

# **Can Interdependence Persist in Tense Times?**

## **Insights from the 2<sup>nd</sup> Paris Goeconomic Dialogue**

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(eds.)

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Artificial Intelligence (AI) was used to assist with transcriptions, as well as the edition of the summary.

# Executive Summary

Ifri's *2nd Paris Geoeconomic Dialogue* brought together in November 2025 experts, academics, and decision-makers around six themes relating to the prospects for interdependence in an increasingly tense international environment: the strategies of emerging economies in a fragmented world; the persistence of global imbalances; the costs and consequences of economic security; the risk of financial fragmentation; industrial and technological rivalry; and the prospects for preserving trade cooperation. This *Study* summarizes its main insights and includes edited transcripts of some of the introductory remarks made on this occasion.

## Résumé

Le second « Dialogue géoéconomique de Paris » de l'Ifri a réuni en novembre 2025 experts, universitaires et décideurs autour de six thèmes relatifs aux perspectives des interdépendances, dans un contexte international de plus en plus tendu : les stratégies des économies émergentes dans un monde fragmenté ; la persistance des déséquilibres mondiaux ; les coûts et les conséquences de la sécurité économique ; le risque de fragmentation financière ; les rivalités industrielles et technologiques ; et les perspectives de préservation de la coopération dans le domaine commercial. Cette étude en résume les principaux enseignements et comprend des transcriptions éditées de certaines des remarques introductives formulées à cette occasion.

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# Introduction

Interdependence usually builds up in a context of political stability; it is a prerequisite for closer economic and financial relationships to make sense and warrant the necessary investments; it is also indispensable to make the ensuing vulnerabilities acceptable. What, then, could be the consequences of increasing tensions, when interdependence is already widespread? In other words, *can interdependence persist in tense times?* This overarching question was the general theme of Ifri's 2<sup>nd</sup> *Paris Geoeconomic Dialogue*, a high-level conference gathering experts, academics, and decision-makers from both the private and public sectors.

The Dialogue was structured around six themes, from emerging-economy strategies and global imbalances to the costs of economic security, the risk of financial fragmentation, industrial and technological rivalry, and the prospects for preserving at least partial trade cooperation. The objective was to combine academic analysis with practitioner perspectives to identify the trade-offs, governance bottlenecks, and actionable priorities that are likely to shape geoeconomic policy choices in the years ahead.

While the Dialogue was held under the Chatham House rule, some of the speakers accepted that a transcript of their introductory remarks be published. They appear in this *Study* as separate, authored chapters. This introduction, written under the sole responsibility of the editors, proposes a brief summary of what we see as the main takeaways. While it is organised by main theme below, a few broader points are worth mentioning.

Firstly, there is a widespread sense that **globalization is going through a rupture**, with potentially deep consequences; yet, **interdependence is still very much here**. The shifts in global equilibria, the emergence of new competitors, and the weaponization of trade policies changed the environment, but they did not significantly reduce interdependences at a global level.

What did change, however, is that **economic security is no longer a niche agenda**. It is increasingly shaping the way all countries, big and small, think about their international economic relationships and policies, be it for trade, investment or finance. Yet, in a number of dimensions, **current trends may not be sustainable for long**, hence questions about the next steps and the longer-term trajectory.

Against this background, **trust is more important than ever for international relations**. This is true for both States and firms alike, and it requires thinking about the way trust can be built and maintained — a task made harder by the erosion of the multilateral institutions that once

provided its scaffolding, and by the growing use of economic interdependence itself as an instrument of coercion.

## Emerging countries faced with the reshuffling of international economic relations: Strategies, partnerships, policies

While the Sino-American rivalry attracts most headlines, the choices made by emerging countries will play a key role in shaping tomorrow's world economy. To discuss the correspondent strategies and policies, three presentations were made about specific countries and regions.

In his presentation, **Suman Bery** (o) recalled **India's growth imperative**. To reach developed-economy status by 2047, India needs to accelerate growth from around 6.5% to near 8%. This will require a **significant rise in investment rates**, with roughly one-third of that investment needing to come from abroad. Geopolitical risks thus need to be managed as part of this development endeavor. As a matter of fact, after decades of cautious trade and investment integration, India is now positioning itself to attract global FDI, with Apple's supply chain relocation as the first proof of concept and "China+1" as the driving dynamic. Unlike China, **India's strength lies in services** rather than merchandise trade. This is potentially important, because services exports have been less affected than by trade disputes, at least so far.

**Hakim Ben Hammouda** (o) emphasized that the Global South is not driving fragmentation. Despite the political rhetoric, intra-Global South trade has not been especially dynamic in relative terms. These countries continue to trade primarily with the US and other developed economies, and model-based simulations suggest that the **trade war will not significantly boost South-South trade**. The narrative of a cohesive, self-reliant Global South reshaping world trade is not supported by the data.

Focusing on Southeast Asian economies, **François Nicolas** (o) reckoned that, while they have long navigated US-China rivalry by playing both sides, the trade war is making this balancing act increasingly difficult. In response, **ASEAN countries are seeking diversification and broadening their partnerships**. For instance, Indonesia fast-tracked an FTA with the EU, and an ASEAN-GCC-China summit framework has been institutionalised. Regional integration is also being deepened, with interesting new initiatives, like Singapore's Future of Investment and Trade Partnership.

The discussion came back to **the specificity of services** in the present context, beyond the specific case of India. While services have not been targeted as openly as goods, views were divided about whether that

would remain the case. It was emphasized that visas, digital regulation, and other services-adjacent instruments **can become protectionist tools**. Another difficulty for countries with a comparative advantage in services is that partners frequently treat **services liberalization as politically untouchable**.

Among the other issues dealt with:

- The mere possibility of a sustained weakening of the multilateral trading system **alters bargaining incentives** for all countries, because it changes what they see as threat points;
- **China had prepared diversification** at least since 2018 and can redeploy quickly, while many **others are reacting defensively**. **Components and intermediate inputs** (rare earths being the salient example) may be at the core of the next phase, making mapping and compliance far more granular and difficult;
- **Skepticism** was expressed **about the capacity of RCEP to sustain cooperation**, given the asymmetries and China's demonstrated capacity to weaponize interdependence, and tighter US rules on transshipment;
- **Plurilateral deals**, frequently presented as an option to reform the trading system, could actually **weaken smaller countries' leverage**, because their agreement won't be really sought after;
- For many countries, especially in Asia, the practical **choice is between dealing with China bilaterally with few constraints, or embedding the relationship in an institutional framework**;
- **Some Global South economies are already raising barriers** against Chinese imports to protect the domestic industry;
- **US rules of origin may make a big difference**. A significant tightening may reduce the viability of indirect export routes, which have been flourishing in many cases;
- **Impact on value chains may take time to materialize**. Value chains built over two decades do not unwind quickly, and firms may delay costly reconfiguration in the hope that the political environment shifts again.

Many emerging powers are not structuring their external economic strategy around a binary choice between blocs. Instead, they keep room for maneuver through specific alignments, while trying to protect access to key markets. In this setting, **partnerships with the EU remain feasible**, but they are increasingly judged on what they deliver in practice. This is particularly clear **on critical raw materials**, where cooperation is still needed, yet negotiations tend to focus on who captures value along the supply chain rather than on access alone.

## Global imbalances: Background, prospects, challenges

The world economy is marked by pronounced imbalances, which play a key role in international relations. How will they be affected by the new context, and to what extent can they shape it? Can the Chinese economy be rebalanced? How will Trump's policies affect US macroeconomic imbalances? Is there room left for macroeconomic coordination, and how?

In dealing with these questions, **Dorothee Rouzet** (o) stressed that imbalances are driven by distortive policies, at both the micro and macro levels, and that they have become highly persistent over time. After discussing the main issues for the biggest economies, she discusses possible remedies, pointing out the need to act on the root causes, not only the symptoms.

**Brad Setser** (o) noted that a true fragmentation of the global economy cannot happen when imbalances are so large as those now observed for the US and China: they need to compensate each other. He also emphasizes the global impacts of the bursting of China's property bubble, which is far from being resolved, and points out that market pressures are not working to correct or at least limit imbalances.

**Jean-Pisani Ferry** (o) discussed how geopolitical tensions reframe the analysis of global imbalances, pointing out the return of power-based analysis, à la Hirschman. Against this background, imbalances are not just outcomes; they are also instruments of statecraft. In addition, linkages cannot only be viewed through a macroeconomic lens, because the threat of weaponization requires a granular assessment.

The **articulation between the macro and micro approaches of imbalances** came back in the discussion, with emphasis on their complementarity. **A micro view is needed**, because aggregates tell nothing about strategic dependencies, and Western countries now have important such dependencies with respect to China, more than in the opposite direction. A pessimistic view was even aired that, given the structure of China's command over certain intermediate good inputs, **the only realistic option to minimize the potential for weaponization of trade is less trade**.

In any case, a macro assessment remains necessary, especially when external positions become large enough that **financing and confidence turn into first-order constraints**. The timing of that transition is uncertain, but some participants reflected that **we are not far from the point where the US external deficit and its negative international investment position will become an issue**. As opposed to the years before the global financial crisis, though, the imbalance in the US side primarily originates on the fiscal side.

The notion of **“escalation dominance” frames the geopolitical logic**. Some speakers argue that China’s scale, internal cohesion, and command over certain strategic inputs allow it to credibly threaten supply restrictions, while the US and Europe face higher political and economic costs from unilateral decoupling. As a matter of fact, the US backed down, and the world is increasingly shaped by “weaponized interdependence”, where strategic control over choke points is of paramount importance. One interpretation is that **what the US hopes for, a partial de-risking, actually does not work**, thus raising the question: can you impose decoupling when you don’t have dominance?

**Exchange rates** are widely seen as among the main reasons why the imbalances are persistent. In particular, **many shared the view that the Chinese RMB is significantly undervalued**, and that this should be an important part of the discussion about macro imbalances. The **muted reaction** to the Chinese RMB depreciation against the dollar in 2025 (by around 5%) was noted: 10 years ago, that would have triggered reactions, perhaps charges of currency manipulation, and it would have focused discussions. This has not been the case. Among the possible explanations shared, one is that the Trump administration made a mistake in designating China as a manipulator back in 19, when it wasn’t; another is that there is a sense that China’s currency would float down if it were allowed to float. The difficulty in analyzing the situation properly was emphasized here:

- Reading market pressures is not straightforward, because China is widely using its state banking system as a tool of exchange rate management. Yet, **if China’s financial account remains closed as it is right now, the pressure would clearly be for appreciation**.
- **If China opened its capital accounts, the pressure might well be reversed**, towards devaluation, because the logic of capital flows is in stark contrast with that of macroeconomics and trade.
- Some speakers emphasized that the CCP prioritizes security over growth, supporting Chinese consumption is not a priority in practice, so don’t expect a strong policy push in that direction in the near future.
- The **paradox of the European situation** was also discussed, with a still relatively strong currency, against a background of macroeconomic underperformance.

Among the other issues discussed:

- **Capital Markets Union** is seen as a strategic lever: deeper, more integrated European capital markets could raise investment returns, retain capital, and slowly strengthen the euro’s international role.
- Skeptical views about the **IMF’s potential role** were shared: major powers may not want external discipline, and the Fund’s advice on China can appear internally conflicted, especially if “flexibility”

prescriptions risk translating into depreciation and larger external surpluses.

- IEEPA and Supreme Court opinion (expected to rule it unlawful, as indeed proved to be the case): **expect a wave of 232s and 301s to be unleashed**, with the aim of replicating the previous tariff structure.

## The costs and consequences of economic security

Eroding confidence in world markets and trading partners has raised concerns about economic security. How are countries responding in practice? What are the costs imposed on themselves and on their partners? What are the consequences for international coordination and for macroeconomic conditions? What specific role for the defense industry?

**Emily Blanchard** (o) emphasized that, although the political shift began long before Trump, we are living through a deeply destabilizing period. This is not only a change, but a rupture, and it does not only concern the US. She explained the underlying mechanisms and the importance of breaking with norms. Stressing contagion mechanisms, she characterized the situation as a “massive experiment underway”.

The remarkable **impacts of Chinese economic security policies** were also discussed. The objectives set in Made in China 2025 were pursued with tangible results, and comparable progress should be expected in the next five years, particularly in integrated circuits, machine tools, and biomanufacturing. A noteworthy paradox is that China’s model prioritizes effective competition, resulting in record levels of loss-making enterprises at the core of its manufacturing sector, which structurally exports deflationary pressure to everyone else. **The Chinese trajectory ahead was described as utterly risky for Europeans**: import substitution in high-tech is accelerating, export reorientation toward ASEAN and Europe is growing, and coercive potential through dominance in foundational technologies, from rare earths to legacy chips, is expanding. Interdependence can persist in tense times, but increasingly on Chinese terms.

The discussion then centered on **how supply chains can remain stable in a world where geopolitical risk** is now structurally embedded in trade and technology. Trust is essential in this context, and it still exists at the operational level of firms and customers even when governmental relations are highly politicized. **Demand for critical tools and inputs remains strong across blocs**, including in jurisdictions subject to export controls, and this creates an underlying commercial pressure to keep channels open. The technology space across all three blocks is not as politicized at the firm level as it is at the government level.

There is still a lot of desire to engage; to what extent that's possible is for policymakers to decide.

A second set of comments probed China's domestic political economy. Participants asked **why China appears slow or unwilling to close overcapacity** today, despite having previously imposed harsh capacity reductions, and whether this reflects a deliberate policy choice. A speaker hypothesized that **we underestimate how much overproduction is a feature**, not a bug, of the industrial policy model, with the end goal of localizing supply chains.

