

FROM GLOBALIZATION TO DEGLOBALIZATION: ZOOMING INTO TRADE

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SUMMARY

After decades of increasing globalization both in trade, capital flows but even people to people movements, it seems the trend has turned towards deglobalization. This article shows some evidence of the decrease in merchandise, capital and, to a lesser extent people to people flows. In addition, zooming into trade, the article offers an account of the importance of the strategic competition between the US and China to foster the deglobalization trend further. This is true for trade but even beyond in the tech and finance space. Finally, the demise of the WTO could be one of the most relevant turning points towards deglobalization, especially as far as trade is concerned. This should bring downward pressure to growth globally.

KEYWORDS

De globalización, Trade, US-China trade war, WTO.

1. Globalization as cornerstone of international economics turning the page

As probably the most prominent economic process in the 21st century, globalization has attracted wide research interests and considerable support from academia for many decades, especially after the Second World War. There are many benefits which economic research has attributed to globalization, from higher economic growth to poverty reduction and even lower inflation. For instance, Khan & Riskin (2001) finds that China's poverty reduction can be attributed to the opening up of its economy. What's more, Rogoff (2003) argues that the globalization process helps push down inflation and any reversal of the free flow of production factors will re-introduce price pressure. In addition, Tomohara and Taki (2011) put forward that globalization brings higher wages for local employers as foreign companies are given market access.

However, the economic literature on globalization has taken a less positive turn since 2008. Hillebrand (2010), for example, argues that protectionism may improve income equality in some countries although he still thinks that a retreat from globalization will lead to profoundly negative implications to the global economy.

On the basis of the increasingly heated debate on where we stand with globalization versus deglobalization and its importance for the global economy, this paper aims at shedding some light on the trend and current degree of deglobalization focusing on trade.

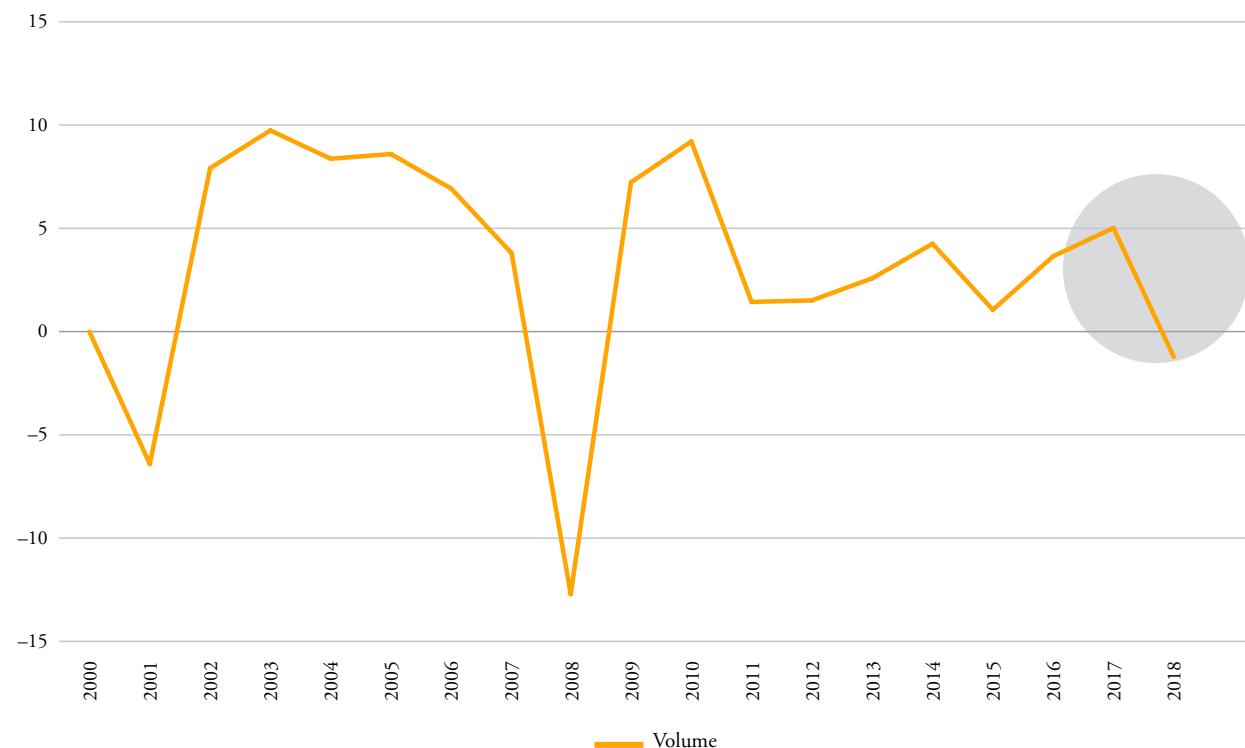
There seems to be enough evidence by now to argue that the globalization process, including the free flow of trade, capital and people, has stalled since the global financial crisis in 2008. Regarding the movement of merchandise, after a sharp decline in 2008, the general expectation was that trade would continue to grow at rates similar to those previous to the crisis. Actually, this has not been the case. Chart 1 shows that trade volume grew by an average of 3.5% from 2009 to 2018, which is much slower than the 7.6% average growth before the 2008 financial Crisis. Furthermore, we are now at a zero growth rate in trade, which is understandable on the back of the US-China trade war and several other protectionist waves, such as the US with Europe but also between Japan and Korea.

