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Deglobalization: Have we reached the Limits of Interconnectivity?

Globalization is often viewed as a net positive for participating countries, promising growth, more efficient of supply chains and lower costs. However, recent global crises – from COVID-19 to the Russia-Ukraine War – have revealed cracks in the dependence on globalization. The reliance of supply chains being strongly linked to international trade have proven to be dangerous, as countries are unable to respond to these shocks and are thus at the mercy of external factors outside of their control. With the added pressure of an arguably less stable political climate of today – where diplomacy require countries having to take sides, condemn, or support the actions of other countries – the notion of the world being in a period of *reverse globalization* (or *deglobalization*) has been posited. My internship at the Czech Republic branch of SIEMENS – a multinational corporation (MNC) – has shed light on how sensitive global businesses are to outside changes; the economic state of a customer's country (inflation, interest rates, foreign exchange rates etc.) can greatly impact the financial performance of an MNC. I would have regular discussions with my supervisor about the economic performance of countries outside of the Czech Republic, highlighting the importance of outside circumstances to export based companies. The topic of globalization moving backwards was brought up multiple times during the program, through the internship and lectures. However, what is the actual credibility to this claim? Through the lens of the world's two biggest economies – U.S. and China – I wish to explore if there is any evidence of reverse globalization, and what this would mean for various stakeholders.