It was also asked **whether China could continue to prioritize export-led growth** while access to the US market narrows and European markets become less accommodating: is this model still feasible, or does it inevitably force a shift toward domestic-demand-led growth, especially given the regime's need to maintain employment and income growth?

About the logics of weaponized interdependence, **China's baseline assumption is that other actors will eventually "fold,"** and that **China calibrates coercion** by testing Western willingness to impose sustained costs. Coercion is described as a two-step pattern: a visible, high-impact move to signal capability, followed by smaller, repeated applications that encourage self-deterrence by others. In addition:

- **China has been deepening economic ties with developing markets for years**, through trade and investment, and these markets, especially those with strong demographic growth, absorb substantial volumes of Chinese exports.
- Participants discussed the **limits of unilateral weaponizing of demand** by restricting market access: because Chinese trade is highly flexible, the effect is muted when only one large market acts. It would take a coordinated move for this approach to make a difference.
- **The capacity of the global South to absorb Chinese production, exports, and maybe overcapacity, should not be underestimated.** It can keep going.

The discussion then shifted to Europe's strategic posture on technology. A participant argues Europe may be over-focusing on frontier technological control and not enough on rapid diffusion and adoption of already available AI, which could boost productivity quickly. Other points discussed included:

- Relying on "strategic indispensability" is risky without a strong home market; choke-point leverage is fragile if domestic demand is weak.
- Regulatory and compliance constraints can slow European uptake of the most advanced AI capabilities, reinforcing the case for an EU strategy centered on adoption, productivity gains, and scaling internal demand.

- ▀ Europe is comparatively under-resourced in strategic and analytical capacity for economic security, especially relative to US administrative capabilities.
- ▀ A participant stressed that, perhaps surprisingly, there is a lot of focus on the part of the Trump administration on a positive agenda, on building out U.S. capabilities with European support.

## Finance: Can fragmentation be avoided?

Financial fragmentation was approached less through headline indicators than through *market plumbing*: clearing and settlement infrastructures, payment rails, and access to liquidity. The premise is that these back-end architectures determine where liquidity concentrates, how cross-border finance behaves under stress, and where the effective chokepoints lie. In that setting, the United States' ability to project financial power, via sanctions risk, but also via privileged access to critical channels, affects expectations and risk management even when no new measures are announced. Dollar dominance, in this view, remains tightly linked to liquidity and to the depth of US safe assets.

**Brigitte Daurelle** (o) emphasizes that fragmentation is primarily an *infrastructure* question. **Europe's constraint is partly structural**: fragmented markets and infrastructures limit scale, liquidity, and autonomous crisis-management capacity; consolidation is slow because private incentives and transition costs do not align. The options discussed ranged from integration and support for EU-based infrastructures to exploratory work on wholesale CBDC / tokenized settlement to modernize settlement and reduce reliance on external chokepoints.

The role of infrastructure, as well as innovation, was discussed, emphasizing their capacity to shape international finance evolutions. For instance, **Europe could move faster** on retail cross-border payments and wholesale digital settlement, even if political constraints and limited institutional bandwidth remain binding. More generally, **payment innovations** (CBDC/tokenized settlement, faster retail rails) **may move faster than reserve-asset substitution**, which remains constrained by trust, depth, and crisis capacity.

The inertia created by **network effects** was also stressed: under open capital markets, there is a strong tendency toward a dominant currency/market because liquidity behaves like a natural monopoly. This makes a “multipolar” monetary order difficult to stabilize under openness, unless one accepts a loss in efficiency and shock absorption.

As a matter of fact, what looks like “fragmentation” is often better described as the **politicization of finance**: a tightening of conditionality around key instruments (investment packages, bilateral arrangements, liquidity backstops). If access to global shock absorbers is politicized,

countries may respond by reducing exposure to cross-border financial integration, accelerating **defensive regionalisation**. In other words, the politicization of backstops such as swap lines may induce **significant damage to the dollar's safe-asset status**; the result might be **less cross-border financial integration** (defensive regionalisation), rather than a clean switch to alternative reserve currencies. **Fragmentation could thus come from the core weakening**, rather than from emerging economies collectively “escaping” dollar finance.

**Stablecoins backed by US Treasuries** could expand dollar use as a medium of exchange even if the store-of-value function is questioned, but it is unclear whether this genuinely helps finance US deficits, and it might create run/duration risks if stablecoin balance sheets concentrate in bills or create new liquidity dynamics.

**Europe's common currency** and potential infrastructure consolidation could be an advantage in a Balkanising world, whereas **Asia lacks an obvious anchor** and has historically relied on reserve accumulation as self-insurance.

## Industry, technology and geopolitical competition

Industrial policy is increasingly used to shape market structure. It therefore overlaps more directly with trade-defence and security measures and makes cross-border investment and technology transfer harder to manage with stable rules. A key point discussed was China's expanding export controls on upstream materials, treated as a structural strategy to manage access to critical inputs and strengthen downstream positioning. Because these controls are mostly driven by political interests, they reduce predictability for firms and change escalation dynamics when leverage over inputs is asymmetric.

In his presentation, **Denis Redonnet** (o) framed **EU economic security as a mix of risk reduction, partnerships, and enforcement tools**, with implementation as the binding constraint. Predictability requires consistent application across member states. Another limit is the EU's difficulty in working with firms at sufficient technical granularity to produce actionable risk assessments. In that context, **Chinese export controls are seen as a lasting feature** that calls for credible and predictable EU responses within the Single Market.

**Mathilde Lemoine** (o) stressed that **industrial policy reallocates capital toward targeted sectors and reshapes market structure**, with spillovers into trade defence and security. Rivalry produces layered standards and rising compliance burdens, which increasingly affect firm strategy. She also noted that many countries pursue selective partnerships

rather than bloc alignment, in a policy environment that is more openly transactional.

An additional contribution (o) offered a stark diagnosis of **America's technology security policy**, concluding that it has shifted from a coherent strategic framework — denying China semiconductor and AI capabilities underpinning next-generation weapons — to a **transactional, deal-driven process with no national security logic**. The institutional architecture has been hollowed out, and China has achieved something historically unprecedented: twice this year, explicit rare earth supply threats forced Washington to walk back controls it had just imposed. Strategic paralysis dressed up as flexibility, with firms already quietly relocating development and production offshore.

The most urgent issue is **critical materials**, especially rare earths, with a disproportionate systemic impact, compared to the small nominal value of trade flows concerned. **Monitoring is not enough** because market incentives alone do not deliver diversification when a dominant supplier can undercut alternatives through scale and pricing. The direction discussed was a mix of public instruments (support, price or demand guarantees, insurance-like mechanisms, contract-style tools) and partnerships, with the political economy question at the centre: who pays, and **how to sustain consensus** for costs that are immediate while resilience gains take years.

Among the other issues discussed:

- ▀ Economic security tools run into **feasibility constraints under deep interdependence** and heavy compliance burdens.
- ▀ **Export controls are becoming more political and less predictable**, which raises escalation risks when critical inputs are concentrated.
- ▀ EU leverage can be assessed through **both import and reverse dependencies**, but acting on the diagnosis remains the hard part.
- ▀ **Some strategic dependencies sit in services**, which complicates implementation without making it irrelevant.
- ▀ **Critical-mineral resilience requires deliberate intervention**, and the bottleneck is often burden-sharing and domestic consensus.

## Trade: Can (some) cooperation be saved?

The rules-based trading system is increasingly weakened, if not destabilized. For all practical purposes, the United States has already left the WTO, and the only rule its trade policy seems to follow is to make its power pay. Meanwhile, several trade agreements are still being discussed or

signed, showing that others do not intend to follow the same path. What are the prospects for international trade? Will the multilateral system retain some significance? Will ad hoc partnerships or plurilateralism flourish? Will blocs emerge?

**Marion Jansen** (o) argued that **subsidy disciplines are the hardest area** for ambitious reform because all major players use subsidies. This makes incremental progress more realistic than a grand redesign. She also suggested that cooperation can start from shared diagnostics on concentration and vulnerability, where facts are often easier to agree on than motives, and then move through plurilateral initiatives and transparency mechanisms.

**Sébastien Jean's** analysis (o) identifies a multilateral trading system caught between two structurally disruptive forces. **US unilateralism** has eroded the foundational premise of the WTO — that commitments will be respected — while **China's manufacturing surplus**, now projected to exceed \$2 trillion, **reflects policy interventions of historically exceptional scale**. His own research shows the correlation is not coincidental: EU export losses track precisely the sectors where Chinese industrial policy has been most intensive. The question then becomes what Europe, and third countries more generally, can do. A viable path forward lies in **building coalitions of trusted partners** around an insurance logic of supply chain resilience and rules-based reciprocity.

While the system's limits were acknowledged in the discussion, it was also emphasized that it still works in many respects. Even in a politicized environment, day-to-day WTO functions shape behavior in many areas, and the United States remains engaged in selected functions even while contesting core elements of the system. A plausible path combines modest, issue-by-issue reform with coalitions of members, keeping the **WTO as a reference point** even if ambition stays limited.

The discussion returned to whether a rules-based system can meaningfully constrain the weaponization of trade. Several interventions questioned the fit of WTO rules for today's challenges, since **the system was not designed for economic security and de-risking**. The boundary between legitimate resilience and protectionism is increasingly contested.

A second line of debate asked whether the system could remain coherent when the two largest actors are seen as either disregarding rules or using them selectively. A technology-sector perspective argued that **"two worlds" already exist in tech**, and that as AI and chips spread into automobiles, aerospace, and other sensitive industries, bifurcation could extend beyond tech. For Europe, positioned between the blocs, the implication would be **adaptation to partial separation** rather than a return to uniform openness.

In the responses, one panellist argued that **full “de-weaponization” through the WTO is not realistic**, largely because national security exceptions leave wide room for maneuver. Still, WTO committees can host more rational work on issues that now overlap with economic security, such as export restrictions on critical materials, local content requirements, and cybersecurity standards.

**Subsidies** were repeatedly identified as the central reform battleground, with **three reform demands** pulling in different directions: tightening disciplines to address non-market practices, expanding space for “positive” subsidies (notably for the climate transition), and granting more policy space for developing-country industrialization. Another response pushed a more structural diagnosis centered on China’s state-driven model, especially firm-level subsidization linked to market-share gains.

The end-state will be more nuanced than either full decoupling or a restored multilateral order. **High-tech sectors** with clear security externalities are **likely to move further toward separation**, while **other sectors remain tied together by scale**, specialization, and the international division of labor. In that setting, “saving cooperation” means accepting uneven integration, relying more on clubs and coalitions, and using the WTO as a baseline framework rather than expecting it to deliver comprehensive solutions.

Among the other issues discussed:

- The WTO’s rulebook was not built for economic security, making the line between resilience and protectionism harder to police.
- If enforcement remains weak, rules may shift toward dependency or concentration **thresholds that legitimize intervention beyond certain levels**.
- The likely equilibrium is **selective bifurcation**, with cooperation rebuilt through coalitions and pragmatic arrangements rather than universal bargains.

# India: Managing Interdependence in Tense Times

**Suman Bery**

In my remarks, I would like to explain what India believes it has at stake in what you call the reshuffling of the world and, without being arrogant, what the world has at stake in India. Towards the end, I will emphasize when interdependence comes in.

Where is India today, and why is this global turmoil coming at an important time for India? Let me start with a statement from our Prime Minister: "...without inclusion, real growth is not possible. And the goal of inclusion cannot be achieved without growth. Therefore, we have adopted the path of growth through inclusivity by trying to include everybody" (Hon'ble PM Modi at the Arun Jaitley Memorial Lecture, New Delhi, 2022).

The next point, drawing on the World Bank's 2026 Country Economic Memorandum, is that you would expect a country that is the least affluent member of the G20 to be growing faster than the global economy. The chief economist of the World Bank for South Asia emphasized that India's macro-management has meant that we have been spared financial crises. As we know from both the global financial crisis of 2008 and from the Asian financial crisis a decade earlier, banking crises exact a terrible penalty on long-term growth.

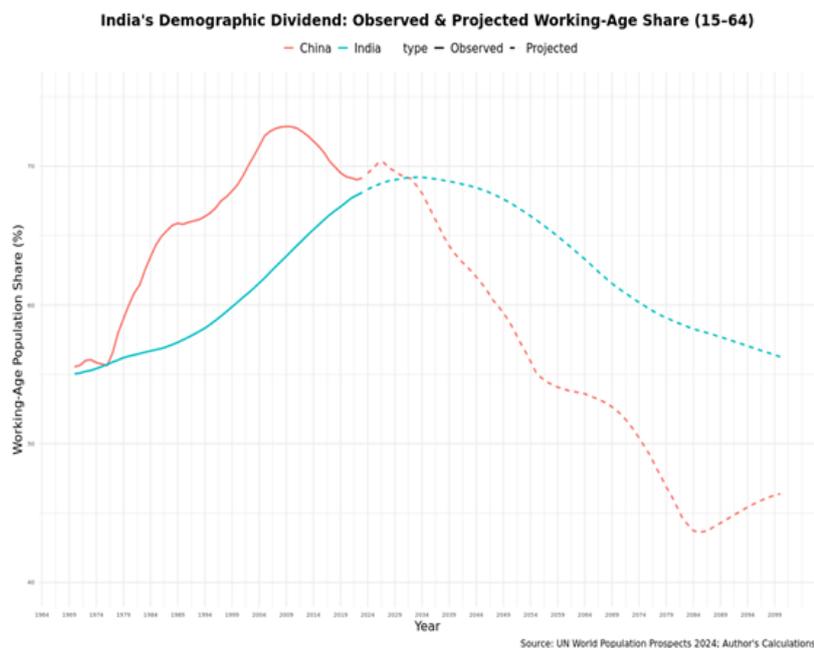
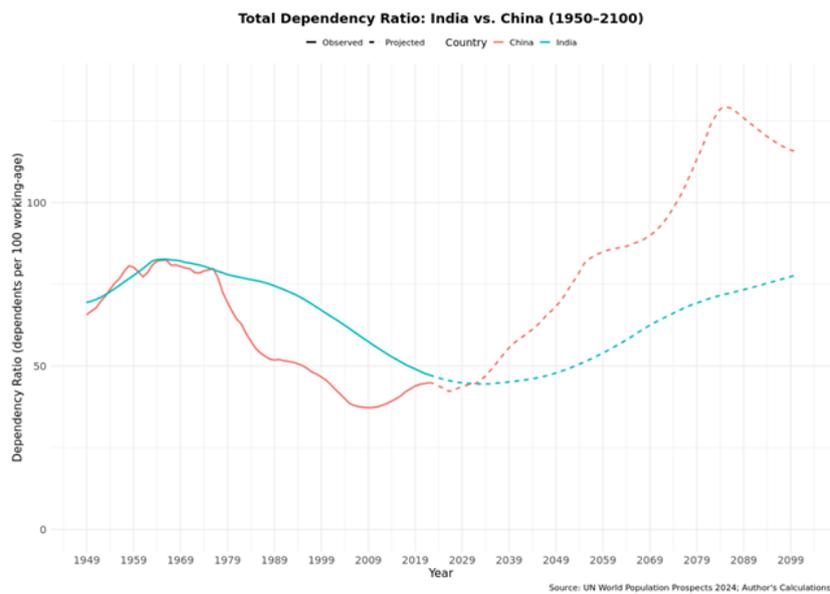
As we look at engaging with the new world order, maintaining healthy aggregate demand while avoiding financial crisis becomes even more important. In the pre-COVID period, India's growth performance for 20 years was impressive. Post-COVID, we are proud, and rightly so, to be the fastest-growing major economy.

