

# EMERGING MARKETS FORUM

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## BACKGROUND PAPER

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### MEASURING GEOGRAPHIC RE-GLOBALIZATION

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## MEASURING GEOGRAPHIC RE-GLOBALIZATION\*

Michael Blanga-Gubbay<sup>‡</sup>

Socrates Majune<sup>§</sup>

Victor Stolzenburg<sup>\*\*</sup>

### ABSTRACT

The world economy is facing a series of challenges including climate change, geopolitical tensions, and a lack of inclusiveness across and within economies. These challenges pose risks for global growth and international trade. Yet, international trade can also be an important part of the solution to them. As the World Trade Organization argues in its *World Trade Report 2023*, raising the participation of emerging markets and developing economies in world trade, or *geographic re-globalization* for short, could at the same time reduce inequality while also making the world economy more secure and sustainable. In this study, we examine recent progress in geographic re-globalization. To capture this progress, we look at a wide set of indicators such as regional shares in trade, import diversification and trade across and within geopolitical blocs. While we do observe some changes in trade flows consistent with geographic re-globalization, these are mostly spurious driven by factors such as surging energy prices. Instead, we observe fragmentation, the re-orientation of trade along geopolitical lines. While this trend could broadly benefit emerging markets and developing economies, it so far benefits only a small set of them. We show that this limited effect may be linked to the continuous presence of policy and structural barriers as well as rising policy uncertainty and an unfavourable macroeconomic environment that slows down geographic re-globalization.

**Keywords:** Re-Globalization; International Trade; Supply Chains; Resilience; Emerging markets and developing economies; Interdependence

**JEL Codes:** F10, F13, F14, F17

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\* The opinions expressed in this paper are those of the authors. They are not intended to represent the positions or opinions of the WTO or its members and are without prejudice to members' rights and obligations under the WTO. Any errors are attributable to the authors. This study is based on previous work by the authors, in particular Blanga-Gubbay and Rubínová (2023, 2024) and Majune and Stolzenburg (2024).

<sup>‡</sup> Economic Research and Statistics Division, World Trade Organization. E-mail: [michael.blanga-gubbay@wto.org](mailto:michael.blanga-gubbay@wto.org).

<sup>§</sup> Economic Research and Statistics Division, World Trade Organization. E-mail: [skmajune@uonbi.ac.ke](mailto:skmajune@uonbi.ac.ke).

<sup>\*\*</sup> Economic Research and Statistics Division, World Trade Organization. E-mail: [victor.stolzenburg@wto.org](mailto:victor.stolzenburg@wto.org).

## 1. INTRODUCTION

Over the past 15 years, the world economy has been subject to a series of crises. This comprises major global shocks such as the financial crisis of 2008 and 2009 or the COVID-19 pandemic as well as localized shocks such as the 2011 Tōhoku earthquake and tsunami or the current Red Sea crisis. While the scope and sources of these shocks vary, they all have led to significant disruptions to international trade flows. The uneven impact of some of these shocks across the income distribution within and across economies further laid bare that inequality is at historically high levels in many economies. This has contributed to a backlash against globalization, especially in advanced economies. Moreover, one set of crises, including the war in Ukraine and the trade conflict between China and the United States, is the result of rising geopolitical tensions that have put concerns over (over-)dependencies on certain trade partners for strategic goods to the forefront of the policy discussion.

A result of these different developments is that globalization is increasingly being seen by some as a source of risks rather than a source of resilience and shared prosperity. Terms like re-shoring, near-shoring or friend-shoring dominate the policy discussion on how to make supply chains more resilient, whereas efforts towards further trade liberalization are more muted. However, such a conclusion regarding the impact of globalization is not supported by the data. As the WTO (2023b) shows in its *World Trade Report 2023*, international trade, aided by certainty provided by the multilateral trading system, continues to be a source of resilience. To reinforce this role, the evidence suggests that re-globalization is the most promising path with re-globalization being defined as "extend[ing] trade integration to more people, more economies, and more issues" (WTO, 2023, p. 22). The reason for this is that an inclusive globalization that covers new topics, such as trade in digital or environmental products, and that integrates a broader set of economies and people within these economies provides the flexibility that is required to respond to unexpected shocks and to address global challenges like climate change.

In this study, we assess if the world economy has made progress in re-globalizing with a focus on the question whether there has been an integration of more economies into the global trading system, which we refer to as geographic re-globalization. We examine different indicators and apply different methodologies to identify patterns of diversification, especially towards economies that have been at the margins of globalization so far.

We find that there are indeed visible shifts in world trade that could be consistent with geographic re-globalization. For instance, indicators of market concentration have declined, and market shares in global trade have shifted towards emerging and developing economies. In addition, major economies such as the European Union or the United States source from a larger set of trade partners. However, a closer look at the data reveals that this evidence shows at most very limited progress in geographic re-globalization. We find, for example, that falling market concentration and rising trade shares of developing economies are driven, at least in part, by a compositional effect related to surging energy prices rather than actual diversification.

Instead, we observe that the data so far shows primarily fragmentation, a reorientation of trade and investment along geopolitical lines, partly linked to the decoupling of China and the United States. While this does contribute to diversification to some extent, the primary beneficiaries of European and US diversification efforts are economies that are already well integrated into the global trading system, such as Canada, Hungary, Mexico, or Viet Nam. As a result, diversification benefits in the aggregate are limited as no new players have been able to gain significant market shares. We then discuss potential reasons for these findings and highlight that the continuous presence of policy and structural barriers as well as rising policy uncertainty and an unfavourable macroeconomic environment are important deterrents of geographic re-globalization.

This study is organized as follows. Section 2 presents first evidence on shifts in world trade concluding that the data cannot be taken as strong evidence for geographic re-globalization. Section 3 discusses policy and structural factors that may slow down geographic re-globalization efforts. Section 4 concludes.

## **2. IS THE WORLD RE-GLOBALIZING GEOGRAPHICALLY**

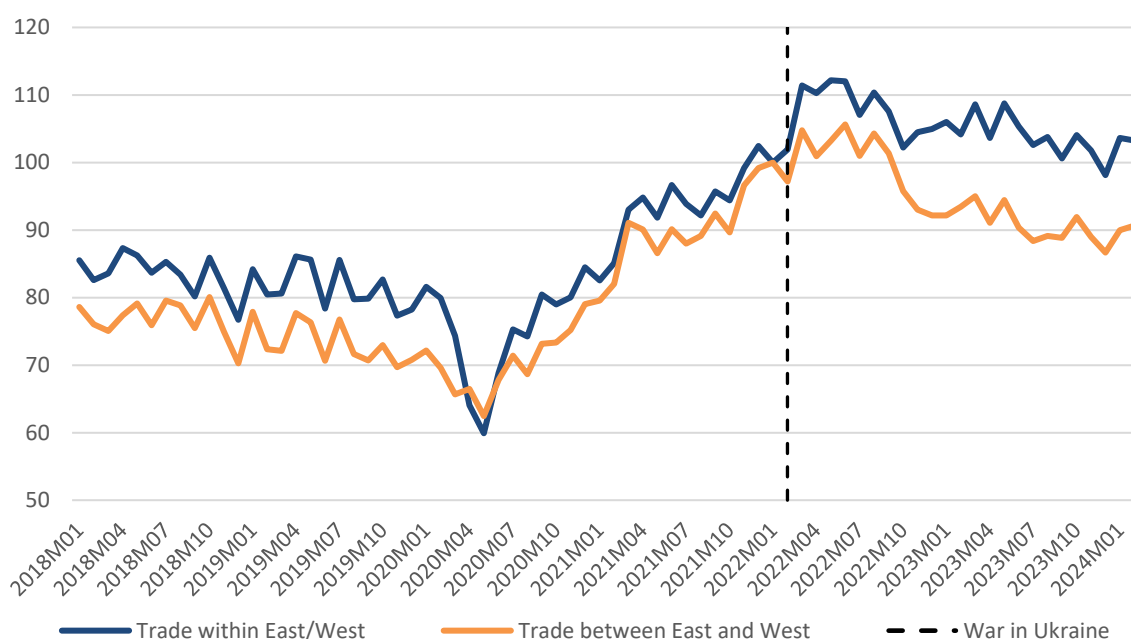
In this section, we first look at recent trends in the geographical reorientation of international trade. In particular, we examine the most recent evidence on fragmentation and the decoupling between China and the United States. This is important because such shifts may give rise to geographic re-globalization if they benefit economies that have been at the margins of trade so far. Having established that fragmentation and US-China decoupling appear to be persistent phenomena, we then analyse whether this has led to a diversification of international trade and geographic re-globalization. We do not find strong evidence in this regard. Instead, the main beneficiaries of the current reorientation of trade are economies already well-established within the trading system. That said, we do find that many of these beneficiaries are emerging markets and developing economies (EMDEs).

