Geostrategic analysis

The EY-Parthenon Geostrategic Business Group's monthly analysis explores key geopolitical developments and their business impacts.

September 2024 edition

EY Parthenon
Building a better working world

Table of contents

EY-Parthenon Geostrategic Business Group (GBG)
Translating geopolitical insights into business strategy

Read more.

Top development

Recent events underline the geostrategic importance of Iran's role as a "middle power"

What happened

Ongoing hostilities in the Middle East and direct attacks between Iran and Israel have raised the prospects of a regional war as covered in previous EY-Parthenon Geostrategic Analysis.

Iran elected a new President in July, considered by observers to be more reform-oriented than his conservative opponents. While Iran's foreign policy is unlikely to significantly change, President Masoud Pezeshkian has previously indicated openness to interaction and engagement with the West.

Military and industrial ties between Moscow and Tehran have grown, marked by technology sharing and joint defense projects. The conflicts in Ukraine and the Middle East have led Washington and Brussels to adopt increasingly defensive policy stances toward Iran, which has reduced the willingness for both sides to pursue mutual interests.

What's next

Continuation of hostilities between Israel and Iran (and its regional proxies) remains highly likely while the Gaza crisis remains unresolved. Military vulnerabilities on all sides will spur increased defense spending with increased support from their respective allies. For instance, the US is expediting additional arms deliveries to Israel and accelerating deployments of additional military forces to the region.

The current crisis reinforces Iran's continuing role as a geopolitical "middle power," shaping global dynamics through its interactions with the major powers and other regional players. Most notably, the Russian-Iranian relationship is expected to have both military and economic components since both countries are seeking increased commercial opportunities, notably via rail and road routes connecting the two countries. However, persistent conflicts in Ukraine and the Middle East may lead Moscow and Tehran to focus on addressing their immediate regional concerns. Meanwhile, Iran likely will continue serving as a major petroleum source for China[1], which creates some incentives for maintaining Middle East stability.

While G7 policy makers will focus on calming tensions, the Gaza ceasefire negotiations and later enforcement[2], the apparent acceleration of Iran's nuclear program[3] likely will also require their attention. G7 leaders may look to calibrate effective policy responses that build upon the foundation of existing sanctions and potentially explore other trade and diplomatic tools.

Business impact

Major sectors affected include Industrials and Energy, Consumer and Retail, Financial Services.

Shipping and airlines are likely to continue facing physical security risks when operating in the region. Companies reliant on trade routes in the Middle East should consider diversifying supply routes, purchasing political risk insurance or utilizing inventory management techniques to build resiliency.

Further escalations risk energy supply shocks and short-term price volatility. Commodity traders and energy customers should consider hedging strategies to protect against potential downside risks.

Executives should leverage scenario planning to prepare crisis response plans and bolster resiliency given various potential escalatory paths. The most extreme scenarios could involve severe impact to local personnel amid population dislocation, regional economic contraction and elevated financial markets stress.

For more information, contact Jay Young and Ben-Ari Boukai.

Additional reading: 2024 Geostrategic Outlook

1. Iran's Petroleum Exports to China and U.S. Sanctions | Congressional Research Service https://crsreports.congress.gov/product/pdf/IN/IN12267
2. G7 Leaders' Statement on Gaza | The White House https://www.whitehouse.gov/briefing-room/statements-releases/2024/06/03/g7-leaders-statement-on-gaza/
3. Iran 'one or two weeks' away from producing fissile material for nuclear weapons: US | Yahoo.com https://news.yahoo.com/news/iran-one-two-weeks-away-215340635.html

2 Sector in focus: Wealth and Asset Management (WAM)

Geopolitical fragmentation creates risks and opportunities for investment managers.

What happened

Geopolitical fragmentation has been impacting where investment managers can do business, what they can invest in and who they can work with. The risk of sanctions is significantly affecting business models. Asset owners that are government-backed or linked are facing especially heightened pressure.