Let me turn to inclusion. In terms of consumption inequality, for which data are now available, the World Bank, which carries out such work for many countries, has produced a reasonably good picture.

I have made the point that our economic resilience is evident and highlights our strengths, but our national goal is a developed India as a developed society by 2047. The technocrats among us have chosen to define this using today's World Bank definition of a high-income economy. We are approaching 3,000 dollars per capita at market prices today; the

benchmark is about 13,000 plus. To bridge that gap in the next 21 years, we need to accelerate growth from around 6.5% to roughly 8% on average. On the basis of current forecasts, we expect India to be the third-largest economy in the world by the end of this decade. I will not list all the macroeconomic management and structural transition challenges, but will deal with managing demographic, urban and energy transitions. This requires financing, which is key for us in this golden moment. The Prime Minister has called the next 25 years our “age of nectar” because of the demographic window of opportunity.

Let me now turn to how fragmented the world is, the topic of this conference. For various reasons — whether deliberate, accidental, or reflecting comparative priorities — India has emerged as more successful as a services exporter. I will not go through all the numbers, but, as some of you know, fragmentation and technological revolutions, including possibly AI, play to the strengths of a country that is doing well in services.



If you compare merchandise and services trade, the slowdown in merchandise trade is much more palpable than in services, and India is well-positioned on the services front.

This is particularly important for India at this moment. Figures my colleagues helped me put together show the very different profile of India's demographic dividend compared with China's. From the same starting point, our demographic dividend peaks later, peaks lower, and declines more slowly. This has huge implications politically for India, but also for a world that is increasingly suspicious of cross-border migration.

At the same time, the G7 is in its own demographic transition. The question of whether the horse race will be won by technology or by outsourcing is very much an issue that will need to be faced, for example, in the EU–India trade deal currently under discussion.

These are some of the aspects of what we need to do to increase investment. I know the recent Nobel Prize was about diffusion, but we are still not yet an upper-middle-income country, and I do not think we need to worry yet about the middle-income trap. Because of our services orientation, we want to be at the leading edge in the application of AI, which could be a force multiplier for development and for service exports.

But we also need to raise our investment rate. In the wake of the global financial crisis, our investment rate fell significantly, largely in the private sector. My own hypothesis is that this was in part a response to the global financial crisis and that there is some evidence of survivor bias: proprietors of firms that over-leveraged themselves lost management control. Be that as it may, if we wish to reach our 8% growth target for the next decade, an increase in the investment rate will be important, and that will require financing.

This is the part that really speaks to the topic of the conference. Paradoxically, up to now, our trade integration and our investment integration have been cautious. However, because we are now better prepared — both in terms of labor quality and infrastructure; and because there is a “China plus one” dynamic playing out, we are preparing ourselves for the next decade to be India's multinational moment. We have had one notable success in attracting Apple, and we are already significant, maybe not yet in terms of backward integration, but certainly in terms of value added and the shipment of iPhones.

There will need to be a fiscal dimension to the investment push as well, which is essentially domestic. By most estimates, two-thirds of any increase in our aggregate gross fixed capital formation rate will come from domestic sources, but a crucial third will have to come from abroad, in both portfolio and direct investment. As we discuss what is happening in the global economy, the question of what will impact FDI becomes very important for India.

# The Trade War Benefit the Global South?

**Hakim Ben Hammouda**

I will go straight to the two main points I wanted to highlight in this conversation. With my colleague Mohamed Basset Chemingui, we tried to question and discuss two common ideas in the global debate.

The first idea is that the Global South is a major factor in the fragmentation of the world economy. This is a very common idea; you find it everywhere. We will explain why we do not believe this is supported by economic reality. There is, in our view, a gap between the political discourse and the actual economic changes in the world.

The second idea emerged in the context of the trade war and the decisions taken on 2 April. The assumption is that the trade war is going to increase intra-Global South trade and, as a consequence, increase the fragmentation of the world economy. We disagree with this assumption and will explain why.

These are the two main ideas we question and discuss through two types of elements: a data analysis of trade trends over the last decade, and some preliminary modelling efforts, whose results we would like to share with you.

Let me start with some introductory elements, which you probably already know. In looking at the Global South, we focused on four main BRICS countries. Russia is not included, for reasons you can imagine. We chose these countries because they have the most diversified exports and imports.

Over the last decade, roughly 2015 to 2024, the growth of their total exports and total imports has been at an important level. But the most interesting issue appears when we look at intra-trade. What we did was to examine the intra-trade between these four countries.

The main conclusion, which you can see in the figures, is that within this Global South “block”, China is by far the most important actor. If you look at the decade, the contribution of the other major countries, such as India, Brazil, and South Africa, to trade among themselves is very limited. Their intra-trade has not experienced the same level of growth as their external exports.

**Table 1: Average Yearly growth rate of total exports and imports of goods between 2015 and 2024 for four BRICS countries**

	TOT Exports	TOT Imports
<b>Brazil</b>	6.8%	4.9%
<b>China</b>	5.2%	4.9%
<b>India</b>	5.7%	6.7%
<b>South Africa</b>	3.6%	1.9%

Source: Authors' calculations.

**Table 2: Changes in bilateral imports as a share of total imports in 2015 and 2024 for four BRICS countries**

	Origin	2015	2024
<b>Brazil</b>	China	17.7%	24.9%
<b>Brazil</b>	India	2.5%	2.6%
<b>Brazil</b>	South Africa	0.4%	0.2%
<b>China</b>	Brazil	2.6%	4.5%
<b>China</b>	India	0.8%	0.7%
<b>China</b>	South Africa	1.8%	1.2%
<b>India</b>	Brazil	1.1%	0.8%
<b>India</b>	China	15.8%	18.2%
<b>India</b>	South Africa	1.6%	1.8%
<b>South Africa</b>	Brazil	1.6%	1.4%
<b>South Africa</b>	China	18.3%	21.5%
<b>South Africa</b>	India	4.9%	7.2%

Source: Authors' calculations.

**Table 3: Changes in bilateral exports as a share of total exports in 2015 and 2024**

	Destination	2015	2024
<b>Brazil</b>	China	18.8%	28.0%
<b>Brazil</b>	India	1.9%	1.6%
<b>Brazil</b>	South Africa	0.7%	0.4%
<b>China</b>	Brazil	1.2%	2.0%
<b>China</b>	India	2.6%	3.4%
<b>China</b>	South Africa	0.7%	0.6%
<b>India</b>	Brazil	1.2%	1.5%
<b>India</b>	China	3.6%	3.4%
<b>India</b>	South Africa	1.4%	1.9%
<b>South Africa</b>	Brazil	0.8%	0.3%
<b>South Africa</b>	China	9.2%	11.3%
<b>South Africa</b>	India	4.0%	4.3%

Source: Authors' calculations.

What does this mean? It means that these countries, beyond the political discourse on the Global South, continue to trade extensively with the US and with traditional developed countries. We did many additional breakdowns by product and by period; I will not present all of them here. But the main conclusion is that, unlike what we often hear in political debates, the Global South is indeed experiencing strong growth in exports and imports, yet without a corresponding increase in intra-Global South trade.

We also looked at some of the reasons why the level of intra-trade within the Global South is low: payment systems and other structural factors. Given this, it is difficult to sustain the idea that the Global South is, by itself, a major driver of fragmentation of the global economy. That is our first point.

Let me now come to the second idea, which is linked to the increase in tariffs announced in early April. We tried to run some simulations using a computable general equilibrium model, MIRAGE. I will only present a few preliminary results.

These results are provisional and must be interpreted with a lot of caution. One difficulty is that tariffs have been changing almost on a weekly basis. For this reason, we decided to limit ourselves, which is not ideal, to the tariffs announced in April, without incorporating subsequent changes. Ideally, we should redo the exercise when all these tariffs are more stable; that would give more robust results.

We focused on two main effects. The first is what we call the depressive effect on the Global South. We looked at deviations from a reference scenario for the period 2025–2028, not only for Global South countries but also for the United States, in terms of exports, imports, GDP and other variables. The results show that these tariffs have a depressive effect on the main Global South countries, the four large ones, as well as on some groupings such as Mercosur and Turkey.

**Table 4: The impact of the trade war on some groupings and countries**

Changes in average yearly growth rate 2025-28

Country / indicator	GDP	Investment	Exports	Imports	FDI
<b>China</b>	-0,21	-0,23	-0,25	-0,23	-0,23
<b>India</b>	-0,24	-0,30	-0,60	-0,60	-0,30
<b>USA</b>	0,3	0,03	-2,93	-1,78	0,03
<b>EU27</b>	-0,01	-0,02	-0,07	-0,09	-0,02
<b>MERCOSUR</b>	-0,08	-0,18	-0,31	-0,48	-0,18
<b>Turkey</b>	-0,01	-0,03	-0,11	-0,13	-0,03

The second aspect concerns intra-trade: what will be the impact of the trade war on trade within the Global South? Here, the picture is not clear-cut. There are some increases in intra-trade between certain countries (for example, involving India) and some effects in specific cases. But overall, the impact is limited and smaller than what some analysts suggest.

**Table 5: The impact of the Trade war on the Global South  
 Intra-Trade**

Changes in average yearly growth rate 2025-28

<b>Importer/ Exporter</b>	<b>China</b>	<b>India</b>	<b>Turkey</b>
China	-	0.21	-0.12
India	-0.84	-	-0.49
Turkey	-0.36	0.50	-

*Source: Author's simulations.*

So, while there is some increase in intra-Global South trade following the tariffs, it is limited. We cannot conclude, as many papers and articles do, that the trade war will significantly increase intra-Global South trade or make the Global South a strong driver of fragmentation.

To respond to the question of this discussion, I would say that, beyond political statements about the Global South and its alleged contribution to the fragmentation of the world economy, there is still room for interdependence in these tense times.

# **Southeast Asia's Response to the Reshuffling of International Economic Relations**

**Françoise Nicolas**

I will be discussing Southeast Asia and its response to the reshuffling of international economic relations. There are two main reasons why Southeast Asia is an interesting case study. The first reason is that Southeast Asia has undoubtedly been one of the major beneficiaries of globalization. All Southeast Asian countries were deeply connected to global value chains and benefited hugely from this participation. It is therefore interesting to see how they react to changes in globalization. I am not saying that there is deglobalization, but there is a change in the way globalization operates. It is important to see how countries that were so successful at taking advantage of globalization respond to these changes.

The second reason is that, in the case of Southeast Asia, you can observe responses at two different levels. There are responses at the individual state level, and there are also initiatives at the regional level, through ASEAN, but also at the sub-regional level. It is therefore interesting to look at these two layers of reactions. Compared to the two other speakers, I will primarily focus on the governance dimension of Southeast Asian reactions.

Let me start with how Southeast Asian countries see the changes: what is the state of play, and what are the major changes that have taken place? The first major change is the demise of the global rules-based order as we knew it. This order is gone, and it will not come back. Even if Trump leaves office, there will be no return to the previous state of play. That is a major change, and it is of utmost importance for Southeast Asian countries, which have benefited from this rules-based order.

The second major change is that economic security now seems to prevail over economic efficiency. This is a new state of mind, and it affects decisions taken at the individual level. As a result, we see rising threats. Among these, there are two major threats.

The first is coercion, or the coercive use of interdependence. This is particularly important for Southeast Asian countries, because they are relatively small and can therefore be coerced more easily than larger economies. The second is the weaponization of trade dependencies, which is particularly relevant regarding China.

We see a rise in rivalry between China and the United States and the imposition of prohibitive tariffs. For Southeast Asian countries, this has meant a huge increase in tariffs imposed on them, irrespective of their development levels. For instance, the initial level of tariffs imposed on Cambodia was 36%, even higher than for more developed countries that might have seemed more natural targets for the United States. Irrespective of development levels, huge tariffs are being imposed, and this is a real problem for these economies.

