HAS THE WORLD ECONOMY ENTERED A PHASE OF DEGLOBALIZATION?

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Abstract

The paper focuses on the current processes in the world economy, which show many differences from the developments before 2008 or 2020 and which may indicate the beginning of fundamental changes in international economic relations. The author analyses the significance of watershed global economic events such as the global financial crisis of 2008–2009, the COVID-19 pandemic of 2020–2023, and the Russo-Ukrainian war from 2022 onwards for the scope and nature of international economic cooperation. The author examines the effects of these events on various global economic indicators and on the functioning of global value chains and global production networks. In this context, the paper discusses possible variants of the future development of the world economy, ranging from a partial correction of the previous hyper-globalization, through a slowdown or halt of globalization, to a transition to the opposite phase of development – deglobalization. It concludes by comparing the likelihood of these different future scenarios.

Keywords

Globalization, Deglobalization, World Economy, International Trade, Global Value Chains

I. Introduction

Peak globalization is shorthand for the claim that the increasing openness of the economy is a thing of the past, that globalization of the world economy is slowing down, stagnating, or even shrinking in scope since the global financial crisis of 2008–2009. In addition to the global financial crisis, other disruptive events with global economic impact, such as the COVID-19 pandemic of 2020–2023 or the Russo-Ukrainian war from 2022 onwards, may also work against globalization, as governments and transnational corporations may prioritize security, resilience and protection over the functioning of interconnected global value chains and global production networks.

After almost 80 years of the prevailing trend of globalization, the era of globalization thus seems to be coming to an end. There may even be a reverse process in the world economy – deglobalization. Is this scenario for the future development of the world economy exaggerated, over-simplistic or realistic? Will the world be confronted with a slowdown or a halt in globalization, or even deglobalization, in the years to come? Or are the recent and current events only a partial correction of the previous hyper-globalization and the reversal of the long-term trend of globalization will not happen after all? The following text attempts to answer these questions. The methods of description, comparison and deduction will be used to research the aforesaid issues.

II. The risk of widespread deglobalization

According to an analysis by Christian Keller, Managing Director and Head of Economics Research at Barclays Corporate and Investment Bank, and Renate Marold, Director of Investment Sciences at Barclays Corporate and Investment Bank, after nearly 80 years of globalization, recent and current global shocks and the fight against climate change appear to be changing the landscape (Keller and Marold, 2023). Already the global financial crisis of 2008–2009 has caused a slowdown in globalization, which may now turn into deglobalization. In response to the COVID-19 pandemic, the Russo-Ukrainian war and climate change, governments and transnational corporations are prioritizing security and resilience over the benefits of global value chains. This is creating a new mix

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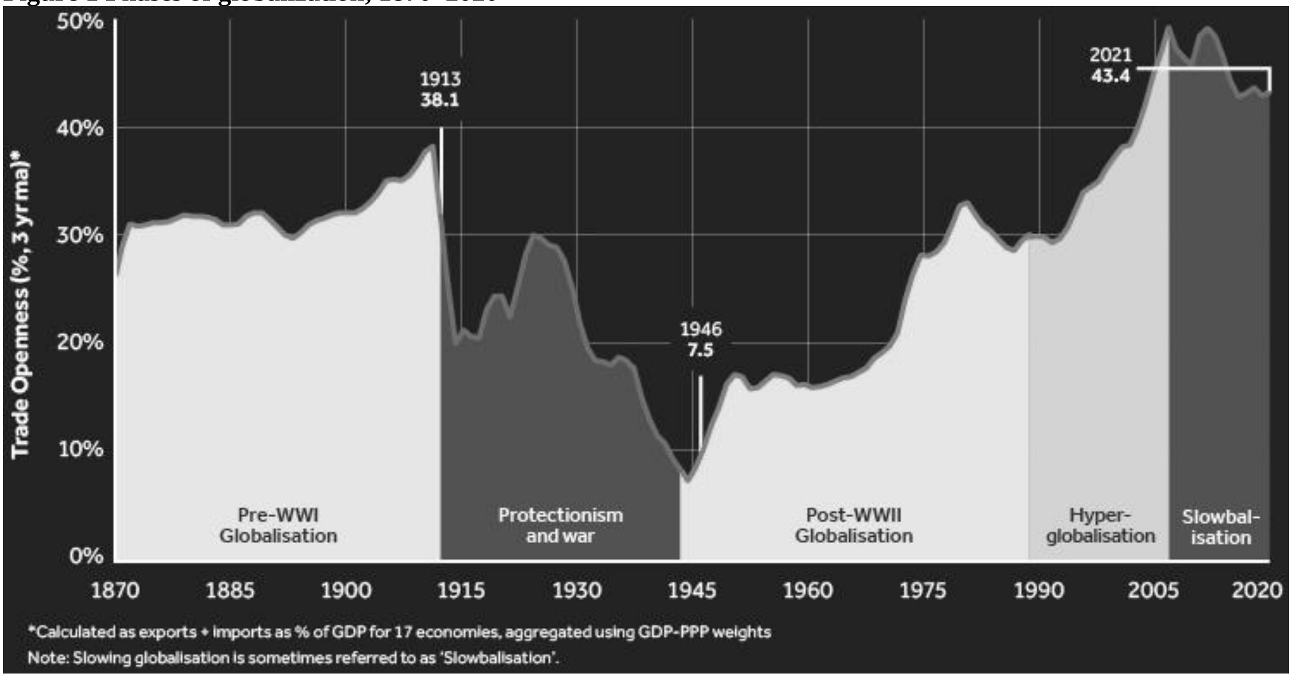
of micro- and macroeconomic measures that are not conducive to further globalization. There are strong signs that the era of globalization is coming to an end.