New laws may further limit investment opportunities in certain markets or sectors, such as the US Treasury releasing its notice of proposed rulemaking that would impose controls[4] on certain outbound investments in China.

Additionally, there is a growing concern among investment managers around cybersecurity and the risk that geopolitical tensions could limit international cooperation to tackle any cyber warfare[5] that may emerge.

What's next

Geopolitical conflicts will continue and new regulations, including around data sovereignty, enhanced security and resilience, and sustainability policy, will impact investment managers' operations. This will likely lead to new cross-border partnerships to ensure a robust infrastructure and optimization of technologies such as artificial intelligence (AI).

The US and some other "Western" governments will likely continue to push firms to divest from certain strategic sectors in geopolitical rivals. While this may adversely impact business for some firms, it could present some opportunities for investment managers from geopolitical swing states such as Singapore, UAE and Saudi Arabia.

Business impact

Investment managers should proactively create operational and portfolio resilience[6], with robust governance frameworks in place to build trust among stakeholders. Firms should prepare for potential power shifts in a multipolar world and related regulatory changes that may lead to divergent policies around sustainability and AI.

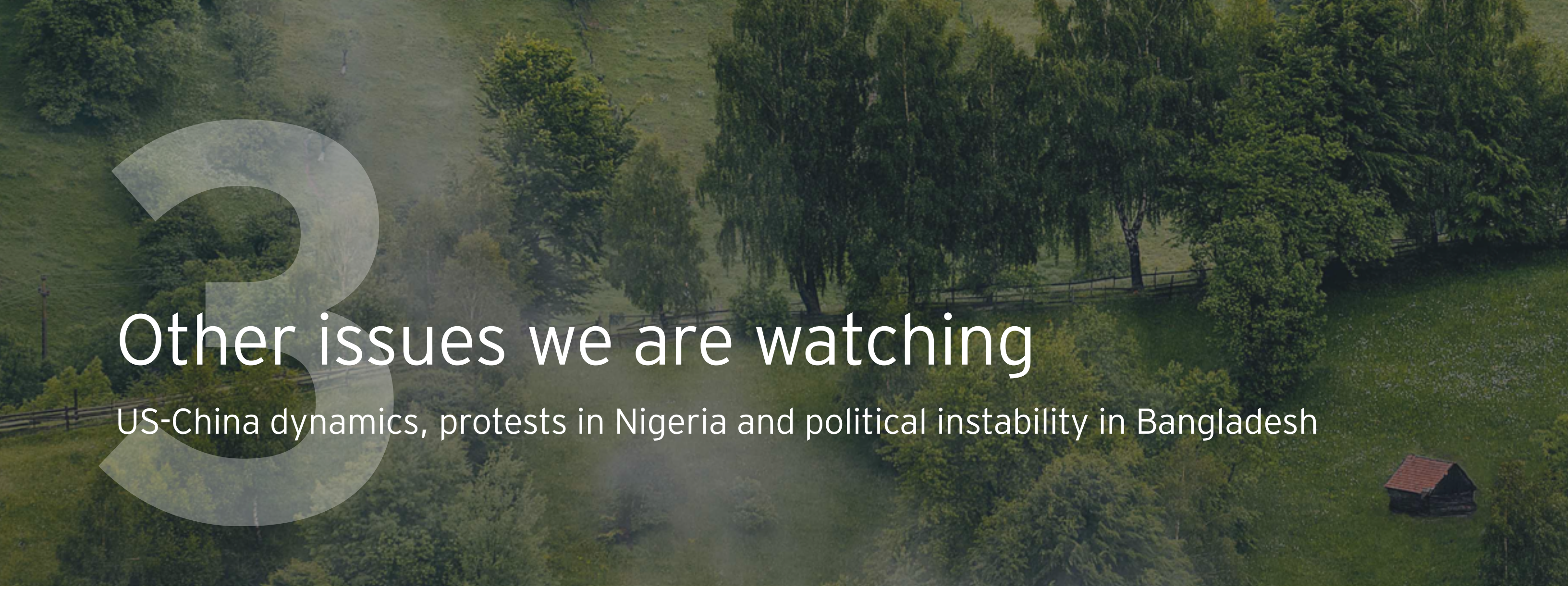
Investment firms should continually test, exercise, and train their staff and systems to reveal scenarios and weaknesses — internally and externally. Collaboration between investment managers, service providers and policymakers is important to navigate a complex cross-border environment and best utilize new technologies and talent.