Another problem is the imposition of high tariffs on transshipments. Nobody exactly understands what “transshipment” is supposed to mean; there is no clear definition. But Southeast Asian countries understood that if they imported goods or intermediate products from China, processed them in one way or another, and then exported them to the United States, they would be in trouble. They have become major targets of US tariffs.

For all these reasons, Southeast Asian countries find themselves in a particularly delicate position in the middle of the US–China rivalry, and especially in the middle of the trade war launched by the United States. What we see, at the end of the day, is that the traditional strategy used by Southeast Asian economies, the so-called hedging strategy, is very much challenged. They used to navigate Sino-US rivalry by siding with one side one day and the other side the next, trying to take advantage of both partners, while insisting that they did not choose any side. This has always been complicated, but it is even more complicated today than in the past. The hedging strategy is under serious strain.

Let me now turn to the responses of Southeast Asian countries. I identify three levels of response.

The first level is what I call the diversification of partnerships. Southeast Asian countries have been trying to talk to as many partners as possible. They have always done this to some extent, but it is now much clearer and more deliberate. A couple of examples can illustrate this. There is now an ASEAN–GCC summit that convenes regularly. This reflects a trend towards engaging in dialogue with the Gulf countries, which is quite interesting. To be honest, if you look at what has happened in the past, several Southeast Asian countries, particularly the Muslim-majority ones, have long been in touch with the Gulf countries. But this is now increasingly institutionalized, at the ASEAN level rather than only at the individual country level. We now have an ASEAN–GCC framework, and also an ASEAN–GCC–China summit.

Another example is that, as a result of the pressures exerted by the Trump administration, Indonesia suddenly accelerated its negotiations with the European Union, and we now have an Indonesia–EU FTA. This is another attempt, this time at the individual country level, to diversify partnerships beyond the traditional ones.

The second level is not about creating new partnerships but deepening existing initiatives or cooperative schemes. The first of these is, of course, the ASEAN trade arrangement. It has changed names a few times and is no longer called the ASEAN Free Trade Agreement. It is now the ASEAN Trade in Goods Agreement (ATIGA). At the latest ASEAN summit, ATIGA was upgraded. Before the summit, 98% of goods were covered by the agreement; now it is even more, close to 99%, almost 100%. More importantly, ATIGA now addresses non-tariff barriers in a more serious way. In theory, non-tariff barriers were already addressed in the past, but this was not really the case on the ground. Now, more effort is being devoted to eliminating non-tariff barriers.

ASEAN is thus making special efforts to develop intra-regional trade. We know that intra-ASEAN trade has long been relatively low, stuck around 20–23% of total trade. The hope is that it will develop further; we will see whether this works.

Another initiative is the Regional Comprehensive Economic Partnership (RCEP), which includes the 10 ASEAN member states plus five other partners: the three Northeast Asian countries (Japan, Korea, and China) and two southern partners (Australia and New Zealand). RCEP is also being deepened. At first, nobody took RCEP very seriously, but it has become a serious arrangement. A major achievement of RCEP, I would argue, is the harmonization of rules of origin, which makes trade in goods within the region much easier. These rules of origin are relatively easy to meet, so goods can circulate more freely and trade can expand. A further positive sign is that, during the latest summit, it was decided to establish an RCEP secretariat. It should have existed from the start, but it took time. Now it is being implemented and will manage the relations among RCEP countries. This is an important institutional step.

A third cooperative scheme that has been deepened is the CPTPP. Of course, CPTPP is not only about ASEAN, but four ASEAN countries are members: Singapore, which was one of the initiators; Brunei, another initiator; and Malaysia. Today, other Southeast Asian countries are interested and are queuing to join CPTPP. This is the case for Thailand and Indonesia, if I am not mistaken. There is therefore a clear interest in deepening this arrangement as well, which is more ambitious than RCEP. It will be interesting to see what emerges from these efforts to deepen CPTPP.

The third level of response is the launching of new initiatives. These are not at the ASEAN level but at the individual country level, particularly in Singapore. The latest initiative is known, for the moment, by the rather

unfortunate acronym FITP: the Future of Investment and Trade Partnership. They will probably have to find a better acronym, because FITP is unpronounceable, but for now, that is the name.

FITP aims to devise new rules and arrangements to facilitate trade and investment. It is an initiative taken by a very small group of countries, including Singapore and Switzerland, among others. At present, 16 WTO members are part of FITP. Although it is still small, it may grow into something much bigger.

This is very similar to the early days of CPTPP. Initially, CPTPP began as an initiative by four countries, the “P4”: Singapore, Brunei, Chile, and New Zealand. These four countries decided to engage in a dialogue on trade. Once they started talking about financial services, it attracted interest from the United States, which joined, followed by other countries, and it became the TPP. Then the United States left, and it was transformed into CPTPP. The important point is that you can start with a small group of countries, enlarge the group, deepen the conversation, and end up with a cooperative scheme that makes sense for the rest of the world. This was the trajectory of CPTPP, and it might also be the case, who knows, for FITP, which addresses issues that are slightly different from those covered by CPTPP.

That is why FITP is of interest. It is important to know that it exists and to keep an eye on what it may become. It may be the beginning of a new scheme, and it may also change the world.

# Global Imbalances and Macroeconomic Policies

**Dorothee Rouzet**

If we start with the question, “why do we care about imbalances?”, the first point is that the size of external deficits and surpluses is on the rise again. The last time this happened was before the global financial crisis, and it did not end well. Today, we have not yet reached the same scale, and perhaps not the same nature of imbalances either, as imbalances are not rooted in a global savings glut this time. But if we look at IMF data, current account balances overall grew by 0.6 percentage points of global GDP in 2025, and that trend has been lasting for a few years.

When we try to define the issue and what can be done about it, the role of the rising Chinese industrial overcapacities often comes up. Excess capacity is visible in many Chinese industries - electronics, chemicals, machinery, metals, etc. - on the back of distorting policies, and without a self-correcting mechanism through the exit of unprofitable firms, as we would see in a market economy.

This is, however, only a narrow way of looking at global imbalances. Even if the distortive policies were scaled back, global imbalances would stay, as they find their origins in the growth models of major economies.

It is also important to stress that current account imbalances span goods, services and income flows. Attention is focused on goods. We started talking about services in the previous sessions of this conference, and it is indeed important to look at the full picture. The US is a large exporter of services, even if it has a large deficit in goods. The EU-US bilateral relationship is a very different picture depending on whether you look at goods only or at the full current account. Japan has a sizeable surplus, but it is driven by primary income flows and probably justified by Japan’s demographic situation, so it does not appear so problematic.

All this said, if we go back to economics, external imbalances are the difference between countries’ savings and their investment, and these gaps have always existed. Having imbalances is not a problem per se. Some imbalances are welfare-enhancing if they are justified by demographics or by the level of economic or financial development. The goal is not to bring every balance to zero, and even less every bilateral balance.

The problem here is, first, the imbalances driven by distortive policies, either at the micro or sectoral level, or macro policies purposefully affecting consumption, investment and savings. And second, that imbalances have become increasingly persistent over time.

Let's look at the three main "culprits" of global imbalances: China, the US, and Europe. In China's case, it is fair to say that external imbalances reflect internal imbalances in the Chinese growth model. To give a few numbers: investment is 40% of Chinese GDP, versus around 20% in the eurozone or in the US. Consumption is less than 40% of Chinese GDP; in the eurozone, it is about 75%, and in the US, about 80%. This does not just happen by itself. It is the result of policies that support production and depress consumption. The result is that, if you believe IMF data, the current account surplus is 2.3% of GDP in 2024 – and there are reasons to think this number is underestimated.

Why do we care? Because these imbalances are rooted in a strategy of overinvestment and industrial domination that creates systemic risks for advanced economies, in terms of industrial viability and sovereignty, but also for developing and emerging countries, which can face unfair competition from subsidized products and find it more difficult to integrate into global value chains. The result is a systemic distortion that undermines not only trade but also sustainable development and confidence in open markets.

Someone's surplus is someone else's deficit. So the mirror issue is the US imbalance: a current account deficit of 3.9% of GDP in 2024.

Again, a few numbers: the US accounts for about 30% of global consumption, but only 15% of global manufacturing value added. What are the internal imbalances? An obvious one is the size and persistence of the fiscal deficit. More broadly, the financial system, which favors consumption, credit and foreign capital inflows, also contributes.

The EU runs a current account surplus of 2.8% of GDP in 2024, according to the IMF. The macroeconomic underpinning is a chronic lack of investment, which leads to exporting savings to the rest of the world. Germany is doing its homework to address it with the planned infrastructure investments, and more broadly, the EU, with higher defence spending and efforts to advance the capital markets union. Hence, and not just because we are sitting in Europe, I would argue that the EU imbalance is less systemic than the other two.

Again, external imbalances are a normal feature of a globalized economy. The issue is that they have become highly persistent. Normally, in a standard economic model, you would expect a spontaneous adjustment through the exchange rate. In countries with a large deficit, at some point, capital inflows would slow, the currency would depreciate, exports would increase, and things would resolve themselves over the medium term.

Why does that not work in the US? Because the dollar is the international currency. Capital flows keep coming in and are willing to finance the US fiscal deficit without noticeable limits. On the other side, in China, capital controls and exchange rate management prevent adjustment through currency appreciation.

This raises an interesting question about the analysis of imbalances. The most common approach is to look through the current account, goods and services, and often mostly the goods balance. But we should also ask to what extent the capital account is driving imbalances through financial flows. It is important to keep the two dimensions in mind.

So, what can be done? It is hard to think of a way to achieve an orderly reduction in global imbalances without some degree of coordination to act on the root causes (imbalances rooted in growth models), rather than on the symptoms (exports, sectoral policies, or bilateral balances).

A first approach is unilateral. This is the current US approach. I do not think it works. I do not think tariffs can reduce internal imbalances in a sustainable way. Tariffs can be used to some extent to restore a level playing field when they target specific issues affected by non-market practices and policies. But otherwise, the result is shifting imbalances from one place or one product to another, without resolving the underlying issue.

A second approach is coordination on micro policies, that is, industrial and trade policies. Again, that can restore a level playing field in a more effective way, but it will not solve imbalances at the macro level. That said, I am not saying it should not be done. Efforts should be pursued to ensure that national industrial policies and subsidies are more transparent and more proportionate, and there is scope for coordination to be effective in that direction. But it will not solve the macro picture where imbalances are rooted in the sources of growth.

The third approach, which is the most effective, but also the most difficult, is coordination on macro policies. We all know what is needed in broad strokes: China needs to consume more, Europe needs to invest more, and the US needs fiscal consolidation.

It is, of course, much easier said than done. Such coordination was tried pre-2008 under the auspices of the IMF, with limited success. In today's context, the main challenge is how to get China interested.

I will leave this as a question: is it enough that the Chinese growth model is showing limits, through the unresolved housing crisis, overinvestment with low profitability, and deflation? If that is what gets China interested in rebalancing, how long will it take for the cracks to widen enough?

Or is it more the threat of a disorderly and costly reduction in imbalances, through escalation in protectionism and a slowdown in global activity, that could be enough of a deterrent to convince everyone that there might be a better way, and to get people around the table?

This is where the biggest challenge lies. And this approach is a distinct but complementary one to the work on non-market policies and to the work on reinforcing supply chain resilience, which are also needed.

# The Challenges of Rising Global Imbalances

**Brad Setser**

I want to emphasize three general themes.

First, contrary to what you hear on almost every panel like this, the world has not, in fact, fragmented over the past six years. The scale of global imbalances indicates that China is running a bigger surplus than ever, and the United States is running a bigger deficit than ever. It is very hard to have a true fragmentation of the global economy if, on one hand, the United States remains the source of demand, and on the other hand, China remains the source of supply.

Second, the traditional division that puts equal weight on the United States, Europe, and China in global imbalances is a bit dated. Europe is correcting. Germany is correcting, perhaps being forced to do so by shrinking exports. With increased investment, Europe is less and less a contributor to global imbalances, setting aside the almost automatic increase in investment income that comes with higher US interest rates.

If you remember one fact, remember this: Ireland's goods surplus is now substantially bigger than the goods surplus of the European Union absent Ireland. And the goods surplus of the EU, absent Ireland, is statistically pretty close to zero.

Third, the French presidency has its work cut out. There is no evidence that imbalances are correcting or are poised to correct. This may, in the end, create future risks, either a breakdown of the current Sino-American trade accord or something analogous to a return of financial stress that forces adjustment.

Over the past six years, if you ignore the COVID shock, there have been at least three major shocks that have hit the global economy.

The first is Russia's invasion of Ukraine, and the associated fracturing of energy and natural gas markets. That shock, at least on the oil side, has essentially passed, but there has been scarring and true fragmentation in the natural gas market. This has profound implications for this continent, though less so for France.

The second shock is Trump's revolution in US trade policy. In Trump's first term, the United States decided to ignore its MFN commitments towards China. In the second term, it decided to more or less ignore its MFN commitments to everyone. The United States has adopted a policy that basically says: if you want access to the US market, you have to give us something. It is, in a way, emulating the policies of a great rival when it comes to coercion, something that is well understood here.

Tariffs have increased by about a percentage point of GDP. The United States now collects about as much in revenue from tariffs as China collects in revenue from income tax.

The third shock was the bursting of China's property market bubble. This has, I would argue, produced more significant changes in the structure of global trade than the other two shocks. The property market correction has led China back to a growth model that relies more on external demand.

Net exports have been contributing, on average, one and a half percentage points to China's growth over the past few years, which is a lot for a big economy. Chinese import volume growth has been pretty close to zero, except during periods when China is doing strategic stockpiling. These are important and profound shifts.

There is a significant risk that this adjustment has not been completed, because the property market correction has yet to run its full course. The pressures are towards a more unbalanced world, not towards a more balanced world.

Let me give a sense of the magnitude of the problem.