Also, according to the European Commission's spring 2022 economic forecast, deglobalization is a risk to the future economic development of the European Union. According to the European Commission, the risk of widespread deglobalization has increased further. Restructuring of global economic linkages could partially reverse the gains from globalization, reduce the benefits from the international division of labor, and lead to lower rates of technological innovation, higher import prices and lower potential output (European Commission, 2022, p. 12).

Figure 1 Phases of globalization, 1870–2020



Source: Keller and Marold (2023)

As Keller and Marold (2023) remind us, the rise of globalization has never been entirely smooth and self-evident. The Second World War was followed by 60 years of increasing globalization. This included a period of hyper-globalization from 1990 to 2008 (see Figure 1).

However, the global financial crisis of 2008–2009, trade wars, income stagnation and economic problems of the middle class in developed economies, as well as growing concerns about overdependence on trade and the economic interconnectedness of the world, led to a subsequent period of relatively stagnant or slow globalization. Today, slow globalization appears to be moving towards deglobalization (see Figure 1).

III. The search for more resilient and closed models of economic growth

As Keller and Marold (2023) argue, recent disruptions in global value chains due to the COVID-19 pandemic, the war in Ukraine, growing ideological differences between various major economies and world regions, as well as the transition to a green economy have forced governments and businesses to rethink external dependencies. They are looking for more resilient models of economic growth that rely more heavily on economic activity within the country and in neighboring regions, and on cooperation with trusted or ideologically close partners. These sentiments go beyond the policy positions of governments and become part of the general corporate rhetoric.

Interestingly, according to Keller and Marold (2022), while the overall sentiment is turning towards deglobalization, deglobalization is not an entirely global issue. Some regions and industries are deglobalizing faster than others. For example, mergers and acquisitions and jobs data suggest that deglobalization is occurring, but it is not occurring evenly across the planet.

The major job displacement associated with deglobalization is occurring mainly in Asia. In the United States, the United Kingdom and the European Union, while domestic employment is increasing, which could indicate a trend towards deglobalization, there is no decline in trade between Western economies, so the net trend in Western countries so far appears to be still towards globalization.

The analysis by Keller and Marold (2022) finds that fewer announced mergers and acquisitions have been completed recently than would be consistent with historical patterns. Moreover, transactions between target firms in the European Union, the United Kingdom, and North America are less likely to be successful if the acquirer is outside these regions, especially for target firms in sectors such as high technology, finance, and retail. Conversely, transactions targeting firms in, for example, the consumer goods industry are more likely to succeed.

However, the slowdown in mergers and acquisitions activity may not only be due to the trend towards deglobalization, but also to regulatory concerns as the European Commission and the British Competition and Markets Authority increase their scrutiny of these transactions.

IV. The impact of the transition to a green economy

According to Keller and Marold (2022), one of the causes of deglobalization may be the transition to a green economy. Energy is a key sector to watch in terms of both globalization and deglobalization. The common motivation of states to address climate change has been a major source of globalized cooperation in recent years. However, the mechanism of the transition to a green economy itself also requires a greater focus on the local level, which encourages deglobalization tendencies.