Geopolitics should continue being prioritized by investment managers as a critical area of focus when making any new capital allocation decisions — be it around their investments, operating models or growth strategy.

For more information, contact Mark Wightman and Meghna Mukerjee

Additional reading: Top 10 geopolitical risks for 2024 | EY – Global

4. Provisions Pertaining to U.S. Investments in Certain National Security Technologies and Products in Countries of Concern | US Department of the Treasury https://home.treasury.gov/system/files/206/NPRM%20-%20Provisions%20Pertaining%20to%20U.S.%20Investments%20in%20Certain%20National%20Security%20Technologies%20and%20Products%20in%20Countries%20of%20Concern.pdf
5. 4 Areas of Cyber Risk That Boards Need to Address | Harvard Business Review https://hbr.org/2023/06/4-areas-of-cyber-risk-that-boards-need-to-address
6. Singapore's GIC looks to buy western groups' China units | Financial Times https://www.ft.com/content/0344a8a6-46a3-44f7-8d71-9f33192bc25f



3 Other issues we are watching

US-China dynamics, protests in Nigeria and political instability in Bangladesh

US-China dynamics will be a focus in Washington

The US Congress was in recess for much of August and returned to Washington on 9 September. The House of Representatives may hold a long-expected "China Week" in September, which would be focused on security issues related to China. While it remains unclear what legislation or activities may be considered, it could include a House vote on the BIOSECURE Act. Separately, the Biden Administration is reportedly planning to release in September proposed rules to restrict Chinese connected vehicle technologies from being used in US cars. And the tariffs on certain strategic products that President Biden announced in May[7] could come into effect this month. Beijing is likely to react to any actions taken by Washington, but the specific nature of their response is uncertain.

Business impact: Executives should closely monitor Washington for heightened rhetoric and activity in this arena leading up to the November elections. The perceived over-reliance of the US on China for certain advanced manufacturing capabilities is likely to continue to drive bipartisan US policymaker support for "de-risking" from China and could lead to new products and sectors labeled as "strategic" for national security. Executives should continue to evaluate portions of their business that may be considered as strategic now or in the future and evaluate potential diversification opportunities and risk mitigation strategies.

For more information, contact Courtney Rickert McCaffrey.

Nigeria protests could lead to short-term operational disruptions

Nigeria is grappling with widespread protests throughout the country. Protest action was at its peak in early August triggered by soaring inflation arising from a series of economic reforms[8] following President Tinubu's one-year anniversary in office. This highlights the challenge of balancing the benefits of long-term economic reforms with the cost of short-term hardship. The post-pandemic economic slump and limited fiscal space for governments to boost economic activity, coupled with a large youth population and high unemployment rate, make the Sub-Saharan African region particularly vulnerable to such protests — with Uganda and Kenya having had protests in July 2024.

Business impact: The ongoing protests pose risks to business continuity across multiple sectors in Nigeria, particularly retail, manufacturing and services. Nigeria's economic outlook remains challenging, with inflation and restrictive monetary policies constraining growth. Despite efforts to increase oil production and improve reserves, operational disruptions and theft could exacerbate supply chain challenges at a time when exchange rate volatility and high inflation are impacting business activity and consumer spending. Companies in various sectors, including energy, may face potential policy shifts such as fiscal and subsidy reforms as the government seeks to stabilize the situation.