Since 2019, East Asia's goods surplus has been up about 900 billion dollars, a little less than a percentage point of world GDP, and more than a percentage point of the GDP of Asia's trading partners. Asia's current account surplus is up a little bit less than measured data suggest, but that is not because Japan and the newly industrialized economies have reduced their surpluses.

Japan and the newly industrialized economies all have current account surpluses substantially larger than their goods surplus, because of accumulated past surpluses and the rise in investment income. The goods balance of East Asia's newly industrialized economies, plus Japan, is around 200 billion dollars, brought down by Japan. Their current account surplus is close to 600 billion dollars.

China, by contrast, now runs a goods surplus of 1.2 trillion dollars, up 800 billion over this period of time. Yet its current account surplus is about 600 billion dollars below its goods surplus, despite years of current account surpluses and despite a large net international investment position.

If you disaggregate that difference, you find that about one-third is easily explained by the tourism deficit. About one third, roughly, comes

from a statistical change China made to its balance of payments data in 2022, which changed the relationship between customs goods data and the balance of payments goods data. And about one third is because China, despite accumulated surpluses, reports a substantial deficit, and a growing deficit, in its investment income account.

Hence, there is reason to believe that Asia's aggregate current account surplus, around 1.3 trillion dollars, rising and now about as large as it has ever been, is actually somewhat underreported.

If you look at the change in China's goods export volumes over the past six years, you will find in the IMF data that exports have increased in volume terms by about 40 percent. Imports have increased in volume terms by about 1 percent. That is one of the most unbalanced shifts in global trade the world has experienced.

And its counterpart has not been primarily in the United States, but in Europe. Over the past several years, European goods exports have actually shrunk in volume. China's outperformance relative to global trade has, as its main counterpart, Europe's underperformance.

If you frame it in savings and investment terms, China's savings rate has remained a little above 40 percent of GDP. Across East Asia, the aggregate savings rate has actually been rising, not falling, and is now also around 40 percent of GDP. Taiwan is up, and China's growing weight within East Asia has an impact.

Is there any hope that this will change? Unfortunately, the signs are not good.

In the United States, you can argue that there has been a policy, maybe not an ideal one, of fiscal consolidation through tariff revenue. A one percent increase in GDP in tariff revenue should, in principle, have an impact on the current account, because it is a form of fiscal consolidation. However, last year that was offset by tax cuts elsewhere, and the president seems intrigued by the idea of sending American consumers checks paid for by the rest of the world.

The AI investment boom also puts upward pressure on the current account, for obvious reasons.

In China, there is no evidence that President Xi is seriously committed to the kind of radical restructuring of the Chinese economy needed to bring down the savings rate, at least in my judgment. The property market downturn continues. Goldman Sachs estimates it will continue for another three years. Starts are down 90 percent from their peak, but residential investment is not down as much.

The IMF is putting hope in the possibility that China will reduce its investment in industrial policies. From a micro point of view, that may create a more level playing field. But from a macro point of view, less

investment means a bigger savings-investment imbalance. It is insufficient on its own, without serious efforts to raise Chinese consumption.

Raising consumption, I think, fundamentally requires a much larger Chinese central government, a much larger commitment to social spending financed by the central government, and a bigger Chinese deficit.

Finally, market pressures are not working to limit imbalances.

If you look at government bond markets, there is no pressure on the United States, at least no more than on Japan or on France. If you look at exchange rates, the market is effectively saying: specialize and concentrate industrial production in Asia.

Euro-yen is at an all-time high for the euro. That is not saying “produce in Europe”. Yen 150 against the dollar is saying “produce in Japan”. The Korean won is at levels seen in the Korean financial crisis and in the global financial crisis, at long-term lows. The Taiwan dollar is weaker now than it was in the mid-1990s, before Taiwan had advanced to the technological frontier in semiconductor production.

The Chinese yuan is at a relatively weak level against the dollar, and quite weak against the euro. It is down 20% in real effective terms from where it was three years ago. Predictably, that is contributing to a widening of imbalances.

I applaud the French presidency’s efforts to address what I consider a quite significant problem for the world and for Europe, and I wish them the best of luck.

# Geoeconomics and Global Imbalances

**Jean Pisani-Ferry**

I would like to share thoughts about the way geoeconomics affects our reading of global imbalances. The question is that we are coming from a world in which external balances were seen as essentially trade-dominated. That was the world in the 1950s and the 1960s, with very limited or no capital mobility, and therefore, the main determinant of the external surplus was foreign trade.

Gradually, a macro view emerged in the 1990s because of real capital mobility, and we transitioned from a trade-based view to a saving-investment-based view. This shifted the focus from the micro side of things, trade, to the macro side, saving and investment.

That was limited initially. As we all know, the Feldstein-Horioka paradox showed that the high degree of correlation between saving and investment doesn't make sense in a perfectly integrated world, and so its existence is a symptom of the lack of integration. But gradually, we overcame the saving-investment views of the Feldstein-Horioka world, and a more completely saving-investment-dominated view emerged, where savings and investment rates are determined separately. They have different causes, and therefore, very large imbalances can build up.

The only limit to those imbalances was a limit of the stock: net international investment positions, at least deficits, could only accumulate to a certain extent, provided they were sustainable. But that was a long-term constraint, and in the short term, this was not an issue.

Imbalances were therefore regarded from a very macro-financial angle, at least in advanced economies. I know that for emerging countries it's not the same, but for advanced economies, that was the dominant view.

How does it change with the emergence of a geoeconomic view? This reintroduces power asymmetries in the analysis of external imbalances. Trade balances are not just outcomes; they are expressions of, or instruments of, statecraft, and economic and financial linkages can be weaponized.

In a way, it is a return to the Hirschman analysis of power and foreign trade. Here I have some quotes from Albert Hirschman, written at the end of the Second World War, in which he said that "The gain from trade and

dependence on trade [are] two aspects of the same phenomenon”. He emphasized, “Commerce can become an alternative to war [...] by providing a method of coercion of its own in the relations between sovereign nations. Economic warfare can take the place of bombardments”. So we are getting back to this.

This view was very influential in economics in the 1960s. Gradually, it declined and became a reference mostly used in political science, and in economics, it became second-order by the early 2000s: it was substituted by a macro view. Interestingly, since the early 2000s, we have seen the rise of this view again, in part in the literature at the crossing of economics and political science.

So what are the implications of this geoeconomic view? Most dependencies can be weaponized. Instead of the very macro view that doesn't look at the causes, we're back to a trade view that looks at the determinants of trade surpluses and deficits, but also looks at where deficits come from and what they consist of in terms of goods. It looks at what an export performance can create, and what sort of dependencies it can create on the export market; the case of Germany comes to mind.

And also, not yet very present except in the policy discussions we're having these days in Europe, there is the fact that we depend entirely on US credit cards for our services, or the users of our services. This creates a dependency on US credit cards.

The implication of the geoeconomic view is that there are many different aspects that matter. It is not unified as in the macro view. It is composed of several micro dependencies.

The reality is also that the US, at some point, came to the famous “small yard, high fence” view of Jake Sullivan, which put emphasis on the very limited character of this approach in critical sectors. But the reality is that there has been a contagion of this approach to other fields.

Can potential vulnerabilities be identified by looking at the balance of payments? In fact, not really. There is no aggregate assessment or aggregate measure of vulnerabilities or dependency. You can look at trade vulnerabilities, and that requires extremely detailed analysis, especially if you want to take into account indirect dependencies, and I put some references here. For financial vulnerabilities, it also requires some stress testing.

It's not something as visible or as simple as it was with the macro view, when you had a deficit giving rise to the accumulation of liabilities, and then at some point, the question was when those vulnerabilities would become unsustainable. Here, you have to take a much more granular approach.

In sum, we are in a fairly constrained world, not only economically and geopolitically, but also analytically. The macro-financial view is still relevant for analyzing vulnerabilities, but it must be complemented with a more micro geoeconomics view. It is not an easy endeavor, because you have to work on different levels and different degrees of granularity.

# Economic Security in a Changing World

**Emily Blanchard**

The world has changed. We all know this, and I will not belabor the point. But it is important to be clear-eyed about what is happening. Governments are throwing sand in the gears of international commerce in profound ways, and with unprecedented vigor—through sanctions, export controls, investment screening, tariffs, and so on. We find ourselves in a fundamentally new world of international economic policy. This time is different, in several important dimensions.

First, these policy tools are no longer only about restricting inward flows—via tariffs and other import restrictions, visa limits, or inward investment screening. They are increasingly designed to restrict outward economic flows as well. Consider, for example, the Biden Administration’s August 2023 Executive Order to begin scrutinizing outward investment from the United States. This is unprecedented in the U.S. context. The U.S. government has signaled interest in restricting what the United States sells to the world—what one might call a form of reverse mercantilism—extending beyond narrow categories of sensitive goods and services to now include investment, ideas, and especially technology.

At the same time, and not unrelated, we are seeing power displace rules and norms. This is another massive shift. There is also a critical shift in how we think about policy itself. Policies are no longer siloed across institutions, ministries, or departments and agencies in the way they once were. Security is not handled only by security officials, trade only by trade officials, and foreign policy only by foreign policy officials. These issues are now compressed and interwoven into a single, messy, overlapping policy space.

We are living through a massively destabilized—and destabilizing—era. I worry that this is a period not just of adaptation and change, but of rupture. In this context, I would offer three observations—about the past, the present, and the future.

Looking backward, it is important to emphasize that this shift in national security policy—and toward economic nationalism—is not simply a Trump phenomenon, as tempting as it may be to think so. The change predates Trump. Many would trace it to the post-global financial crisis

period, when individuals' sense of economic predictability and security plummeted. For many, globalization no longer seemed fair or worth it. This is when, I suspect, prior beliefs were updated, and the politics began to shift under the radar.

These changes took place not only in the United States but across much of the developed world, as workers and citizens rethought how to approach economic policy in a more uncertain environment. The shift in zeitgeist was centered around economic opportunity and household insecurity, but it wove in other challenges as well. Starting at least a decade ago, governments began talking in earnest about security, climate, and fairness as core objectives of international economic policy.

And let me be clear: fairness refers not just to the distributional consequences of globalization and new technologies within countries, but also to distributional concerns across countries. Conspicuously, these concerns extend to fraught geopolitical challenges such as Chinese overcapacity—how low-cost, high-quality exports from China have flooded global markets, to the enormous benefit of buyers, but at the expense of competitors elsewhere. This economic phenomenon of Chinese export growth emerged well over a decade ago, even if the policy tools and rhetoric have become visible only more recently.

So this is not just a Trump issue, and it is not just an American issue. It matters that we recognize this as we look forward. We cannot simply wait for 2028.

Turning to the present: Trump, and particularly Trump's second administration beginning in early 2025, has upended the game. Things that were once said quietly are now said out loud. More importantly, the United States has changed not only what it says, but what it is doing.

It is fundamentally different when the United States steps away from multilateralism. To be sure, revisionist powers like China and Russia engaged in policies like dual circulation and the weaponization of trade first, and in profound ways. But the fact that the United States is now doing it is hugely important. When we pull unilateral levers, we weaken our alliances and risk undermining some of them completely. The new administration has discarded norms—but norms have been the backbone of the global trading order and the rules-based system from the beginning. There were certain things that we simply did not do and, crucially, that we stopped other countries from doing—using tariffs as a foreign policy cudgel, for example. Yes, exceptions have always existed in the General Agreement on Tariffs and Trade, allowing countries to take protectionist actions for national security. But the norm was restraint, and the norm upholder in chief was the United States. That role has eroded.

Arguably, some of the most severe deviations occurred under the Biden administration rather than under Trump. I'll grant you that. But importantly—if somewhat hypocritically—the United States still upheld trade norms for most of its trading partners, and it continued to hold others to a higher standard.

By contrast, by stepping away from trade norms much more explicitly, President Trump has created a permission structure for other countries to follow. He has effectively allowed governments to take what they may have been considering quietly, bring it into the open, and begin to act. I worry that we will look back and conclude that the multilateral system fell apart slowly, and then all at once—and that this moment marked the inflection point.

Worse, governments are now openly weaponizing trade. They are thinking not only about how to do it, but also about how to protect themselves when others do it. They are recognizing that there may be circumstances in which a country—perhaps themselves—might want to corner global markets and production.

China and critical minerals offer a clear illustration of how this can happen. Perhaps this was deliberate, as the Made in China 2025 plan seems to suggest. In other areas, the focus is on technology, and the protagonists are different. This is an area where the United States has critical leverage in some domains. Europe does as well. G7 partners in East Asia hold similar leverage. None seems eager to flex these muscles, but they've begun to do so nonetheless, much to the consternation of each other and of the global business community. Once it begins, where does it stop?

Fundamentally, economic weaponization is about production, technology, trade, and people—all intertwined and overlapping. The challenges and the potential solutions are not confined to any single domain. Accumulating and exercising leverage is complicated, and the consequences of attempts to create and use chokepoints are hard to predict.

This weaponization also extends to cybersecurity. Cybersecurity is not a standalone agenda item here, even if I say that somewhat uneasily as an economist. But it is essential. When we think about capabilities that countries can deploy against one another, there are many options short of kinetic conflict. Many are digital. They can disrupt the security and safety of populations—consider concerns around water treatment systems and other digitally mediated vulnerabilities. There is also the ability to steal frontier technologies from other countries or firms.

Of course, the military dimension is part of this as well. The upshot is that this is a uniquely dangerous moment. It already was before Trump returned to office, but I would argue it is even more so today.

So where are we going? That is the central question. I will surprise no one by saying that it is safe to assume we are barreling into the unknown. We have never been here before.

The world has faced dangerous moments in the past, and moments far more difficult than the one we are in today. That is an optimistic observation, perhaps. But what we face now is deeply unsettling. Why is it so uncertain? What are the contours of the world ahead?