Pressure to increase the share of renewable energy in the long term is driven by the reduction of carbon-intensive transport infrastructure and also through carbon pricing mechanisms that act as de facto tariffs. Growing concerns about energy security and the volatility of fossil fuel prices have also increased interest in domestic renewables. This also supports the move towards deglobalization.

However, as the transition to a green economy is a global challenge, the analysis by Keller and Marold (2022) suggests that a global approach is still needed to complement local and regional solutions. Although the rise of renewables will fundamentally change fossil fuel trade flows, the green transition will need to be supported by the extractive industries, which will be used to build their infrastructure. This will result in increased trade integration of mineral resource countries.

The era of globalization may therefore be coming to an end. What will replace it remains to be seen. But global cooperation will continue to be necessary to solve common problems in many areas, according to Keller and Marold (2023).

V. Developments in international trade

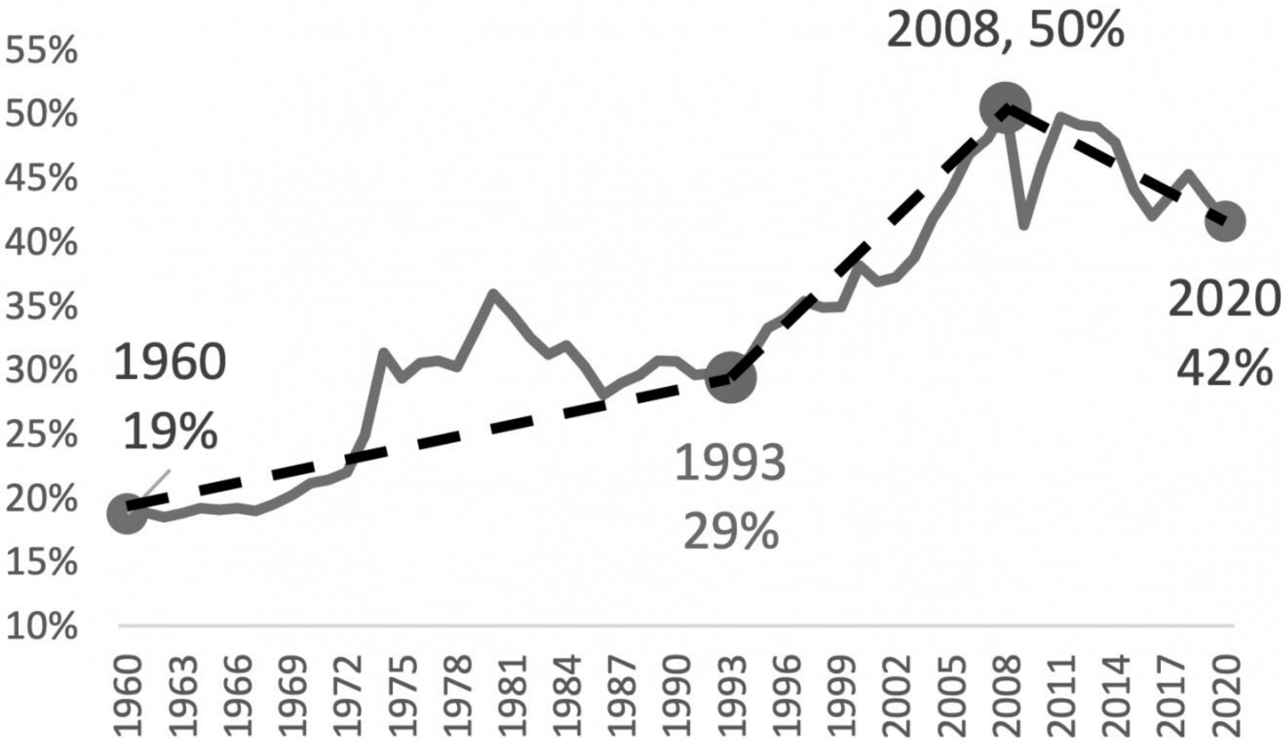
Data on international trade also point to a possible trend towards deglobalization. According to Richard Baldwin, professor of international economics at the Geneva Graduate Institute (IHEID) and associate member at Nuffield College, University of Oxford, the story of the development of globalization and subsequent deglobalization can be simplistically described in a single figure that shows the developments in the share of world exports and imports of goods in global gross domestic product (Baldwin, 2022a).