### **a. Re-examining recent trends: the fragmentation of trade**

To assess whether there is evidence of geographic re-globalization, it is helpful to examine recent geographic shifts in world trade that have already been established. The *World Trade Report 2023* shows, based on research by Blanga-Gubbay and Rubínová (2023), that since the onset of the war in Ukraine trade flows are increasingly subject to political fragmentation, i.e. trade has become increasingly sensitive to political alliances. Looking at trade between hypothetical blocs composed of economies holding similar political views, established based on voting patterns in the United Nations General Assembly and labelled as East and West, the report shows that in 2022 and early 2023 such trade has grown more slowly than trade within these blocs. In a forthcoming study, Blanga-Gubbay and Rubínová (2024) update this work and find that this trend has continued since early 2023. Figure 1 illustrates this by highlighting the persistent rift between trade within politically blocs versus trade across those blocs.

This trend has so far been limited to the least complex products, these are products that do not require customization and can be produced in many economies, and where alternative suppliers are relatively easy to find.<sup>1</sup> Fragmentation in more complex products may occur with a lag; in order to diversify sources for products that are complex to manufacture and produced by very few countries, additional investments are necessary. We might expect to see this trend emerging in the future, as indicated by data showing early stages of fragmentation in foreign direct investment (FDI).

**Figure 1: Trade between geopolitically non-aligned blocs grew slower than trade within the blocs**



**Source:** Blanga-Gubbay and Rubínová (2024), based on Trade Data Monitor.

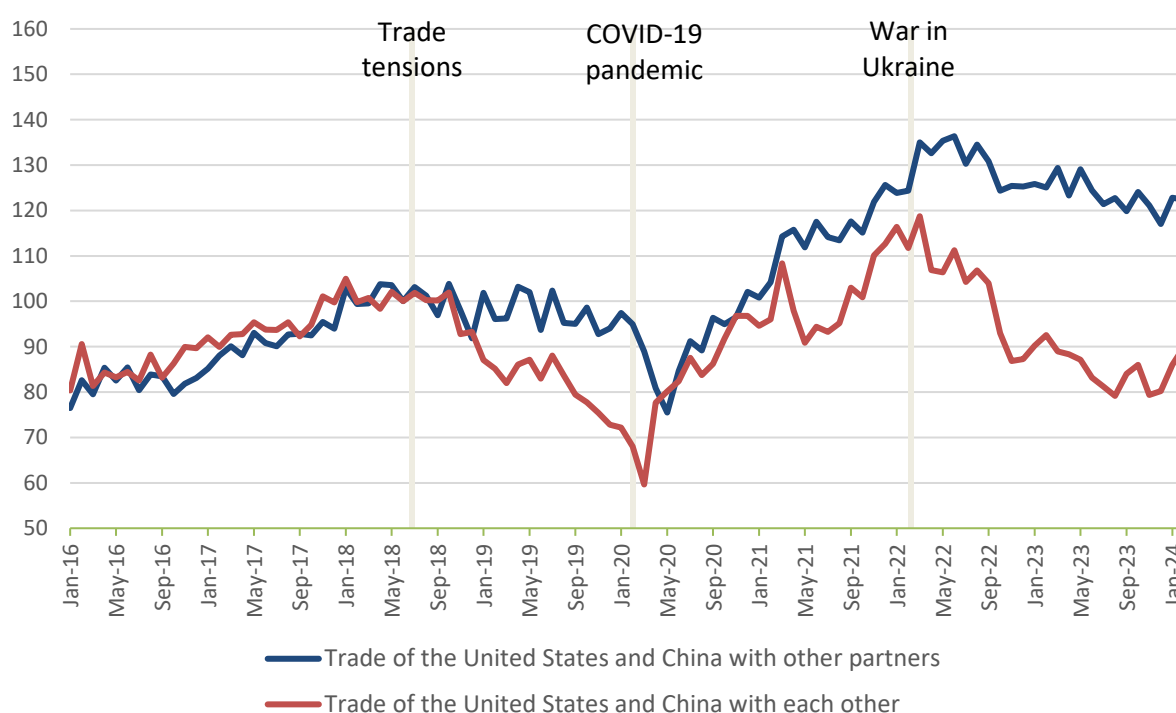
**Note:** Seasonally adjusted series. Russian Federation, Belarus and Ukraine are excluded. Left-hand series indexed at 100 in January 2022. Right-hand series indexed at 0 in January 2022.

An important driver of fragmentation is the gradual decoupling in trade of China and the United States. The trade tensions between China and the United States in 2018 and 2019 resulted in reciprocal tariff increases, with the U.S. imposing an average duty of 19.3% on imports from China, and China imposing an average duty of 21.1% on U.S. imports. These tariffs covered over 66% of Chinese exports to the U.S. and 58% of U.S. exports to China (Bown, 2023). Surprisingly, despite these increased trade barriers, trade between the two economies reached a record high of \$690.6 billion in 2022, suggesting that the tariffs may not have significantly affected the decoupling of their economies.

<sup>1</sup> Complexity captures both the ubiquity and the sophistication of a product. Products are divided into four interquartile groups based on their complexity, defined by the Product Complexity Index (Hausmann et al., 2013).

However, a comparison of trade flows between the two economies and their trade with other partners clearly indicates that the United States and China have been decoupling (see Figure 2). Blanga-Gubbay and Rubínová (2023) recently illustrated that bilateral trade between the United States and China – when compared to their trade with other partners - grew approximately 26 per cent slower since the onset of trade tensions, with an additional slowdown of 19 per cent following the war in Ukraine. These results align quantitatively with recent studies showing that trade tensions had an impact on trade patterns (Freund et al., 2023).

