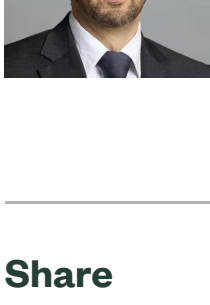


Global Market Outlook

The geopolitical landscape has come through a turbulent year of market-moving elections and continuing conflicts. From technological competition to the heightened threat of military and trade wars, lines are increasingly being drawn between different blocs.




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Elliot Hentov, Ph.D.

Head of Macro Policy Research

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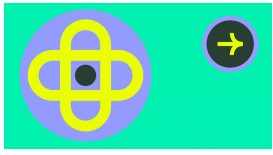
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Geopolitical Outlook 2025

Slow-Moving Fragmentation Continues

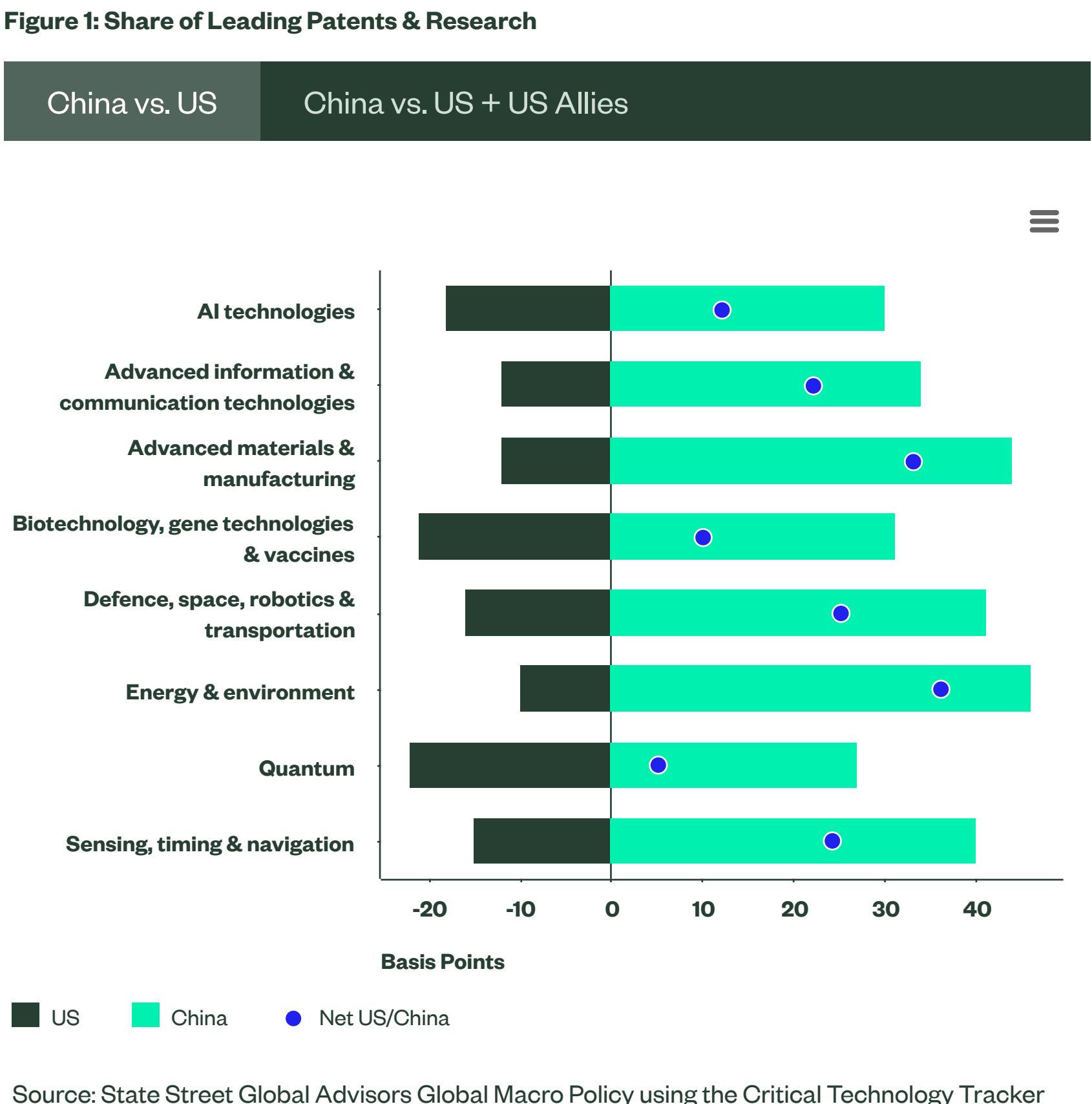
The geopolitical landscape has come through a turbulent year of market-moving elections and continuing conflicts. From technological competition to the heightened threat of military and trade wars, lines are increasingly being drawn between different blocs.