The share of world exports and imports of goods in global gross domestic product increased between 1960 and 1993, albeit at a slow pace, from 19% in 1960 to 29% in 1993 (see Figure 2). This moderate pace of globalization was mainly due to the reduction of transport costs and the reduction of tariff barriers to trade such as customs duties.

This was followed by an acceleration in the growth of this indicator in the following period, with the share of world exports and imports of goods in global GDP rising sharply to 50% by 2008 (see Figure 2). We refer to this period of rapid growth in the share of world trade in goods in GDP as hyper-globalization. Hyper-globalization was driven by the revolution in information and communication technologies (ICT), which initiated the offshoring phase of globalization. Offshoring meant that no longer just goods, but entire companies and factories were crossing borders. As parts and components now crossed borders multiple times, for example first as parts and then as parts incorporated into components or final goods, the share of global trade in goods in GDP naturally increased (Baldwin, 2022a).

Moreover, the offshoring boom was accompanied by a massive transfer of manufacturing know-how to several large emerging markets, including China, which triggered unprecedentedly rapid industrialization and growth in these economies (Baldwin, 2016, Chapter 3). As a result, the share of world trade in goods in GDP also increased as more parts, components and final goods crossed borders between Western countries and newly industrialized economies.

Figure 2 World exports and imports of goods, 1960–2020 (% of global GDP)



Source: Baldwin (2022a)

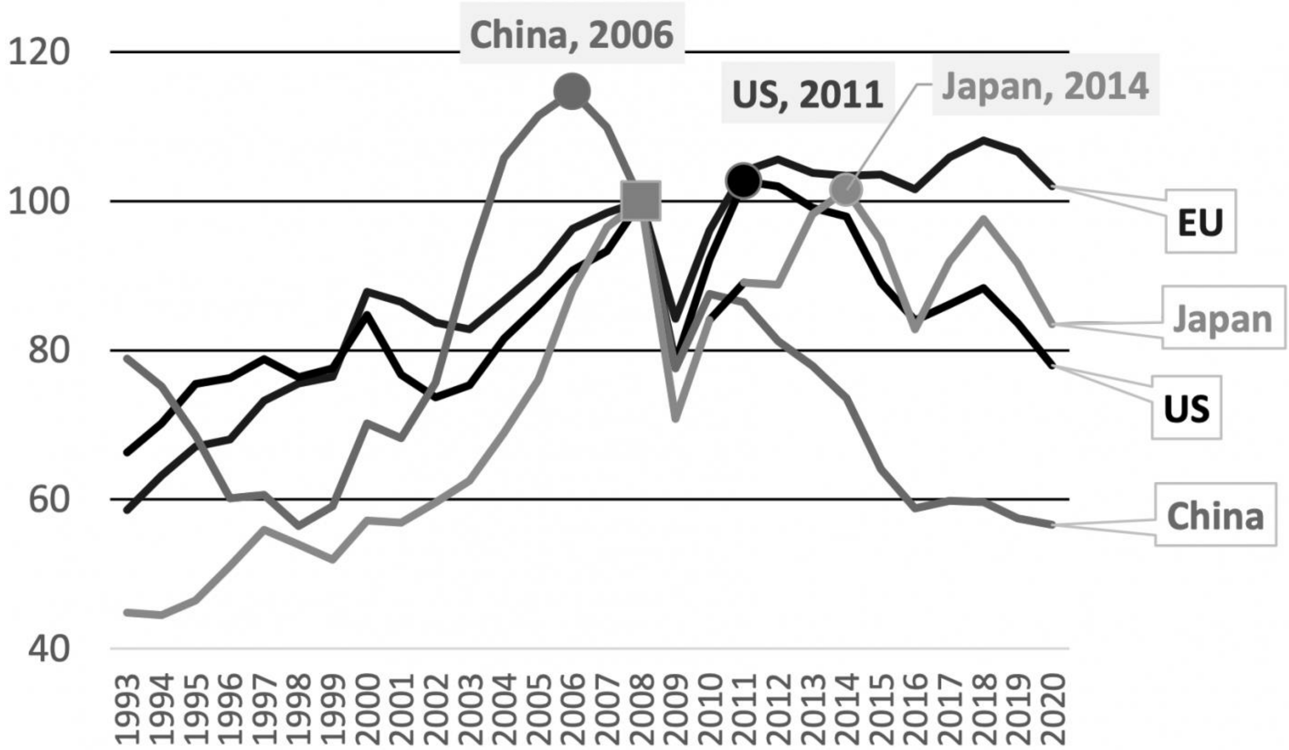
The global financial crisis of 2008–2009 and the associated trade shock have mortally wounded globalization. Since then, the share of world exports and imports of goods in global gross domestic product has fallen to 42% in 2020 (see Figure 2).