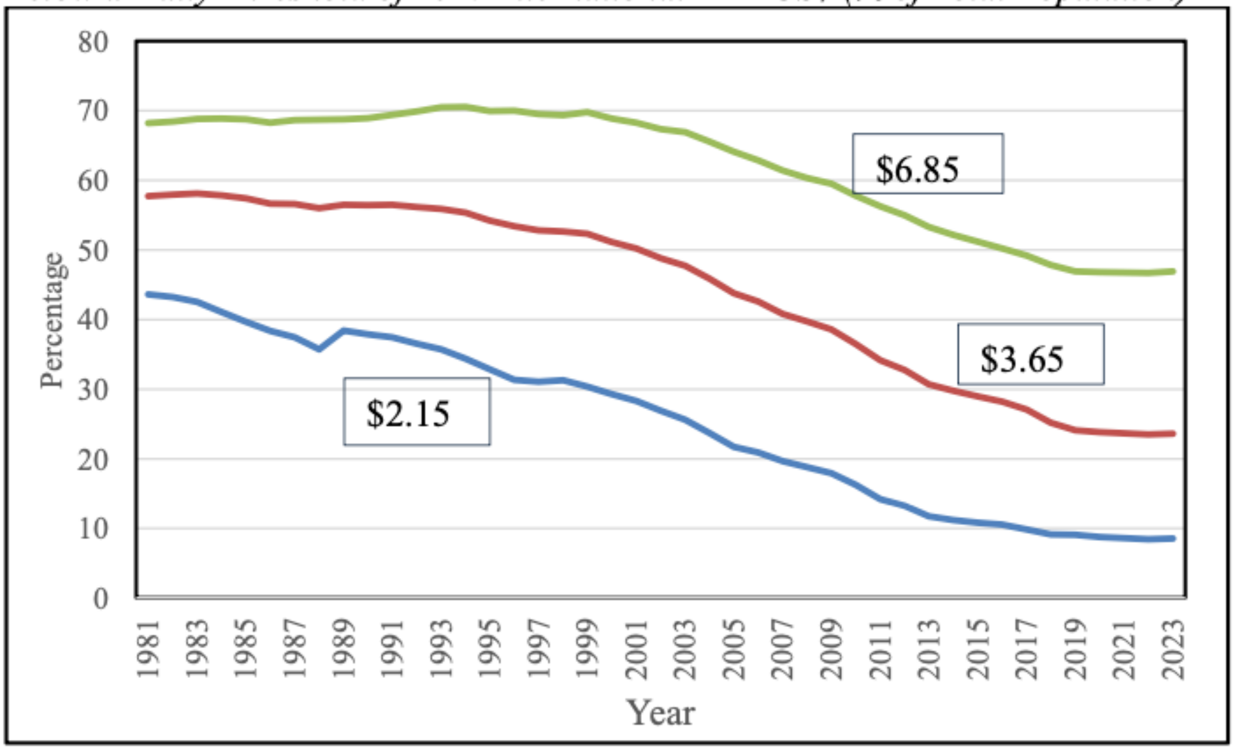
Part 1: The Background to Globalization

Any discussion about reverse globalization first requires an understanding of what globalization is, and the theoretical effects it has in economics. A conventional definition would state globalization as being the "increased flow of goods, capital, people, and ideas across international boundaries" (Stobierski 2021). With the persistent innovation of transportation technology and social media, the current world is a more interconnected than ever before in both the physical and ideological sense; the world is more globalized than ever. However, globalization cannot be traced back to a single point in time; it is a gradual, historical process which started since the dawn of societies when trade and the exchange of ideas could occur between neighboring cities or states. As technologies advanced, and new forms of transporting goods and people developed (such as the steam engine during the industrial revolution, airplanes or shipping containerization), the world began to shrink as the ability to travel greater distances in a shorter amount of time was unlocked, speeding up the process of globalization. It is an evolving process that is everchanging, which thus makes it difficult to track.

To add an additional layer of complexity, there are multiple definitions to globalization. Globalization is often viewed in a purely economic sense, but can also be viewed as "a process wherein a nation-state collaborates voluntarily with other nation-states to achieve improved economic, political, social, and cultural outcomes" (Papanikos 2024). A component of globalization is economic, but there are various noneconomic aspects to this process. Discussing just the economic outcomes – such as gauging globalization through the net trade volumes between countries – gives a less nuanced view of globalization. This is especially the case, since these outcomes are so interwoven with each other. Aspects like politics plays a strong role in economic policy, with consumer sentiment driving the need for increased tariffs or a more insular economic policy. In many countries, “it is the people who advocate for globalization” (Papanikos 2024). Thus, a well-rounded discussion would strive to take all aspects of globalization into account, to grasp the full picture of reality.

In pure economic theory, globalization lead to policies “that promote free trade, customs unions” (Papanikos 2024) which ultimately benefits consumers and producers by lowering prices of goods and costs of raw materials, thereby promoting growth for countries. The theory of comparative advantage states that “the free flow of production can maximize social welfare” (Ru 2020), suggesting that from an economist’s perspective globalization works toward an optimal allocation of resources, maximizing consumer and producer surplus and avoiding deadweight loss. Countries that can manufacture certain goods more efficiently or have access to certain highly demanded raw materials can trade those with countries who do not have the same ability to manufacture or access these goods, resulting in less wasted labor, time and cost. Globalization facilitates this mutually beneficial collaboration between countries, to further develop their countries by promoting economic growth. Consumers enjoy goods at a cheaper price (and at times higher quality) – due to the comparative advantage – and producers gain access to supply chains from others across the globe. Globalization has also been attributed to bringing developing countries to the first world, with the “most significant accomplishment (lying) in poverty alleviation” (Papanikos 2024).

Figure 1. *People Living in Households with Consumption or Income per Person Below a Daily Threshold of 2017 International PPP US$ (% of Total Population)*



Source: World Bank, United Nations and Author's Calculations (retrieved 14 December 2023).

According to statistics from the World Bank, economic globalization has shown a downward trend in poverty levels, as defined by the "percentage of individuals living on less than a fixed amount of US$ PPP per day" (Papanikos 2024). As seen in the figure above, there is an overall decline that is evenly distributed across all three income groups (depending on what fixed amount is used to define the poverty line), and projections show "fewer than 10% of the global population (living) on less than 2.15 dollars per day", with continued economic globalization expecting to further alleviate poverty. Notably, the opening of China was one of the factors that allowed it to become the largest economy in the world today. Its entrance into the World Trade Organization (WTO) in 2001 enabled "a couple hundred million … rural residents to become urban industrial workers in export-oriented industries", resulting in "more than 800 million Chinese people being lifted out of poverty" (Lau 2024). The U.S. has also benefitted from China's rise, as it is estimated that imports from China have helped to "reduce the U.S. core rate of inflation by an annual average of 1.3 percentage points since 1994" (Lau and Tang 2018). These effects of globalization advocate for the tangible positive impact that it has on countries, and the global economy.