The core theme of global geopolitics remains geoeconomic fragmentation. While the world economy may appear largely unchanged compared to the past few decades, this understates the geopolitical forces that risk rupturing long-standing economic and financial ties. Reflecting the shifting landscape, the twenty-first century is less focused on resource competition; territorial expansion (e.g., World War II); or ideological alignment (e.g., Cold War). Instead, it centers on power dominance, with technological superiority a key factor in enabling the dominant bloc to dictate the global economic and political order.

In this regard, some modern technologies are profoundly different in that they do not represent incremental innovation, but rather a technological leap. They also do not lend themselves easily to diffusion, meaning some technological advantages could become entrenched. We have attempted to quantify the position of different blocs in this technological race using the Critical Technology Tracker developed by the Australian Strategic Policy Institute. This tracker ranks patents and research levels across eight fields, and we have assigned a cumulative quantitative score in each category to compare the relative position of the two main antagonists, US and China.

Figure 1 shows that in a direct bilateral comparison, China is well ahead of the US in all eight fields. However, that picture shifts dramatically when we include US allies from Europe and Asia-Pacific regions in the calculations, with China only remaining ahead in the two domains of renewable energy and advanced materials.



Source: State Street Global Advisors Global Macro Policy using the Critical Technology Tracker of Australian Strategic Policy Institute. Research publications mapped to 100 for US+China, then for US+China+Core US allies (UK, France, Japan, Germany, Italy), thus understating full alliance benefit accruing to Western technology complex.

This overarching competition may be taking place in research laboratories, but it is being fought out in global channels that power the industrial-technological complex. These battles have material implications for financial markets. We consider three main arenas of competition: Real (Military) Wars, Trade Wars, and Fiscal “Wars.” While one or other arena can go quiet for a time, the fundamental drivers of increased friction remain intact and are unlikely to dissipate in 2025.

Real (Military) Wars

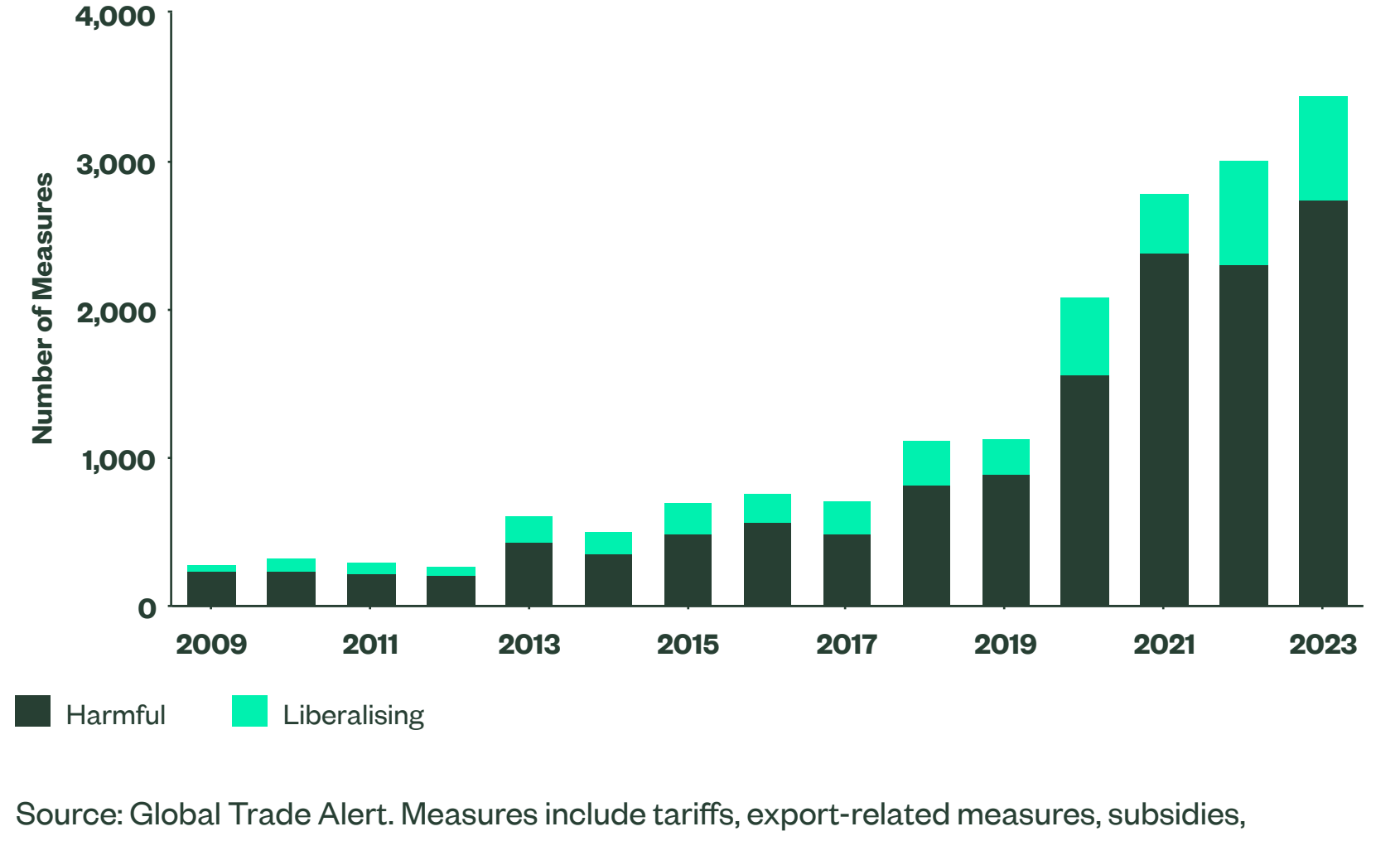
We believe it makes sense for Real Wars, i.e., global conflicts, to be viewed through the lens of geopolitical bloc competition. Within limits, the Cold War is a useful analogy, though today’s military alliances are looser and non-state actors play a more prominent role — the rationale of proxy wars as a tool to weaken the adversarial bloc still holds true. The wars in Ukraine and the Middle East have had a devastating human cost, while also draining bloc resources and eroding political capital. For example, support for Ukraine has involved the emptying of Western arsenals. This means that wars in regions which are geographically remote or seem economically insignificant could still matter for markets, mainly by drawing in major powers or through other spillover effects.

