



CROATIAN NATIONAL BANK

EUROSYSTEM

(De)globalisation!?

Trends and macroeconomic implications

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London, February 6, 2025



Outline

Trends and evidence

Impact of (de)globalization on...

- economic activity
- inflation

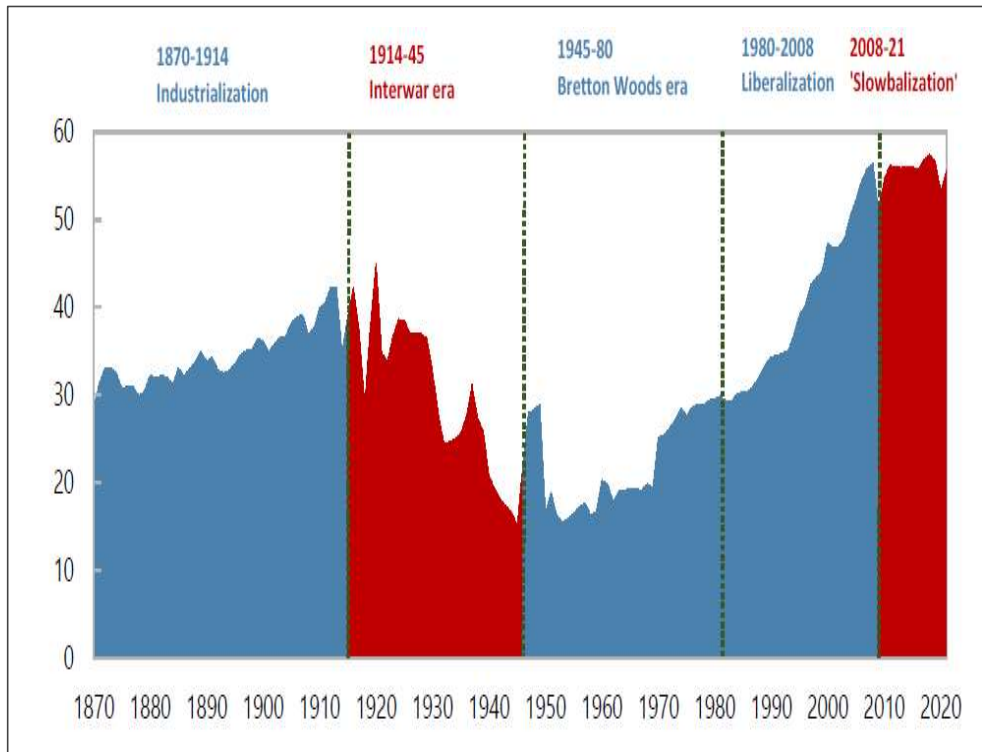
Implications for policy makers

Trends and evidence

There is still no clear evidence of trade deglobalization, but trade globalization has stalled since the GFC

Trade Openness, 1870-2021

(Sum of exports and imports, percent of GDP)



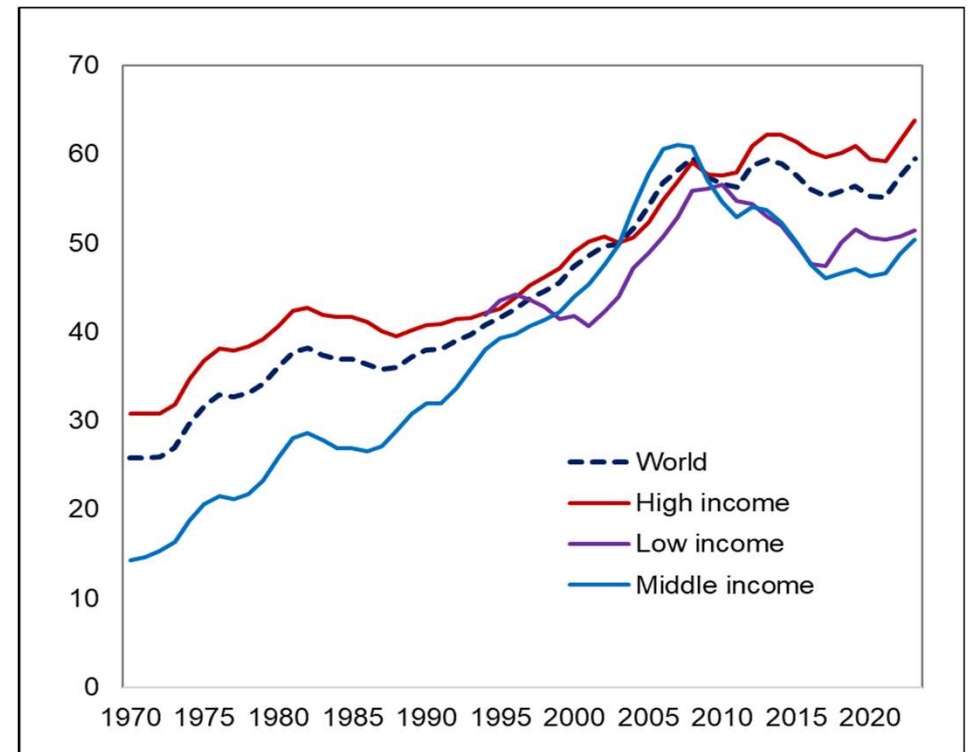
Source: "Goeconomic Fragmentation and the Future of Multilateralism", IMF, January 2023

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Trade Openness, by income groups

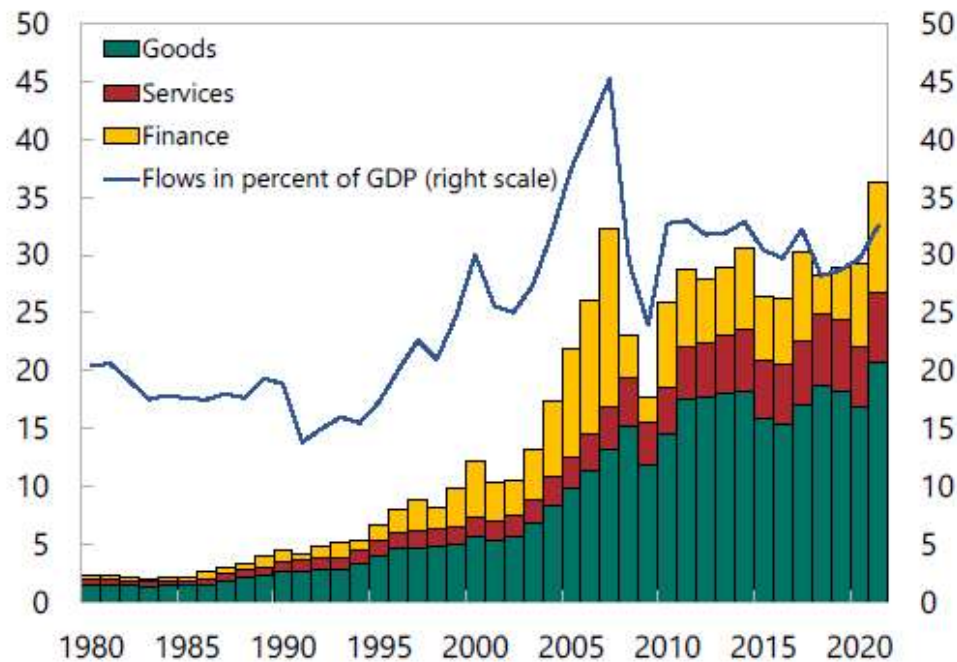
(Sum of exports and imports, percent of GDP)



