The Decoupling of global economy and its implications for Mexico

Susana Muñoz, Partner Chinese Desk.

The discourse about the trade war between China and the United States has intensified in recent months not only as an electoral strategy but rather it has extended also into other fronts damaging the bilateral relationship. This means that the decoupling of the global economy is likely to continue during the run-up to the elections in the United States; moreover, it may even accelerate once the winner is announced in November 2020.

The Trump administration has adopted a series of measures to stop the expansion of China, for instance, export prohibitions on a wide variety of sensitive products, tariffs, forced relocation of North American companies, and even threatening to withdraw from the WTO. More recently, the closure of the Chinese consulate in Houston was announced alleging intellectual property violations and espionage. In retaliation, the Chinese government ordered to close the American consulate in the city of Chengdu, measures that clearly raise the level of the conflict.

However, it is relevant to take into account the complexity to untangle the two largest economies in the world. On the one hand, the restructuring the world economy will have major implications from the destruction of business models to the reconstruction of entire industries. On the other hand, there are geopolitical consequences that are already being drawn on the map.

In this regard, Beijing has made significant efforts to strengthen and consolidate economic ties with emerging markets. Just last week, Foreign Minister Wang Yi held meetings with senior officials in Vietnam, while the conclusion of the negotiations of the Cambodia-China FTA negotiations was announced. In response to the crisis caused by the COVID-19 pandemic, it was also announced an important economic aid package for Latin America, which is one of many other ways China is offering support to emerging countries to combat the virus.

On the technological side, despite the fact that several countries have excluded or banned Huawei and other Chinese applications from their telecommunications system, the expansion of information giants, such as Alibaba and Tencent, in different commercial formats has not been stopped. Furthermore, the country continues to promote the local development of 5G and semiconductors, as well as technological infrastructure, to reduce its dependence on other countries.

What do these changes in the geopolitical paradigm mean for Mexican companies? What are the risks to consider?

Regardless of the current internal discussions of the WTO, Mexican companies can continue to depend on the rules and preferential access that Mexico enjoys under its free trade and investment agreements with more than 50 countries. This allows Mexican companies to continue expanding their operation across borders under clear rules.

However, this scenario of trade tensions between China and the United States may have a short and medium-term impact on Mexico's promotion strategy as an investment destination for the manufacturing sector that seeks to export to the North American markets.

Although it is true that Chinese companies will continue to develop new markets for their products and technologies, it is also clear that there is opposition to US policies within China. This situation is not exclusive to mainland China, but it has also spread to the Hong Kong Special Administrative Region, which has been damaged by recent announcements by the Trump administration.

This week the Global Times newspaper shared the results of a quick online poll asking readers which American consulate would most likely close. 80% of the responses supported the closure of the United States consulate in Hong Kong. Said result reflects a clear anti-American feeling as a result of the US government's interference in China's internal affairs.

In this context of political and commercial tensions, it is evident that our closeness and preferential access to the North American market are not enough arguments for Chinese companies to invest in Mexico. By contrast, it is very necessary to update our approach strategy towards Chinese companies and investors, not only positioning the benefits of the USMCA, but also doing an in-depth job of identifying complementation opportunities in commercial, industrial, technological, and investment projects.

On the other hand, it is essential to offer guarantees for Chinese investments in sectors of interest such as mining, energy, infrastructure, and manufacturing; as well as incentives in sectors where there is still very little Chinese presence.

As the US elections approach, the candidates' speech will intensify and so will the tensions rise between China and the United States and, in consequence, retaliatory measures between both economies. If Mexico, therefore, does not update its strategy and approach with a new speech, such as highlighting our economic openness, commitment to free trade, supply chain integration, privileged geographical location, and legal certainty for investors, our country runs the risk of disappearing from the Chinese map as an attractive investment destination under this scenario.