This should imply a broadly higher geopolitical risk premium, though we have thus far only seen it transmit into higher gold prices. And that too has direct linkages to conflict: the freezing of Russia’s central bank reserves and secondary sanctions on non-Russian entities has catalyzed demand for gold among other central banks. Gold has long benefited from its status as a generic geopolitical hedge, but the remarkable price gains in 2024 suggest that much has been priced in and Trump’s re-election poses short-term headwinds. In addition to gold, crisis periods may encourage more episodic capital flows and potential appreciation of classic safe haven currencies, too.

Trade Wars

When it comes to Trade Wars, the challenge is to identify where the cost of fragmentation will reside. As illustrated by Figure 2, trade disruption continues to rise, and it is not simply a function of tariffs. Non-tariff barriers and sectoral interventions are increasingly a factor and create pressure to alter existing trade and capital relations. Trade between the US and China will likely continue to deteriorate, but the speed and magnitude of that will determine who will feel the pain of adjustment (and who might benefit). Higher US tariffs on Chinese imports imply a stronger dollar and a weaker renminbi, but emerging market currencies will not react in a uniform manner.

Among EM countries, we see trade as the greater differentiator. Some countries will retain favorable trading conditions and become more competitive compared to Chinese exporters — Vietnam and Mexico have been beneficiaries of increased trade barriers since 2018. Other countries could attract greater investment from Chinese firms seeking to re-route production to evade tariffs. But the outlook for these countries is not identical given the risk that ‘policy will chase trade’ — Chinese foreign direct investment today becomes a political liability tomorrow as they attract punitive trade sanctions. It has become increasingly clear that what matters most is membership in a trade bloc.



Source: Global Trade Alert. Measures include tariffs, export-related measures, subsidies, contingent trade-protective measures and trade-related investment measures.

Fiscal “Wars”

Lastly, we highlight the use of fiscal policy by governments to achieve their geopolitical aims. The combination of domestic politics and geopolitics implies continued loose fiscal policy across large economies. Reduced trade reliance and greater security risks will require governments to secure supply chains, invest in new technologies, and increase military preparedness. Much of this spending may enjoy a high fiscal multiplier, as defense expenditures tend to be highly localized within blocs, and are manufacturing-intensive and cluster-informing. Higher public capital expenditure is likely to flow into energy and industrial infrastructure. As this spending supports growth, some of the positive impulses could raise real rates as potential growth estimates improve. However, as discussed in our macroeconomic outlook, increased government spending will result in fiscal deficits unless spending in other areas is cut.

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