EXPORT ANALYTICA QUARTERLY INSIGHT

Q1/2025

WAR AND PEACE IN 2025

Perhaps the most frequently mentioned term in the first quarter of 2025 was **'war.'**

While efforts to seek peace intensified in relation to the wars in Ukraine and Gaza, in the economic sphere, **trade war** emerged as a buzzword in response to a series of tariffs introduced by the new US administration and reciprocal measures adopted by the affected countries.

In Europe, this was accompanied by processes aimed at strengthening **European defence**, as the EU responded not only to the war in Ukraine but also to calls from Washington urging Europe to take greater responsibility for its own fate.

The political-military expression of these efforts has been the formation of the **'coalition of the willing'**, which aims to guarantee a ceasefire in Ukraine. The security-economic dimension of the response to the EU's needs has been translated into plans to **enhance the EU's military capabilities through more defence spending and better coordination and cooperation at the EU level**. This plan materialized in the White Paper for European Defence Readiness 2030, published on March 19, 2025.

In global trade, the **EU aims to uphold its role as a stronghold of free trade**. Rising tariffs from the US are prompting the EU to **reassess and adjust its relationships with other global partners**, while considering an adequate response.

Under these circumstances, **increased defence spending and production may emerge as a new engine for economic growth across Europe**. Yet, financing remains a crucial issue, as in addition to defence, several other pressing matters require significant resources: green, energy, and digital transitions, support for Ukraine, the continued expansion of the EU, the completion of post-COVID economic recovery, and overcoming the EU's technological gap, to name just the most essential ones.

These issues urgently bring to the forefront the eternal **dilemmas of European financing: priorities, scope, and funding sources**. They will undoubtedly form an important philosophical tripod in the upcoming discussions on the **new multiannual financial framework of the EU beyond 2027**. However, the world is extremely turbulent, and the EU cannot afford to wait until then for answers—it needs them practically immediately.

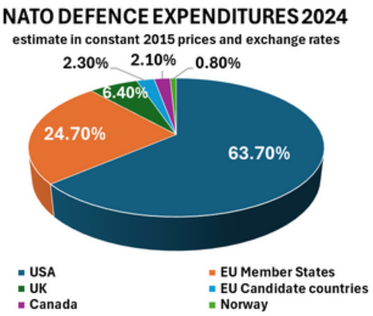
EUROPEAN DEFENCE INDUSTRY

CALL TO ARMS

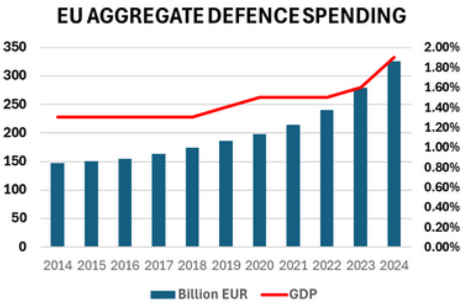
In Davos in January, President Trump demanded that NATO allies raise defence spending to 5% of GDP. In February, the British Prime Minister set out a commitment to increase defence spending to 2.5% of GDP from April 2027, with an ambition to reach 3% in the next parliament. The President of the European Commission, Ursula von der Leyen, in March proposed to activate the national escape clause of the Stability and Growth Pact, to allow Member States to increase their defence expenditures by up to 1,5% of GDP. In March, the German parliament approved a spending surge to support the revival of economic growth and defence spending.

There is no country in the NATO or the EU that currently spends more than 5% of its GDP on defence, and only Poland spends more than 4%. Aggregate defence spending of EU member states last exceeded 3% of GDP in the 1960s. Since then, it declined until the mid-2010s, when it dropped to 1.3% of GDP. It was the Russian annexation of Crimea and the beginning of the war in Donbas that brought about a change. Since then, European defence spending has been rising, but even in 2024, it only reached an estimated 1.9% of the EU's GDP.

On the other hand, when the Russian full-scale invasion of Ukraine started in 2022, Europeans allocated approximately €240 billion to defence, nearly matching China's expenditure of €275 billion and surpassing Russia's by threefold, accounting for 12% of the worldwide total, according to the Letta report. Therefore, long-term underfinancing of European defence is only a part of the diagnosis. The problem goes deeper than that. We can see three dimensions of the problem: **finances, capabilities and strategy**.