**Figure 2: There are strong signs of decoupling between US and China**

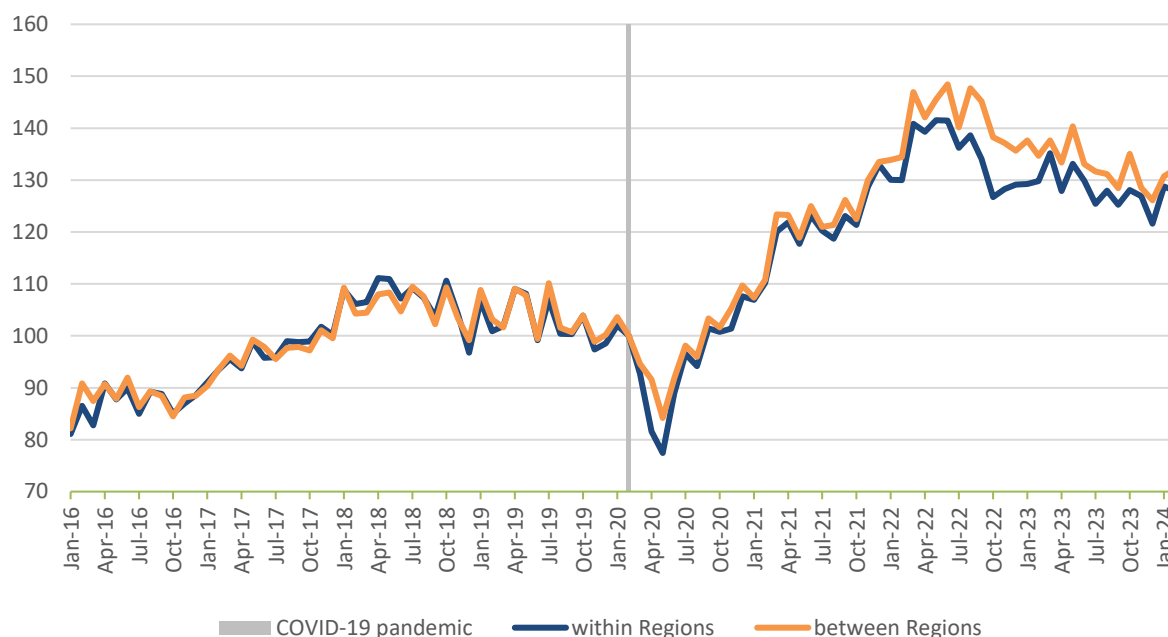


**Source:** Blanga-Gubbay and Rubínová (2024), based on Trade Data Monitor.

**Note:** Seasonally adjusted series. Russian Federation, Belarus and Ukraine are excluded. Series indexed at 100 in June 2018.

Finally, despite expectations that recent geopolitical tensions and the disruptions caused by the COVID-19 pandemic would lead to an overall trend toward regionalization of global trade or near-shoring, the data do not support this narrative. The results reported in Figure 3 indicate no evidence of near-shoring or a significant regionalization of global value chains following the pandemic. In fact, Africa’s intra-regional trade has grown even more slowly than its extra-regional trade since the COVID-19 pandemic. This highlights Africa's dependency on the rest of the world, particularly in times of global shocks. The trend in Africa appears to be driven by complex products, reflecting increased imports of vaccines and medical equipment during the pandemic, rather than any shift toward regional sourcing.

**Figure 3: Despite talks of nearshoring, there are no increasing trends in regionalisation**



**Source:** Blanga-Gubbay and Rubínová (2024), based on Trade Data Monitor.

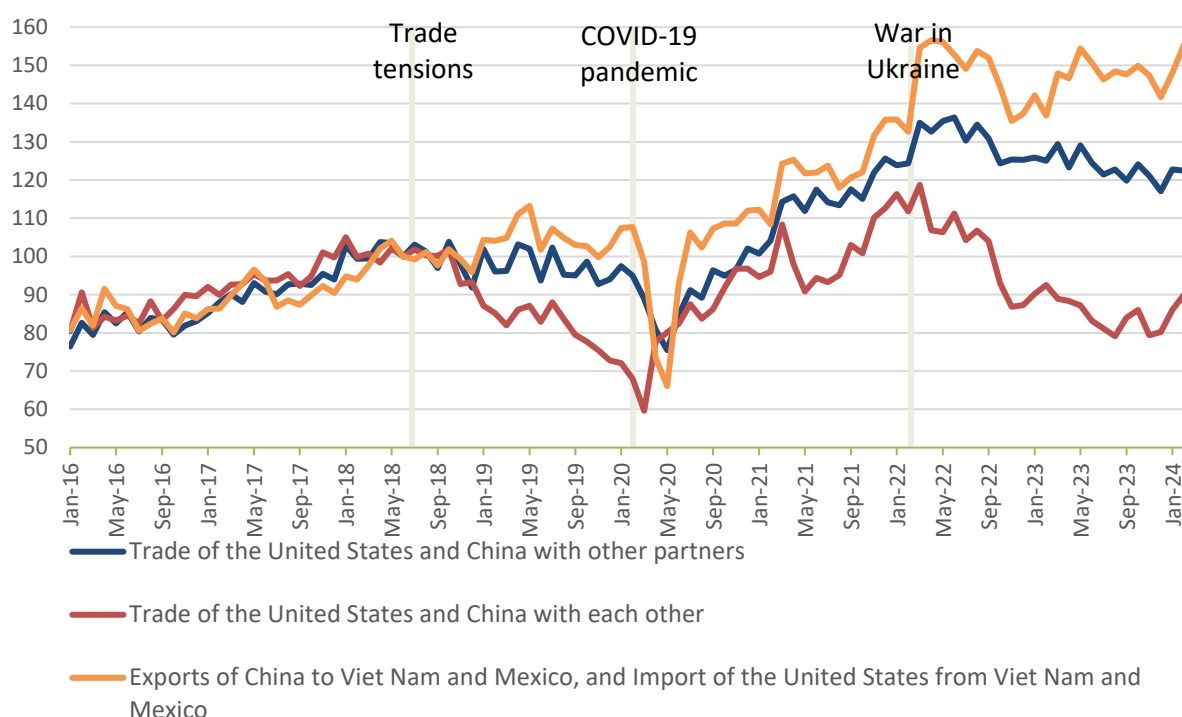
**Note:** Seasonally adjusted series. Russian Federation, Belarus and Ukraine are excluded. Series indexed at 100 in February 2020.

### b. Does fragmentation lead to geographic re-globalization?

Fragmentation can lead to geographic re-globalization if economies start sourcing from new suppliers, especially if those new suppliers have had limited trade participation beforehand. Such a shift would make trade more inclusive by distributing trade participation more evenly across the globe, and it would make trade more resilient by building a more diversified network that is less exposed to regional shocks. We consider such a scenario in so far likely as there is no evidence of nearshoring and because fragmentation occurs so far mainly in non-complex products, which can be produced by a large set of EMDEs.