However, this is not to say there are no inherent downsides to globalization. Putting the issues of cultural deterioration and social erosion (issues regarding immigration leading to social or religious tensions) aside, there are several negative economic implications that arise because of growth that stems from globalization. Despite it being conducive for "economic growth, capital pursuits and the working class in developing countries" research has shown it being detrimental to "middle and lower classes in developed countries and the bottom people in developing countries". The rapid growth of developing countries through globalization have exacerbated "inequality within Western countries" (Ru 2020). In developed countries, globalization increases competition as the number of competing firms expands beyond state or even national borders. Countries that have competitive advantage thus start to displace the jobs that the middle and lower classes tend to do. This is seen in the rise of China in the export industry and the labor effects that inflicted the U.S. as a result. The increased imports caused "higher unemployment, lower labor force participation, and reduced wages in labor markets that house import competing manufacturing industries" (Autor, Dorn, and Hanson 2013) as domestic firms struggle to compete with practices more efficient competitors. For developing countries, the bottom classes of people suffer from exploitation by corporations that demand long working hours with low paying wages, in countries that have looser workers' rights and a lack of labor unions. Shortcomings of globalization undeniably exist, but "an economy that trades voluntarily with the rest of the world always enjoys a positive net benefit in the aggregate" (Lau and Tang 2018), and it can be argued that it is the responsibility of the government to prevent these inequality gaps that arise from globalization through economic buffers and putting policies in place.

With the economic theory of net benefit from globalization in mind, it starts to become worrying when the forecast of a possible future with reverse globalization is in sight. Would the benefits that have unfolded from the rise of globalization gradually start to strip away? What are the signs that show reverse globalization is even happening?

Part 2: COVID-19, Political Conflicts & Reverse Globalization

While globalization is an evolving process that has been occurring for many years (and at different rates for different countries), there have notably been periods in which the rate of globalization has been significantly higher. This is most observed in the period still often referred to as "the golden era of globalization", where the end of the Cold War set the scene for a period of what has been termed "hyperglobalization" (Jana Titievskaia et al., 2020). Spearheaded by the U.S., hyperglobalization "represented … market globalism, economic neoliberalism and consumerist individualism"; the consumerist mindset spurred demand as people sought to spend more money. This was supported by the proliferation of "bilateral and multilateral preferential trade agreements" (Gong et al. 2022) and an increase in offshore production abroad, which sought to make supply chains and trade were more interconnected than ever. The end of the Cold War also gave aspiration to a level of global economic integration and governance, evidenced by the creation of institutions such as the WTO. China then joined the WTO in 2001, with members "jointly (lowering) their trade barriers towards China" (Autor, Dorn, and Hanson 2013), leading to an unprecedented level of global integration.

This rapid upward trend of globalization started to slow down as a result of the 2008 global financial crisis, with this subsequent trend becoming so noticeable it was famously termed “slowbalization” (Titievskaia 2020). This saw the slowing down of international trade, cross-border investment, cross-border banking, supply chains, and the momentum of globalization failed to return to its previous level. As the global economy was shaken by the crisis, many countries focused inward to deal with mass unemployment and cope with recessionary pressures and mindsets towards “global openness also hardened following job losses due to relocation of factories” and “austerity measures” (Titievskaia 2020). Thus, the cracks in globalization began to form as the dangers of an interdependent global economy were highlighted. However, this was only a slowdown in the extremely high levels of globalization. Deeper cracks would form, when another global crisis would strike in the form of COVID-19.