Source of data: NATO



Source of data: EDA

EU REARM PLAN / READINESS 2030
5 PILLARS TO SURGE DEFENCE SPENDING

1. **SAFE (Security and Action for Europe)** - new financial instrument to provide EU member states with loans backed by the EU budget (up to €150bn). Joint procurement by at least 2 countries will be needed - the recipient must be an EU member state, while the partner country can be EU member state, a country from EFTA, EEA, or Ukraine.
2. **Coordinated Activation of the National Escape Clause** will allow EU member states to increase defence spending beyond the existing rules of the Stability and Growth Pact, up to 1.5% of GDP annually for the next 4 years. The European Council called on the Commission to explore additional measures to enable increase in defence spending.
3. **Increasing the Flexibility of EU Instruments** - it will primarily involve redirecting cohesion funds towards strengthening defence and security capabilities. The European Council has also called on the Commission to identify additional sources of EU level funding.
4. **Contribution from the European Investment Bank**: EIB intends to double its annual investments in defence related projects to €2bn. The EIB Group also proposes adjusting eligibility criteria to align supported activities with the new policy priorities of the EU.
5. **Mobilising private capital** - as up to 44% of SMEs in the EU defence sector have major concerns about access to capital, the EU aims to mobilize private investors to channel their savings into investments in the defence sector. Through the Union of Savings and Investments the EU expects to mobilize hundreds of billions of euros annually.

The need for the European defence industry to produce more and faster was already emphasized by **European Defence Industrial Strategy** (EDIS) in March 2024. More cooperation and collective action was seen as crucial. That´s why EDIS proposed several key benchmarks:

- by **2030**, the value of intra-EU defence trade should represent at least **35%** of the value of the EU defence market.
- By **2030**, at least **50%** of Member States defence procurement budget should be devoted to procurement from the EU's Defence Technological and Industrial Base (EDTIB), and **60%** by **2035**.
- By **2030**, Member States should procure at least **40%** of defence equipment in a collaborative manner.

7 PRIORITIES TO CLOSE CAPABILITY GAPS

If financing is the quantitative dimension of the problem of European defence, its qualitative dimension is the elimination of gaps in critical capabilities. In this context, the European Commission and the European Council have identified seven priorities:

- Air and missile defence
- Artillery systems
- Ammunition and missiles
- Drones and counter-drone systems
- Military Mobility
- AI, Quantum, Cyber & Electronic Warfare
- Strategic enablers and critical infrastructure protection

AN EMERGING STRATEGY: FROM LETTA, DRAGHI AND NIINISTÖ TO WHITE PAPER ON DEFENCE

In 2024, three prominent leaders authored reports that, though having different focuses, all devoted significant attention to strengthening European defence. The Letta report (April 2024) addressed the future of the single market, the Draghi report (September 2024) focused on European competitiveness, and the Niinistö report (October 2024) examined civil and military preparedness.

The reports concurred that European defence had long been underfunded. However, they also emphasized that increasing resources alone would not be enough. Strengthening European strategic autonomy would require a change in approach, including: enhancing cooperation to build EU´s Defence Technological and Industrial Base (EDTIB), overcoming fragmentation to enhance the scale and speed of production, integrating European defence market to fully exploit its strength, and shifting the overall philosophy to place security at the forefront as a public good—security as the foundation of everything.

These principles have been reflected in the **White Paper for European Readiness 2030** (March 2025), which outlines **six strategic directions** aimed at fostering a stronger and more innovative defence industry in Europe:

- reinforcing **industrial capacities** across the EU
- securing **supply chains** and reducing dependencies
- building a **true EU-wide Market** for Defence
- **simplifying rules** and cutting red tape;
- boosting R&D to foster **innovation**
- attracting **talent** and enhancing skills and expertise

Simultaneously, cooperation with **Ukraine**, and integration of Ukrainian defence industry into the EDTIB, including Ukrainian first hand knowledge transfer on innovations from battlefield, could provide EDTIB with extra boost.

TRADE WARS

TRADE WAR

The new US administration imposed several trade tariffs in the first weeks after Donald Trump´s inauguration. The Tax Foundation estimates that the average tariff rate on all imports will rise from **2,5%** in 2024 to **8,4%** in 2025, which would be the US's highest average rate since 1946.

OECD Economic Outlook (March 2025) models the impact of tariffs on all non-commodity imports into the US (manufactured products - e.g. industrial and consumer goods). The report states that if these tariffs were to increase permanently by 10 p.p., the following consequences could result:

- The world economy could shrink by 0.3% by the third year
- The average increase in global inflation would be 0.4 p.p. over the first three years
- The volume of global trade could fall by almost 2%
- US output would fall by 0.7%, and inflation would rise by 0.7 p.p. per year
- Canada and Mexico would be particularly hard hit

DEVELOPMENT OF TARRIF RATE AND FREE FTA

The *"Tariff rate, applied, weighted mean, all products (%)"* measures the average tariff imposed on imported goods, weighted by the import shares of each product. This metric provides insight into a country's trade openness and protectionist policies.

