Letter n°114

Europe, the Long-Naive Dream of an Open World.

« A day will come when there will be no battlefields, but markets opening to commerce and minds opening to ideas » Victor Hugo, speech at the Peace Congress in 1849.

- ***The EU's Tradition of Openness:***

For a long time, the EU upheld the ideal of an open world, echoing Victor Hugo's vision, and as a commercial power, it advocated for lower tariffs. However, as German Minister ***Sigmar Gabriel*** once said, ***"In a world of carnivores, Europeans are the last vegetarians."***

EU openness remains high, at 38% of GDP, a greater percentage than in China or the United States. Exports of goods and services account for 29.4% of EU GDP, compared to 20.8% for China and 11.2% for the US.

In recent years, however, the EU has become more aware of China's commercial aggressiveness and the protectionist threats under Trump, prompting action.

- ***Calls for Deglobalization:***

In both Europe and the US, deglobalization has three main drivers: the rise of populism, criticism that globalization worsens inequality, and growing tensions with China. Globalization is under scrutiny, with its benefits downplayed and five major issues highlighted:

- Trump's tariffs: Tariffs against China and European countries increased.
- COVID-19: It exposed dependency on strategic sectors like pharmaceuticals and energy.
- Ukraine invasion: It underscored dependence on Russian energy.
- Energy transition: There is now a need for local investment in renewable energies.
- Military dependence: Europe became more aware of its military dependency.

These factors encourage relocation of industries, state intervention in economic management, and discussions on European common policies.

Since the COVID-19 crisis and the invasion of Ukraine, which highlighted EU dependencies, the traditionally consumer-focused EU is adjusting its stance, particularly toward China, albeit less drastically than the US.

This shift in EU policy can be observed through three trends: vigilance, pursuit of independence, and a nuanced approach.

The EU's Heightened Vigilance :

- ***Shift in Trade Policy:***

Previously open to global competition, the EU favored purchasing power over profit margins and competition over market dominance. Now, the EU is clearly shifting, as demonstrated by replacing longtime Commissioner for Competition Margrethe Vestager with Teresa Ribera, who supports consolidation among European firms to better withstand international competition.

Starting in 2026, the EU will tax imports of goods produced with high greenhouse gas emissions and close public procurement markets to foreign state-subsidized companies.

- ***Relation with the United States:***

EU-US relations have strengthened, with EU exports to the US exceeding €500 billion, over 4% of EU GDP. The EU's trade surplus with the US is €160 billion, including €60 billion from Germany. Trust in transatlantic relations has improved under President Biden, although the IRA (Inflation Reduction Act) does present competitive challenges, sometimes encouraging EU companies to invest in the US over Europe.

European companies employ 5 million Americans, while American companies employ nearly as many Europeans. Sales from American subsidiaries in Europe reached $3.4 trillion, surpassing all US exports worldwide, with American investments in Europe exceeding $4 trillion and European investments in the US totaling over $3.2 trillion.

A Trump re-election could upend these dynamics, as he has proposed tariffs of 10-20% on all EU imports.

The EU: A Surplus Region Seeking Greater Independence

- ***Surplus Status:***

Manufacturing represents 15% of EU GDP, compared to 11% in the US. In the first half of 2024, the Eurozone's trade surplus reached €107 billion. While exports to the rest of the world fell by 0.8% to €1.43 trillion, imports dropped by 8.2%, reflecting sluggish economic conditions.

However, this surplus conceals weaknesses. For instance, the EU's market share in semiconductors has fallen from 24% to 7% over 20 years. Despite ambitions for digital sovereignty, the EU has allocated only €20 billion to semiconductor initiatives, while China has committed $400 billion.

- ***The Quest for Independence:***

The EU is ramping up rare metal extraction and pursuing lithium mining projects in France, Austria, Finland, Portugal, and the Czech Republic to reduce dependence on China. Such efforts are crucial if the EU is to meet its goal of a 25% market share in global battery production by 2030 (up from 2% in 2020).

To compete with Chinese solar panel dominance, Europe is investing in nuclear energy and supporting wind energy development through major players like Vestas, Siemens-Gamesa, and Nordex, although Chinese competition remains strong.

A Nuanced Approach to Chinese Influence

Europe is more cautious than the United States in its relations with China because it has 2.5 times more manufacturing jobs, and over a third of its manufacturing output is exported, compared to one-fifth for the United States.

