2021 Trends in International Trade

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Four months into the new year, four trends in international trade have emerged:

- China’s reign as the “factory of the world” appears intact;
- Brexit is biting with respect to total trade with the EU;
- a global shortage of inputs is disrupting supply chains;
- and global shipping costs are soaring.

This article discusses each of these developments and notes some potential implications to businesses.
China is registering record volumes of exports

China has been the principal beneficiary of the pandemic-induced global surge in consumer demand for electronics, furniture, and medical goods. During the first two months of 2021, China’s exports were up 60 percent over the previous year, while their output expanded by a record 18 percent over the first quarter of the year. At the same time, industrial production, domestic consumption, and investment all increased by more than 30 percent since January of 2021.

Since joining the World Trade Organization in 2001, China has consistently remained a leading destination for foreign direct investment. Most recently, the country led the world in new multinational investments at $163 billion in 2020. These investments have embedded the country into the supply chains of virtually all manufactured products. China now accounts for roughly one quarter of the world’s production and is the largest trading partner for 64 countries—a list that has grown to include the EU, which overtook the United States in 2020.

China has further expanded its commercial ties with countries from Asia to Europe through its Belt and Road Initiative (BRI). Launched in 2013, BRI consists of infrastructure projects and investments that are believed to reflect China’s ambitions to grow its economic and political influence. Turkey has played an important role in facilitating these partnerships, serving as a “middle corridor” from Beijing to London.

At the same time, China holds an advantage in global shipping, hosting 7 of the world’s 10 largest ports. This is advantageous because the global shipping industry has prioritized investments in large shipping containers (defined as more than 15,000 twenty-foot equivalent units) that commonly travel from China to Europe and to the United States; large containers help shipping companies achieve economies of scale.

Notably, the cost of importing from China has increased in recent years due to the global trade war with the United States and steadily increasing labor costs within the country. These developments have invited speculation about the possibility of multinationals shifting production away from China towards other, lower-cost destinations within the region. While there are notable examples of this happening—Apple switching production of iPhones, iPads, and Macs to other countries within the region, for example—it does not appear to be reflective of a larger trend at the moment.
Brexit is biting

In the first months since Brexit entered into force, total trade between the UK and the EU registered its largest decline since record-keeping began in 1997. This reduction in bilateral trade was unique among Britain and its non-EU trading partners, suggesting that UK-EU trade declines reflected Brexit-related protocols. Although UK exports to the EU slightly improved in February, numbers were still about 15 percent lower than in the month preceding Brexit’s implementation, raising concerns about the persistence of this trend.

Although the UK-EU trade agreement reached at the end of 2020 was intended to ease trade frictions between the trading partners, non-tariff barriers have remained. In particular, border checks—which currently only apply to UK exports to the EU—and disparities in the implementation of standards appear to be the biggest culprits.

In one example, British manufacturers of non-branded drugs have been withdrawing medicines from Northern Ireland due to the high costs of meeting post-Brexit protocols, which now require British-manufactured medicines to undergo separate safety inspections. Prior to Brexit, British manufacturers were only required to submit a single regulatory dossier and abide by one set of standards and regulations.

Further, costly customs procedures ranging from complex labelling and packaging requirements to export declaration forms are adding administrative costs for UK exporters into the EU. Further, onerous proof of origin requirements—which stipulate the minimum percentage of components in a manufactured good required to qualify as originating in the UK—have proved challenging for firms to navigate.

A concern raised by some UK-based firms is that these extra administrative expenses will render them less competitive than EU-based firms or to those based in Northern Ireland, that do not incur these expenses. In the short term at least, large multinationals may prove better equipped to navigate this landscape than smaller-to-medium-sized enterprises. For example, they may be able to divert production to their EU-based facilities and have the resources to finance the increased administrative costs.

Regardless of the size of the firm, Level-International (LI) is well positioned to assist firms seeking access into the EU market. LI’s tax advisory expertise helps firms lower their tax fees and compliance costs, ensuring a seamless process for international businesses.
### Shortage of global inputs

Owing to unprecedented consumer demand, abetted by e-commerce transactions; bottlenecks in the global shipping industry, owing to a lack of sea containers; and natural disasters, which have affected petroleum refineries; there is widespread scarcity throughout the global supply chain for everything ranging from plastic resins, to semiconductors, to commodities.

This trend is prompting concerns among manufacturers of shrinking profit margins and from consumers of price increases. To take plastics manufacturing as one example, shortages in that sector have already translated into increased prices in Asia and Europe. Eurozone inflation, which increased to 0.9 percent in January, was driven largely by non-energy industrial goods. Further, input prices within the eurozone grew at a faster rate than at any other time over the past decade. Inflation uncertainties are further fueled by foreign exchange flows, large financial stimulus in mostly Western countries and geo-political instabilities.

### Spiking Shipping Costs

Unexpectedly high demand for various products including consumer electronics, personal protective equipment, and automobiles have strained global shipping capacity, leading to dramatic increases in the cost of international shipping.

According to the Shanghai Containerized Freight Index, a spike in e-commerce has contributed to a doubling of the rates to move containers, which are now at record highs. In one example, the cost of moving goods from East Asia to Europe have increased by more than six times what they were last April, reaching $8,455 per 40-foot container. Likewise, the rates from Asia to the U.S. West Coast are nearly four times higher than they were this time last year.

At the same time, compliance with coronavirus protocols (e.g. social distancing and quarantines) and infections of employees at port terminals are resulting in lower productivity. These factors have translated into container congestion and delays in product deliveries. Moreover, a shortage of shipping containers has exacerbated these challenges for a number of countries, such as Turkey.
Are these short-term anomalies or long term trends?

With the exception of China’s dominance in global manufacturing, it is entirely possible that the other trends discussed in this article are short term phenomena. For example, the widespread vaccination campaign could spell relief at the shipping ports, which could facilitate more rapid clearance of cargo. The gradual end of lockdowns could shift consumption away from consumer electronics and more towards services, the consumption of which has been depressed during the pandemic. These developments could stabilize shipping costs.

Perhaps the biggest point of concern is the likelihood of inflation. As previously noted, eurozone inflation has risen to its highest rate since the start of the pandemic, but still remains lower than the European Central Bank target. Meanwhile, the U.S. Federal Reserve has lifted their inflation forecasts. In addition, many Chinese exporters ranging from furniture manufacturers to apparel and toy manufacturers have reportedly been raising prices on exported goods.

For the moment at least, long-term inflation appears to be less of a concern; even as raw materials prices have increased, there appears to be limited evidence to suggest that they are meaningfully affecting prices economy-wide.

Please contact Mihir for your queries and to discuss further on the international trade trends.

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