To determine whether fragmentation has led to geographic re-globalization, we first look at studies that examine which economies have benefitted from US-China decoupling. Different papers discuss the emergence of Mexico and Viet Nam as "connecting" economies in the restructuring of global supply chains serving the U.S. market (see e.g. Alfaro and Chor, 2023; Ouyang and Shi, 2024). This is also illustrated in Figure 4, which replicates Figure 2 but with Chinese exports to Mexico and Viet Nam and U.S. imports from the same economies drawn separately. Trade with these two economies evolved in tandem with the rest of the world with only a minor uptick after the start of the trade tensions. However, since the onset of the war in Ukraine, trade with these two economies has significantly outpaced not only the China-U.S. bilateral trade but also their trade with other economies. Other sources cite the USMCA partner Canada along with India, Malaysia, Singapore,

**Figure 4: Decoupling between US and China and the potential mitigating role played by "connecting" economies**



**Source:** Blanga-Gubbay and Rubínová (2024), based on Trade Data Monitor.

**Note:** Seasonally adjusted series. Russian Federation, Belarus and Ukraine are excluded. Series indexed at 100 in June 2018.

and Thailand as economies that both have increased their imports from China and their exports to the United States.<sup>2</sup>

The emergence of connecting economies does to some extent help diversify trade and could be considered as initial geographic re-globalization. In line with this, Majune and Stolzenburg (2024) find that the relatively large share of China in the trade of highly concentrated products dropped from 38.5 per cent in 2015 to 35.9 per cent in 2022. In contrast, the shares of many EMDEs expanded, with, for example, Brazil gaining 58 per cent, Indonesia gaining 40 per cent and Viet Nam gaining 18 per cent. However, and not fully surprisingly, the beneficiaries of U.S.-China decoupling are economies that are already well integrated into the global trading system. Their existing trade networks and established supply chains enable them to adapt more quickly to shifts in demand and sourcing patterns, positioning them favourably in this evolving landscape. This means though that these trade reorientations are unlikely to substantially enhance global value chain resilience or lead to meaningful diversification as they fail to broaden the set of available suppliers.

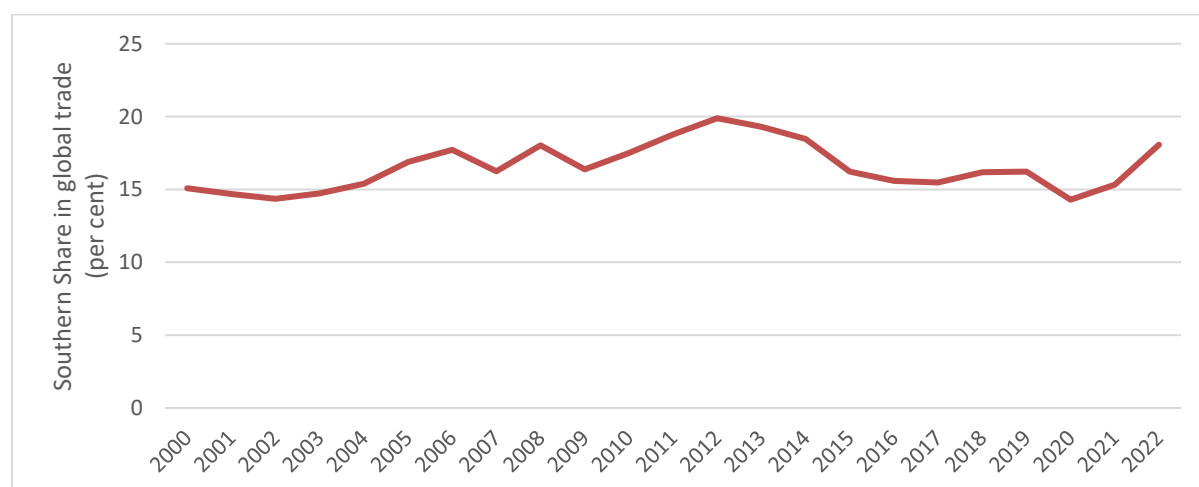
<sup>2</sup> See e.g. Nomura (May, 2024): The great reshuffle in global supply chains. Available at: <https://www.nomuraconnects.com/focused-thinking-posts/the-great-reshuffle-in-global-supply-chains/>.



To verify whether fragmentation mainly benefits economies that are well-integrated into the trading system or whether this is limited to US-China decoupling, we next compute several indicators that can capture geographic re-globalization more broadly. We begin by examining the simplest indicator available, namely regional shares in trade. While geographic re-globalization encompasses shifts in trade shares to any economy that has a relatively limited share in trade, we focus here on the trade share of the three regions that have historically had the lowest level of trade integration and are home to the majority of EMDEs: Latin America and the Caribbean (LAC), Middle East and North Africa (MENA), South Asia (SA), and Sub-Saharan Africa (SSA), which we refer to as *South* for simplicity. These regions' trade share is compared to the combined share of East Asia and Pacific (EAP), Europe and Central Asia (ECA), and North America (NA), which we refer to as *North*. The North here comprises the three regions that are typically called Factory Asia, Factory Europe, and Factory North America in the analysis of global supply chains (see e.g. Baldwin, 2013), which further illustrates their dominant position in international trade and the importance of shifting trade towards other regions to achieve a more diversified trading system for resilient supply chains.

To do the analysis, we obtain import data from UN Comtrade for the period between 2000 and 2022, the latest year available with near global coverage. Figure 5 shows that the trade share of the South has indeed expanded in recent years. Relative to its recent trough in 2020, it increased by almost 30 per cent from 14.3 per cent to 18.1 per cent. However, we find that this is mostly a compositional change. We re-calculate the regional trade shares but remove trade in mineral fuels and related products due to the importance of mineral fuel exports for some of the economies in the South and due to the sharp increase in the share of mineral fuels in global trade in 2022, which grew by 45 per cent driven by rising energy prices. Accounting for this cuts the growth of the Southern share by approximately half. Moreover, even when including mineral fuels, Figure 5 shows that South's current peak is still below its all-time peak in 2012 when it accounted for 19.9 per cent of trade. This suggests that, overall, the reorientation of trade has only led to limited gains for the South.

**Figure 5: A rising trade share of the South in recent years**



**Source:** Authors' calculations based on UN Comtrade.

**Note:** South: LAC, MENA, SA, and SSA; North: EAP, ECA, and NA.

Aggregate trade shares might be subject to confounding factors, such as compositional changes. Hence, we proceed by computing more detailed diversification indicators for the global economy. To do so, we move to data at the bilateral product level.<sup>3</sup> The simplest measure to capture diversification is a count of the average number of partners an economy imports individual products from.<sup>4</sup> This measure has steadily trended upwards as can be seen in Figure 6. The average number of import partners for a given product has increased by 55 per cent over the 23-year period analysed. It now stands at 31, up from 20 in 2000. This global trend is in line with evidence for some of the biggest economies. The ECB reports for instance that the average number of trade partners has increased considerably for both the Euro Area and the United States (Ilkova, Lebastard, and Serafini, 2024).

However, a closer look at the data suggests that the increase in the average number of trade partners is not a sign for geographic reglobalization. We re-calculate the average number of trade partners but drop very small partners from the count. To be precise, we drop partners that supply less than 1 per cent of total imports since we consider that such suppliers are unlikely to have the capacity to significantly increase their exports in the short run if a major supplier faces a shock. When doing this, we find that the average number of trade partners has in fact remained remarkably stable over time rather than increase. This finding holds both for the world overall and for some of the largest trading economies (see Table 1). This means that the increase in the average amount of trade partners we observe in Figure 6 is driven entirely by small transactions that are unlikely to increase resilience or amount to meaningful diversification towards new partners.

An economy can diversify its import patterns not only by importing from a larger set of economies but also by shifting imports from a dominant supplier towards smaller suppliers. To capture this, we establish Herfindahl–Hirschman Indices (HHIs) at the economy–product level. HHIs are a measure of market concentration. The HHI is able to capture both forms of diversification since it is equal to the sum of the squared market shares across all suppliers of a given product to a given economy.<sup>5</sup> By taking the square of the market shares, the HHI puts more weight on large suppliers and, thereby, accounts for patterns where a small number of suppliers account for the majority of the market and by summing across the market shares of all suppliers it also accounts for increases in the number of suppliers.