COVID-19 is an interesting case study, as the nature of it being a global pandemic effectively forced countries to close its borders, acting as a point of reference for potentially seeing the effects of “deglobalization”. The term “deglobalization” started to replace “slowbalization” (Titievskaia 2020) as the media and economists started to consider if the world was entering a new era of globalization, which would see the contraction of economic integration and a shift towards a more domestic focused approach. Looking at the statistics from this period, world merchandise trade “decreased by 7.4% in 2020 relative to 2019” (Liu, Ornelas, and Shi 2022), with the fall being attributed to the pandemic. The pandemic had forced governments to take measures to prevent the spread of the virus, which had a negative impact on international trade. However, the COVID-19 period cannot be used as an exact case study of reverse globalization; the nuanced nature of pandemic makes it an atypical case. Research showed that “more deaths in the main trading partners of a country (excluding China)” resulted in that country importing significantly "more from China" to offset the reduction in imports. In addition, there was significant heterogeneity in impact of goods imported. Positive trade effects were observed for industries that provided medical goods, whereas the negative effects persisted for a long time for non-essential durable goods (Hayakawa and Mukunoki 2021), due to the nature of this crisis being a medical emergency. In spite of these factors, on average moving from the pre-pandemic situation to the 2020 average saw a 10% reduction in imports from China (Liu, Ornelas, and Shi 2022). The effect of this contraction in global trade had negative impacts for the global economy as a whole, with estimates at the time projecting a 4.4% contraction in global GDP for 2020 by the International Monetary Fund (IMF) (Kumari 2021). The U.S. alone saw a contraction of "19.2% from its peak in the fourth quarter of 2019 through the second quarter of 2020" (Mutikani 2021), as it struggled to fight the pandemic recession. Likewise, China also struggled with the global crisis impacts with the outbreak of COVID-19 dropping economic growth from 6% in December 2019 to 2.2% in 2020 (Li 2023). This drop in performance is further accentuated when comparing MNCs with domestic companies (DCs), shedding more light on the vulnerabilities that arise with globalization. In a study measuring the stock price reactions of MNCs and DCs in 73 countries during the COVID-19 period, findings show that on average there was a significantly larger drop in value for MNCs compared to DCs, with MNCs exhibiting 1.7% lower returns on average compared to DCs during this period (Guedhami et al. 2022). This decline was owed to MNCs having a dependence on international supply chains which made them more vulnerable to border closures. Furthermore, lockdowns caused operational and logistical challenges for day-to-day operations. This challenged the traditional view of international diversification protecting companies from country internal shocks and highlighted the need for better risk management for these international companies.

Conversations about deglobalization or the end of the globalization is not an entirely nascent idea. Worsening relations between the U.S. and China, emphasized by the 2016 trade war and tit-for-tat tariffs sparked discussion about deglobalization. The COVID-19 pandemic only accelerated the conversation, and Russia's invasion of Ukraine in 2022 only served to make the reality of a reverse globalization a greater possibility. Global relations between countries are starting to see some fracturing, as the ideologies of countries shift towards nationalistic and populistic politics (Titievskaia 2020). The culmination of all of these factors have pushed mainstream media to consider the idea of reverse globalization, as the world seemingly becomes more divided and fragmentation of economies start to occur (Wolf 2022). However, it has been rightly noted that the repeated sensationalized statement claiming the "end of globalization" has been proven false each time (Lincicome 2023). Yet, these concerns are not entirely unfounded as there are signs that suggest the contraction or restructuring of businesses and supply chains.