Source: World Development Indicators, World Bank

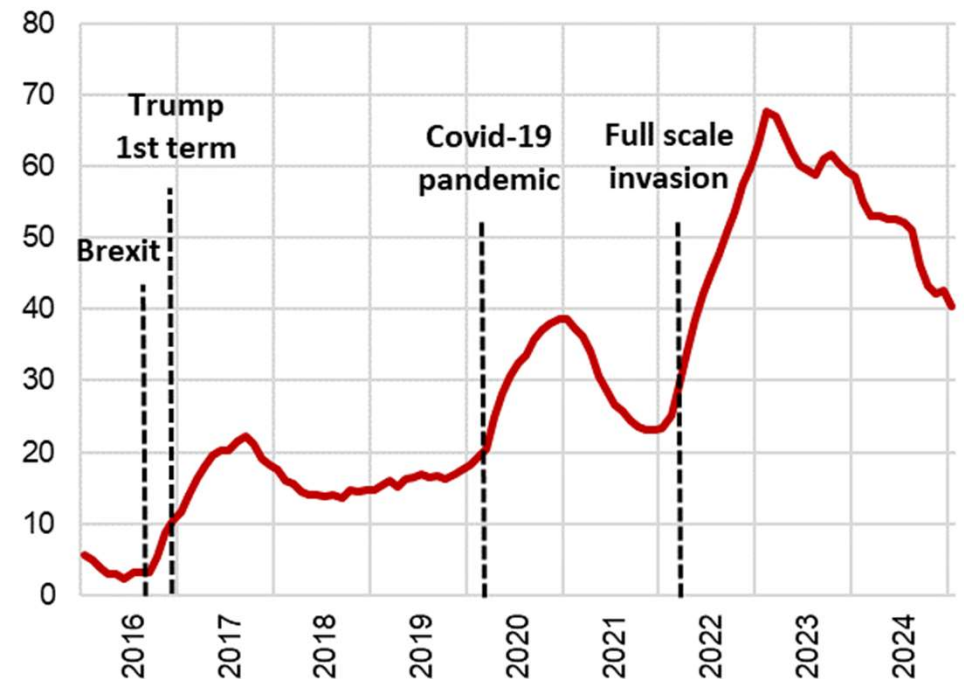
Slowing globalization is evident since GFC, but comes into focus only following major global events

Global Flows of Goods, Services and Finance
(\$ trillion, unless indicated otherwise)



Source: "Goeconomic Fragmentation and the Future of Multilateralism", IMF, January 2023

„Deglobalization” search interest

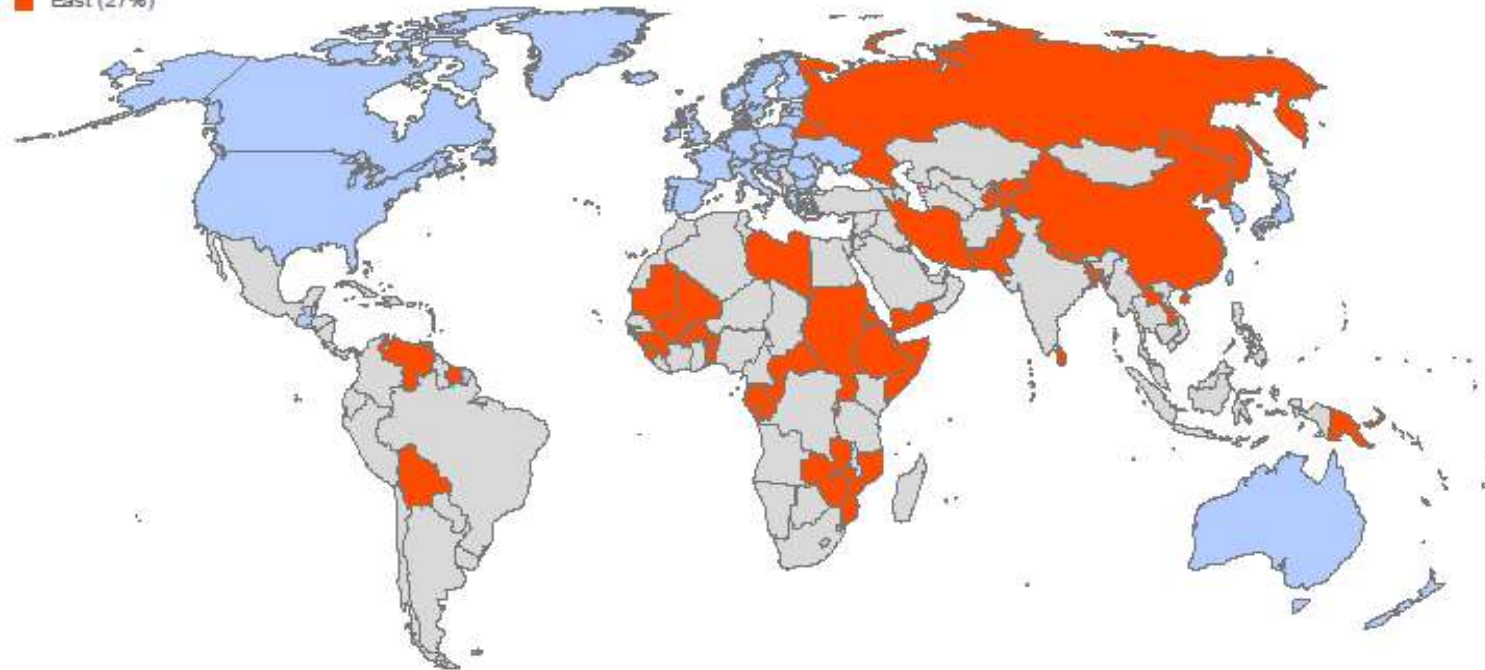


Source: Google Trends

Nevertheless, rising tensions and inward-looking policies are contributing to trade fragmentation along geopolitical lines

(percentage of world GDP, based on PPP)

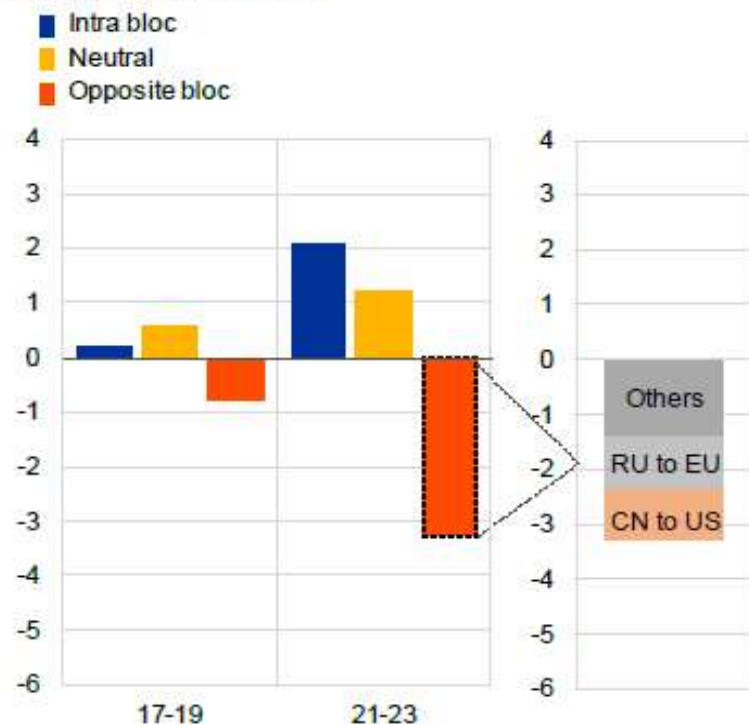
- West (42% world GDP PPP)
- Neutral (31%)
- East (27%)



Data suggest trade reconfiguration between major blocks centered around the US and China

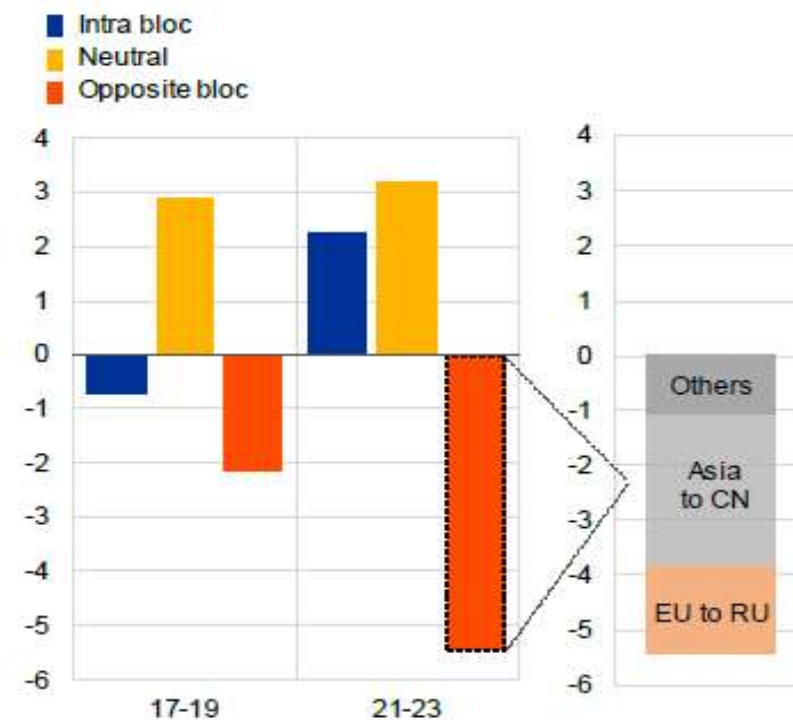
Western block import shares

(percentage point changes)