In line with the deceleration in trade, cross-border capital flows have also declined. This is true generally but also for the most stable (and possibly produc-

Chart 1

Global trade in volume

% YoY



Source: UNCTAD, Bloomberg, Natixis.

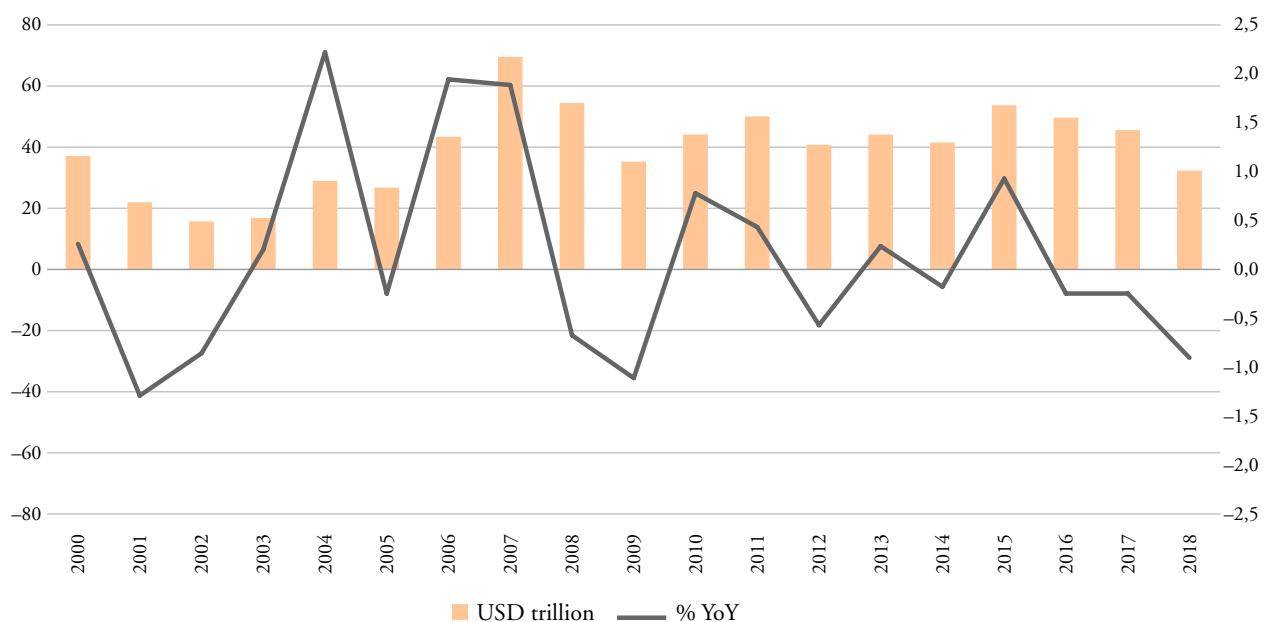
tive) type of capital flow, namely foreign direct investment (FDI), which has declined sharply to the level of 2008 (chart 2). In fact, the average growth rate of outward FDI since 2000 points to a minimal 0.8%, with a decline of -28% in 2018 owing to escalating trade tensions. It is hard to know whether FDI is no longer growing because of lack of demand or because of constraints for investors to operate. In any event, the difference in returns among recipient countries are such that the much lower FDI nowadays could be seen as a critical sign of fragmentation of global capital markets. As if FDI trends were not enough, portfolio flows into emerging economies have also slowed down since the European Sovereign Crisis in 2010 (chart 3). The exception has been Emerging Asia until 2017 but portfolio inflows into Asia have started to come down too since 2017 (chart 4). The picture for cross-border lending is more mixed. Total cross-border lending has not come back to the levels before 2008 but there is