As previously mentioned, globalization is phenomenon not easily tracked. Whilst it is possible to look at quantifiable measures that are somewhat connected to globalization, such as the net trade (volume of exports and imports) as an indicator of the level of globalization, it fails to capture the full extent of globalization as a means of interconnectivity. Shifts in supply chains, exchange in ideas and partnerships are not captured in this metric of net trade. In fact, there is no singular metric that can be used to determine the level of globalization in the world. Thus, we will instead observe various policies or statistical changes that indicate a shift in the current landscape of globalization. The numerous economic crises have caused countries to be more cautious and consider domestic priorities such as unemployment rates and inflationary pressures. This has moved to regions like the EU to shift towards both "free **and** fair trade" (Titievskaia 2020). This sentiment was echoed by the U.S., with accusations of unfair trade practices being the spark which started the trade war between the two countries. This sentiment of China enjoying unequitable gains from trade is echoed in today's world, as western countries such as Canada following suit with the U.S. in imposing 100% tariffs on Chinese electric vehicles, 50% on solar cells and 25% on lithium-ion batteries and other goods such as steel (Mukherjee and Sriram 2024). The U.S. has accused the Chinese government of dumping, by subsidizing these industries to boost production and exporting these goods at a low cost to other countries. Moreover, along with the COVID-19 shock and current geopolitical tensions, other factors such as emerging disruptive technologies and environmental concerns (climate change and the push for the green technologies) have pushed countries to reverse certain aspects of globalization (Gong et al. 2022). Pro-reshoring movements – returning the production to the company's original country – and policies that indicate the desire to domesticize value chains can be seen in major economies, including both the U.S. and China. The Biden administration pledged "billions of dollars to restore the resilience of US key supply chains" that were made vulnerable due to excessive offshoring and globalization. Similarly, in China policies such as the "Made in China 2025" and "Belt and Road Initiative" seek to take control and secure key supply chains for its domestic technology sector, by reducing the reliance on foreign technology imports and regionalizing trade routes. The U.S. has also stated that it will "no longer accept full dependability on far-away suppliers of vital products and services", of which these value chains have been monopolized by "China or India" (Brakman, Garretsen, and Van Witteloostuijn 2020). These global value chains (GVCs) by multinational corporations have also begun to trend towards a just-in-case logic as opposed to a just-in-time one, relying less on day-to-day material imports and instead hedging by returning to "stock buffers" to make them more "shock proof". It is predicted that this strategy may even be forced upon the business world by governments that demand local supply, due to the vital nature of those sectors (Brakman, Garretsen, and Van Witteloostuijn 2020). Disruptive technologies and technological innovations will undoubtedly also affect global value chains, as they alter the way in which production can be organized “across time and space”, changing the geographical constraints and method of production (especially with the robotization and automation) (Gong et al. 2022). However, while it these changes with reshoring, buffer/risk-assessment strategies and restructuring of value chains are occurring, it is not necessary that the international trade flows or capital flows will decrease. Instead, the world may move to an international economy that is “less global and more regional”, where there is an “increased penalty of distance, which favors economic integration with nearby countries” (Brakman, Garretsen, and Van Witteloostuijn 2020). This point is crucial, as the effect of the political tensions between the U.S. and China cannot be understated in the shifts that are occurring in globalization. Shifts and restructuring in value chains are occurring during a time in which the U.S. feels its hegemonic status being threatened by a rising China. Thus, the recent tariffs being placed by the U.S. may have political intentions in attempting to stay ahead of what it views as its main competitor in global status and may be a sign of more to come. Many see this period as the bifurcation of the world economy, as the U.S.-China relations start to decouple (Altman and Bastian 2023).