Eastern block import shares

(percentage point changes)



Source: "Navigating a fragmenting global trading system: insights for central banks", Occasional Paper Series, No 365, ECB

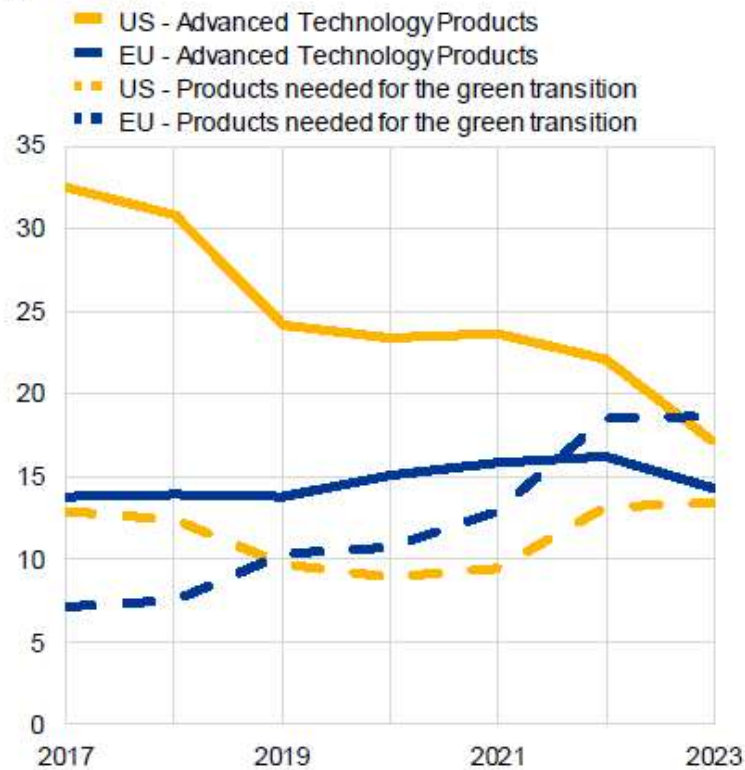
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Shifts in trade flows are most evident in key electronics products, while there is very little shift in energy transition related products

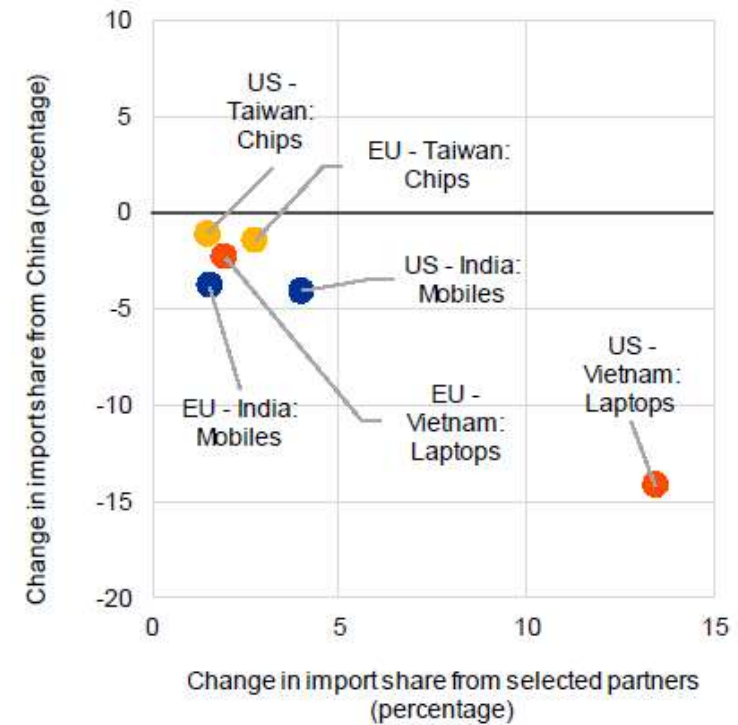
Share of imports from China by product category

(percentage)



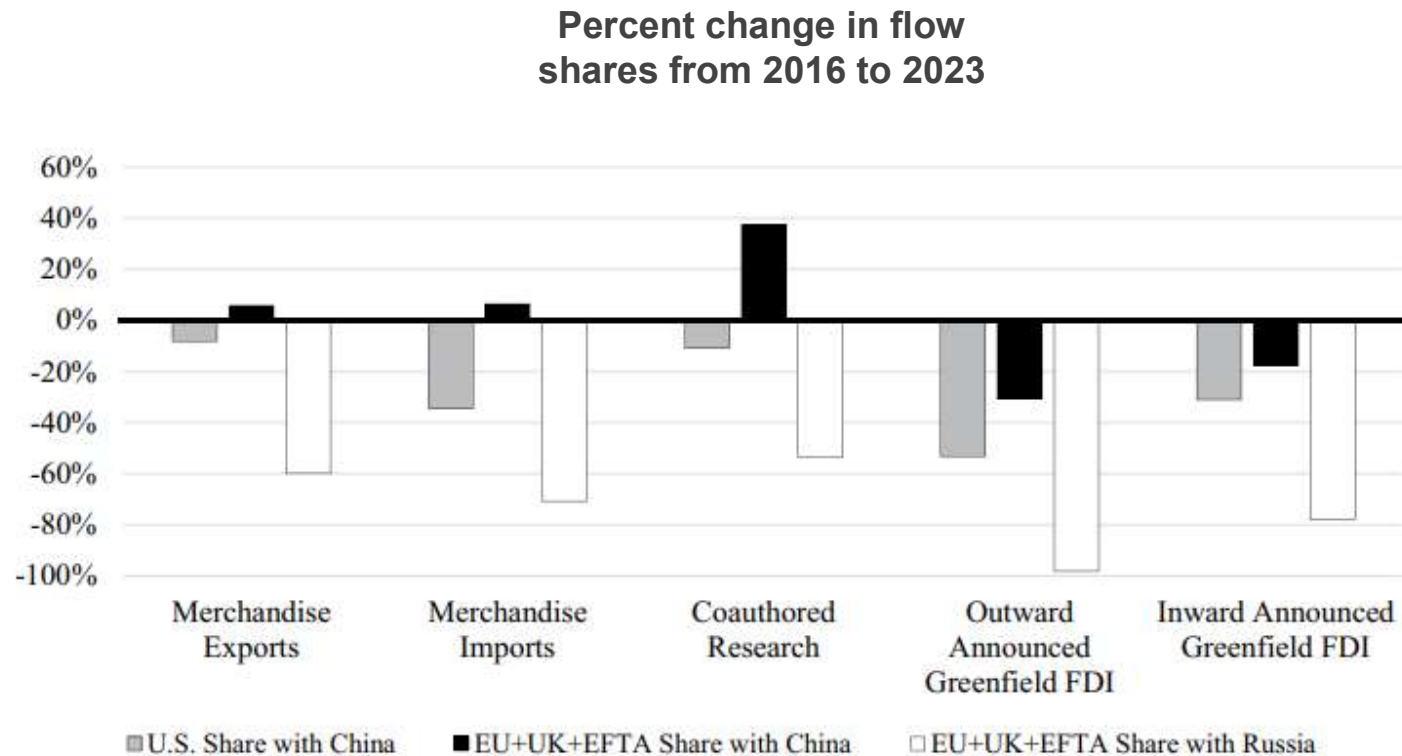
Reorientation of imports from China to other partners for EU and US in selected advanced technological products

(percentage)



Source: ECB based on TDM data and Conteduca et al. (2024).

