SOCIO-ECONOMIC VOICES

"Impact of Geo-strategic Developments on the Global Economy"

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What are the consequences of the current geo-strategic disruptions on the global economy? This is a question which is increasingly getting asked as we enter 2024. To put it in context there are at least five issues which need immediate consideration; these are (a) regional conflicts and tension build up, (b) management of climate change and decarbonisation issues as that is creating weather disruptions, floods, etc., (c) elections are due in forty countries; these can lead to regime change and policy change, (d) how to use disruptive technology like AI for value addition without creating social disruption and major unemployment issues, (e) is the issue of deglobalisation a bit overstretched.

So far as regional wars are concerned any plausible resolution is not immediately visible, notwithstanding the battle fatigue in the field and funding hesitancy on the part of USA the Ukraine-Russia war is continuing. This in its turn can keep fuel and food prices at an elevated level. This has also constrained energy availability in the Eurozone area; both consumers and firms have been affected adversely. The brutal conflict between Hamas and Israel has the potential to spill over to other MENA countries. This can lead to higher energy prices and blockages in the shipping routes to Europe from Indo-Pacific region. Both these developments can add to cost and lead to higher inflationary expectations, leading to tight money period getting extended. The third area of tension build up is in South China Sea and Taiwan Strait. There is also increased Chinese activity in the Himalayan border area with India. These developments have the potential to adversely impact cross-border trade, flow of capital, investment and technology. According to the recent Global Financial Stability Report of IMF- the build up of tension between USA and China since 2016 has reduced overall bilateral allocation of portfolio investments and bank finance by 15%. According to the IMF study investment funds are quite sensitive to the divergence in the foreign policy outlook of the recipient country.This buildup of tension between USA and China will provide opportunities to other emerging economies like Mexico, India and Vietnam. This would be in terms of friend shoring of manufacturing by US companies and funds flow. These flows can include both long term investments and portfolio funds.

Unipolar world of the nineties which emerged after the collapse of Soviet Union has been replaced by multipolar rivalry in trade, investment, infrastructure development, technology and funds flow. Currently most of the economic and financial engagements are bilateral or at best regional. This trend will continue well beyond 2024. The ineffectiveness of multilateral institutions became quite apparent during the pandemic days. The level of confidence in multilateral institutions across countries is low. Given this context it is important to realise that an issue like climate change or decarbonisation road map would need multilateral intervention. ‘Debt for environment swap’ is one such area which can bring back into focus the role of multilateral institutions. The rationale of debt swap essentially entails acquiring the debt at a discount. The creditor accepts a part of the debt knowing that full amount cannot be recovered, the equivalent of the reduced amount the debtor Government has to spend in local currency for climate related projects.

This is not an easy task, however if executed properly then it can become instrumental in making climate and environment related policies mainstream. It is indeed encouraging that the debt swap for climate received attention during COP28.

The year 2024 will be marked by elections in a large number of countries , the possibility of a regime change exists in some of them. Suffice it to say, that regime change may not lead to a dramatic shift in policies, some alteration is possible.

The expectations of policy alterations can create some uncertainty in the areas of investment, taxation and tariff regimes, banking finance and funds flow. While the basic premise of US foreign policy will not change, the war funding in Ukraine can get affected depending on who is returned to power. Some of the key economies which will be facing elections in 2024 are India, USA, Indonesia, Mexico, Taiwan, Russia, Bangladesh, South Africa and several European countries.

Another key area of interest in 2024 will be AI including generative AI. Soon AI will start finding mainstream applications, it is expected that some of the tedious and dangerous jobs will be taken over by AI, such that people can focus more on the creative aspects of the jobs. However, this has the potential to threaten a large number of jobs and create massive unemployment. There is little doubt that AI can lead to a breakthrough in productivity. To give an example- insights from massive database of breakdowns or accidents can be obtained easily without much of statistical expertise.

The apprehension of de-globalisation is somewhat overstretched, according to an earlier UNCTAD study 80% of world trade takes place in global value chains linked to multinationals. The UNCTAD report on GVC and development shows how raw materials of one country goes to another country for processing, which in its turn goes to a third country for finishing and a fourth for consumption. At best, value chains can get reconfigured for de-risking or more cost advantage. Some of the countries like India, which have a manufacturing base may like to have a higher share in value addition, that is understandable. In fact, new value chains would emerge and hither to forgotten economies would become important. For example, cobalt is an essential input for EV (electric vehicle) batteries, mobile phones , computers, etc. two third of the cobalt production is located in DRC Congo. So DRC Congo has to be a key player for catering to emerging demand structure.

These geo-strategic developments need to be taken into account for building the scenarios of 2024. The basic trends suggest interest rates have peaked in majority of the countries, inflation too has started easing, though above the Central Bank target. Fortunately, the energy as well as commodity demand are not robust enough for a steady growth in prices, supply seems to be adequate. However, sharp spikes cannot be ruled out in view of supply disruptions on account of the wars and trade route blockages. According to the multilateral institutions like OECD and several others world GDP growth in 2024 at 2.7% will be marginally less than that of 2023 (estimate 2.9%). Real GDP growth rate across countries would be somewhat uneven, emerging countries continue to do better than advanced economies; however China is likely to settle down at a new normal of 4%. The good news is the pick up in Indian growth rate has made it the fastest growing large economy in 2023, a trend which is expected to continue.

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