Globalization - What's next?

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Preparing for a world in transition

2020 was a year marked by disruption and change as COVID-19 swept across the globe forcing world economies to hit pause, significantly impacting international trade and capital flows. Halfway through 2021, as many countries emerge from lockdown, global business activities are rebounding and the landscape has shifted. But how has it changed? And what should happen next?

Peter Zeihan, geopolitical strategist, speaker and author of bestselling books *The Accidental Superpower*, *The Absent Superpower* and *Disunited Nations*, joined BLG's leadership team and event hosts John Murphy, Prema Thiele and Alan Ross QC for a webinar presentation where he shared his perspective on the future of globalization. This compelling discussion set out a vivid account of how geographic, demographic, and industry trends affect the Canadian economy and broader global system. He also examined critical questions concerning the future of globalization and significant movements in trade, capital flows, immigration, food scarcity and their ongoing impact on Canadian agribusiness, energy, manufacturing, infrastructure and technology, among other areas.

Here are few of the discussion's main takeaways.

American-led international trade: the glue keeping the world together

Zeihan began by discussing how global free trade hinges on the viability of the international alliance ushered in at the end of WWII. While successful for decades, the failures of the alliance are becoming more apparent. Zeihan pointed to the formal breach of international trade rules under the Trump administration, and signalled that Biden did not appear to be in any rush to reassert those rules. Zeihan posits that "without the United States maintaining the global network, trade doesn't work. Countries either need to be part of the American network or need to go it alone." Canada, Mexico, Korea, Japan, and the United Kingdom secured their positions in the U.S.' new trade portfolio as the country prioritized domestic trade policy.

He also argued that, as a result, globalization may well be over. COVID-19 has accelerated this process. The world's new normal will include a rise in economic nationalism among countries with healthy demographic structures and a collapse in global consumption.

Why geopolitics and demography are converging to end the era of globalization and what millennials have to do with it

Unprecedented global depopulation is shrinking consumer demographics, which Zeihan believes will not recover on a global scale in our lifetime. The population structure that supported the international trade system is declining. Global consumption has already peaked, while global production and global investment capital are currently peaking.

When looking at the American demographic structure, the same trends are apparent, with the exception of its millennial population, which is one of the world's most robust. The density of this population segment ensures that the American consumer-led economic model will weather the storm.

In parallel, Mexico possesses a solid consumer-led demographic profile saturated with a youthful, population allowing the country to excel in manufacturing and assembly, which leaves valued added processes and design to America. Additionally, Mexico's consumer base requires a high level of American export. In 2019, it became America's number one trading partner, a position it will not give up in our lifetime.

By contrast, Canada's demographic structure comprises mostly high-value, mature workers in the forty to sixty-five year old range. Since Canada does not have a large enough population, in the twenty to thirty-something bracket, that is needed to increase consumption, the country will need to count on the export of its goods, making Canada an economic competitor to the U.S.

What are some of the global trends and how will they impact Canadian industries?

Agriculture

Modern agricultural patterns result from three distinct factors: low-risk global trade, limitless Asian demand, and unlimited cheap credit. As international trade breaks down, demand declines, ushering in the beginning of a new supply challenge.

Unlike many other countries around the world, Canada has the upper hand given that the country's harvest season does not follow global consumption patterns. Accordingly, agribusiness producers are in a unique position to sell at top dollar anywhere. This allows Canadian agribusiness to become a leading global food producer.

Energy

The United States reduced the break-even cost for shale oil production below $45 a barrel, effectively driving down the price of natural gas, a by-product of those oil projects. Natural gas has displaced oil and coal as the largest source of electricity in the U.S. due to its abundance and low cost, propelling the U.S. into a new industrialization phase capitalizing on natural gas.

This is both a best and the worst-case scenario for Canada. On the one hand, American natural gas is being sold to Québec at prices comparable to Québec hydropower, giving Canada access to another cheap energy resource.

On the downside, of course, energy sales are Canada's single largest export unit, and energy taxes fund a large portion of the federal budget. Additionally, Alberta is subject to new pricing where the floor for American energy is set at $45. All these factors make for a particularly challenging competitive environment.

Manufacturing

To excel in the changing world order, Canada will need to commit more strongly to corporate America and merge efforts in various sectors, notably in aerospace. This will most likely require some tough political decisions as Canada faces increased US competition in this sector. Québec's leading aerospace company, Bombardier, is at the heart of this issue as it is subject to heavy tariffs due to its ties with Airbus's British aerospace company.

Furthermore, Canada will need to produce fundamentally different product streams, and Zeihan's advice is to borrow now while rates are low: "We are running out of road here. If you're going to borrow to retool your industrial plants, now is the time – 2023 may well be too late."

Infrastructure

Zeihan remarked that capital flight into Canada is going to generate a significant source of funding. The Chinese have moved more than $2.5 trillion out of China within the last year. In his view, there is no reason why Canada cannot capture a larger piece of this outflow without it falling entirely into residential real estate. Canada needs to consider creating financial products that will leverage this influx of capital into the country and funnel it to much needed infrastructure development.

Technology

Canada must consider applying technology solutions to address the challenges arising from the disproportionate ratio between young (consumer) and old (retiring) in its population structure. Canada is the fourth fastest aging society globally and the eldercare system will place an enormous drain on resources. The key for Canada is figuring out how to automate that which is not yet automated. Zeihan suggested that Canada should borrow heavily to implement and drive technologies that already exist, such as those explored in Japan for the last 30 years, freeing Canada's future labour force to work on higher-level work.

Peter Zeihan wrapped up the webinar by refocusing the conversation on how businesses can reorient themselves to succeed in the post-pandemic and post-globalization world.

His most significant takeaway: “borrow big and borrow now.” In his view, the borrowing conditions that exist today will not reoccur in the foreseeable future and businesses should do everything in their power to invest in processes and production. Capital availability will become the single most significant limiting factor for the western hemisphere for the next 30 years.

By

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