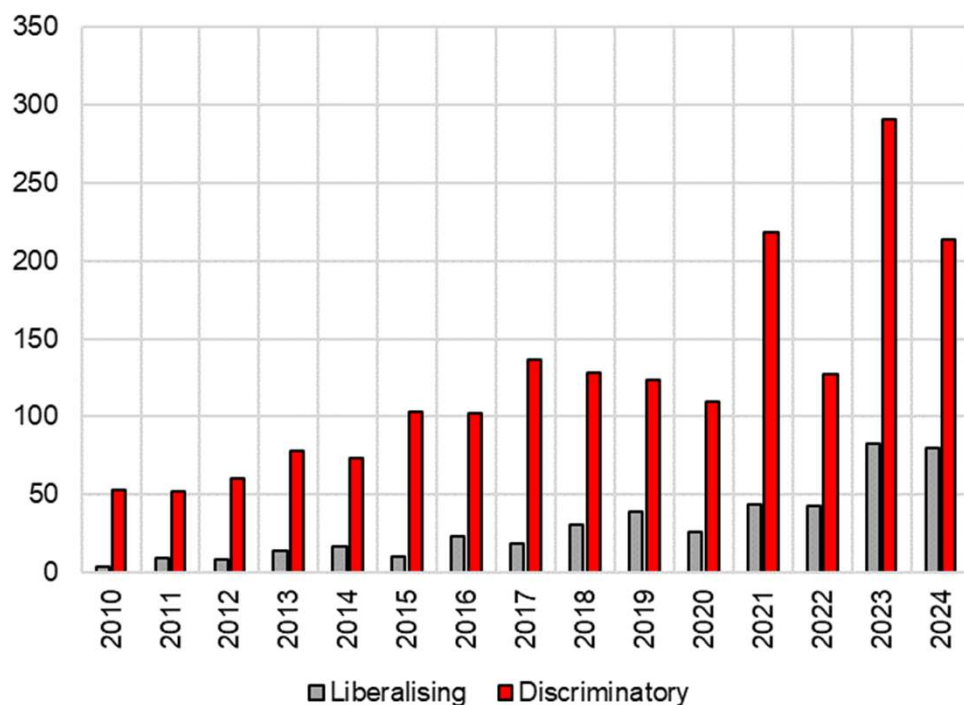
Reconfiguration goes beyond trade into investment flows and even multilateral R&D



Source: "Challenging the deglobalization narrative: Global flows have remained resilient through successive shocks", Journal of International Business Policy, October 2024

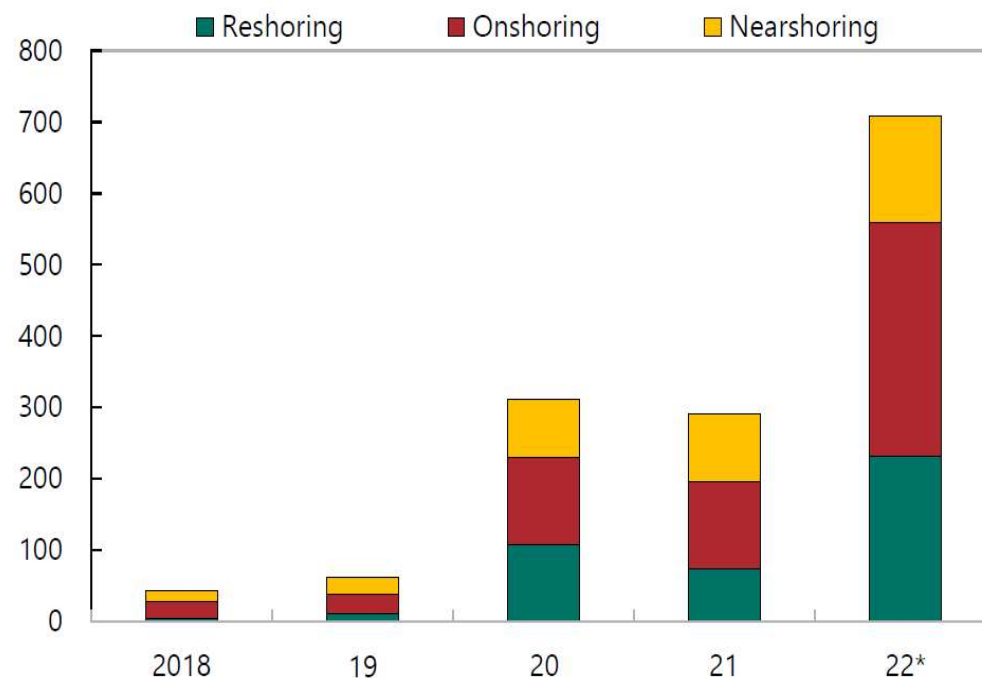
With rise in protectionism, various types of „shoring” become new normal

Trade policy decisions



Source: Global Trade Alert

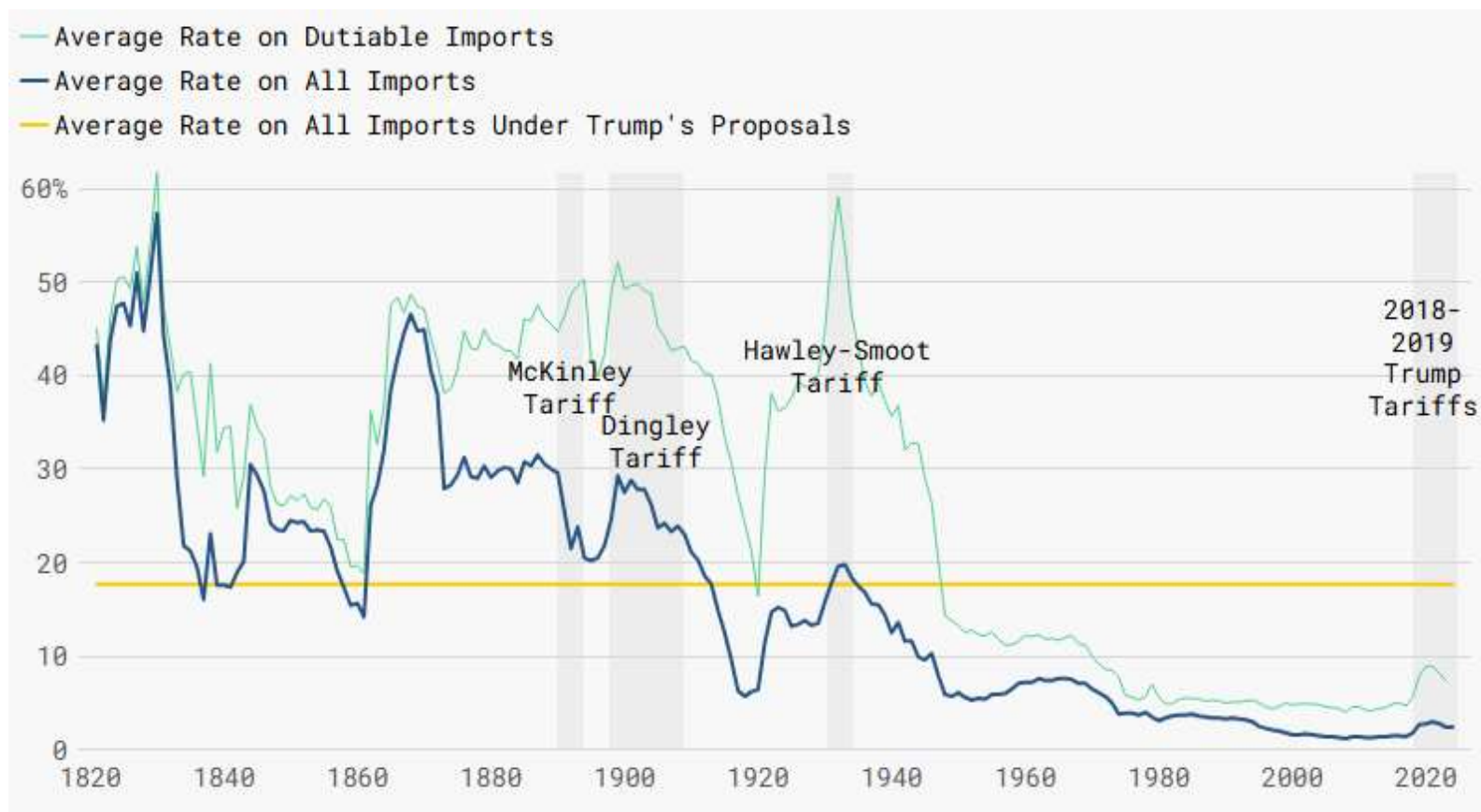
Mentions of key terms in Corporate Presentations



Source: "Goeconomic Fragmentation and the Future of Multilateralism", IMF, January 2023

Are we on a verge of a trade war?