For more information, contact Angelika Goliger and Hulisani Muloiwa

Bangladesh political instability creates domestic and geopolitical uncertainties

Following widespread civil society protests fuelled by perceived injustices and economic strain, Prime Minister Sheikh Hasina of Bangladesh resigned[9] on 5 August, ending her 15-year rule. An interim government, led by Nobel Peace Prize laureate Mohammad Yunus, has been formed with the backing of army leaders. A new election timeline is being negotiated to include Hasina's Awami League party and the leading opposition, Bangladesh National Party (BNP). Concerns around future political and religious suppression linger.

Business impact: The garment industry — which accounts for nearly 80% of the country's exports — faces ongoing operational and trade disruptions. Infrastructure projects, including those in the power and water sector, will likely face delays and future investment risks may be elevated. The need for international financial support to alleviate the economic crisis is likely to make Dhaka's geopolitical relationships with both India and China more complex. While the immediate policy environment is expected to remain stable, the potential for economic and governance reforms after the election is held necessitate ongoing political risk due diligence for existing and future investments.

For more information, contact Adam Barbina.

7. President Biden Takes Action to Protect American Workers and Businesses from China's Unfair Trade Practices| White House https://www.whitehouse.gov/briefing-room/statements-releases/2024/05/14/fact-sheet-president-biden-takes-action-to-protect-american-workers-and-businesses-from-chinas-unfair-trade-practices/
8. IMF Executive Board Concludes 2024 Article IV Consultation with Nigeria | International Monetary Fund https://www.imf.org/en/News/Articles/2024/05/08/pr-24144-nigeria-executive-board-concludes-2024-art-iv-consultation
9. Hasina falls, flees | The Daily Star (thedailystar.net) https://www.thedailystar.net/news/bangladesh/news/hasina-falls-flees-3670201

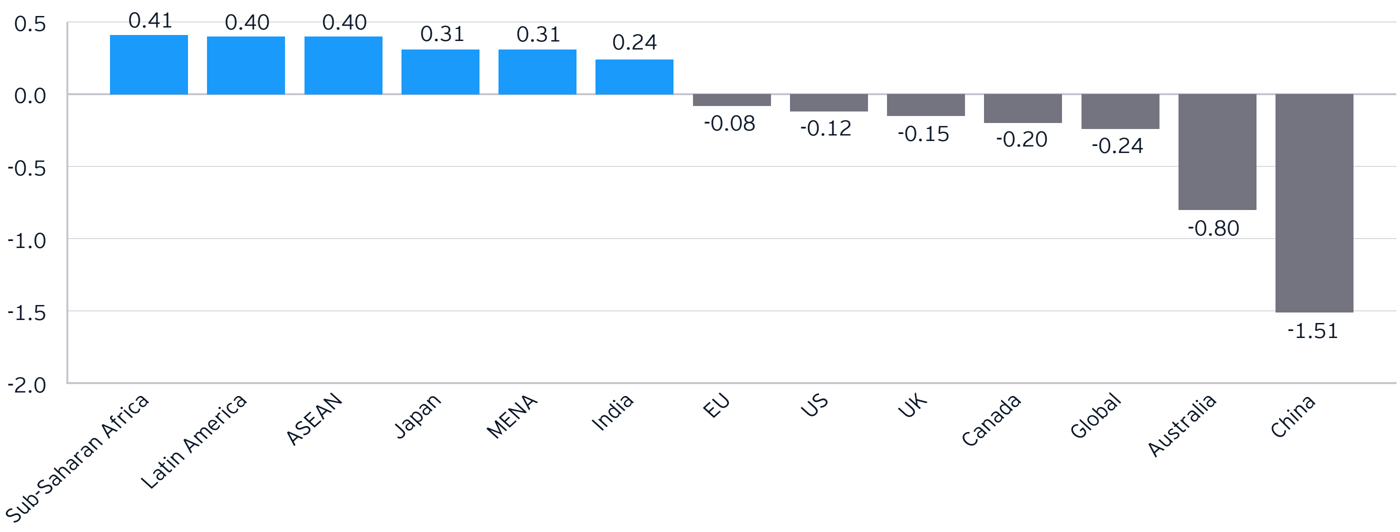
Geostrategic indicator of the month

Scenario analysis of geopolitical tensions between China and the West.