First, governments are increasingly pursuing extraterritorial objectives. They are asking how to shape not only production, innovation, technology, and deployment within their own borders, but also patterns of economic activity beyond them. They are even asking how to shape trade among third countries—trade that neither enters nor exits their own markets. We worry about the leverage exercised by country A over country B, even when we are neither country A nor country B. This is deeply destabilizing.

The global rules-based order was built on the premise that countries manage trade and production within and across their own borders, but do not attempt to manipulate economic activity far afield. But in many spheres of national and economic security today, that is precisely the objective. This represents a fundamental shift.

And again, it is not only trade. It is innovation and technology diffusion. It is not only what we make, but how we make it, and with whom. We simply do not have rules for that world.

Compounding this challenge is the fact that all of this is messy—and it will all remain messy. Our rules and institutions are at existential risk. That is evident internationally. The WTO is in a more perilous position than it has ever been in. It saddens me. I wrote my dissertation on cooperation through the WTO and in Geneva, but this is where we are.

There is also a domestic dimension. Within many countries, institutions are weaker than in the past. Here I am thinking particularly of the United States, of course. I do not think we can overstate the long-term consequences of hollowing out the administrative state. Rebuilding it will take time.

Whether we like it or not, the United States is very large—an elephant in a china shop. When we turn around, even if we do not mean to, we create economic ripples in the rest of the world. We should be careful about how we act, the changes we make, and even the statements we issue. What is said and done by the Treasury Secretary, the Chair of the Federal Reserve, or the Secretary of Commerce matters far beyond our borders. But today we appear increasingly incautious, at times even cavalier. I worry deeply about what has already been damaged and cannot be undone.

There is massive experimentation underway in how these new policies are implemented. Even with capable administrative states, mistakes will be made. It is important that governments show grace toward one another as we experiment and, inevitably, stumble forward together. That is difficult even in the best of times—and these are not the best of times.

Structurally, governments face major challenges. The United States will eventually rebuild its administrative state. I am an optimist and a patriot, and I believe that will happen. But it will take sustained effort.

Coordination across countries will also be difficult. One of the greatest challenges in managing this new era of economic security is agreeing on what the core problems are and how to prioritize them. In economic security, we often have to infer the intentions of other governments because intentions are not observable, and neither are our assertions about them inherently credible. Add to this: coordinating among democracies is especially hard, because reaching consensus is especially difficult and political leadership can turn on a dime.

All of this is fairly dismal—but this conference is, after all, about economic security. So, in closing, let me offer two things I am watching closely.

First, I am watching how trust is evolving among countries. I am especially concerned about the United States at the moment. But in some other parts of the world, I do see trust strengthening, and that gives me cautious optimism. Trust matters.

Second, I am watching for evidence of dynamic strategies. To what extent is the promise of future cooperation casting a shadow (or glow) over the present? Axelrod's insight was that cooperation can be sustained in complex systems as long as the future meaningfully enters today's decisions. I'm looking for signs of how governments are factoring the future into their choices, rather than simply reacting moment to moment.

These two elements—trust and a credible future—are precisely what international institutions are meant to provide. And in a world defined by economic weaponization and uncertainty, we need them more than ever.

# The Future of Financial Market Infrastructures

**Brigitte Daurelle**

It is a pleasure to be here today to discuss an issue that sits at the crossroads of finance, geopolitics and European sovereignty: the evolution of our financial markets, and the future of the infrastructures that underpin them.

As someone who has spent more than twenty years in financial market infrastructures — leading several European Central Securities Depositories, and now as an independent director of CLS Group, another global financial market infrastructure (FMI) — I have seen how central these infrastructures truly are, and how profoundly the geopolitical environment around them has shifted.

## Market infrastructures: From technical plumbing to strategic assets

For a long time, FMIs — CCPs, CSDs, trading venues, payment systems — were viewed as specialized technical utilities: essential, but largely invisible, and in Europe, essentially domestic. This view is no longer sustainable.

In a world marked by geopolitical tensions, the return of industrial policy and the weaponization of financial interdependence, market infrastructures have become strategic assets. They determine where liquidity concentrates, who controls financial channels, and ultimately which economies hold leverage.

Recently, Christine Lagarde captured this with remarkable clarity at the Frankfurt Finance & Future Summit: Europe cannot afford to maintain fragmented and sub-scale infrastructures if it wants efficient markets and genuine strategic autonomy.

Her warning is fully aligned with the conclusions of the Draghi Report, which stresses that Europe's competitiveness, innovative capacity and ability to finance its priorities all depend on the emergence of a truly integrated capital market. Fragmentation is not a minor inconvenience — it is a structural brake on Europe's growth, attractiveness and strategic influence.

## The weaponization of finance and Europe's Achilles heel: fragmentation

Let's take a broader perspective. Over the past decade, the United States has shown how financial power can be used as a geopolitical instrument — through the dominance of the dollar in commercial exchanges, through the global reach of its sanctions regime, and through its capacity to influence access to key financial channels.

In such a context, Europe is structurally weaker. And the atomization of its market infrastructures — the backbone of its financial system — is a major strategic disadvantage. Because fragmentation weakens liquidity — and liquidity shapes power.

Europe still counts 295 trading venues, 14 central clearing houses and 32 central securities depositories. This disperses liquidity, reduces market depth, and makes price formation less efficient than in integrated markets such as the United States.

The consequences are immediate:

- higher issuance and trading costs
- more operational friction
- less predictable outcomes for global investors
- and a reduced ability to attract listings.

It also pushes some of our most dynamic companies to seek capital abroad, where liquidity is deeper and infrastructures unified. And the issue is not limited to capital markets. In retail and card payments, Europe has no pan-European infrastructure, which leaves us dependent on non-European players such as Visa, Mastercard and increasingly Apple Pay. This creates strategic vulnerabilities and limits Europe's ability to shape the future of payments. In short: market infrastructures are either fragmented — or non-existent.

Meanwhile, the dominance of the dollar reflects a simple reality: the United States benefits from a single, integrated capital market, supported by unified infrastructures that concentrate liquidity and reinforce its global influence. Europe does not — at least not yet.

## Zooming in: CSDs as a revealing case study

Let me now turn to an example that illustrates the challenge particularly well: central securities depositories. I often told my teams that CSDs are the nuclear power plants of finance:

- they hold the definitive record of who owns what
- they ensure the simultaneous exchange of cash and securities
- and if that record were lost or corrupted, we would face not only financial chaos but also deep social and political instability.

They are, by design, highly systemic. And yet Europe operates 32 CSDs, compared with just two in the United States — one for government securities and one for private securities.

Why is consolidation so difficult? Two main reasons. First, it is technically complex. Merging CSDs is far more difficult than merging trading venues. It requires the painstaking harmonization of corporate actions, tax procedures, settlement timelines, reference data and market practices.

When I led the consolidation of the Belgian, French and Dutch CSDs within the Euroclear Group, it took nearly three years of negotiation and harmonization before the first line of code was written. Dozens of experts on our side, and just as many at each major bank across the three marketplaces, were involved. These projects are long, costly, politically delicate and operationally risky. No surprise private actors hesitate.

Second, ownership structures are fragmented across groups with different incentives and regulatory environments. Expecting spontaneous convergence is unrealistic. Conclusion: left to market forces alone, consolidation will not happen.

## **Fragmentation in Europe: A strategically unsustainable status quo**

The costs of maintaining this fragmented landscape are well known: higher cost of capital, inefficiencies for investors, duplicated cyber-resilience investments, slower market integration, and reduced ability to attract global liquidity.

Target2-Securities was a major step forward, harmonizing settlement under ECB leadership. But Europe's post-trade architecture is still, to use a familiar expression, "half-pregnant".

If we want a genuine Capital Markets Union — not as a slogan but as a functioning reality — we must complete the integration of our infrastructures, and ultimately create a single CSD platform for Europe. This requires political leadership.

## Technology and the future of money

A major technological shift is accelerating these pressures: tokenization. Tokenization promises efficiency, transparency and programmability. But it is not a magic wand. It will not solve fragmentation on its own. Tokenized markets require robust, integrated and resilient infrastructures.

And tokenisation raises a fundamental question: On what money will tokenized markets settle? The United States is moving toward a model dominated by stablecoins — in practice, a partial privatization of money issuance. Europe must choose a different path. This is why working on a European wholesale CBDC is essential.

A wholesale digital euro will be critical if Europe wants to:

- support tokenized financial markets
- avoid dependence on foreign private providers
- and maintain monetary sovereignty in a digital age, where money remains a common good that must be issued and managed centrally, neutrally, for the benefit of all citizens.

## What must change: Four strategic imperatives

1. Allow the emergence of European champions — including by adapting competition policy. We cannot pretend to build a unified capital market while treating every potential consolidation as a threat. Scale is not the problem — it is the precondition for sovereignty.
2. Accelerate the issuance of a wholesale central bank digital currency. It is indispensable for supporting tokenized markets while preserving public trust and monetary control.
3. Relaunch and lead the consolidation of CSDs. This must be driven by European authorities. Brussels and Frankfurt must set the direction and provide political cover to overcome national resistance. And consolidation does not require a single legal entity on day one — but a single operational platform with harmonized processes.
4. Sustain and accelerate the ECB's work on a pan-European payments solution. Europe's dependence on non-European payment schemes is a major vulnerability. A true pan-European payments solution is essential to reinforce Europe's financial autonomy.

## The role of Member States: Transferring sovereignty where it matters

Two areas require genuine political courage:

- ▀ Supervision. A single market needs a single supervisor for its critical infrastructures. This is not revolutionary – it is rational.
- ▀ A true European common bond market. The US has Treasuries – a huge, unified market backed by a single efficient FMI. Europe has 27 government curves. At a moment when global investors seek diversification, a jointly issued European safe asset – available at scale – would deepen our capital markets, strengthen financial stability and enhance Europe’s global attractiveness.

## Conclusion: Keep the course, and accelerate

Let me conclude with a simple message. Europe is not starting from scratch. We have world-class infrastructures, exceptional expertise and regulators who often set global standards. But our window of opportunity is narrowing.

If Europe wants to remain a global financial power, it must keep the course – and accelerate.

Accelerate the integration of its infrastructures.

Accelerate in enabling European champions.

Accelerate the delivery of a digital euro.

Accelerate in providing a true European safe asset.

Accelerate in treating market infrastructures not as technical utilities but as strategic assets.

The world is moving fast. Europe cannot afford to move slowly.

# Thoughts about EU's Economic Security

**Denis Redonnet**

There is a shift underway because the environment around us is changing fast. I will also say a few words about the management of immediate risks that have materialized over the last few months, notably the vast expansion of Chinese export controls across a range of materials. This has been a very important moment and will crystallize further developments.

Finally, more specifically for the EU, I will share a few thoughts on how we continue to try to get the governance of all this right in a new context, which is more difficult at the EU level than elsewhere.

## How EU economic security thinking has evolved

We are increasingly moving away from a vision of economic security priorities that was very defensive, focused on industrial chain resilience, vulnerabilities, and deep assessments thereof, which intensified around the time of COVID, toward a framework that is much more concerned with the risk of weaponization.

As a result, we are shifting from a resilience-centered, defensive approach toward more statecraft-oriented concepts. For example, how do we ensure technological edge, leadership, or even indispensability, including in Europe, in areas where we hold critical technologies?

This implies a rebalancing of the overall approach to economic security, shifting away from an exclusive focus on protection toward a growing importance of the promote pillar. The promote pillar is more complicated because it brings in industrial and technological policy settings, which remain incipient and are difficult to implement at the EU level. But it is becoming clearer across the policymaking community, within the Commission, among member states, and across governments, that we must put more resources and effort into the promote pillar, rather than trying to solve everything through protection tools simply because some of those tools are federalized at the EU level.

The third P also matters, namely, partnership. I will come back to this in a moment.

## The Commission's near-term policy orientation

Without speculating about forthcoming political decisions, let me describe some orientations that are likely to appear in an upcoming policy piece, sometimes referred to as a “Doctrine”, essentially a Brussels-style communication on the strategic use of economic security instruments. It is very instrument-oriented, similar to a white paper. It will not yet include detailed legal proposals, but it should highlight issues that were not central to the 2023 economic security strategy.

One key point is that we must be able to leverage the strength of the internal market much more affirmatively than we have done so far. We have always leveraged the internal market for sustainability purposes, through the so-called Brussels effect, sometimes even overusing it. The question now is how to leverage the single market and the Brussels effect for economic security and infrastructural security.

Vis-à-vis China, this raises the question of whether we move beyond the current approach, which progressively restricts China's access to the internal market through tailored, investigation-based deployment of level-playing-field and trade defence instruments, toward something more wholesale. I cannot say how far policy will go in that direction or through which instruments, but the direction of travel is to leverage our strengths, including the ability to weaponize reverse dependencies when necessary.

Within the civil service, a significant amount of work is underway to identify reverse dependencies vis-à-vis China and vis-à-vis the US. In the context of the crisis surrounding Chinese export controls, the political leadership of the Commission has received submissions from the civil service listing possible countermeasures and the legal bases that could be actionable if conditions were met. At present, those conditions are not met because there is some stabilization. But the future remains uncertain.

Reducing dependencies vis-à-vis the US is also being actively examined as part of economic security due diligence. This work does not necessarily need to be publicized, but it is being carried out.

## Costs, trade-offs, and repurposing the toolbox

A second issue that needs to be discussed more openly in Europe is the question of the costs and trade-offs associated with resilience policies. This issue has not yet been fully socialized within governments, or between the Commission and member states, because it is complicated in a non-unitary setting. Who bears the cost of inefficiencies linked to de-risking parts of our

economic integration? It does not come for free. The key question is how these costs are allocated and who bears them.

