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COFACE ECONOMIC PUBLICATIONS

By Julien Marcilly - Chief Economist
Mélina London - Junior Economist
and Matthew Fontes-Baptista - Junior Economist, based in Paris, France.

World trade: despite a sudden interruption, global value chains still have a bright future

EXECUTIVE SUMMARY

In the midst of the COVID-19 pandemic, global trade has been dragged down by numerous factors: a global recession, skyrocketing uncertainty, restriction and rising cost of transport and localized protectionism targeting supply of food and critical medical wares. On the bright side, tight border controls have had a limited impact on trade and are being eased gradually in Europe, in order to revive the tourism industry and limit labour shortages in the agricultural sector. In the longer-term, multiple calls to relocate production domestically also constitute risks to the future of global trade. Nevertheless, shielding production from foreign supply shocks seems like an impossible quest: to imagine a full relocation of manufacturing processes at the domestic or regional level highlights issues of rising production costs and lack of domestic skills. Even if these two issues are addressed, this new local production process will still be dependent on raw material supply, which is highly location-dependent. Mitigating the exposure to one specific country by diversifying suppliers is also a tricky challenge. At first glance, finding alternatives to the top supplier country (i.e. China in most sectors) is possible. However, major input producers are also strongly connected to one another, which means that the exposure will not disappear even when input supply to other major hubs in the sector is diversified. Overall, the good news is that global value chains still have a bright future.

World trade in 2020: a sudden interruption

World trade has been dragged down by the global recession, skyrocketing uncertainty…

Global trade dynamics are linked to economic activity: if the GDP of two countries increases, the value of goods and services they trade with each other increases as well. However, this link changes over time. Dynamic world GDP growth between 2002 and 2008 went hand in hand with a strong growth of global trade, at around 6% per year. Both slowed down significantly during the following decade and the world trade growth to world GDP growth ratio has remained at around 1 since 2011, i.e. twice as less than between 1990 and 2006. Nevertheless, during crisis periods, magnitudes differ: while global GDP growth declined by "only" 1.7% in 2009, the volume of good and services traded internationally plummeted by 12%. Therefore, the magnitude of the expected decline of global trade this year is hard to assess. According to our in-house model, which uses oil prices, business confidence in the US manufacturing sector, South Korean exports and the Baltic dry index of maritime transport as explanatory variables for global trade, the latter would decline by 7% in the third quarter of 2020 compared to the previous year and by 5% on average in 2020. However, as explained