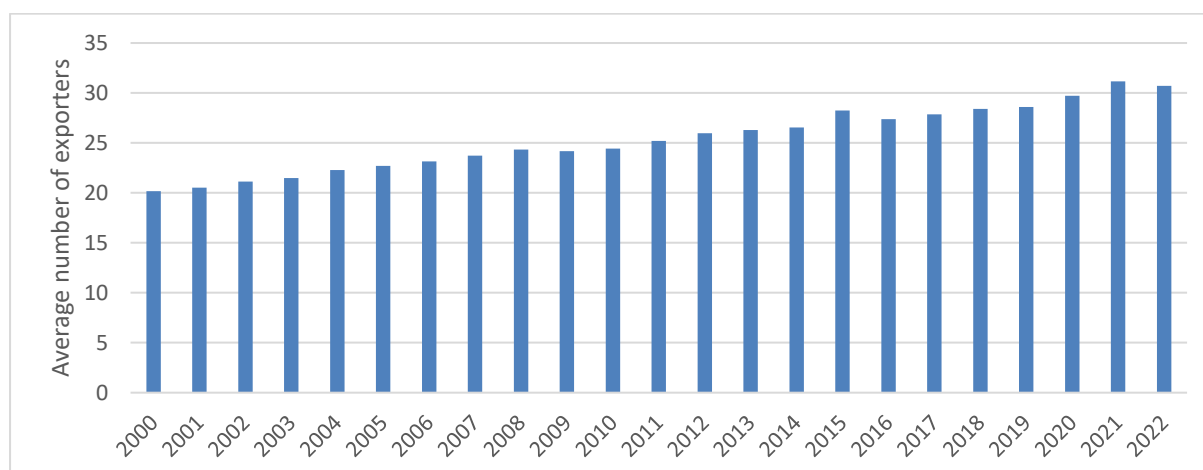
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<sup>3</sup> As product-level, we define goods classified at the 6-digit level of the Harmonized Commodity Description and Coding System (HS) as is common in the literature.

<sup>4</sup> Formally, we calculate the average number of exporters across all importers and products as  $(\sum_{k=1}^K \sum_{i=1}^I C_{ikt}) / (K * I)$  where  $C_{ikt}$  is the number of exporters an importer imports a product from.

<sup>5</sup> Formally, the HHI for a product  $i$  in importer  $k$  in year  $t$  is defined as  $HHI_{ikt} = \sum_{s=1}^S (MS_s)^2$ , where  $MS_s$  is the market share of supplier  $s$  in the imports of product  $i$  in economy  $k$ . To provide a hypothetical example, if the Republic of Korea were to supply 80 per cent of semiconductors to Chile and Japan 20 per cent, then the HHI for semiconductor imports of Chile would be a relatively high  $(0.8)^2 + (0.2)^2 = 0.68$  due to the large share of imports coming from a single supplier and due to the small number of suppliers. If, in contrast, Chile would have a diversified sourcing pattern in semiconductors from 10 economies that each provide 10 per cent of imports, its semiconductor HHI would be a low 0.1.

**Figure 6: The average number of exporters that economies import from increases**



**Source:** Authors' calculations based on UN Comtrade.

**Note:** The figure depicts the number of exporters of a given product to a given economy, averaged across all importers and HS 6-digit products.

**Table 1: The number of relevant trade partners does not increase over time**

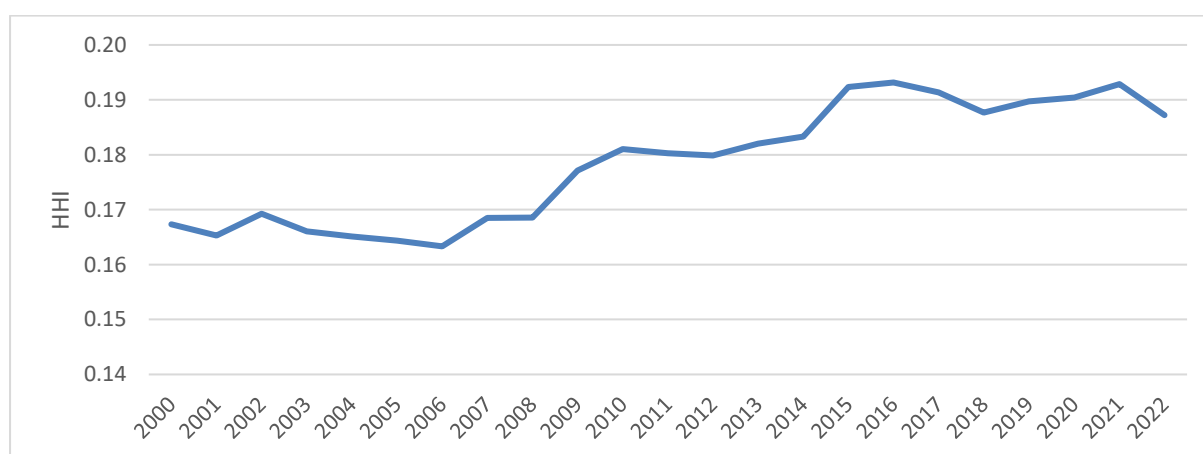
	Trade partners (overall)				Trade partners (market share > 1%)			
	World	USA	EU	China	World	USA	EU	China
2000	20	38	46	22	7	10	9	8
2001	21	39	47	23	7	10	9	9
2002	21	40	47	25	7	10	9	9
2003	21	40	47	26	8	10	9	9
2004	22	41	48	28	8	10	9	9
2005	23	42	49	29	8	10	9	9
2006	23	42	50	30	8	10	9	9
2007	24	43	51	32	8	10	9	9
2008	24	42	51	33	8	10	9	9
2009	24	41	51	33	8	9	9	9
2010	24	42	52	35	8	9	9	9
2011	25	43	52	35	8	9	9	9
2012	26	43	52	36	8	9	9	9
2013	26	43	53	36	8	9	9	9
2014	27	43	53	37	8	9	9	9
2015	28	44	53	37	8	9	9	9
2016	27	45	53	38	8	10	9	10
2017	28	46	52	39	8	10	9	9
2018	28	46	52	41	8	10	9	10
2019	29	45	51	40	8	9	9	9
2020	30	45	47	41	8	10	9	9
2021	31	47	47	41	8	10	9	9
2022	31	48	46	40	8	10	9	9

**Source:** Author's calculations based on UN Comtrade.

**Note:** The table lists the average number of economies an economy sources a given product from. On the right hand side, only partners are counted that supply at least 1 per cent of the total imports of that product to the economy.

Figure 7 shows that index rose between 2006 and 2016 by almost 20 per cent from 0.163 to 0.193. This signals more concentration as opposed to diversification. The index stabilized thereafter and in 2022 dropped back to 0.187, its lowest level since 2015. However, as the concentration index is a weighted average across all products, it might change because of a fall in concentration for individual products or because of a shift in trade towards more diversified products. When decomposing the change into these two components we find that the fall is entirely driven by a shift towards diversified products, most importantly mineral fuels. In contrast, concentration has increased for the average product reinforcing that the data do not support geographic re-globalization so far.

