Weekly Summary

Economics of Climate Change

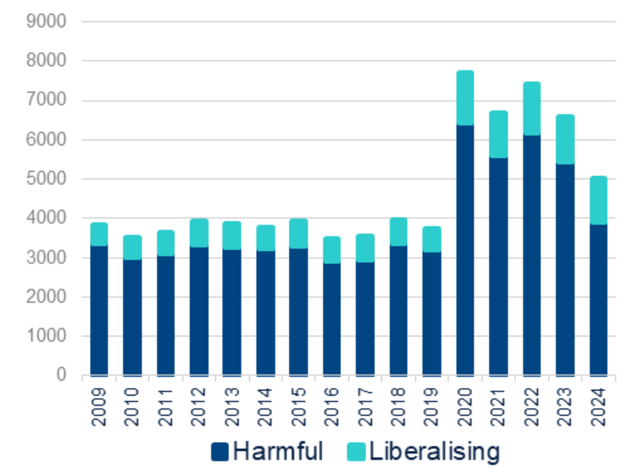
April 4, 2025

Geoeconomic Fragmentation, a Vulnerability for the Climate Transition

The geoeconomic fragmentation triggered by geopolitical concerns makes climate transitions more vulnerable, for example in the EU, which depends on politically distant suppliers of decarbonization inputs, or in emerging economies, which rely on external flows of sustainable finance.

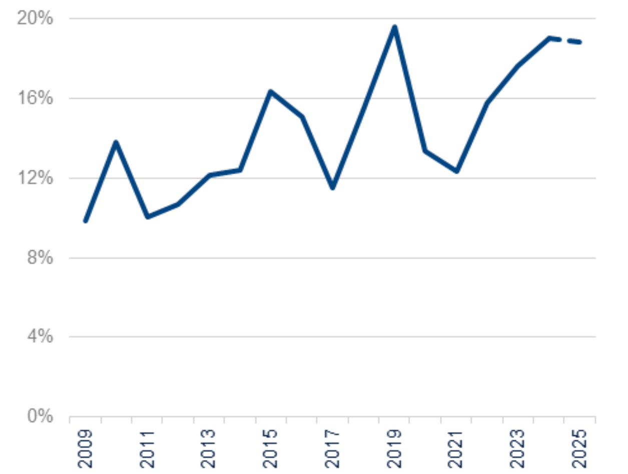
Trade tensions, structural change in the last decade. The current decade is seeing a much less favourable environment for global trade in goods, services or investment, a situation of which the incoming shock deployed by the US government is only an additional (big) leap. According to information compiled by Global Trade Alert, which tracks policy changes affecting global trade and investment, the number of restrictive measures for global trade announced each year on average during the current decade has grown by 75% compared to the previous decade (**Figure 1**).

Figure 1. **NUMBER OF NEW GLOBAL TRADE INTERVENTIONS PER YEAR**



Source: BBVA Research from Global Trade Alert (Reporting lags understate the totals for recent years)

Figure 2. **Global Trade in Renewable Energy Products[1]. Harmful Interventions (%)**



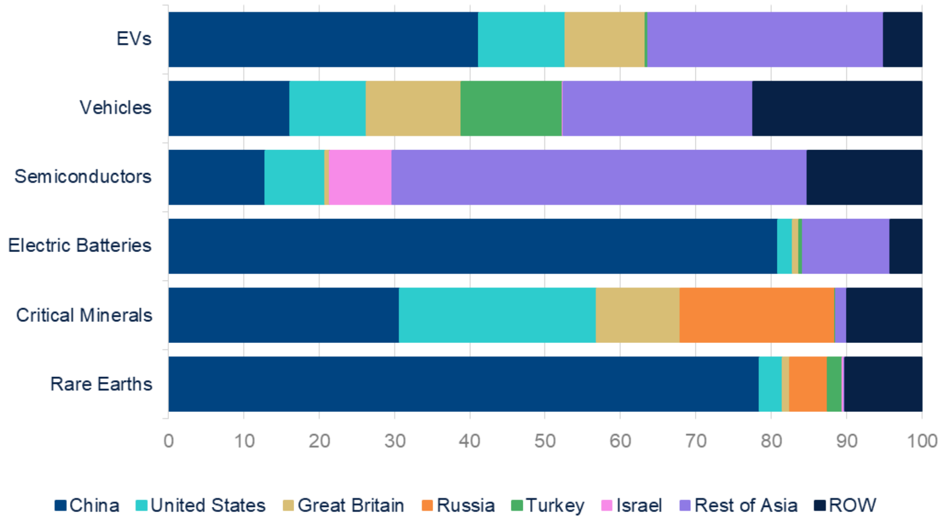
Source: BBVA Research from Global Trade Alert (Reporting lags understate the totals for recent years).