However, according to Baldwin (2022a), assessing globalization by the developments in the share of world trade in goods in GDP is too simplistic. It cannot simply conclude that the post-2008 world has entered an era of deglobalization. Indeed, this assessment contains a number of omissions and, on closer examination, it is clear that the whole issue of globalization and deglobalization is much more complex.

According to the analysis by Baldwin (2022a), the 2008 peak in the share of world exports and imports of goods in global gross domestic product is spurious. This is an average global figure, but a more detailed breakdown of this figure into individual major economies shows that each reached a trade peak at a different period, and one major economy did not even experience a decline in the share of goods trade in GDP.

The world's largest economies reached their trade peak either before or after 2008. China, as the world's second largest trader in goods, reached its trade peak before 2008 (in 2006). The United States, the world's third largest trader in goods, reached its trade peak after 2008 (in 2011). Japan, the world's fourth largest trader in goods, also peaked after 2008 (in 2014). The European Union, the world's largest trader in goods, has not reached a trade peak, but its share of goods trade in GDP has been stagnating for the last decade (see Figure 3).

Figure 3 Exports and imports of goods of the world's largest traders as % of GDP, 1993–2020 (index, 2008 = 100)



Source: Baldwin (2022a)

Thus, of the world's four largest traders in goods, one peaked before 2008, while two peaked after 2008. The world's largest trader in goods – the European Union – has not peaked, but its share of goods trade in GDP has been stagnating for ten years. The confluence of these disparate partial trade peaks and one stagnation then gives the false impression of one peak in the share of world trade in goods in GDP in 2008. The post-2008 world then appears to have entered an era of deglobalization, but this may be a fallacy (Baldwin, 2022a).

VI. Slowing globalization rather than deglobalization

On the other hand, it is evident that the globalization of goods markets is no longer growing at the same pace as it did from the 1990s to 2008. The phase of hyper-globalization is indeed over. The reasons why this has happened are discussed in Baldwin (2022b).

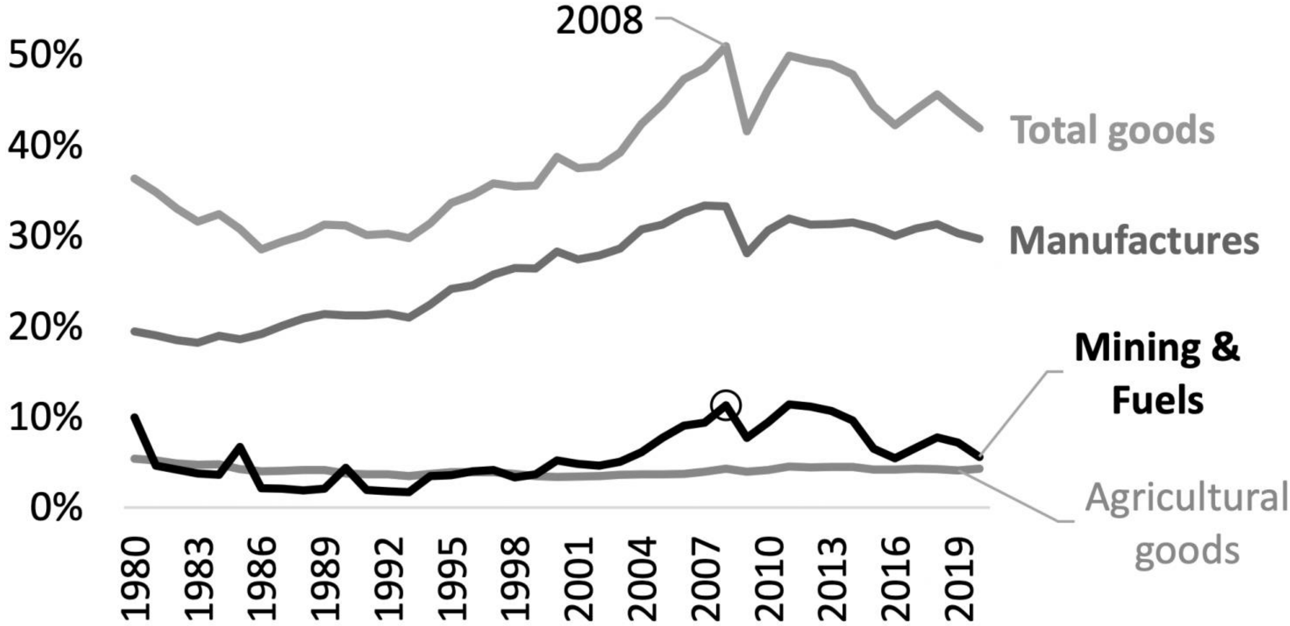
According to Baldwin (2022b), one reason for the decline in the share of world trade in goods in GDP after 2008 is the developments in relative prices. World trade in goods and world gross domestic product have very different compositions. Thus, in the share of world trade in goods in GDP, the numerator (trade in goods) has a very different composition from the denominator (GDP).

