Adapting Strategies to Evolving Trade Policies and Global Value Chain Dynamics

Research Pulse

Trade policies significantly reshape global value chains, influencing firm strategies. Companies adapt through locational, market, and supplier switching while upgrading production processes to enhance value. Trade restrictions, such as U.S. tariffs on China, affect not only the targeted countries but also global supply chains, raising costs for dependent firms. Tariffs on low-value imports have become a prominent focus on international policy agendas, with governments increasingly targeting these products. Research shows that affected firms have increased R&D investments, often supported by government subsidies, to navigate these challenges.

Reshaping firm strategy is vital in navigating rising protectionism

Trade policies are often a major factor in reshaping Global Value Chains, but firms' strategic choices play a crucial role in structuring value chains to ensure resilience and sustainability (Gary Gereffi, 2021). Companies moderate the impact of trade policies by locational switching and upgrading production profiles:

Locational Switching: Adjusting production sites, target markets, or suppliers to adapt to changing trade landscapes.

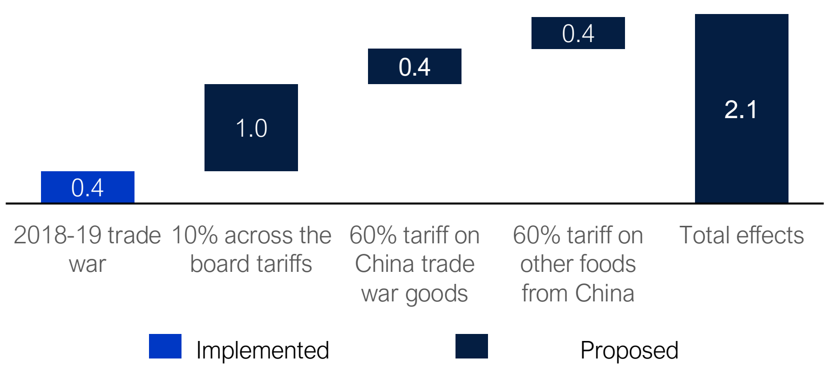
I. *Production Switching*: Relocating production to countries minimally affected by restrictions.
II. *Market Switching*: Redirecting products to alternative markets. Companies may pivot from exports to domestic sales in response to trade restrictions.
III. *Supplier Switching*: Adjusting sourcing partners, as for the U.S. ban case on Huawei. The latter turned to domestic or non-restricted foreign suppliers to maintain its supply chain.

Upgrading Production Profiles: Enhancing production processes, improving product quality, capturing more value, and moving into higher value-added roles. This "upgrading" allows firms to progress from assembly work to original equipment manufacturing (OEM) and onward, to design and eventually branding. As companies advance along this path, they also become more competitive, potentially shifting from being suppliers to direct rivals to their former clients. Thus, understanding and anticipating these strategic shifts is crucial for all players in the supply chain, as these former suppliers are no longer just vendors—they may transform into competing brands.

Global impact of U.S. trade restrictions on supply chains and production costs

The impact of trade restrictions often extends beyond the immediate countries involved or the targeted products. For example, Western companies that outsource to or invest in China to export goods to the U.S. are directly impacted by U.S. trade restrictions on China. Consequently, U.S. tariffs on Chinese imports also impact non-Chinese firms. Additionally, higher tariffs on Chinese intermediate goods may raise production costs for U firms that rely on these imports; Tesla, which uses Chinese components in its U.S. manufacturing, faces increased costs under higher tariffs. The negative effects of the tariffs imposed by the Trump administration in 2018 for the U.S. economy amounted to significant shifts in its supply-chain network, a reduction in the variety of available imports, and increasing costs in the domestic prices of imported goods (Wolf, 2024).

Impact of Trump tariffs on import costs for buyers
Total cost as a % of GDP



Source: Peterson Institute for International Economics

Additionally, president-elect Trump has proposed a blanket tariff of 10 percent on all imports, with an aggressive 60 percent tariff specifically targeting Chinese goods.

