic security can actually increase the level of coherence of these tools with international trade agreements.

Having said that, the main recommendation for all G20 members to counter rising blocs in trade and industrial policy is to 1) accept that member countries will now pursue some economic security policies and 2) work together to minimize the negative effects of such policies while increasing the level of economic resilience.

The following more specific recommendations are based around seven pillars of economic security, as formulated by the G7 in 2023. This is not because they are the only formulation in town, but because they are ones around which a significant number of G20

member countries are already acting – simply due to the significant overlap of membership between the G20 and the G7.

Among the latter set of countries, the very formulation of these seven pillars is only one recent instantiation of the growing economic security agenda. For example, in 2021, Japan appointed a minister for economic security, Sanae Takaichi, as part of a diverse portfolio. Similarly, in early 2024, the European Union adopted five initiatives: inbound foreign investment screening, coordination of export controls, risk identification of outbound investments, research and development of dual-use technology, and the enhancement of research security. These initiatives, which share significant overlaps with the G7 list below, reflect an early distillation of the European Economic Security Strategy of June 2023.

It does little good to underestimate the extent to which some of these measures are taken in response to real and perceived policies of other G20 members. This is not to single out G7 countries who have more openly than many others expressed the boundaries of their economic security policies. It simply means that the repercussions of said policies are real and all should work to minimize the fallout of economic-security policies. As is the nature of such policies the countries pursuing them also have much to lose. In such a spirit we offer recommendations on how G20 members should think of this effort.

3. Recommendation on “building resilient supply chains”

Support the creation of value chains that are additive and more diverse than in the past. This can help add value to the global economy and, in effect, triggering counterproductive fragility in existing supply chains. New value chains can be created in addition and not in lieu of existing supply chains, thus also contributing to resilience through both

redundancy and novelty. While in a world of shifting trade patterns this may be a tall order^[4], it is nonetheless an essential mindset.

4. Recommendation on “creating resilient critical infrastructure”

G20 countries should recognize that infrastructure is increasingly an arena of hybrid warfare and commit to counteracting this trend. Member countries should make commitments to forgo threats to infrastructure, allowing more of it to remain primarily within the realm of economics rather than security. Cyber or physical attacks on critical infrastructure—such as ports, pipelines, or electricity grids—by malicious actors are a major concern at the international level and could disrupt the smooth functioning of global supply chains.

5. Recommendation on “addressing non-market policies and practices”

Participants in the global economy should recommit to engaging on an equal footing in the marketplace, especially in arenas in which security concerns are of lower intensity. This means that while trade is shrinking between more geopolitically distant partners it is not to disappear. G20 member states should focus on making the remaining trade as smooth as possible.^[5] This can be done with a commitment to market practices.

6. Recommendation on “tackling economic coercion”

G20 countries ought to establish a working group dedicated to identifying strategies for mitigating economic coercion. Simultaneously, efforts should be made to reach a consensus on a universal definition of economic coercion and establish criteria for identifying instances of such coercion.



7. Recommendation on “countering harmful practices in the digital sphere”

We increasingly see the digital sphere being divided by geography. G20 states should commit themselves to an open digital sphere and set a minimum standard for acceptable conduct. In particular, it is key to strengthen cooperation on cybersecurity and countering the weaponization of the digital sphere.

8. Recommendation on “collaborating on international standard-setting”

Even with a more divisive global economy there is much to be gained in terms of global wealth and health by standard-setting. Especially, on questions of common concern such as disease and medicine or climate and environment the global standards should be emphasized to allow for the most flexible responses to both fast and slow-moving threats. Our shared responses should not be hampered due to divergence on manufacturing or operating standards.

9. Recommendation on “adopting a country agnostic approach on economic security”

Economic security tools shall entail objective criteria and possibly avoid the targeting of specific countries. This is key to avoiding a spiral of reactions that could be even more harmful to the global economy.

10. Recommendation on “preventing leakage of sensitive critical and emerging technologies”

The securitization of growing realms of technology is a strengthening trend. Member States should take active steps to forswear practices such as cyber espionage. International cooperation at the G20 level is key to adopt a common framework to

coordinate actions aimed at preventing the leakage of critical technologies, especially in the digital domain.