A third issue concerns whether existing tools, such as competition statutes and trade defence instruments, need to be repurposed toward economic security objectives. These instruments were not designed with economic security or resilience in mind, but in practice, they play a role in the ability to de-risk. Repurposing them has become central to the discussion.

## Partnerships

On partnerships, we see a clear need to intensify economic security cooperation with like-minded countries facing similar challenges. Cooperation with Japan, for example, has never been as intense as it is today, largely because of the significant commonality of interests.

We will also need to assess whether stabilizing the transatlantic relationship allows for deeper cooperation with the US on economic security. At this stage, this remains unclear, as the transatlantic trade situation is not stabilized.

Beyond that, there is the question of partnerships, particularly on critical raw materials and rare earths, with emerging economies. In those areas, our agenda remains one of more economic integration, not less. These chosen partnerships are a priority and a core component of an economic security strategy. The difficulty lies in pursuing them while managing the real-time materialization of economic security risks.

## The immediate shock of China's export controls

Since the spring, the expansion of Chinese export controls across a broad range of upstream materials feeding into key industrial value chains has been a major problem. It came close to materializing in a highly disruptive way.

We have a clear view of what this policy represents. It is not simply retaliation or the ad hoc weaponization of dependencies. As it has been rolled out over the last two years, the Chinese export control policy is establishing a managed trade regime across a vast zone of sourcing and inputs. Its purpose, as we interpret it, is to consolidate existing dependencies and pursue downstream industrial dominance. This is therefore a systemic strategy and requires a systemic response.

The immediate response, given the very high level of dependency, particularly on rare earths and first-stage transformation, has necessarily involved engagement with China to facilitate and accommodate implementation. A triangular dynamic has been unfolding between the EU,

the US, and China. The adjustments made by China have been applied on an *erga omnes* basis. Claims that the US is receiving uniquely better treatment are, in my view, inaccurate.

We are currently discussing a shift from individual licensing, notably around the rare earth measures of April and earlier measures on critical raw materials in 2024, toward a system of general licensing. The devil lies in the details. China appears to want to apply general licensing even to materials that do not correspond to the logic of dual-use export controls, and to design this system in a way that imposes quantitative limitations. This is precisely how stockpiling is prevented and managed trade is created.

In addition, until the October measures were suspended, China intended to base this system on a statute providing extraterritorial reach, inspired by US policy. This has been temporarily suspended, but from the European perspective, nothing has been resolved. It is, as cyclists would say, a false flat. Decisions will have to be made beyond mitigation.

In principle, there are three levels of possible pushback. The first is normative pushback, through G7 pressure and political denunciation of what we see as predatory industrial policy. The second is a legal challenge, including the question of whether to bring the issue to the WTO, and whether even a successful case would force course correction on something this systemic. The third, if tensions increase, would be countermeasures.

All of this is likely to resurface in the coming months, given the depth of the phenomenon.

## **Reducing dependencies and the EU governance challenge**

Another major priority for us is reducing dependencies. A set of measures will be announced next week as part of an economic security package under what President von der Leyen has called a Resource EU initiative, inspired by RepowerEU. The objective is to intensify and accelerate frameworks already in place, notably those stemming from the Critical Raw Materials Act adopted two years ago.

On governance, the challenge remains significant because the EU is not a unitary state. This creates issues of unity of purpose and requires faster convergence among member states in their perception of threats. It also requires intensified joint risk assessments, which are at the core of the 2023 economic security strategy.

Execution and uniform application are also challenging. In practice, proper execution often requires EU-level tools and some degree of delegation of competence. This will likely remain necessary in emerging technologies, particularly with respect to strategic trade controls and investment controls.

We have a first-generation EU framework for screening foreign investment and coordinating dual-use export controls. We have sought to exploit the full potential of these frameworks, for example, by adopting EU controls through delegated acts to avoid fragmentation.

We are revising and strengthening statutes, notably on inward investment control. Outward investment control will likely be examined more intensively from next year, at least initially, through monitoring rather than a full control regime.

None of this resolves the need for a different way of working with member states and with the private sector. The main lesson of the last two years is that we lack the ability to interact with industry at the level of granularity required to make risk assessments truly actionable, particularly in advanced AI, advanced semiconductors, quantum, and biotech.

This raises difficult questions about our relationship with industry. How do we co-construct these assessments? Through cooperative mechanisms, trusted advisory groups with security clearances, or mandatory reporting requirements? My view is increasingly that we will need to move in that direction. Nothing is decided at this stage, but the need to act faster and at greater depth than we have over the last two years is clearly there.

# Chosen Rivalries, Chosen Partnerships: Industrial Policy and the New Geoeconomics

**Mathilde Lemoine**

Over the past years, my work has focused on a central transformation of the global economy: the return of sovereignty as a structuring force in markets, investment and power relations. Industrial policy, long perceived as a secondary or defensive instrument, has re-emerged as a core component of economic strategy, reshaping not only trade flows but also technological trajectories and geopolitical balances.

In recent publications, I have shown that sovereignty-driven policies are no longer marginal. According to my calculations, after aggregating across major economies, they represent around 5.3% of global GDP, making them a macroeconomic force comparable to traditional drivers of global growth. This shift marks the emergence of what I describe as a new geoeconomics, in which capital allocation, technological development and international relations are organized according to strategic priorities rather than purely economic efficiency or competitiveness.

This new configuration is often described as fragmentation or de-globalisation. My analysis suggests a different interpretation. What we are witnessing is not the collapse of interdependence, but its re-hierarchisation. States are not withdrawing from global markets; they are redefining the terms of their engagement. Dependencies are no longer accepted by default. They are selected, managed, and, in some cases, deliberately constrained.

The logic gives rise to chosen rivalries in sectors where technological capacity determines power and chosen partnerships in areas where cooperation remains indispensable. It also explains why industrial policy has become inseparable from geopolitical competition, particularly in the context of the US-China rivalry, and why technology is now systematically interpreted through strategic and security lenses.

Against this backdrop, the objective of my speech is to clarify how industrial policy, technological competition and geopolitical rivalry interact to reshape world markets and international hierarchies. The argument

developed here rests on three key dynamics that together define the new geoeconomic landscape. First, the transformation of industrial policy into a vector of power. Second, the way the US–China rivalry structures sovereignty strategies and technological trajectories. Third, the emergence of a world of chosen rivalries and chosen partnerships rather than fragmentation, and what it implies for interdependence and adaptation.

These new partnerships shape the way firms and emerging economies adapt. Industrial policy has become primarily a tool of power rather than a tool of competitiveness. It is no longer focused on supporting competitiveness, but on organizing power through the allocation of capital.

This is not a theoretical argument. At this stage, according to our calculations, the amounts committed worldwide to implement these sovereignty policies (energy, food, digital, media, etc.) are impressive. An overview of sovereignty policies around the world shows the scale of the investment currently being made by most countries to reduce their food dependency (increased domestic fertilizer production in the United States, food reserves and increased subsidies for farmers in China, improved self-sufficiency in Japan and Korea, etc.), diversify their suppliers of rare earths and materials, and improve digital, energy, industrial, and media infrastructure. Beyond the military sphere, governments are mobilizing the private sector as an instrument of sovereignty. A non-exhaustive survey of the measures implemented, excluding military spending, shows a cumulative effort equivalent to 5.3 percent of current global GDP, or nearly six trillion dollars worldwide. The pleasant surprise of this survey is that the European Union is not lagging behind. Of course, the programs are spread over several years, and caution is needed, as these calculations are based on government announcements.

Sovereignty has become a driver of global investment and a new source of growth. Global growth should therefore be sustained over the next few years by these new policies, which consist not only of restrictions on trade flows but also of the creation of a new productive order.

Their effects are threefold. First, they redirect investment flows toward strategic domains such as energy systems, critical minerals, semiconductors, and the food industry. Second, sovereignty policies alter the structure of global trade rather than reducing it. Third, they increase the role of public decision-making in capital allocation, thereby modifying market pricing mechanisms. This evolution is particularly significant for the private sector and must be taken into account.

As a result, global growth decelerates only modestly in 2025 against expectations. Part of the negative impact of tariffs on consumption and trade is offset by sovereignty-related investments, which have become a macroeconomic driver.

Technological change is increasingly guided by strategic priorities rather than efficiency considerations. States have become the main architects of technological trajectories. Technology plays a central role in reinforcing the dependency of Asian economies on China. The process of disseminating innovation has been “redesigned” rather than halted, thanks to the reconfiguration of dependencies.

The second point concerns the way the US–China rivalry structures sovereignty, investment, and technological hierarchies. The central geopolitical fact is that China has become the world’s leading industrial power, while the United States is responding through industrial policy aimed at preserving technological primacy.

This rivalry underpins a geopolitical reading of technology. The issue is not limited to specific sectors such as semiconductors or nuclear governance, but relates more broadly to capacity and autonomy. The United States restricts access to key inputs and channels capital toward domestic ecosystems. China expands upstream dominance in order to become indispensable. Europe emerges as a space in which standards, technologies, and capital are increasingly contested.

One consequence is a slowdown in technological diffusion, as core components of the digital and energy transitions are transformed into instruments of power. Parallel technological corridors are emerging, characterized by differentiated standards, data regimes, and security constraints.

Adaptation patterns are visible at the macro level. States construct protective frameworks and redirect investment flows. Firms adjust by managing regulatory risk, segmenting supply chains, and operating under dual compliance systems. Both states and firms operate within the constraints imposed by the US–China rivalry, focusing on securing access to inputs and avoiding activity in prohibited technological spaces.

The third point concerns the emergence of a world of chosen rivalries and chosen partnerships. Contemporary sovereignty is interdependent. Nations are redrawing their map of dependencies by selecting them rather than eliminating them. This is a new form of sovereignty, that of “useful vulnerabilities,” based on selective control of flows.

This sovereignty is already having visible consequences on the world order. First, the desire to reduce dependence between China and the United States is giving rise to new centers of integration (corridors, blocs, and regional hubs). The slowdown in global trade masks the growth in trade between “neutral” corridors (India-Gulf-Europe, ASEAN-Africa, Brazil-ASEAN). Trade between major emerging countries (BRICS+) is also

increasing significantly, while foreign direct investment is being redirected in line with new accepted vulnerabilities.

This is not a world of fragmentation, but one in which interdependence is recognized and organized hierarchically. This dynamic can be described as the rise of chosen rivalries and chosen partnerships.

Chosen rivalries concern domains in which capacity directly determines power, including artificial intelligence, defense, advanced technologies, and critical infrastructure. Chosen partnerships apply to domains where cooperation remains strategically necessary, such as climate policy, energy corridors, and access to strategic minerals.

This framework helps explain how emerging economies are adapting. They leverage great-power rivalries to secure financing, technology transfer, and access to markets. Their growth strategies depend on selecting which dependencies are acceptable, operating within a logic that can be described as chosen vulnerability.

In conclusion, industrial policy is no longer primarily a tool to enhance competitiveness. It has become a state-driven instrument for organizing power, shaping technological hierarchies and reallocating capital according to strategic priorities. In this new geoeconomic environment, markets no longer operate independently from political objectives; they are increasingly structured by them. As the scale of sovereignty-driven industrial policies continues to expand, the question of financing could rapidly move to the forefront. The challenge is not simply to design ambitious industrial strategies, but to sustain them over time. Here, inequalities between states should become increasingly visible. Not all countries have the same fiscal space, financial depth or institutional capacity to support long-term investment in strategic sectors. In this context, States with access to deep capital markets, strong public balance sheets and credible frameworks should be able to anchor investment and shape technological trajectories. Others could face binding constraints, forcing difficult trade-offs between ambition, credibility and execution.

This dynamic has direct implications for firms. As industrial policy becomes more state-driven and more selective, companies should be confronted with increasingly differentiated strategic environments. Their future performance will not only depend on competitiveness, but on their capacity to absorb strategic constraints, to align investment decisions with sovereignty priorities, and to operate across unequal financing conditions. In this new geoeconomic order, corporate power and profitability will reflect the ability to navigate these asymmetries rather than to optimize global value chains alone.

Ultimately, the emerging hierarchy of interdependence will be shaped less by trade openness than by financing capacity. Industrial policy, technology and geopolitical competition converge on a central issue: who can afford sovereignty, for how long, and at what economic cost.

# Export Controls in a Transactional Era

I come from a national security and technology transfer background, which in the United States has historically been kept separate from economic and geopolitical considerations. Government institutions traditionally avoided trade negotiations, economic strategy, and industrial policy. The prevailing assumption was that markets would self-correct and that any restrictions on trade should be narrowly tailored to clearly defined national security objectives.

As noted previously, there was significant confusion around the Biden administration's policy of regulating and prohibiting inputs needed for China's indigenous production of advanced-node semiconductors. This included semiconductor manufacturing equipment and advanced computing capabilities used in artificial intelligence, such as high-end chips and supercomputers. Although the Biden administration framed these measures as national security policy, they were widely perceived as part of a broader economic strategy intended to advantage US industry. That perception was not consistent with the intent of the policy.

These measures reflected a broader assessment of national security risks related to China. Advanced semiconductor and computing capabilities were treated as emerging or enabling technologies underpinning a wide range of downstream applications. The core rationale was to deny China inputs deemed critical to the development of advanced AI-enabled capabilities, including algorithms that could improve the speed and effectiveness of weapons systems. Despite this, the measures continued to be interpreted primarily through an economic lens rather than as national security instruments.

That policy architecture has now been hollowed out. The personnel who developed and understood this approach are no longer in place. The current administration lacks internal expertise on artificial intelligence, semiconductor manufacturing equipment, and related domains. Career staff with relevant experience, at senior and junior levels, have been removed. The interagency process has largely ceased to function, the National Security Council no longer plays an effective coordinating role on these issues, and regular policy meetings are no longer taking place.