The indicator:

The EY Macroeconomics team simulated a potential increase of 20 percentage points in average bilateral tariffs on 2025 trade in goods between China and a group of leading Western countries (consisting of Australia, Canada, EU, UK and the US). The EY UPGRADE computable general equilibrium model finds that this rise in tariffs would reduce global real GDP by 0.24% below the baseline level after three years, with the largest declines occurring in China (1.51%) and Australia (0.8%). In contrast, some economies, such as those in Sub-Saharan Africa and Latin America, would reap modest benefits from trade flow diversion and increased competitiveness.

Scenario analysis reveals geopolitical tensions between China and the West would negatively affect the global economy
Impact on Real GDP in 2027 (percentage deviation from baseline scenario)



Source: EY simulation using the EY UPGRADE CGE model
Note: In the short term, the slowdown in China and the group of Western countries is likely to adversely impact other regions, which may not be fully captured by the model we use. Baseline scenario refers to the baseline level of a specific economic variable (e.g., real GDP) in a given year in the absence of a trade war.

Business impact:

Increased tariffs would lead to higher procurement costs, at least in the short to medium term, as companies would face pricier imports of raw materials and components. This could result in inflationary pressures, with consumers paying elevated prices for goods. This would likely reduce consumer demand more broadly, which could affect sales and revenue for a variety of companies. Global supply chains may experience disruptions as companies seek alternative suppliers in new markets or try to onshore or reshore some operations. This could create growth opportunities for companies in alternative markets, although it could also generate challenges in hiring and retaining workers.

Additional reading: Global economic outlook: thriving in a new normal

Contacts

Oliver Jones
London
oliver.jones@uk.ey.com

Angelika Goliger
Johannesburg
angelika.s.goliger@za.ey.com

Mary Karol Cline
Washington DC
mary.k.cline@ey.com

Courtney Rickert McCaffrey
Washington DC
courtney.r.mccaffrey@ey.com

Adam Barbina
New York
adam.l.barbina@parthenon.ey.com

Ari B. Saks Gonzalez
Mexico City
ari.b.saks.gonzalez@mx.ey.com

Ben-Ari Boukai
Washington DC
ben-ari.boukai@parthenon.ey.com

Jay Young
Dallas
jay.young1@parthenon.
ey.com

Famke Krumbmüller
Paris
famke.krumbmuller@
parthenon.ey.com

Jan Kallmorgen
Berlin
jan.kallmorgen@parthenon.
ey.com

Nobuko Kobayashi
Tokyo
nobuko.kobayashi@
parthenon.ey.com

Alessandro Faini
Paris
alessandro.faini@
parthenon.ey.com

EY | Building a better working world

EY exists to build a better working world, helping create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via ey.com/privacy. EY member firms do not practice law where prohibited by local laws. For more information about our organization, please visit ey.com.

About EY-Parthenon
EY-Parthenon teams work with clients to navigate complexity by helping them to reimagine their eco-systems, reshape their portfolios and reinvent themselves for a better future. With global connectivity and scale, EY-Parthenon teams focus on Strategy Realized – helping CEOs design and deliver strategies to better manage challenges while maximizing opportunities as they look to transform their businesses. From idea to implementation, EY-Parthenon teams help organizations to build a better working world by fostering long-term value. EY-Parthenon is a brand under which a number of EY member firms across the globe provide strategy consulting services. For more information, please visit ey.com/parthenon.

EYG no. 008691-24Gbl

2408-15893-CS
ED None

ey.com