Over the **past 25 years**, the global trend has been toward **lowering** applied weighted mean **tariff rates** and promoting trade liberalization. Since the mid-1990s—particularly after the Doha Round stalled—there has been a marked shift toward **bilateral and regional free trade agreements**, with the number of cumulative RTAs in force climbing from 53 in 1996 to 374 by 2024. China's WTO entry led to major tariff drops, boosting trade and growth. India has also reduced tariffs, though some sectors stay protected to aid local industries. However, recent years have seen reversals in some regions due to protectionist policies and trade disputes, highlighting the dynamic nature of international trade relations.

TRADE WAR DEVELOPMENT IN 2025

Date	Country/Region	Category	Tariff Name (%)
26.3.	World	Auto and parts	Auto Parts Tariffs (25%)
25.3.	World	Venezuela sanctions	Venezuela Oil Tariffs (25%)
20.3.	World	Critical minerals	Critical Minerals Boost
12.3.	World	Steel and aluminum	Steel Aluminum Tariffs Start (25%)
12.3.	European Union	Steel and aluminum	EU Retaliation on Tariffs
12.3.	Canada	Steel and aluminum	Canada Steel Tariff Response (25%)
6.3.	Canada	Fentanyl and immigration	USMCA Exemption for Canada (10% Potash)
6.3.	Mexico	Fentanyl and immigration	USMCA Exemption for Mexico (10% Potash)
4.3.	Canada	Fentanyl and immigration	Canada Tariffs Take Effect (10% Oil/25% Other)
4.3.	Mexico	Fentanyl and immigration	Mexico Tariffs Take Effect (25%)
4.3.	China	Fentanyl and immigration	China Tariff Rate Increased (20%)
4.3.	Canada	Fentanyl and immigration	Canada Retaliation Announced (25%)
4.3.	China	Fentanyl and immigration	China Retaliation Measures (Varied)
1.3.	World	Lumber	Lumber National Security Probe
25.2.	World	Copper	Copper Security Investigation
21.2.	China, World	Investment Policy	America First Investment Memo
21.2.	EU, UK, Canada, Türkiye	Digital Services Taxes	Digital Tax Dispute Memo
13.2.	World	Trade Policy	Reciprocal Trade Policy Memo
10.2.	World	Steel and aluminum	Section 232 Metal Tariffs (25%)
5.2.	China	Fentanyl and immigration	China Duty-Free Restored
4.2.	China	Fentanyl and immigration	China Retaliation Announced (Varied)
4.2.	China	Fentanyl and immigration	China Tariffs Implemented (10%)
3.2.	Mexico	Fentanyl and immigration	Mexico Tariffs Paused (Paused)
3.2.	Canada	Fentanyl and immigration	Canada Tariffs Paused (Paused)
1.2.	Canada	Fentanyl and immigration	Canada Retaliation Tariffs (Varied)
1.2.	Canada, China, Mexico	Fentanyl and immigration	Broad Tariffs Announced

Source of data: Chad P. Bown (PIIE)

US measure | US measure paused | Countermeasure | US investigation

IMPLICATIONS FOR SLOVAKIA

The National Bank of Slovakia (NBS) estimates that US tariffs, along with retaliatory measures, could reduce Slovakia's GDP by nearly 3% by the end of 2027, cut exports by €5 billion, and eliminate 20,000 jobs.

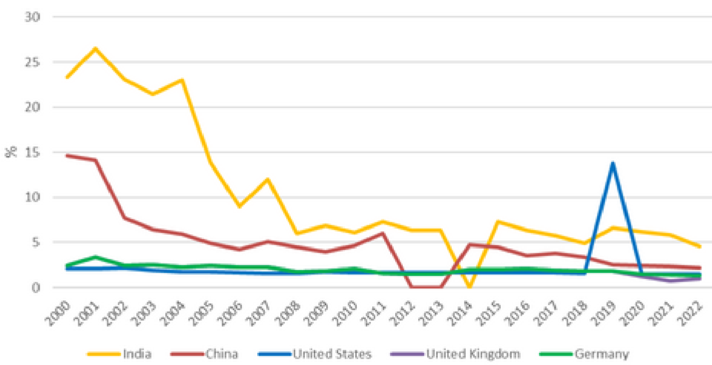
Similarly, the Association of Industrial Unions and Transport estimates that a deepening trade confrontation could reduce Slovak exports by €4.4 billion by 2029.