A tightening of de minimis exemptions

Over the last few decades, many manufacturing companies have concentrated their production in China due to the twin advantages of low-cost and high-volume production. Chinese dominance as a global

is expected to place additional strain on trade of 1 billion U.S. import shipments.

exporter across a wide range of manufactured goods has prompted a rise in protectionism among China's main trade partners. The current U.S. administration recently imposed tariffs on $18bn worth of Chinese exports, with the most significant increase being a quadrupling of the U.S. tariff on electric vehicles to 100 percent. In late September, the Biden administration proposed executive actions to address "unfair competition" from Chinese retailers exploiting the de minimis loophole. These new regulations, likely to be implemented in 2025, will exclude apparel and other products primarily sold by Shein and Temu from tariff exemptions, resulting in higher prices for U.S. consumers. The number of de minimis shipments in the U.S. had surged from 637 million in 2020 to 1 billion in 2023 (Economist, 2024).

Global trade barriers affecting domestic consumers and retailers beyond the U.S.

In addition to the U.S. several countries have already taken measures to protect domestic businesses from low-cost competitors, with the result of increased tariffs falling on domestics consumers and importers, at a time when consumers are being cautious with their spending (Mary Amiti, 2019). This environment will also likely weigh on sales for Chinese retailers and create logistical challenges for others; for instance, Nike has suspended cross-border online sales to Turkey due to revised import duties. As tax incentives for cross-border online purchases are removed, buying imported goods online could become more expensive for consumers. This change might make it less appealing for international brands to rely predominantly on online channels to reach foreign customers. Instead, they may choose to invest in more local infrastructure—such as physical stores or warehouses—to maintain competitive pricing and improve product availability in these markets. (Economist, 2024).

Summary of new duties and threshold on the importation of low-value goods an countries with significant trade relationships with China

Country	Measures on imported goods	Implementation
Turkey	De minimis reduced to €150 for online goods, customs tax rate raised to 60% for non-EU countries	August 2024
US	Exempting textile apparel and footwear from the $800 de minimis threshold	End 2024
EU	Elimination of the €150 de minimis threshold	Proposed in 2024, no set at present
South Africa	Introducing VAT on all imported clothing items	September 2024
Brazil	20% tax on cross-border purchases up to $50	July 2024

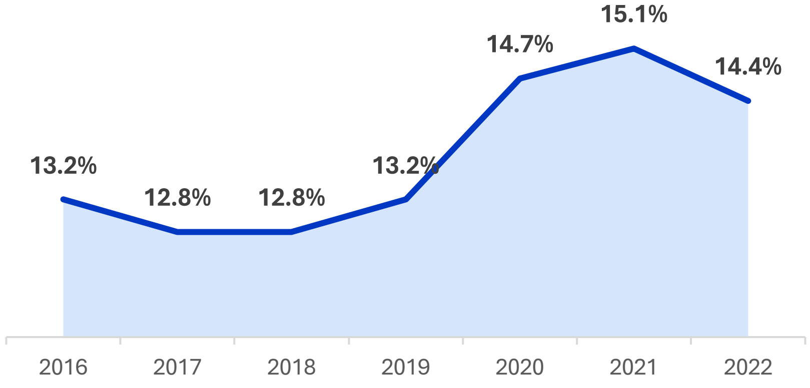
Source: Industry Outlook 2025, EIU

Increased R&D spending to support supply chain disruption

Research on Chinese firms affected by the 2018 U.S. tariffs indicates that these companies responded by increasing their ratio of R&D intensity by over 16%, a change largely supported by government subsidies (Han Hu, 2024). Factors such as inventory adjustments and risk-taking behaviours prompted firms to enhance their R&D spending in response to potential supply chain disruptions. The beneficial effects of sanctions on R&D investment are particularly significant among state-owned enterprises (SOEs) and firms led by executives with foreign experience. Nevertheless, while export controls have spurred R&D activities, they have not significantly improved innovation output, underscoring the necessity for greater efficiency in translating R&D investments into measurable results.

China's market share in global exports has increased as a result of the trade conflict with the U.S., demonstrating that a swift strategic shift among companies is essential for success and growth. While China's share of U.S. imports has decreased from **21.6%** in December 2017 to **13.5%** today, its overall share of global goods exports has risen from **12.8%** to **14.4%** during the same period, reflecting a shift in production locations and an enhancement in production capabilities (Ahya, 2024).

China's share of the global goods export market significantly higher compared to 2018, when trade tensions first arose
China percentage (%) of global exports, Y.o.y.



Source: Financial Times

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