In addition, with the aim of promoting prosperity among the G20 members, other recommendations should be considered, such as:

a) Strengthen commitment to transparent and well-audited supply chains that can facilitate companies' compliance with increasing requirements internationally to document ownership, the absence of forced labor, carbon emissions, and other requirements throughout the value chain and their suppliers. More coordination and creation of common standards on a voluntary basis between G20 countries would be particularly beneficial and would mitigate ongoing tension due to concerns over the weaponization of interdependence.

b) Renew commitment to the WTO with the aim of improving its functionality and adopting reforms aimed at prioritizing climate goals and stable trade relations.

c) Use working groups to explore the least common denominator among the G20 countries as a starting point for future negotiations on more technical aspects.

Scenario of outcomes

The current trajectory diverges on an agreed definition of economic security, increasingly fostering zero or even negative-sum thinking. This path will likely entail escalating costs and potentially less resilient GVCs due to economic security measures.

The alternative path outlined above emphasizes the exploration of positive-sum relationships within the G20 and, crucially, with third countries. Smaller economies face even greater challenges in adapting to a landscape marked by restricted market access, rising prices, or other consequences of heightened economic security.

Adopting these recommendations doesn't signify a departure from a realm of heightened economic security. Given the current trend among most G20 members towards managed trade, achieving an entirely open market is not feasible in the foreseeable future. However, even within managed trade frameworks, positive measures can be pursued.

In principle, there is no reason why shared positive agendas should not be attainable. In some cases, such as climate-related issues, these agendas may align with the interests of most, if not all, G20 countries. Despite acknowledged limitations, G20 nations should aim not only to establish minimum international rules for economic security tactics but also to foster a more efficient global economy.

The urgency for clean energy and a green transition has significantly increased demand for minerals like cobalt, lithium, nickel, graphite, and rare earth elements (REEs). However, while natural deposits of these minerals are widespread globally, their mining, processing, and refining are geographically concentrated. China notably dominates the global market for several critical minerals and holds substantial reserves, alongside expertise in mining and refining. Many countries in the Global South possess abundant



natural reserves of critical minerals but lack refining capacities, resulting in a trade pattern where ores mined in one location are processed elsewhere. Failure to implement recommendation #1 could allow certain countries to significantly influence critical mineral trade, affecting supplies and prices. Such control over critical mineral supply chains undermines global economic security through inclusive trade. On the contrary, technological advancements play a pivotal role in providing new solutions that could bolster countries' economic security, thereby reducing strategic dependence on single suppliers. For example, emerging innovations, such as sodium-ion batteries, have the potential to be game-changers by substituting critical minerals like lithium and cobalt with more affordable, widespread and readily available alternatives, particularly sodium.

Achieving consensus across the G20 is crucial to mitigate risks stemming from the rise of economic security, as efforts to diversify sourcing continue through friend-shoring and near-shoring of supply chains. Geopolitical imperatives for relocating supply chains among friendly countries often conflict with the logic of location-agnostic geographical specialization driven by economic efficiency. This specialization has integrated SMEs and workers from many parts of the Global South into global supply chains, creating new jobs, reducing poverty, and fostering consensus. However, as chains shift, they may erode these benefits, particularly if driven more by politics than economic efficiency. This could adversely affect overall economic security.

Global trade faces mobility challenges as major shipping routes, such as the Suez Canal and Panama Canal, confront geopolitical and climate threats. Insufficient alternatives for transporting goods between continents will continue to elevate trade costs through extended transit times, higher shipping charges, and increased insurance premiums. Protecting major trade routes and shipping lanes should be a top priority at the G20 Summit. Finding cooperative solutions, including joint military naval operations, is

essential to enhancing the security of key maritime routes and ultimately reducing the risk of disruptions to global supply chains. The rapid development of new connectivity options, like the Middle Corridor or the India-Middle East-Europe economic corridor (IMEC) – the latter announced by G7 countries, India, Saudi Arabia and UAE on the sidelines of the G20 Leaders’ summit in Delhi – is essential. The creation of new land bridges – with related infrastructure connectivity such as railway lines – is key to offer alternative routes to the main global maritime chokepoints. Alongside efficient multi-modal transit options, such new connectivity routes must ensure security to prevent further losses for businesses and sustain global trade.



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