Trade restrictions to renewables are also increasing. In this scenario, some of the products most directly related to the transition to a decarbonised economy have also been affected, with a percentage of total restrictive measures rising from 13% in the last decade to 16% on average in the current decade. It is worth noting the upwards long term trend (**Figure 2**).

1: Critical Raw Materials, car batteries, and solar & wind energy technology components.

Geoeconomic fragmentation (GEF) is here, and the EU is vulnerable.[2] The raising of trade tensions is a key evidence of a GEF process, a policy-driven reversal of global economic integration, motivated primarily by strategic considerations such as national security, sovereignty, autonomy, or economic rivalry.[3] The EU might be particularly vulnerable to GEF in relation to the transition towards decarbonization, primarily due to its heavy reliance on imports from a few providers of critical inputs such as rare earths or electric batteries -both of which play a vital role in accelerating the use of renewable energy sources and the adoption of electric vehicle (**Figure 3**). These materials are predominantly sourced from politically distant countries,[4] posing risks of supply disruptions and heightened geopolitical tensions.[5] Additionally, initiatives such as the EU's Carbon Border Adjustment Mechanism (CBAM), intended to address competitive disadvantages for European businesses resulting from uncoordinated global climate policies, would stir international concerns and retaliatory measures, potentially exacerbating fragmentation.

Figure 3. **EXTRA-EU EU IMPORTS BY PARTNER AND KEY PRODUCTS (%)**



Source: BBVA Research, calculations from UN Comtrade data.

2: Navigating a fragmenting global trading system: insights for central banks. ECB Occasional Paper No 365.
3: GEF does not include reversals driven by autonomous factors such as technological advancements, demographic shifts, or policies primarily motivated by prudential, environmental, labour, or human rights considerations. Ibid 2.
4: It remains to be seen what political and policy distance, and even in the institutions of multilateral governance, will remain between the US and the rest of the world (ROW) given the virulence and uncertainty of the unleashed trade war.
5: Furthermore, the EU currently lacks sufficient domestic extraction capabilities and faces considerable lead times and environmental challenges in developing these capacities, intensifying its dependency on external sources.

Box 1. How Geoeconomic Fragmentation can Impair the Allocation of Sustainable Investments[6]

GEF exacerbates the already uneven distribution of sustainable finance between advanced economies and emerging markets or developing economies (EMDEs). Due to divergent regulatory standards and investor concerns about geopolitical risk, private investment flows critical for the climate transition may decrease. Specifically, differences in Environmental, Social, and Governance (ESG) regulations and heightened geopolitical uncertainties can limit cross-border capital flows and make it harder for EMDEs to attract necessary funding. Sustainable investment flows to EMDEs remain disproportionately low compared to advanced economies, driven by lower ESG scores in EMDEs, not explained solely by size, industry, or financial performance differences. Additionally, geopolitical fragmentation can cause increased financing costs for countries perceived as geopolitically misaligned, restricting their ability to finance transition efforts

All in all, geoeconomic fragmentation would undermine the global climate transition by intensifying trade tensions and supply chain vulnerabilities. The increasing number of restrictive trade measures, such as those affecting renewable energy, highlights a challenging environment, also exacerbating the unequal distribution of sustainable finance between advanced economies and emerging markets.

Highlights of the Week

- **Global | Record-Breaking Annual Growth in Renewable Power Capacity. IRENA**. With 585 GW of capacity additions, renewables accounted for over 90% of total power expansion globally in 2024.
- **Global | Promising new technologies face market uncertainty in pivotal moment for global energy innovation - News - IEA.** The report highlights recent progress and emerging risks across the energy innovation landscape worldwide, with investment trends uneven across different regions and sectors.
- **Global | OECD urges strengthened co-operation to sustain trillion-dollar ocean economy**. The report identifies key priorities for policymakers to secure a resilient and sustainable future ocean economy, balancing economic opportunity with environmental responsibility.

6: Ibid 2.

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