- ***Changing Tone Toward China:***

Today, the EU no longer hesitates to forge a common stance toward a China that is always quick to exploit divisions among EU members to access European markets. The European Union's trade deficit with China reached €400 billion in 2022 and remained at €300 billion in 2023. Failing to establish barriers against China means accepting an influx of subsidized Chinese products into Europe, and accepting the disappearance of entire industrial sectors.

The EU today is fighting against dumping and subsidies, with the recent implementation of tariffs on Chinese electric vehicles as a topical example of this shift.

The EU is also more proactive in authorizing or rejecting Chinese foreign direct investments (FDIs) in strategic sectors, as the European Commission reports that approximately 49,300 European companies are already under Chinese influence.

Anti-dumping procedures against China are multiplying across several sectors, such as chemicals, electrical equipment, and automotive.

The European Parliament has voted for a motion demanding the end of imports of products made through forced labor in China's Xinjiang region.

Transitional tariffs of up to 45% on Chinese cars (17% for BYD, 18.8% for Geely, 35.3% for SAIC) are now set to be set for the next five years.

Germany, Europe’s leading trade partner with China, reduced its imports from China by 19% to €156 billion and its exports by nearly 9% to €97 billion in 2023. Currently, China and the U.S. are comparable trade partners for Germany, each with €250 billion in trade.

In response to European measures against Chinese cars, retaliatory actions have emerged, such as targeting cognac sales, along with declines in luxury stock values on European exchanges.

- ***Relativizing Chinese Market Penetration:***

China represents 9% of European imports and 5% of its exports.

Despite their efforts, Chinese electric vehicle manufacturers have gained only one market share point in Europe over the past year, with 93,000 units sold and only a 10% share of the EV market.

BYD sold just 24,000 vehicles in the first eight months of the year, making up only 0.3% of registrations. All Chinese brands combined account for just 10% of electric car sales and 3.1% of the total market.

To bypass trade barriers, BYD plans to establish production capacity in Turkey, with 150,000 electric or hybrid cars, more than half of which will be destined for the European market under the EU-Turkey customs union. BYD is also planning a factory in Hungary and is considering one in Spain. Chery also plans to produce vehicles in Spain.

Some groups still believe in the benefits of collaboration. For example, Stellantis, after acquiring 21% of Leapmotor’s capital for €1.5 billion, is offering Leapmotor 70 sales points in France and even more across Europe for electric vehicles. The goal is to sell 500,000 cars by 2030, 80% of which are aimed at the European market. This partnership should allow the Chinese group to avoid customs duties.

Overall, the EU’s dependence on trade with China has recently begun to decline. With Russia, trade has decreased sixfold since the invasion of Ukraine.

Conclusion: ***« What depends on you is whether or not you accept what doesn’t depend on you » Epictetus per a principle of Marcus Aurelius.***

- Facing the prospect of a 10%, or even 20%, tariff on all its exports to the U.S. if Trump is elected, the EU must respond.

- The European Union is very open, but 70% of European countries' trade occurs within the EU zone. If reshoring occurs, this percentage could increase.

- The idea for European countries is to repatriate activities from Asia and establish them in Morocco, Turkey, or Eastern Europe. There are two main reasons for this:

  On the one hand, reshoring often clashes with wage costs, taxation, and the lack of availability of qualified labor. Despite various subsidies and robotization efforts, reshoring and shorter supply chains cannot match the low-cost production from Asia.

  On the other hand, given the labor market, reshoring efforts come at a challenging time, as companies in many countries are struggling to find employees. Politically, it is paradoxical to see far-right groups, opposed to immigration, being the most vocal advocates of protectionism, as bottlenecks are likely to multiply.

Geneva, November 4, 2024

Bruno Desgardins

Bruno Desgardins
CIO
Switzerland

SingAlliance Pte Ltd
16 Raffles Quay
#12-01 Hong Leong Building
Singapore 048581
T: +65 6303 5050
E: info@singalliance.com

SingAlliance (Switzerland) SA
16bis rue de Lausanne
1201 Geneve
Switzerland
T: +41 22 518 85 85
E: info.switzerland@singalliance.com

SingAlliance (Hong Kong) Ltd
Unit 904-907, 9/F Dah Sing Financial Centre
248 Queen's Road East
Wanchai, Hong Kong
T: +852 2639 3659
E: info.hongkong@singalliance.com

SingAlliance Pte Ltd
(DIFC Representative Office)
The Gate, Level 13 East, Office 10, DIFC
PO Box 121208 Dubai, UAE
T: +971 (0) 4 401 9158
E: info.dubai@singalliance.com