Average US tariff rate



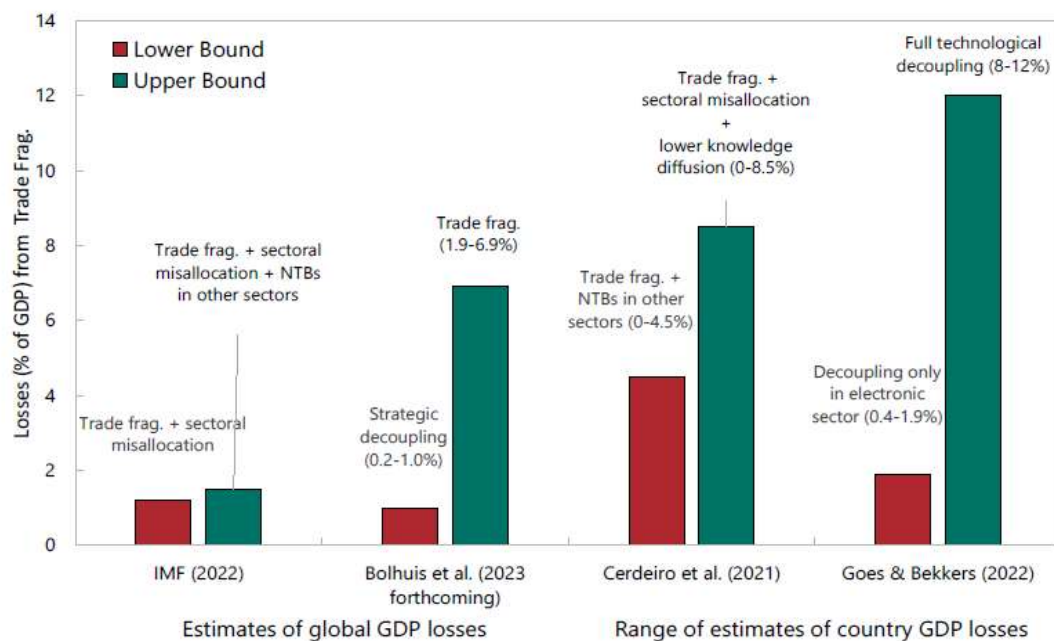
Impact of deglobalization on economic activity

Consequences of deglobalization could be severe for both producers and consumers...

1. **Less efficient resource allocation and lower productivity** - Shifts in specialization away from industries where countries have comparative advantages; limited access to foreign markets.
2. **Disruption to global value chains** - Relocation of supply chains to domestic or regional markets (reshoring or nearshoring) may initially disrupt production. Long-term adaptation could stabilize production, albeit with lower efficiency.
3. **Technology diffusion** – Lower openness reduces competition and technology transfer.
4. **Lower investments and other capital flows** – Declining cross-border capital flows could mostly impact EM that are in need of stable foreign financing and seek technology and knowhow transfer through FDI.
5. **Migration** – Demographic trends in AE could be under additional strain due to lower cross-border labour flows.
6. **Regionalization and uneven growth** - Increased reliance on regional trade agreements may create growth disparities among regions.

Recent studies show that geoeconomic fragmentation is likely to be costly

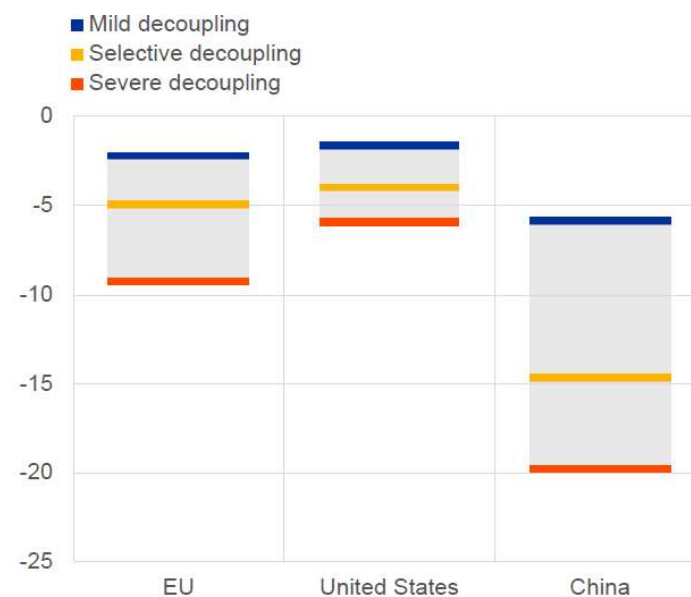
Long-Term Losses from Global Trade Fragmentation



Note: Estimates of long-term losses (percent of GDP) from Global Trade Fragmentation from various studies. Numbers refer to GDP losses that are not directly comparable across papers as some refer to global GDP while others refer to specific regions or countries. Numbers in brackets represent ranges of losses based on assumptions about the severity of fragmentation and trade elasticities, and /or geographical ranges. The height of each bar corresponds to the upper limit of the range. NTBs = non-tariff barriers to trade.

Source: "Geoeconomic Fragmentation and the Future of Multilateralism", IMF, January 2023

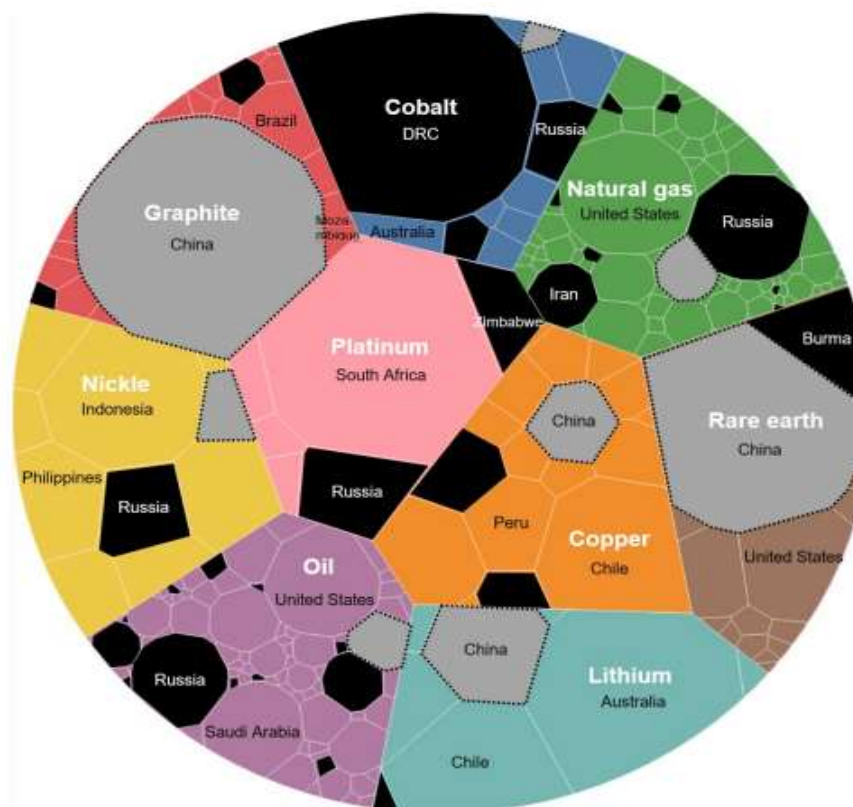
Real GDP by region (percentage deviation from steady state)