In its place, a decisional system has emerged that is highly centralized and transactional. Decisions are made top-down, often by the Secretary of Commerce or the president, on a case-by-case basis and frequently in

connection with unrelated negotiations or objectives. The operative goals are to demonstrate deal-making capacity, to use inherited regulatory leverage to induce US and non-US firms to invest in the United States, and to generate outcomes that can be presented as benefiting the US Treasury.

To date, there has been no sustained discussion, over roughly nine months, of the national security risks or benefits associated with artificial intelligence or advanced semiconductors.

By contrast, the Biden administration, regardless of agreement with its conclusions, operated with a coherent theory. It held that frontier AI models should be restricted to a small group of countries, on the view that enabling advanced AI capabilities beyond that circle could lead to catastrophic outcomes. In that framework, advanced AI was treated as a strategic technology of exceptional destructive potential.

The current administration does not operate within that framework. The emphasis is on using regulatory leverage to extract economic gains.

A key structural change in the US approach to economic and national security has been China's assertion of escalation dominance, particularly through its ability to regulate rare earth exports to the United States. The threat of cutting off supplies of germanium, gallium, magnets, and other critical materials created acute vulnerability for the US auto industry and other sectors.

Twice this year, the administration adopted measures consistent with a more traditional, hawkish, decoupling-oriented approach. In June, it imposed controls on electronic design automation software, aviation components, ethane, and other items considered choke points for China. In September, it significantly expanded the list of restricted Chinese entities from roughly 1,300 to more than 20,000 through the affiliates rule, extending controls to entities owned or controlled by listed firms. These measures had significant effects on China's semiconductor and AI industries.

In both cases, China responded by threatening to cut off rare earth supplies to the United States. The message was explicit: without these inputs, key US industries would be unable to function. In both instances, for the first time in the history of US export controls, national security judgments were revised in response to supply-cutoff threats. This has left policy effectively frozen and outcomes uncertain.

Formally, existing rules indicate that controls could be reimposed one year from November. Some parts of the US government appear to anticipate a scenario in which China violates current arrangements, creating grounds to reimpose restrictions. In practice, however, policy remains locked in a transactional limbo, without a coherent national security vision, and constrained by China's leverage over rare earths.

This produces a highly uncertain and chaotic environment. For firms, uncertainty is extreme. Companies are avoiding joint ventures and mergers and acquisitions, and are instead quietly planning offshore development and production in order to manufacture outside the United States and reduce exposure to shifting rules.

The result is a deep and destabilizing level of uncertainty across the ecosystem.

# From Subsidies to Supply-Chain Resilience

**Marion Jansen**

My intervention adopts a more optimistic perspective. It is also useful to recall where a major challenge to the multilateral trading system seemed to lie two years ago. At that time, the most significant concern was the growing portfolio of supply-chain-related rules, including the EU Deforestation Regulation. This raised difficult issues for the multilateral trading system because it entered a domain the WTO has struggled to address, namely, non-product-related process and production measures. It also risked creating a parallel dispute settlement path, since litigation over the implementation of relevant EU measures would take place in national courts within the European Union.

Turning to the current context, my intervention is framed using a sentence from the OECD Ministerial Declaration of 2024: OECD members committed to "responding to comprehensive strategies that use non-market policies and practices that distort a global level playing field as well as other practices that create strategic dependencies and systemic vulnerabilities, which can then be exploited through economic coercion."

The argument I would like to make is that within the multilateral trading system, responses to non-market policies and practices have traditionally focused on eliminating those policies and practices with a view to re-establishing a level playing field. An alternative would be to focus on addressing the consequences of those policies, namely strategic dependencies and systemic vulnerabilities. This approach has the characteristic of circumventing the need to establish the existence of non-market policies and practices, like market-distorting subsidies. In the current context, there may be potential to establish collaboration around such an approach among subsets of countries, but there is also a potential pathway to multilateralize such cooperation over time.

To develop this argument, let's have a deeper look at recent experiences with the existing approach under the framework of the multilateral trading system. OECD work provides evidence of China having pursued a systematic strategy to build specific industries and accumulate market power. In principle, the multilateral system has an instrument to address this, namely the Agreement on Subsidies and Countervailing

Measures (ASCM), with agriculture treated separately. The logic is to discipline subsidies, but it requires identifying the subsidy and demonstrating harm.

In practice, the ASCM has not delivered outcomes that key members consider satisfactory. There is a widespread perception that disputes concerning Chinese subsidies have too often been lost at the WTO. Dissatisfaction with subsidy case outcomes is commonly cited as one driver of the Appellate Body crisis. Subsidies have therefore been central both to concerns about the global level playing field and to the weakening of the WTO's enforcement capacity. Reform of subsidy disciplines is therefore likely to be a core element of any WTO reform agenda.

The feasibility of progress on subsidy disciplines, however, has diminished. Until recently, OECD work on subsidies was oriented toward producing technical inputs that could support ASCM reform discussions. This included building a firm-level database to measure subsidies relative to firm revenue, providing a direct indicator of distortion. Over the past two decades, firms in China have received, on average, between two and four times, and in some cases four to eight times, the subsidies received by non-Chinese firms in the dataset. The largest discrepancies appeared in sectors such as solar panels, where China now holds around 80 percent of the global market. Highly subsidized sectors overlap with those at the center of current global tensions, including steel, wind turbines, shipbuilding, electric vehicles, and semiconductors. In parallel, plurilateral work was developed at the OECD that could, in principle, inform WTO discussions, including guidelines on state-owned enterprises and recommendations on competitive neutrality.

The political context shifted, however, and subsidy negotiations at the multilateral level have become considerably more difficult. In Abu Dhabi, some members still sought to place industrial policy on the agenda, but in the absence of consensus, the issue did not feature in the ministerial declaration. Overall, the outlook for near-term subsidy renegotiation is weak, including because the number of actors using subsidies has increased, while not all countries have the fiscal capacity to follow suit. The alternative approach would entail a shift in the policy starting point. Rather than focusing on the cause of the problem, such as subsidies used by a specific actor, policy increasingly begins from the observable market outcome. The starting point becomes market power, concentration, vulnerability, and dependency. The stated objective would be to reduce strategic dependencies and systemic vulnerabilities, potentially regardless of the origin of the distortion. This is a different logic, and a growing number of initiatives appear to reflect this logic.

A striking feature is that many of these initiatives are sector-specific rather than generic. One partial exception is work under Japan's G7 presidency on Principles for Resilient and Reliable Supply Chains. Beyond

that, most initiatives are organized by sector and differ in form. This stands in contrast with the first approach discussed in my intervention, which is largely generic rather than sector-specific. There are only limited multilateral sectoral agreements, such as the WTO Agreement on Trade in Civil Aircraft.

Examples of new sector-specific initiatives include the G7 Critical Minerals Action Plans, which aim to coordinate investment and reduce uncoordinated spending that could lead to over-investment and inefficient use of public funds. Another example is the emergence of a new language in free trade agreements. The Japan–Australia agreement includes specific subsections on essential food and on energy and mineral resources, coupled with cooperation mechanisms intended to preserve access during crises.

Domestic policies also increasingly reference global market structure. The EU Critical Raw Materials Act, for instance, includes targets for domestic production shares of critical raw materials, with the remainder sourced internationally. This reflects new tools that are explicitly sectoral and oriented toward reducing vulnerability.

Finally, there are collaboration mechanisms that do not yet establish binding rules but create shared transparency and coordination. Examples include the Agricultural Market Information System (AMIS) and the OECD MEDICON network (focusing on the pharmaceutical industry), which aim to share data and improve visibility of stocks and inputs, reducing panic dynamics and enabling effective sourcing during crises. Another example is the G20 Global Forum on Steel Excess Capacity, facilitated by the OECD, which takes excess capacity as the starting point rather than subsidy attribution.

The broader conclusion is that a new form of cooperation is emerging, often plurilateral, and organized around observable market risks rather than attribution of policy behavior. The focus is on over-concentration, vulnerability, and dependency. This approach may offer a pathway to avoid spirals of tariff escalation, subsidy races, and uncontrolled retaliation. Importantly, there is already an institutional anchor that could allow these initiatives to be brought back into the multilateral system over time. The MC13 ministerial statement from Abu Dhabi referred to supply chain resilience as an objective. This may signal the emergence of a new approach to rule design, with the long-term aim of embedding resilience and limiting excessive dependencies within a revitalized multilateral framework.

# The World Trading System under Dual Pressure

**Sébastien Jean**

The most immediate challenge to the multilateral trading system today comes from the United States. Recent developments amount to a unilateral increase in protection and a series of threats, with no serious retaliation except from China. This matters because the multilateral trading system has always rested on common adherence to a set of principles and on the credibility of enforcement. Its equilibrium condition is a shared belief that commitments will be respected. Compliance is sustained because each participant expects others to comply. That cornerstone has been destabilized.

Against this background, one may wonder whether it is possible and desirable to move forward by countering this trend, somehow “against” the United States. From a European perspective, the answer is negative, given dependencies in security, finance, and digital services and infrastructure. As Adam Smith put it, defence is of more importance than opulence. Reducing these dependencies is necessary, but they will not disappear in the short or medium term.

A second question is whether the world trading system can function without the United States. In principle, a coalition of willing partners could attempt to move forward. The United States might also become less central as a market if it retreats from the world trading system, although limited manufacturing capacity suggests it will remain a key market in the short and medium term. More consequential is the likelihood that the United States will seek to constrain its partners’ policies toward China. The US–UK bilateral deal announcement in May referred to strengthening cooperation on economic security, including excluding Chinese providers and coordinating to address non-market policies of third countries. The EU–US joint statement, as reflected in Commission communication, referred to strengthening economic security alignment, supply chain resilience, and innovation through complementary actions addressing non-market policies of third parties. If these formulations are translated into concrete operational requirements, they are likely to become a source of tension between the EU and the United States.

Other recent developments point in a similar direction. Mexico's September 11 announcement of higher MFN tariffs on a large set of products does not name China, but is widely understood as targeting Chinese competition. There is also increasing discussion of ownership-related requirements in US agreements, which would further constrain partners' policies toward third countries, primarily China. In practice, therefore, any attempt to build forward without the United States would remain heavily constrained by US leverage.

The more fundamental issue, however, is whether the multilateral trading system can function without the United States while incorporating China in its current form. The scale of China's challenge must be taken seriously. China's surplus in goods, including manufacturing, has increased sharply since COVID. The manufacturing surplus alone is projected to exceed two trillion US dollars this year, representing more than 11 percent of global manufacturing exports. This magnitude is historically exceptional.

The issue is not that industrial policy would be unprecedented in the trading system. Non-market economies have long participated in the WTO. The challenge is quantitative, driven by the size of the economy and the scale of the distortions. The multilateral trading system was built on the premise of a liberal understanding made explicit in the Havana Charter, which was never ratified. The GATT contains only a loose, non-binding reference to that premise, with Article XXIX stating that "The contracting parties undertake to observe to the fullest extent of their executive authority the general principles of Chapters I to VI inclusive and of Chapter IX of the Havana Charter".

The key analytical question is therefore the link between China's large surpluses and its policies. The connection is strongly suggested by official statements and by the scale of intervention. IMF assessments place industrial policy support around 4.4 percent of GDP in a sector accounting for roughly a quarter of domestic value added. Exchange rate non-adjustment also plays a role. This is not an allegation of manipulation, but an observation that adjustment has not occurred.

To assess consequences in a simple way, products can be grouped by the intensity of industrial policy intervention, measured as the number of policy measures per unit of exports. For a research project in progress, forthcoming in a few months, I performed such assessments based on the monitoring efforts of industrial policy measures carried out by Global Trade Alerts, combined with Chinese customs data on foreign trade. Even acknowledging the noise and imperfections of the underlying data, a clear pattern emerges: categories subject to higher policy intensity display larger increases in China's net exports since the period around 2017–2020. In the

surge of China's export surplus observed since 2020, policies do seem to have made a significant difference.

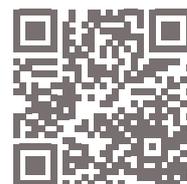
This raises the question of the materiality of impacts on partners. Extending the same assessment to European net exports also uncovers a rather clear pattern: EU net exports declined most in products where China's policy interventions were most intense. China's gains have been associated with European losses in trade, and those losses correlate with the intensity of policy intervention. The magnitude is significant in terms of changes in commercial positions and shares in global markets. Differences in outcomes across sectors, conditioned by the level of Chinese policy intervention, have been visible for several years.

The question then becomes what Europe, and third countries more generally, can do. Many countries are not willing to pick sides. The "new Cold War" framing is unconvincing. Most governments seek to avoid alignment choices. At the same time, they must contend with a disruption of common beliefs, a weaker value of commitments, and a weakened multilateral trading system, given the challenges described above.

The central issue is whether a basis for cooperation can still be sustained. The initial WTO objective of limiting terms-of-trade manipulation remains relevant. However, economic security has become more central. Governments now prioritize vulnerability reduction, autonomy, and uncertainty management. If cooperation is to move forward, it will need to be organized around an insurance logic that reflects these priorities.

From that insurance logic follows a focus on enhancing supply chain resilience and, more broadly, on building open groups of trusted partners willing to sustain reciprocal commitments to stick to rules-based exchanges. In the current context, this is unlikely to be achieved through the WTO. A plausible route is to build political momentum among trusted partners outside the WTO framework, precisely because the necessary cooperation is no longer fully multilateral.

There is an appetite for new forms of cooperation organized around economic security. Domestic adjustment and investment efforts remain necessary, including in Europe. But a path forward exists, and political momentum can be built in that direction.



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