World trade in goods is made up of about three-quarters manufacturing products and the rest is roughly evenly split between agricultural commodities and extractive products. World GDP consists of roughly two-thirds services and only one-third goods. Given this mismatch, changes in relative prices can have a large impact on the resulting share of world trade in goods in GDP (Baldwin, 2022b).

A more detailed breakdown of the developments in the share of world trade in goods in GDP by commodity group is also important. Figure 4 shows the developments in the share of world trade in goods in GDP by commodity group from 1980 to 2020. The data in Figure 4 show that about 60% of the decline in the share of world trade in goods in GDP after 2008 was due to a reduction in the share of world trade in extractive industry products (minerals and fuels) in GDP. The remainder was due to a decline in the share of world trade in manufacturing products in GDP.

The overall share of world trade in goods in GDP fell from 50% in 2008 to 42% in 2020. The share of world trade in extractive products in GDP fell significantly from 11% in 2008 to 6% in 2020. However, the share of world trade in manufacturing products in GDP declined only slightly from 33% in 2008 to 30% in 2020. These figures do not yet indicate that an era of widespread deglobalization has begun.

Figure 4 World exports and imports of goods by commodity group, 1980–2020 (% of global GDP)



Source: Baldwin (2022b)

According to Baldwin (2022b), the discussion of globalization tends to deal with the developments in trade in goods as a whole. Based on the decline in the overall share of world trade in goods in GDP, hasty conclusions are then drawn about the advent of an era of deglobalization. To this are added arguments such as the trade war (in particular the cycles of retaliation between the United States and China), Brexit, the rise of populism or the decline in support for open trade in the G7 countries. Some analysts use them to demonstrate a broad departure from multilateralism, free trade and globalization and the rise of deglobalization. However, the finding that around 60% of the decline in the share of world trade in goods in GDP after 2008 was due to a reduction in the share of world trade in extractive products in GDP, while the share of world trade in manufacturing products in GDP fell only slightly, relativizes the conclusions about the onset of deglobalization.

VII. Slowing globalization and the possibility of deglobalization from a microeconomic perspective

The issue of the development of globalization and the possible onset of deglobalization need not be examined only from a macroeconomic perspective. It is also possible to observe these trends at the microeconomic level. Adam Pilarski, senior vice-president at Avitas, analyzed the possibilities of further development of globalization or the trend towards deglobalization from the perspective of the aviation industry and air transport (Pilarski, 2020).

According to Pilarski (2020), for many decades we have been experiencing an era of globalization that is the holy grail or nirvana for economists. This is due to the fact that economics, by definition, is concerned with the optimal allocation of scarce resources, and thus with the shifting of production to where it can be produced most efficiently. Therefore, from an economic point of view, globalization brings many positives. Moving resources (including people) to where they can be used most efficiently is of course also beneficial for aviation.

The trade-off between producing everything at home while providing work for local people and buying from abroad entails transport costs but also provides cheaper products. This has been debated among economists for centuries. David Ricardo, in his 1817 paper, postulated that free trade is beneficial to the whole world because of the principle of comparative advantage, which allows countries to specialize in what they do best.