Note: "Severe decoupling" scenario assumes that higher barriers to trade de facto halt trade flows between the East and West blocs. "Mild decoupling" assumes a decoupling across all sectors, but the level of trade between East and West reverts to the one observed in the mid1990s. "Selective decoupling" assumes, more in line with recent evidence, that trade restrictions target products whose supply is more prone to be weaponised (i.e. advanced technologies, raw materials and energy commodities). Source: "Navigating a fragmenting global trading system: insights for central banks", Occasional Paper Series, No 365, ECB

Global production of selected commodities is highly concentrated

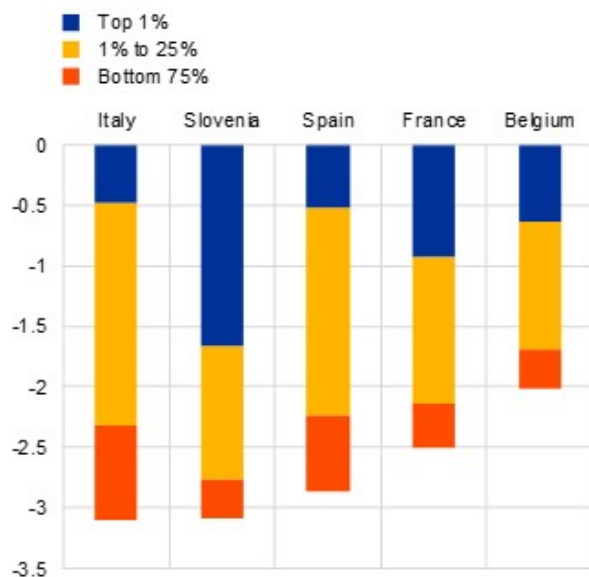
World production of selected commodities



Note: Different colors represent different commodities. Countries under sanctions are colored black, and China is colored grey.
Source: Aiyar, S. et al. (2023), Geoeconomic Fragmentation and the Future of Multilateralism, IMF Staff Discussion Notes No. 2023/001

Decoupling from China would be costly for Europe, but with heterogenous effects accross countries and sectors

Decomposition of value-added change by exposed firm size
(percentage)



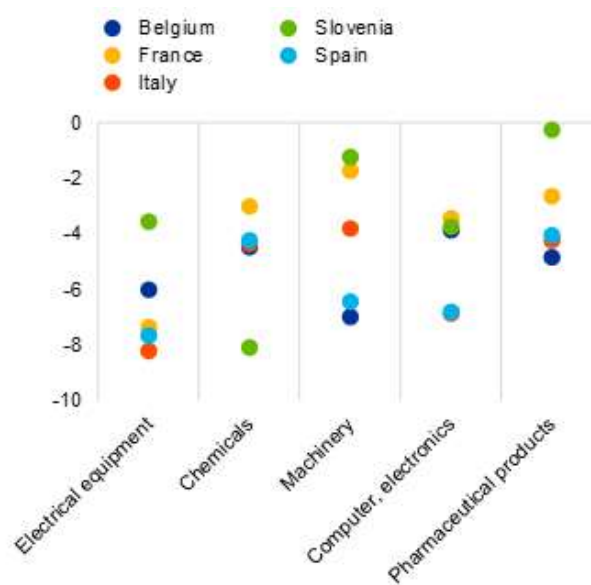
Notes: Firm size measured as value added. Percentile calculations include only exposed firms operating in the manufacturing sector.

Sources: Panon et al. (2024)

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Aggregate value-added change across sectors
(percentage)



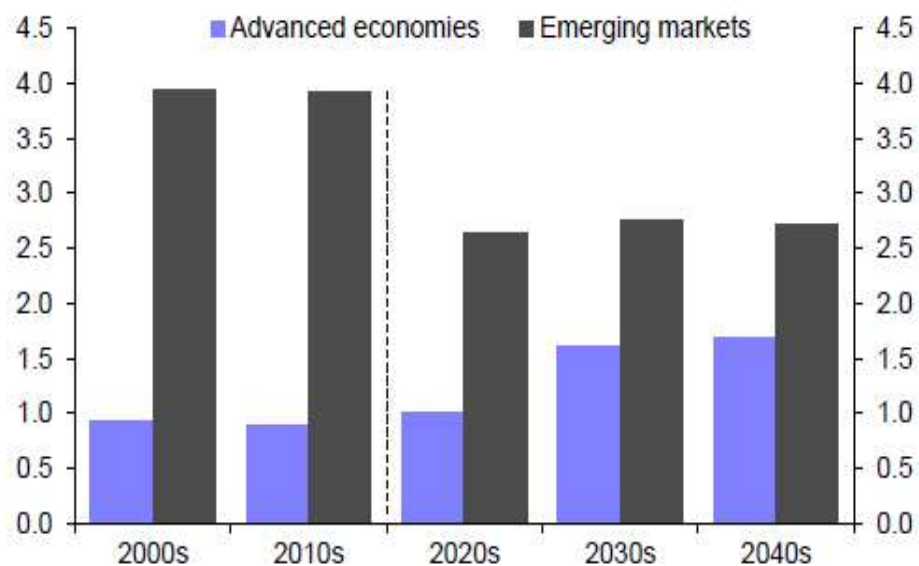
Notes: The chart reports the change in value added (in %) across the most exposed sectors, from a 50% drop in supply of critical inputs from geopolitical distant countries. The red circle denoting Italy is hidden by the light blue circle (Spain) in the case of the computer industry.

Sources: Panon et al. (2024)

- **China accounts for 30% of extra-EU imports of critical inputs.**
- A 50% reduction in imports of critical products from geopolitically distant countries would result in losses of value added in the manufacturing sector from 2.0% to 3.1%, with large firms driving the impact.
- The electrical equipment industry stands out as most affected sector, followed by chemicals, basic metals, electronics, and machinery.

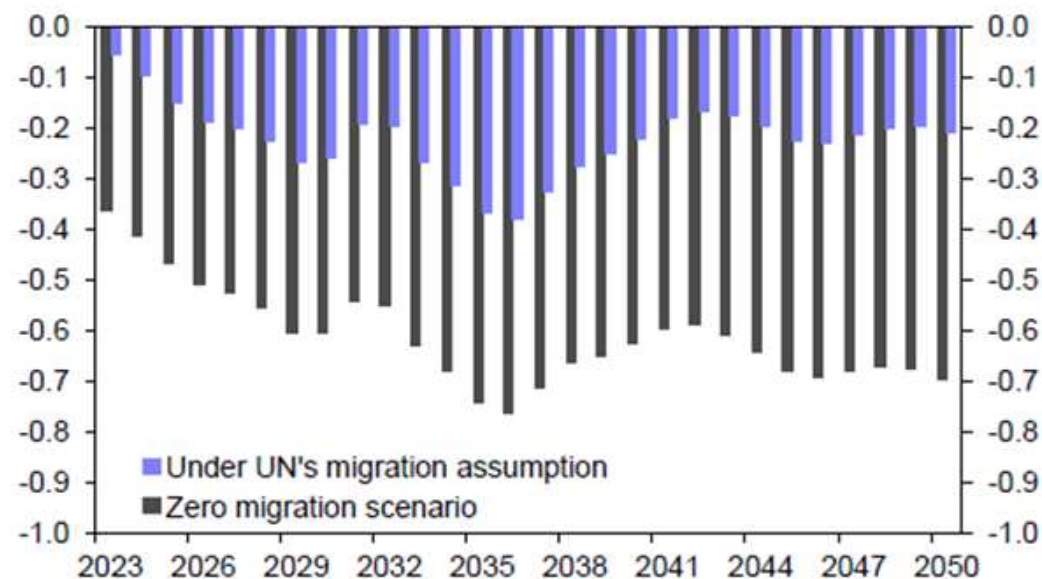
Slowing trade and investment could affect productivity in EM, while reduction in migration flows could exacerbate labour shortages in AE

Output per Worker in Advanced and Emerging Economies
(% yoy)