**Figure 7: The average concentration of imports has fallen recently**



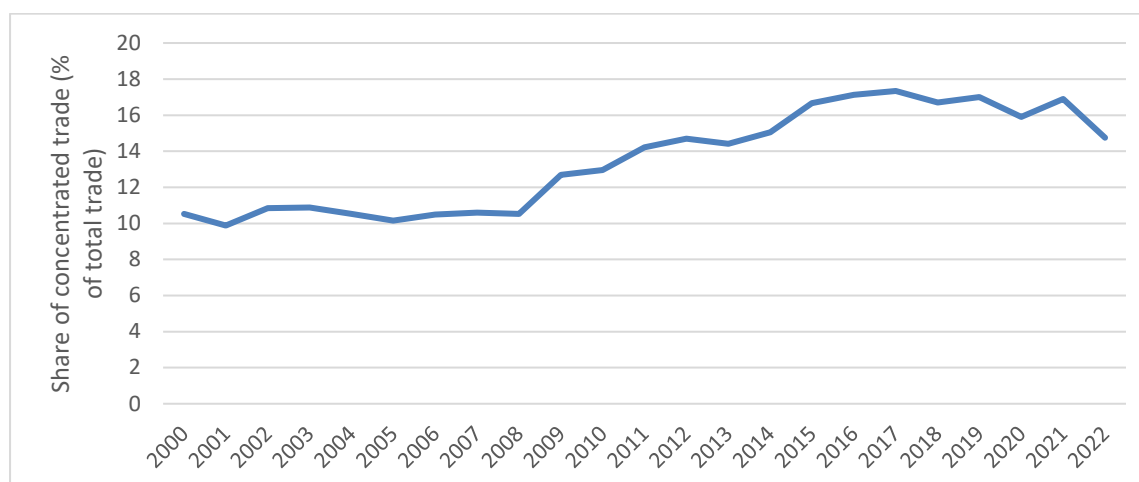
**Source:** Authors' calculations based on UN Comtrade.

**Note:** The figure depicts the weighted average HHI across all HS 6-digit products and economies from 2000 to 2022. The HHI captures concentration of imports at the economy-product level across different exporters. Exporters with a market share below 1 per cent are excluded.

The finding of increased concentration is in line with work by Majune and Stolzenburg (2024) on potential bottlenecks in international trade. They propose an index that captures the share in global trade of products with a highly concentrated market structure.<sup>6</sup> Figure 8 shows that this index developed very similar to the average concentration of imports rising substantially between 2008 and 2017 before stabilizing and falling by a considerable 12 per cent in 2022, reaching levels last seen in 2014. Here again, we find that the fall in the share of concentrated trade is mainly due to a shift in trade shares towards the relatively diversified mineral fuels rather than actual geographic re-globalization. In fact, the number of products which the methodology identifies as highly concentrated has increased by almost 10 per cent from 1057 in 2021 to 1153 in 2022.

<sup>6</sup> Majune and Stolzenburg (2024) define trade of a product as concentrated if its export market shares exhibit an HHI higher or equal to 0.25. This is the case if there are only four or less exporters of a good, or if there are more than four exporters but a maximum of three exporters dominates the market. This follows a definition by the US Department of Justice which considers industries whose sales across firms exhibit an HHI higher or equal to 0.25 as highly concentrated. Majune and Stolzenburg (2024) further exclude products with very low trade values.

**Figure 8: The share of trade in highly concentrated products has fallen recently**



**Source:** Majune and Stolzenburg (2024).

**Note:** The figure depicts the share of trade considered concentrated as defined in Majune and Stolzenburg (2024).

We conclude this section by discussing evidence based on foreign direct investment (FDI), which acts as a leading indicator for trade. Changes in FDI have the potential to reinforce fragmentation trends in the near future. The IMF (2023) recently highlighted that also FDI is becoming increasingly concentrated among geopolitically aligned economies. Recent evidence also shows though that FDI fragmentation is limited in scope, occurring selectively in industries with strategic value, such as computer manufacturing and information and communications. This seems to reflect a targeted response to national security policies rather than a broad disintegration of investment ties between non-aligned economies (Tan, 2024)

Importantly, as observed for trade, the shift in FDI has mainly benefited economies that are already well-integrated into the global trading system. U.S. outward FDI has shifted from China to advanced Europe, Central America and other parts of Asia (Tan, 2024). For example, Costa Rica – which has a Free Trade Agreement with the U.S. – recently attracted \$1.2 billion in new INTEL investments. Other evidence shows that Chinese outward FDI is also shifting towards established traders, with increasing investments in Mexico and Central and Eastern Europe (CEE).<sup>7</sup> This suggests that our findings on the impact of fragmentation for geographic re-globalization are likely to grow stronger as these investments lead to future trade flows.

To sum up the findings this far, we observe that with fragmentation there has been a recent shift in world trade that could lead to geographic re-globalization. However, a wide set of indicators shows that this is not the case. Trade is on average not more diversified than prior to the onset of fragmentation and neither did economies increase the number of relevant partners that they source

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<sup>7</sup> The Economist, (September 19<sup>th</sup>, 2024): "Near-shoring is turning eastern Europe into the new China" <https://www.economist.com/europe/2024/09/19/near-shoring-is-turning-eastern-europe-into-the-new-china>

a given product from. The reason for this is that these changes in trade flows have mainly shifted trade among economies that are already well-integrated into the global trading system. Some of these economies are EMDEs and, hence, these shifts can be considered as initial geographic re-globalization as they help close some of the inequities in the global trading system. At the same time, they fail to broaden participation in trade across a larger set of economies.

### **3. WHY HAS RE-GLOBALIZATION REMAINED LIMITED SO FAR**

In this section we highlight some factors that can contribute to explain the limited evidence for a broad geographic re-globalization. The findings so far have highlighted that shifts in trade are limited both sectorally, targeting sectors with low sunk costs or high policy exposure, and geographically, targeting economies with established trade networks. We consider that potential reasons for these trends are a challenging macroeconomic and policy environment as well as a lack of progress in addressing structural issues such as high trade costs.

A large literature illustrates how uncertainty about future trade policies or the business environment can deter investment and affect trade flows (see e.g. Handley and Limão, 2022). Research also suggests that uncertainty can cause firms to invest in economies that already host similar firms. Larch and Navarro (2023) develop a model where only the most productive firms invest in new foreign locations in light of high uncertainty. All other firms use the information revealed by this initial investment and follow to the same location or avoid investing. The authors then confirm the model's predictions using firm-level data from Colombia. Such a pattern is in line, for instance, with large investments into Viet Nam by numerous firms following Samsung's setting up of production there or FDI into Costa Rica following Intel's initial investment. Ragoussis et al. (2024) further show that uncertainty has led to a growing concentration of cross-border investments among a few multinational firms.

Uncertainty as a driver of firm decisions is particularly relevant now because measures of trade policy uncertainty are rising, and measures of economic policy uncertainty remain at elevated levels. Figure 9 shows two commonly used measures of economic and trade policy uncertainty based on newspaper mentions of various terms capturing such policy uncertainty. Both measures are at historically high levels and have been elevated throughout the recent period. The most recent data further indicates a renewed surge in uncertainty which, according to the literature, will make a broad geographic re-globalization less likely in the near future.