The NBS concludes that the industries most at risk include manufacturing, transportation, and trade, which rely heavily on global supply chains. Although Slovak U.S. Steel Košice primarily serves the European market, increased competition from third countries could still harm its operations.

Globally, trade war could lower economic growth by about 1.2 p.p. over 2025–2027. As the 11th most open economy in the world, Slovakia could be significantly affected, especially given its heavy dependence on the automotive sector and the fact that around 4.1% of its exports go to the US. Of these exports, 70% is made up of cars and their components.

According to the Institute of Financial Policy, the total US demand generates roughly 2.4% of value added in Slovakia, and in the automotive industry, up to 10%.

TARIFF RATE, APPLIED, WEIGHTED MEAN, ALL PRODUCTS (%)



Source of data: World Bank

RISK OF GEOECONOMIC FRAGMENTATION

The increasing fragmentation of the global economy is a significant risk. Broader escalation of trade wars could dampen global growth, fuel inflation, and force central banks to adopt more restrictive monetary policies, potentially leading to sharp and disruptive adjustments in financial markets.

In addition, the US has paused its financial contributions to the World Trade Organization, as part of a broader review of funding to international organizations. As the WTO's top financial contributor (about 11% of its budget), the absence of US funding could strain the organization's capacity to deliver on its core functions, including dispute resolution and trade monitoring. The US's potential withdrawal could undermine the WTO's authority and call into question the viability of a rules-based global trading system. This, in turn, may prompt more significant fragmentation of international trade rules, pushing countries to pursue or rely on regional and bilateral dispute settlement mechanisms. Such a shift could intensify trade tensions and decrease overall predictability in global commerce.

On the one hand, the EU, which is a bastion of free trade, is facing tariffs from the US. On the other hand, it is contending with subsidized products from China. So far in 2025, the EU has taken measures against subsidized glass fibre yarns, electric bicycles, erythritol, titanium dioxide and biodiesel from China, aluminium road wheels from Morocco, subsidized from China, and started monitoring ethylene and ammonia products and industrial chemicals, which are rapidly filling the EU market. The flow of cheaper aluminium and steel products to the EU is the direct consequence of the US tariffs on these metals.

UNCERTANTIES, RISKS AND OPPORTUNITIES

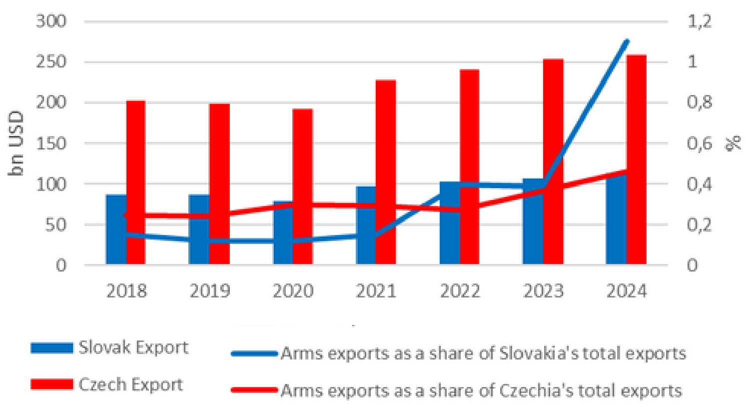
ARMS EXPORTS INCREASE IN 2024

The Stockholm International Peace Research Institute reports that the **five largest arms exporters** in 2020–24 were the **US, France, Russia, China and Germany**. The US remains the largest arms exporter with a global share of 43% in the last 5 years. In contrast, arms exports from Russia have declined sharply over the past 10 years. The US accounted for 64% of arms imports by European NATO states in the last 5 years.

The **top five arms importers** in the last 5 years have been **Ukraine, India, Qatar, Saudi Arabia and Pakistan**. Asia and Oceania accounted for 33% of total arms imports in 2020-24, followed by states in Europe (28%), the Middle East (27%), the Americas (6.2%) and Africa (4.5%). China's arms imports have fallen by 64% as the country increasingly replaces imports with its own domestic arms production.