Is this enough evidence to conclude that reverse globalization is occurring? Despite warning signs, evidence suggests that the situation is not as drastic as the media proclaims, and quantitative data suggests that globalization has not gone in reverse. The DHL Global Connectedness Index shows that despite these factors, the global flows have not decreased and has in fact surpassed the levels of pre-pandemic conditions. The volume of world trade flows in goods was shown to reach “10% above pre-pandemic levels” (Altman and Bastian 2023) in the mid-2022, with trade in services also being back above. Despite the slow economic conditions of growth causing trade to weaken, the IMF's latest forecast still calls for "trade to grow at a modest 2.4% pace in 2023" and a "more typical 3.5% rate in 2024", predicting an upward trend in growth. Moreover, other evidence of globalization outside of trade also shows improvement. Foreign direct investment (FDI) flows from international companies had collapsed in 2020, but also went "back above pre-pandemic levels in 2021" and show no signs of collapse despite the COVID-19 pandemic and war in Ukraine. The COVID-19 pandemic had resulted in sluggish trade and capital flows but spiked international data flows with internet traffic (information/data flows) doubling in 2020 – with online interactions replacement in-person activity – and continued to frow "20% to 30% per year in 2021 and 2022". Moreover, whilst international people flows suffered the greatest decrease, this indicator also shows signs of recovery as the latest UN forecast predicts travel to foreign countries to be "just 5% to 20% below its pre-pandemic level in 2023".

There is also evidence to show that the decoupling of U.S.-China relations is not as severe as posited. DHL also examined 11 types of "trade, capital, information, and people flows" between the two countries, finding that U.S. flows declined in "eight out of 11 categories, falling on average from 9.3% to 7.3%", whilst China's flows declined in "seven out of 10 categories … from 17.8% to 14.3%" (Altman and Bastian 2023). While there has been a substantial reduction, the two countries are still the largest trading partners and most interconnected countries in the world, and the value of trade between the two had even "grew to a record high in 2022". Evidence also shows that countries have not moved to form regional blocs yet. The average distance traversed by international flows have been found to take place over longer distances, with it reaching "a record 5,100 kilometers in 2021" leading to the conclusion of "no robust evidence of a rising trend in levels of regionalization through 2021" (Lincicome 2023). While this does not rule out the possibility of future changes, this highlights that the current situation is not as dire as it appears to be. The fact that international flows are already somewhat regionalized, with “more than half of trade already (taking place) within roughly continent-sized regions” (Altman and Bastian 2023) limits the scope of increase for further regionalization. Furthermore, whilst re-shoring or nearshoring efforts by countries have been undertaken, many companies opt for other strategies for risk mitigation, such as “digitization and dual sourcing”. This puts the current situation of globalization in the world into greater context.

Part 3: Conclusion

Rather than a trend towards deglobalization, some see the current landscape with supply chains as “re-globalization” (Lincicome 2023). Countries are simply reorganizing their sources of goods and services, as a response to the gaps that were revealed through the various global crises. Supply shocks are “as old as internationalized production itself” and so the restructuring that we see today are just countries adjusting to the vulnerabilities of these global shocks, to better protect themselves for the future. This is not an unwise decision, as globalization and interconnectedness increase the risk of future viral infections and geopolitical conflicts (that stem from immigration, differences in religious views etc.). The world is simply adapting to the current situation; it does not necessarily mean the end of globalization.

Like many things in economics – despite best efforts to forecast future scenarios – only time will reveal the answer to how globalization will change. With globalization being so closely linked to political decision making and world view, it is possible that further fracturing occurs as China threatens to displace the U.S. and its hegemonic status. Protectionism policies serve as both an economic and political tool that can inflict greater damage to growth in globalization. Despite these road bumps, some believe in a “linear theory of economic history” which suggests an ”almost continuous trend towards economic globalization" (Papanikos 2024). There may be dips and contraction throughout history, but there is a strong economic, cultural, and social incentive to move towards globalization and collaboration. What are the possible impacts of the current trends we see today? Producers may see a rise in manufacturing costs, as they look for alternative sources of capital and raw materials, or reshore their factories to boost resilience against global shocks. Consumers may have to deal with rising inflation, as the price of goods and services increase with less efficient manufacturing practices and producers transferring increased costs to consumers. Governments will have to facilitate these changes, financially supporting essential businesses that undergo restructuring, and providing grants to consumers to cope with inflationary pressure. The extent of these effects is unclear. However, one thing is certain: globalization – an essential component of the global economy – will not disappear anytime soon.

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