The expansion of free trade has brought about a steady growth in the world economy and trade. These trends have also benefited air transport, both passenger and freight. Interestingly, we have also seen much lower inflation as we have imported cheap products from abroad, especially in the last few decades. However, despite its benefits, free trade has been vilified by its opponents (Pilarski, 2020).

Manufacturers have always been in favor of open markets as long as it benefited them by expanding their markets. They were less keen on the right of foreign firms to compete in their own markets, which could lead to job losses. The realization that, from a global perspective, this arrangement was efficient and allowed the world to maximize total (global) production from our planet's limited resources did not sit well with people who had worked for decades in an industry that eventually ran into trouble under the pressures of globalization (Pilarski, 2020).

There have long been voices against globalization, promoted by various populist and nationalist leaders. Ross Perot, for example, spoke out against free trade during his 1992 US presidential campaign. During one of the debates, he stated that if the United States adopted the North American Free Trade Agreement (NAFTA), many jobs would disappear to Mexico. He then won 18.9% of the popular vote in the 1992 US presidential election. The NAFTA agreement was indeed adopted, but the job drain was not. Opponents of globalization in the US had to wait another few decades before raising the issue again.

While the theoretical benefits of globalization are clear (world production will increase), the distribution of these gains among countries and within countries among different groups of people or entities is not clear and can easily lead to conflict. In addition to the distribution of these gains, there is also the issue of control (Pilarski, 2020).

Aviation illustrates this issue perfectly in the case of the production of the Boeing 787. The aircraft was designed to be largely outsourced, which ensured low costs for the designers, but also required giving up some control. Things did not go to plan and the aircraft was delayed by three years and also experienced a fleet grounding for three months in 2013. This ultimately led to huge costs for Boeing, which was forced to take large parts of the manufacturing supply chain into its own hands. Similar developments have been encountered in other industries that have struggled to find a balance between cost savings and control (Pilarski, 2020).

The COVID-19 pandemic then further complicated the situation. Most of the world's economies found themselves in an artificial coma due to lockdowns and disruptions in global value chains, with international trade and international and domestic air transport worse off than most other segments of the economy.

Resistance to globalization has many sources. Some are political, exemplified by the rise of nationalism, which pits the interests of one's own population against the rest of the world (us versus them) or favors one section of the population against another (elites versus common people).

This trend is further reinforced by the desire to gain more control over the production process and reduce the risk of supply chain disruptions. Paradoxically, this can be partly achieved by the drive for greater automation, which can thrive despite the pandemic (Pilarski, 2020).

All of this may shift the economy from the practice of JIT (Just In Time, sourcing parts at a precise time from around the world) to the new concept of JIC (Just In Case, or pre-ordering parts to be prepared for complications in the supply chain and thus reduce uncertainty). Of course, this can only be achieved at the cost of higher costs and the company is now slowly moving towards less risk but also less benefit of a diversified supply chain (Pilarski, 2020).

According to Pilarski (2020), it is not yet clear if we are entering an era of deglobalization. However, the move away from globalization is accelerating for now. Current events are accentuating these trends. Only time will tell whether this will be a permanent shift or a temporary decline in globalization. Overall, aviation will be negatively affected by these developments, whether the world goes down the road of a mere slowdown in globalization or outright deglobalization.

VIII. Conclusion

After 60 years of globalization after the Second World War, and in particular after the period of hyper-globalization from 1990 to 2008, globalization slowed to a halt as a result of the global financial crisis of 2008–2009. This phase of slower or stagnant globalization continues to this day, and as other negative global events such as trade wars, the COVID-19 pandemic, the Russo-Ukrainian war or the preference for cooperation between ideologically close countries have added to this trend, many economists have begun to predict that the era of globalization is coming to an end and the world is entering a phase of deglobalization.

The developments in some economic indicators confirms the possible onset of deglobalization, but a number of indicators show that such a radical turn has not yet taken place and the world has not entered the deglobalization phase. Rather, the combination of various indicators suggests that there has been some correction of the previous hyper-globalization or a slowdown in globalization after 2008. The claim that the world has entered an era of deglobalization is still too simplistic and premature. It remains to be seen whether the development of the world economy will continue along the current trend of slower globalization, or whether it will enter a phase of deglobalization, or whether it will follow yet another scenario.

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