



OPINION PIECE

Re-globalization or fragmentation: choices and challenges

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Globalization is still the keystone of international trade following the COVID-19 pandemic, although there seems to be a growing trend toward trade protectionism around the world. Two prevalent features of trade globalization are the coupling of global trade integration with production disintegration (Feenstra, 1998), that is the rising integration of world markets brought about the expansion of global value chains. There is no doubt that protectionism is increasing the cost of trade, but these two features have not collapsed despite crises.

Nevertheless, the recent increase in trade protectionism is presenting trade globalization with serious challenges. There is a growing tendency for world trade to become more localized and organized around regional trade groups, supported by related regional production supply chains: research has long established the dominant presence of Factory Europe, Factory North America and Factory Asia for supply chain trade (Baldwin and Lopez-Gonzalez, 2013) and protectionism could reinforce this dominance.

It is important to stress that, compared to the multilateral trade system overseen by the WTO, regional trade blocs are an inferior choice. The reasons for this are at least three-fold: regional trade blocs weaken the resilience of supply chains; they may enlarge the income gap between the rich and the poor; and they may not be beneficial for global environmental sustainability.

Before the pandemic, policymakers may only have needed to consider how much their own economies would gain from trade and who would gain and lose from various trade policies. In contrast, today policymakers, and international trade cooperation more broadly, need to consider a multitude of factors, including how to balance state security, domestic supply chain resilience, the income gap between the rich and the poor, inclusiveness, and environmental sustainability.

The potential effects of bloc-based regionalization or fragmentation on supply chain resilience are due to the fact that fragmentation could result in fewer economies engaging in production supply chains due to increased

artificial trade costs, such as tariffs and/or non-tariff barriers. Accordingly, the remaining economies that continue to engage in supply chains would reallocate their trade shares. As a result, some economies could lose out from this reallocation, and the resilience of the global supply chain could be weakened. Hence, bloc-based fragmentation could generate a threat to global supply chain resilience.

Trade openness is also important for poverty reduction although it does not imply poverty reduction by default. Understanding this point is crucial for developing economies, since, despite the view that opening up trade naturally reduces poverty, the opposite can also occur: trade can enlarge income inequality within economies if the gains from trade flow to the rich and hence widen the income gap between rich and poor. Recently, China has been an example of an economy that managed to reduce poverty through trade. China successfully reduced the population living in poverty from 55.75 million in 2015 to zero in 2021, an amazing achievement.

For developing economies, bloc-based regionalization could worsen the income gap between the rich and the poor and between urban and rural areas, although more empirical evidence on this is needed. The economic rationale is as follows. As fewer economies engage in regional supply chains, the cost for economies not engaged in supply chains of importing intermediate inputs increases, compared to the cost of those inputs for economies engaged in global supply chains. If an economy's export volume cannot increase simultaneously, the value-added from engaging in regional supply chains will decrease. With diminishing gains from trade, the poor would have a smaller share of the cake, and hence the income gap would widen.

It is also important to have a correct understanding of the nexus between trade and the environment. The consensus of the 2021 United Nations Climate Change Conference (COP26) was that every economy must share the responsibility of protecting the Earth and reduce carbon emissions. But there is debate on how the world's economies should share the emission costs



and, in particular, whether exporting producers or importing consumers should bear the costs. Exporting economies may argue that importing economies should pay the bills for carbon emissions, since importing economies consume the carbon-emitting products. However, importing economies may take the opposite view and argue that exporting economies earn income and even create domestic employment opportunities by producing carbon-emitting products. On this basis, a fair solution seems to be to split the bills between exporting producers and importing consumers.

Finally, a key question that needs to be addressed is the following: if bloc-based fragmentation is a second-best solution for international trade cooperation, how can we revive globalization? Re-globalization, i.e., expanding the

multilateral trading system toward new topics and new actors, seems an appropriate solution. Of course, as part of this process, it will be necessary to resolve some challenges in the WTO system, such as those currently facing the WTO Dispute Settlement Body, to ensure that multilateral cooperation continues to function and develop.

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