SLOVAK ARMS EXPORTS DEVELOPMENT

In 2024, Slovak arms exports more than doubled, compared to the previous year, to €1.15 bn. Arms exports made up 1.1% of Slovakia's total exports, marking a significant increase from just 0.15% in 2018. Meanwhile, the Czech share of arms exports rose from 0.25% of total exports in 2018 to 0.46% in 2024. Last year, Slovakia's global share of arms exports was 0.2%.



Source of data: UN COMTRADE, Statistical Office of the Slovak Republic

DRONES ON THE RISE: TRANSFORMING MILITARY STRATEGIES AND ECONOMIES

Not only the Ukrainian front but also the experiences from the Nagorno-Karabakh War and conflicts in the Middle East are moving drones from a supplementary capability to the forefront as a new disruptive technology with the potential to change the way wars are fought and rewrite military doctrines. This is evident in the prominent position drones have gained among the prioritized capabilities at the EU level. Along with the capabilities of drones, their vulnerabilities are coming to the fore, and hand in hand with this, the importance of both drone development as well as counter-drone technologies is growing. In addition to the military and technological dimension, this undoubtedly also has an economic dimension. Data on the scope of the global military drones market vary, but even the more conservative estimates valued the global military drone market in 2023 at €12-15 billion, with significant growth expected in the coming years. The growth of the sector will be further driven by its expansion from traditional areas of aerial drones to ground, naval, and underwater drones, as well as the increasing versatility of drones, which is expanding from the originally predominantly ISR area into combat, search and rescue, or electronic warfare domains.

OPPORTUNITIES IN THE MIDST OF GEOECONOMIC TENSIONS

Geoeconomic fragmentation is driving the EU to take action by diversifying its trade partners and investment flows. This shift creates opportunities to engage with rapidly developing markets in regions such as Africa, Southeast Asia, and Latin America. A key tool in this strategy is eliminating trade barriers, promoting free trade and building partnerships. An example of this approach is the visit of the President of the European Commission to India in February, highlighting the EU's commitment to deepening strategic partnerships. The EU maintains preferential trade agreements with numerous countries worldwide, covering nearly 32% of its foreign trade. Since 2019, it has signed five new agreements (Vietnam, the UK, New Zealand, Kenya, Angola), while eight agreements have entered into force. Since January 2025, the EU has expanded or modernized existing agreements with several states (Mexico, South Korea, Singapore). These negotiations have initially been spurred by the EU's efforts to diversify supply chains and solidify post-Brexit economic ties, coupled with a worldwide focus on trade resilience. Now they can become part of the answer to US protectionism.

GEOCALENDAR Q2/2025

4 April 2025	**First EU-Centra Asia Summit in Samarkand, Uzbekistan**
28 April 2025	**Federal Election in Canada**
16 May 2025	**Meeting of the European Political Community in Albania**
19 May 2025	**EU-UK Summit in London, UK**
03 May 2025	**Federal Election in Australia**
4 - 18 May 2025	**Presidential election in Romania**
18 May - 1 June 2025	**Presidential election in Poland**
28 May 2025	**OPEC and non-OPEC Ministerial Meeting**
15-17 June 2025	**G7 Leader´s Summit in Kananaskis, Canada**
24-26 June 2025	**NATO Summit in The Hague, Netherlands**
26-27 June 2025	**European Council**

THE NUMBER OF REGIONAL TRADE AGREEMENTS IN FORCE

- In 2023, trade made up 96% of the EU's GDP, showing just how deeply connected the EU is to global markets.
- World trade accounted for 59% of its GDP.
- The EU's exports of goods and services made up 51.9% of its GDP, while the global average was much lower, at 29.3% of GDP.

Source of data: World Trade Organisation

SCENARIOS

The objective of the following scenarios is not to predict the future, but to explore a range of plausible alternative futures and identify challenges and opportunities to stimulate discussion on possible consequences of the decisions made today.

The following **security development scenarios** use the success or failure of the EU's efforts to strengthen its defence capabilities as the main change driver.

ACHIEVING EU STRATEGIC AUTONOMY

In this scenario, the key assumption is the successful revitalization of European defence. While this success can bring positive momentum, it may also introduce new tensions into transatlantic relations. Therefore, the full success of this scenario would require an additional layer: a new level of cooperation in the North Atlantic area.

The EU's success could be further amplified if quantitative improvements are complemented by qualitative advancements. That would mean that the upcoming revitalization of the EU's defence technological and industrial base is upgraded by the rapid integration of new technological trends. This would include the overall transformation of armed forces to adapt to new conditions that have the potential to reshape military doctrines, such as automation, drones, AI integration, and advanced cyber capabilities.