Sources: „The macroeconomic effects of fracturing”, Capital Economics, October 2022

G7 Working Age Population
(% yoy)

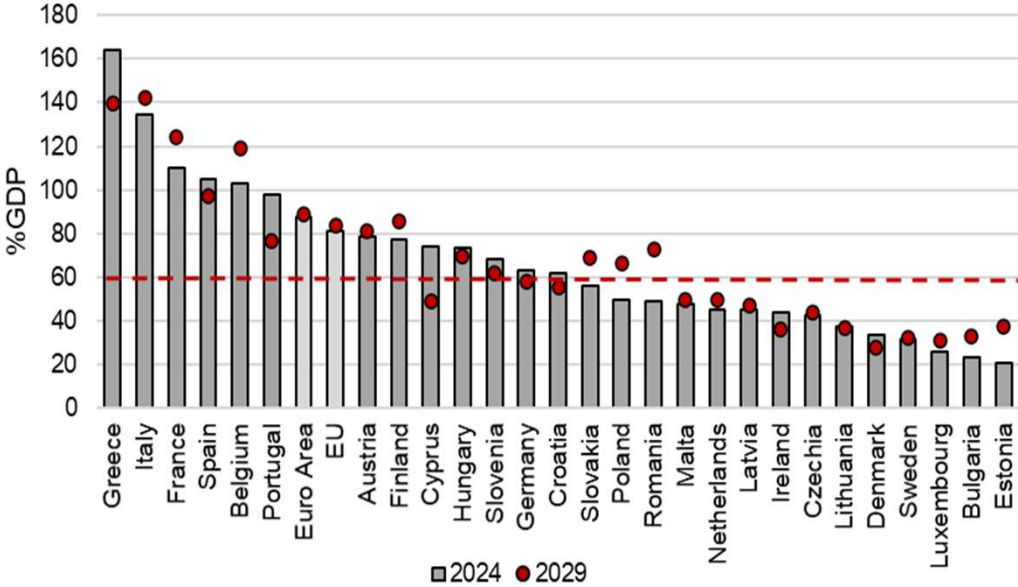


Note: UN's migration assumption expects migration to continue in line with the UN's central assumption, while Zero migration scenario assumes total stop on migration.

Sources: „The macroeconomic effects of fracturing”, Capital Economics, October 2022

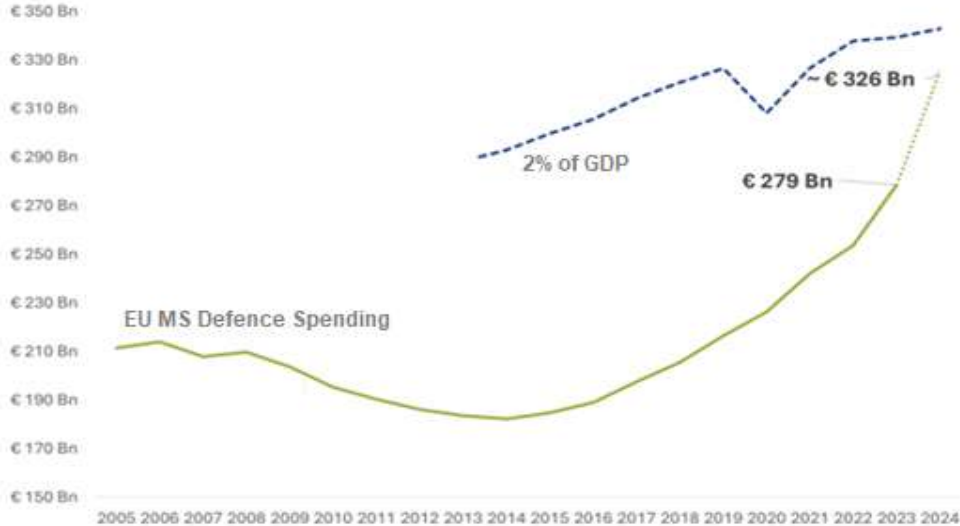
Geopolitical fragmentation leads to higher military spending, further burdening already strained public finances in EU

Public debt ratio in EU member states (2023)



Note: Dotted line represents 60% of GDP threshold. Data for 2029 refer to IMF WEO Outlook projection (October 2024). Source: Eurostat

Defence spending in EU member states

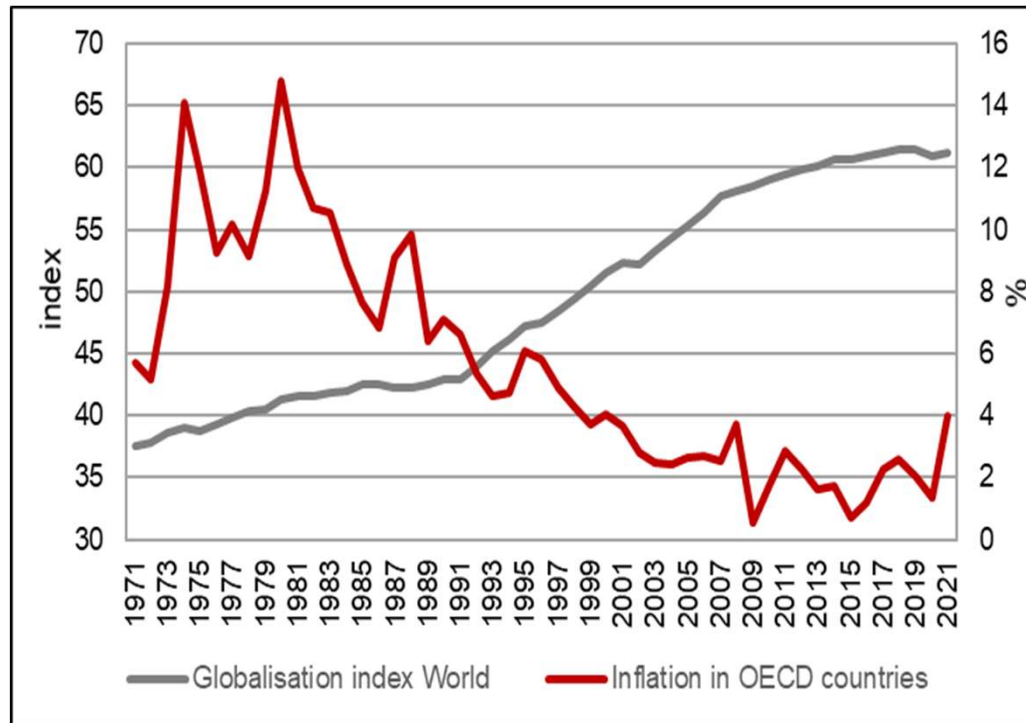


Source: "Coordinated annual review on defence - Report 2024", European Defence Agency

Impact of deglobalization on inflation

Globalization over the past 50 years has been disinflationary

Globalisation index and inflation in OECD countries



Note: The index measures globalization on a scale from 1 to 100, where higher values indicate a higher degree of globalization.

Sources: KOF Swiss Economic Institute, OECD

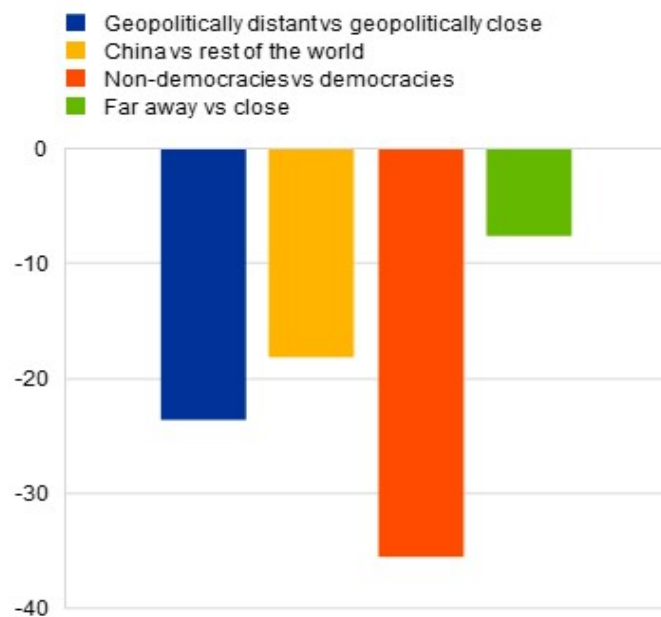
- Globalization tends to have a **disinflationary** impact through four channels:
 1. **Increased trade integration** - enhances competition that results in lower prices
 2. **Greater role of emerging markets** – introduces lower-cost goods and services
 3. **Expansion of global value chains** - increases efficiency and reduces production costs
 4. **Reduced bargaining power of workers** - Limits wage growth pressures