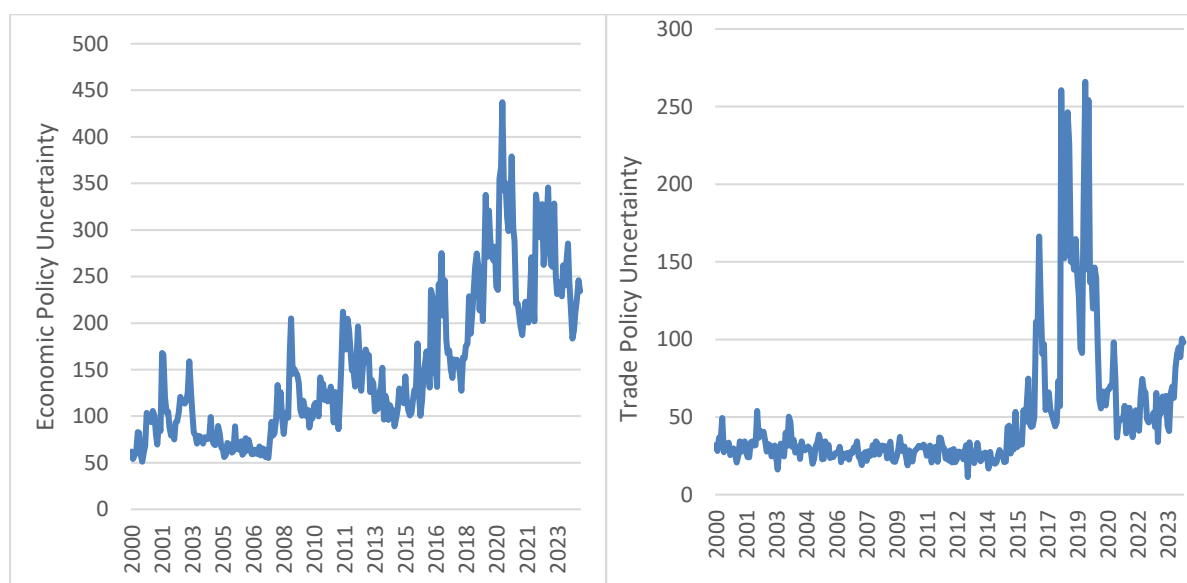
One reason for heightened trade policy uncertainty is an increase in unilateral measures that cause concern among trading partners. WTO members can bring forward such concerns in various committees. Data on such concerns, which mention for instance China's export restrictions on gallium and germanium, the European Union's Deforestation Regulation, Indonesia's export restrictions on raw materials, or the United States' Inflation Reduction Act, indicates a clear uptick in recent years. The total number of concerns increased by a factor of seven between 2000 and

2022 before slightly decreasing in 2023 (see Figure 10). In fact, the trend in trade policy concerns looks fairly similar to the trend in policy uncertainty.

High policy uncertainty coincides with and relates to an increasingly challenging macroeconomic environment. While inflation has been coming down recently, interest rates remain high in many advanced, emerging and developing markets compared to most of the period since the financial crisis of 2008/2009 (see Figure 11). This has an impact of rising debt levels in EMDEs. Central governments in EMDEs have increased debt issuance from USD 3.0 trillion in 2022 to USD 3.9 trillion in 2023, surpassing the 2021 peak of USD 3.2 trillion (2024). These developments might further deter broad geographic re-globalization, not least due to the higher financing costs of new investments that high interest rates entail.

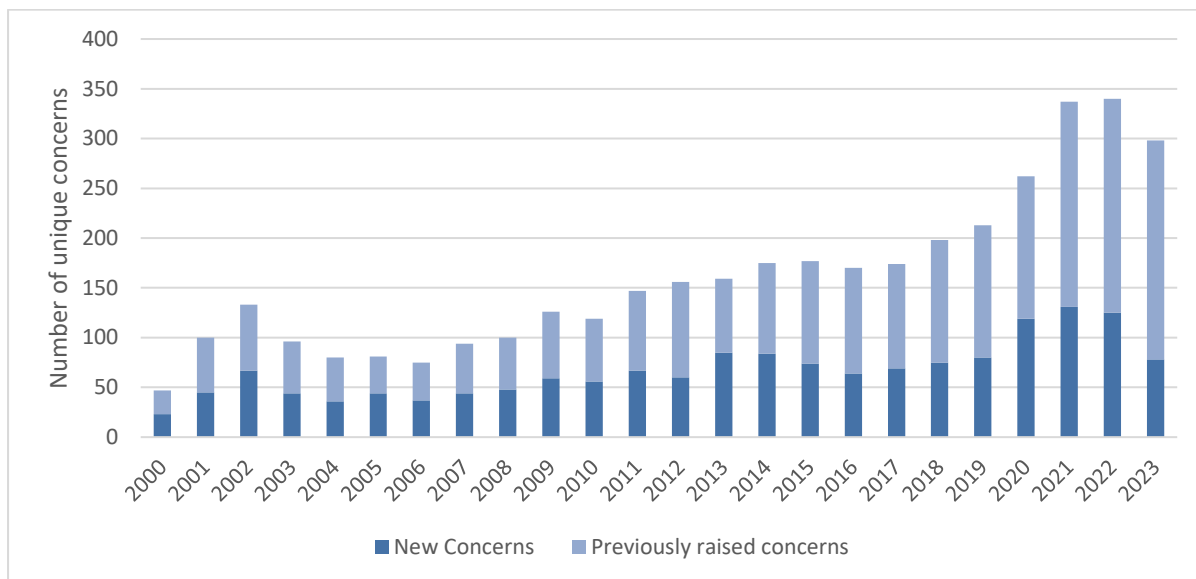
Another relevant issue holding back geographic re-globalization are existing structural and policy barriers. The *World Trade Report 2023* highlights that trade costs remain substantially higher in EMDEs compared to advanced economies. The differences are caused by a combination of factors including infrastructure but also tariffs and non-tariff measures. Little progress has been made in this area according to recent WTO research highlighted in the *World Trade Report 2024* (WTO, 2024). Extending the WTO's composite trade cost indicator, which captures the cost of domestic trade relative to international trade, to 2020, the report finds for instance that trade costs in the services sector of least-developed economies (LDCs) were on average 50 per cent higher than in advanced economies. Even in upper middle income economies trade costs were still 12 per cent larger (see Figure 12).