A key prerequisite for success will be finding a meaningful balance between sovereignty and efficiency, not only in defence but also in related foreign policy and fiscal matters. Progress in the defence sector could also help the EU to offset some of the negative consequences of current global economic turbulence. Additionally, it could pave the way for a new form of strategic cooperation between the EU and the UK.

MULTIPOLAR CONFRONTATION

This scenario represents a combination of potential military-technological success and simultaneous political failure of European efforts. It could materialize if the revitalization of the EU defence industry fails to be accompanied by the consolidation of transatlantic relations. Instead, the push for EU strategic autonomy could provoke resistance in Washington, further deepening divisions within NATO.

Such a development could eventually lead to an arms race, especially if other existing or emerging power centers respond to the EU's efforts with similar military expansions. Another critical risk factor could arise if escalating global tensions and military build-ups prevent the establishment of an adequate ethical and legal framework for the application of new disruptive military technologies. The absence of such a framework could have far-reaching and unpredictable consequences for the global security architecture.

FRAGMENTED IMPLEMENTATION OF EUROPEAN DEFENCE REVITALIZATION

Lack of consensus on defence transformation priorities or an absence of agreement on pooling of sovereignty could lead to a fragmented approach in implementing the EU's ambitions to strengthen its defence. This fragmentation could result in significant inefficiencies in resource allocation, further undermining an already weakened EU economy. Weak progress in bolstering EU defence could reinforce Washington's perception of Europe's declining strategic relevance, accelerating its shift in focus towards Asia and the Pacific. This would not only redirect U.S. military and financial resources but also push Washington to prioritize partnerships within the Indo-Pacific powers.

The absence of a cohesive European security vision may lead to further inefficiencies in defense spending, weakening the EU's crisis response capabilities and leaving it vulnerable to external threats. Russia, in particular, would exploit these European divisions to further erode EU unity. A deeply politically fragmented EU could ultimately have fatal consequences for the broader European project, undermining the EU's long-term stability and prosperity.

The following **economic development scenarios** use the continuation of the US administration´s tariff policies as the main change driver.

ESCALATING TRADE WAR GENERATING STAGFLATIONARY PRESSURES

This scenario assumes that the US will continue or intensify tariff measures, leading to reciprocal actions from China, the EU, and other major economies. Tariff measures could be followed by increased global competition in fields such as technologies or access to critical raw materials.

This would result in significant supply chain disruptions, a global trade slowdown with major impact on multinational corporations, manufacturing-heavy and export-reliant economies.

Inflationary pressures would rise as import costs increase, potentially leading to higher consumer prices and reduced global demand, which could ultimately trigger a global recession and partial de-dollarisation of global trade as countries would seek alternatives.

In this scenario, the fate of EU cooperation would be decided by the outcome of a contest between centrifugal tendencies favoring the protection of narrow national interests and pro-integration forces, which would see greater coherence as the only way to effectively safeguard European interests and strengthen the EU's position on the global stage.

GLOBAL TRADE REALIGNMENT LEADING TO A MULTITRACK WORLD

Businesses in this scenario would adapt by diversifying supply chains to avoid tariff-heavy regions. Nearshoring and regional trade agreements would gain in importance, reducing dependency on traditional global supply routes.

However, this may lead to a more fragmented global trade with the formation of clusters of states, each operating with its own supply chains, regulations and ecosystems. These clusters do not necessarily have to follow regional logic. They may be organised based on common values and beliefs (free trade vs protectionism).

EU might emerge as a leader of a pro-free-trade cluster of states promoting rules-based international trade. However, global trade would witness a departure from globalisation as only a few actors (either companies or states) could effectively operate in multiple clusters, and distrust would significantly undermine international trade and economic co-operation.

DE-ESCALATION & NEGOTIATED STABILITY

In this scenario, the US uses an *escalate-to-deescalate* strategy where tariffs are a negotiation chip or a punitive measure rather than a policy *per se*.

Combination of international pressure and domestic turbulence (inflationary pressures, financial markets disruption, economic stagnation), may ultimately push the US administration to engage in negotiations, leading to a more stable, though probably cautious and tense international trade environment.

Major actors may reach broader economic agreements (beyond tariffs) to balance competitiveness without triggering trade wars. These agreements can reduce uncertainty, encourage investments and international collaboration, leading to renewed economic growth. While tensions may remain in strategic sectors (technologies, critical raw materials), broader economic relations may improve.

COUNCIL of SLOVAK EXPORTERS

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EXPORT ANALYTICA