Opinion **Markets Insight**

The myth of deglobalisation hides the real shifts

Despite distortions by the pandemic and the rise of China, cross-border trade looks healthy

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A worker on the production line of the Zhejiang Geely Holding Group. China's declining export-to-production ratio reflects the fact that its economy grew much faster than the rest of the world © Qilai Shen/Bloomberg

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The trade war of former US president Donald Trump and the supply chain snarl-ups caused by Covid turned deglobalisation into a mainstream topic. And two developments in the past two years suggest that the process might indeed have begun.

The first of these is the fact that global trade in goods in 2023 declined by a little over 1 per cent even though global GDP expanded by a trend-consistent 3.2 per cent, according to the IMF. This is unusual. However, we see this pullback in part as a normalisation after the extraordinary rebound in 2021-22 of the world economy following the pandemic. As a result, by the third quarter of 2022, global trade was almost 9 per cent above the pre-Covid level, and ahead of trend.

This was driven by the rapid easing of supply-chain problems, and amplified by the need to restock depleted inventories, which prompted a rebound in production and in cross-border trade. But some moderation was always likely once these effects had run their course. Moreover, it is now widely accepted that consumer demand is shifting away from goods and towards services — all part of post-Covid normalisation — and this dampens global trade. That said, the latest data suggests renewed expansion in trade since the start of 2024, albeit modest.

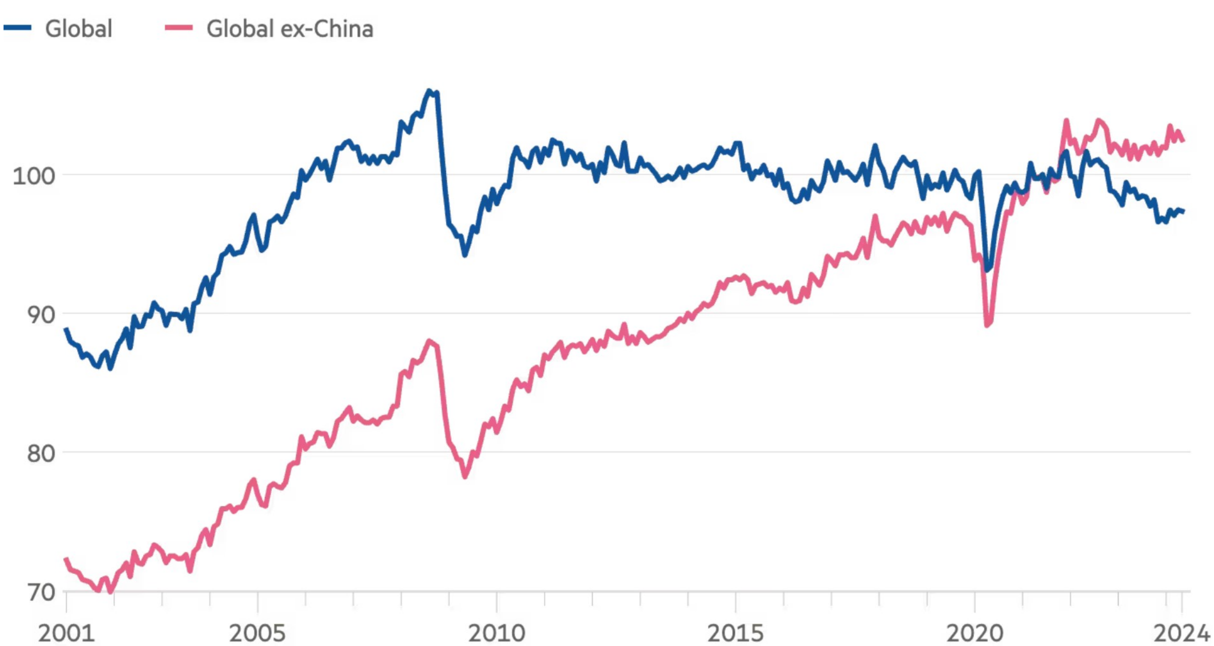
The pattern of export growth across regions since the fourth quarter of 2019 also contradicts the notion of deglobalisation. Emerging market economies' export growth (about 15 per cent) has far outstripped that of advanced economies (about 1 per cent), strongly suggesting that globalisation is in fact continuing — after all, it is exactly the process whereby EM economies gain export market share versus the historically dominant advanced economies.

The second indication can be found in the ratio of global trade (in goods) to global industrial production, as based on data provided by the authoritative Dutch central planning bureau. This ratio has been in decline since around mid-2022, suggestive of a deglobalisation trend.

Many economists believe deglobalisation would be inflationary as well as costly in growth terms — prompting a closer look at the data. It turns out that the recent downturn in this ratio, and the broadly flat trend since the end of the great recession, have been overwhelmingly influenced by China. The ratios of exports to industrial production and of imports to production in the country peaked as far back as the mid-2000s and have since more than halved.

China has a strong impact on global trade

Ratio of global trade to global industrial production (ratio of indices)



Central Planning Bureau: World Trade Monitor

But China's declining export-to-production ratio reflects the fact that its economy grew much faster than the rest of the world. It follows that an increasing proportion of its production is being absorbed by domestic buyers. And the declining import ratio mainly reflects the country's move up the value-added scale. As its manufacturing sector's technological sophistication rises, many of the goods that used to be imported — especially automobiles, capital goods, electronics and semiconductors — are now produced domestically.

Meanwhile, China's share in global exports has continued to increase, across practically all the major merchandise goods categories. Until recently, this was true also on the import side, but after a spike higher in 2020, its share in global imports has dropped back to its pre-Covid level.

Hence, a better way to describe what's going on than deglobalisation is to say that the rest of the global economy is becoming less important to China, but the country continues to become more important to the rest of the global economy.

Given China's strong and highly idiosyncratic impact on global trade, we also calculated the ratio of global trade to global industrial production excluding China. Unlike the global data, rather than stagnating since the end of the great recession and then declining for the past two years, the ratio has continued to rise. If anything, it accelerated through the post-pandemic economic rebound, and remains at a level above its trend. A far cry from deglobalisation indeed.

In short, there seems no evidence of a shift to deglobalisation — despite all the hoo-ha. And while strategies such as nearshoring or friendshoring are being pursued in various economies, they imply geographic shifts in cross-border trade, not deglobalisation. Meanwhile, re-onshoring faces enormous obstacles in advanced economies, not least extremely low unemployment rates. More generally, the shifting of patterns in global goods trade is as old as economic history itself.