... while deglobalization could mostly be inflationary through several channels

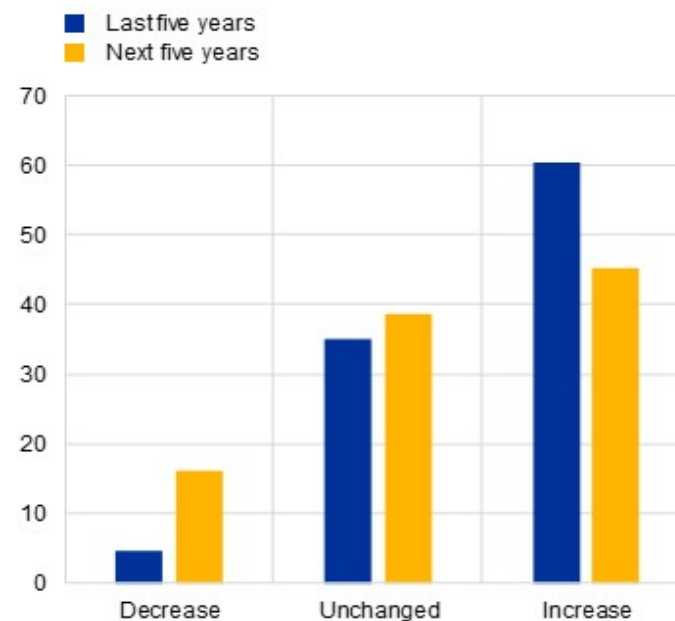
1. **Tarrifs and other trade barriers** -> **inflationary effect** directly through higher prices, but also due to lower total supply
2. **Higher energy prices** -> **inflationary effect** due to lower availability of all sources of energy
3. **Increased procurement and production costs** -> **inflationary effect** due to lower availability to move production to low-income countries
4. **Increased labour costs** -> **inflationary effect** due to inability to substitute relatively more expensive domestic labour by relatively less expensive labour in low-income countries
5. **Reduced external demand for domestic products and services** -> **disinflationary effect**

Evidence suggests that rebalancing towards geopolitically closer countries would increase costs of production

Difference in import price between country groups
(percentage difference, median of products)

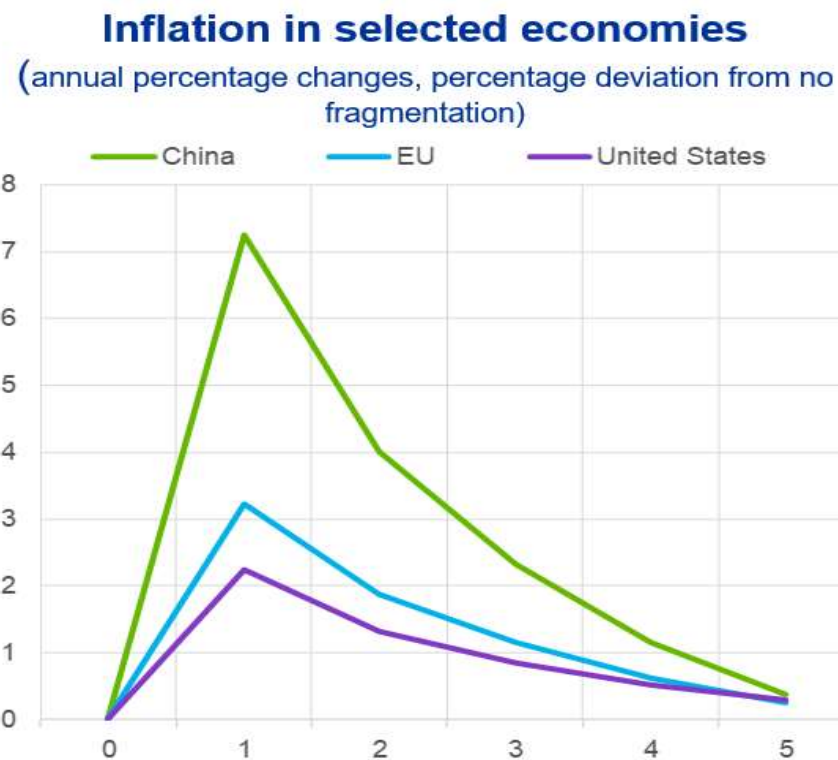
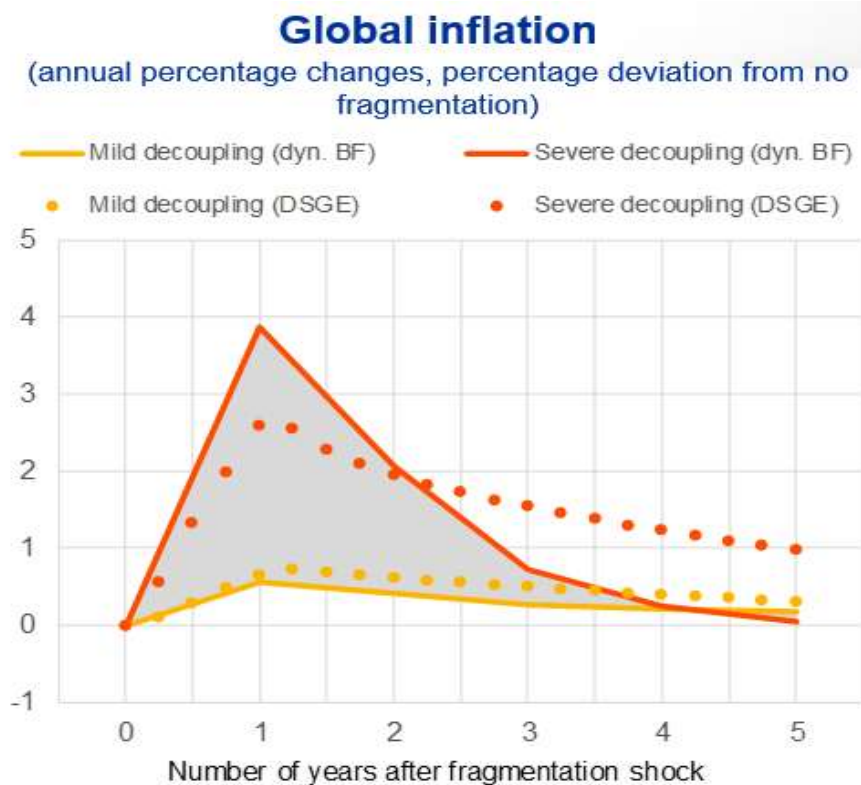


Overall impact of production location and input sourcing decisions on prices
(percentages of responses)



Source: "Navigating a fragmenting global trading system: insights for central banks", Occasional Paper Series, No 365, ECB

Inflationary effects of trade fragmentation may be persistent



Source: "Navigating a fragmenting global trading system: insights for central banks", Occasional Paper Series, No 365, ECB

Implications for policy makers

Policy implications

Avoid broad based protectionism

...resilience legitimate concern, but tit-for-tat trade war is welfare reducing

Foreign dependencies are policy relevant

...monitor production networks to understand foreign dependencies and risks

Adopt targeted policies

...to account for heterogeneity across sector, firms, regions

Fragmentation matters for monetary policy

...larger, more frequent supply shocks; may affect economy differently from trade integration shocks

Insights for central banks

Look beyond aggregate trade data

...use granular approach to monitor fragmentation

Regular business surveys

...for timely understanding of firm's exposure to fragmentation risks

Richer set of analytical tools

...to assess impact of fragmentation shocks on activity and prices

Monitor price pressures along supply chain

...by factoring in the sectoral dimension of price pressures



Thank you very much for your attention!