**Figure 9: Economic and trade policy uncertainty remain elevated**



**Source:** Davis (2016) for Economic Policy Uncertainty and Caldara et al. (2020) for Trade Policy Uncertainty.

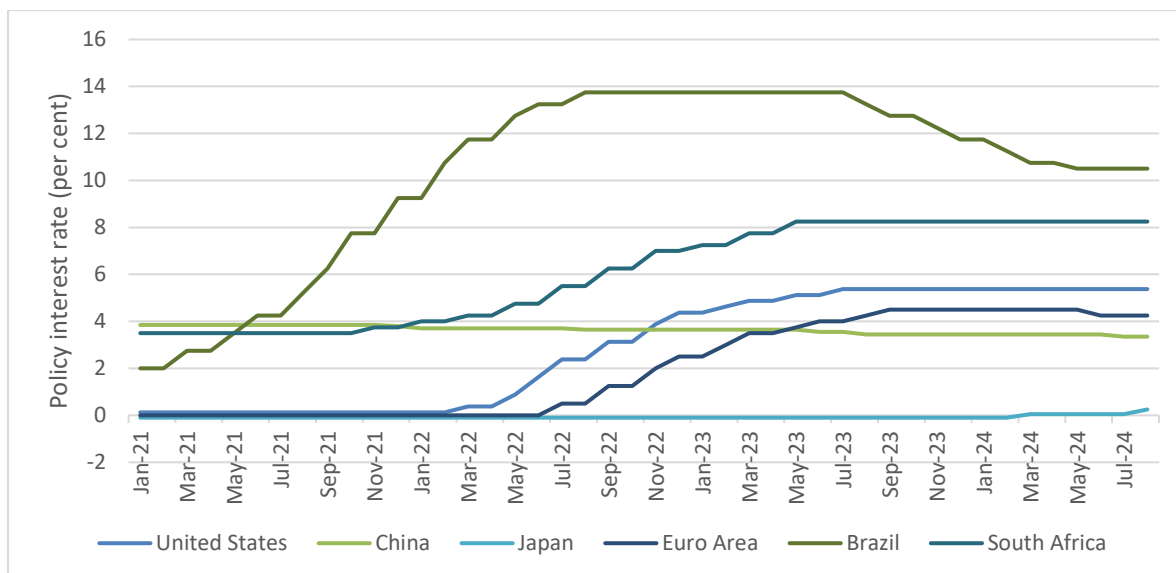
**Figure 10: Trade concerns raised at the WTO are increasing**



**Source:** WTO Trade Concerns Database.

**Note:** Trade concerns raised in the WTO's Council for Trade in Goods (CTG), Committee on Market Access (CMA), the Committee on Import Licensing (IL), the Committee on Sanitary and Phytosanitary Measures (SPS) and the Committee on Technical Barriers to Trade (TBT).

**Figure 11: Interest rates remain high in many economies**

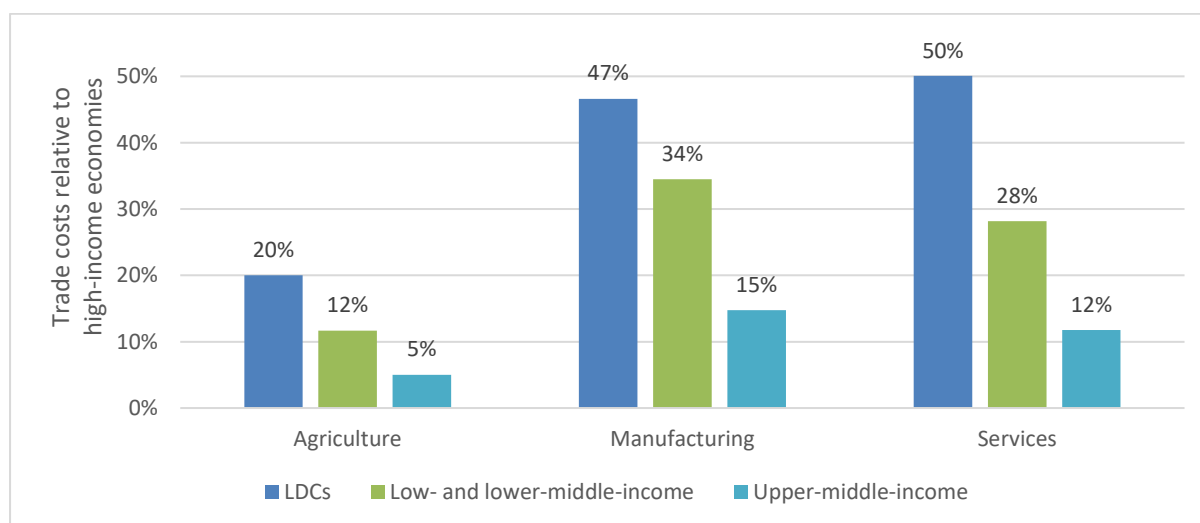


**Source:** Bank for International Settlements.



The *World Trade Report 2023* further argues that re-globalization encompasses not just the integration of more economies but also of more people and issues into the global economy, especially as these aspects are interlinked. The report shows for instance that global carbon pricing could unlock the so-called green comparative advantage of economies and shift economic activity towards EMDEs with relatively low costs of renewable energy production. Another issue is the limited access to digital tools in some EMDEs, which prevents their expansion in the fastest growing sector of international trade, digitally delivered services.

**Figure 12: Trade costs in EMDEs are substantially higher than in advanced economies**



**Source:** WTO (2024).

#### 4. CONCLUSION

In this study, we examine whether there has been a diversification of trade towards underrepresented economies, i.e. geographic re-globalization. We find, first, that the recent dominant trade in the geographic reorientation of trade, fragmentation, has persisted. Trade between geopolitical blocs continues to grow slower than trade within geopolitical blocs. Second, we find that fragmentation has not led to broad geographic re-globalization. Instead, fragmentation has given a boost to some EMDEs that help connect the different political blocs. This does contribute to diversification but the effect is limited as the beneficiaries are all well-established economies in the global trading system. We also observe that investment data might signal that these trends to grow stronger as many connecting economies continue to receive large FDI inflows. Third, we discuss that a challenging macroeconomic environment and structural and policy barriers are preventing a broader geographic re-globalization at the moment.

We consider that, despite these obstacles, the current shifts in trade continue to offer an opportunity to EMDEs that remain at the margins of the global trading system. Many connecting economies already face capacity constraints as indicated by increasing export prices. For instance, U.S. tariffs on Chinese products not only have increased unit prices of imports from China, but have also raised

unit import prices from alternative source locations, principally Viet Nam and Mexico (Alfaro and Chor, 2023). Similarly, a recent study from the Bank for International Settlements highlighted a notable increase in network firm distance for supply chains involving suppliers from China and customers in the United States. The lengthening of these supply chains suggests that firms from other jurisdictions, notably in Asia, have interposed themselves in the China-U.S. supply chain, charging additional markups and increasing costs to importers and consumers (Qiu, Shin, and Zhang, 2023). This can open the door for new players. There is already anecdotal evidence that, for example, Mexican firms are offshoring tasks to other Central American economies. For instance, FDI inflows in the Dominican Republic surged by 115 per cent in 2022 mostly due to investments from Mexico (ECLAC, 2023).

However, growing fragmentation comes also with significant risks, especially if it does not lead to a broader geographic re-globalization. The role of connecting economies depends on economies accepting indirect exposure to non-aligned economies. This might not be the case for much longer and would imply significant costs for EMDEs. WTO estimates based on Goes and Bekkers (2022) suggest that relative to a re-globalization scenario a full fragmentation of trade would reduce global GDP by 8.6 per cent, with costs in developing economies and LDCs particularly high at 10.2 per cent and 11.3 per cent respectively (WTO, 2023a). The reason for this is that EMDEs are more dependent on knowledge flowing with FDI from advanced economies. Moreover, evidence suggests that EMDEs receive more FDI from economies with which they are not politically aligned (IMF, 2023).

To prevent this negative scenario of full fragmentation and to benefit from re-globalization, EMDEs need, on the one hand, to push against rising trade policy uncertainty by defending the multilateral trading system. And, on the other hand, they need to provide a stable business environment at home. As the *World Trade Report 2024* argues, making trade more inclusive and integrating more economies requires a comprehensive strategy that merges open trade and greater international cooperation with complementary domestic reforms.

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Tel:(1) 202 393 6663 Fax: (1) 202 393 6556

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Email: [info@emergingmarketsforum.org](mailto:info@emergingmarketsforum.org)