a shift towards more lending into Emerging Markets and less into developed economies (chart 5).

As people-to-people movement, either in terms of migration or tourism, globalization is still on the go. In fact, the number of international migrant has been rising, suggesting movements of labor remains actively increasing (chart 6). The relatively more short-term visitors' arrival data also confirms the pattern with a steady growth rate of 4% (chart 7). However, we start to see some signs of increasing restrictions. As shown in chart 6 & 7, both migrant and visitor numbers in the world is experiencing slower growth. What's more, featuring many anti-immigration movements, immigration controls have been significantly tightened especially in the US with a rapid increase in visa denials (chart 8). This is an obvious barrier for further integration of the labor market globally, given the importance of the US labor market.

Chart 2

World outward FDI flow

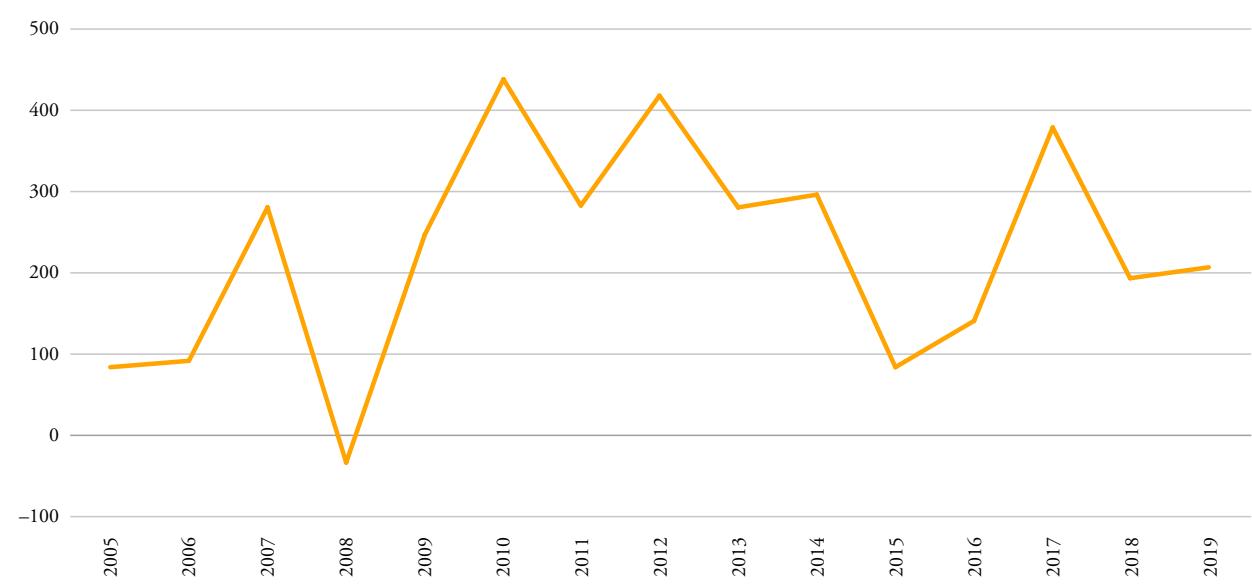


Source: UNCTAD, Natixis.

Chart 3

Total Portfolio Flows into Emerging Markets

USD bn



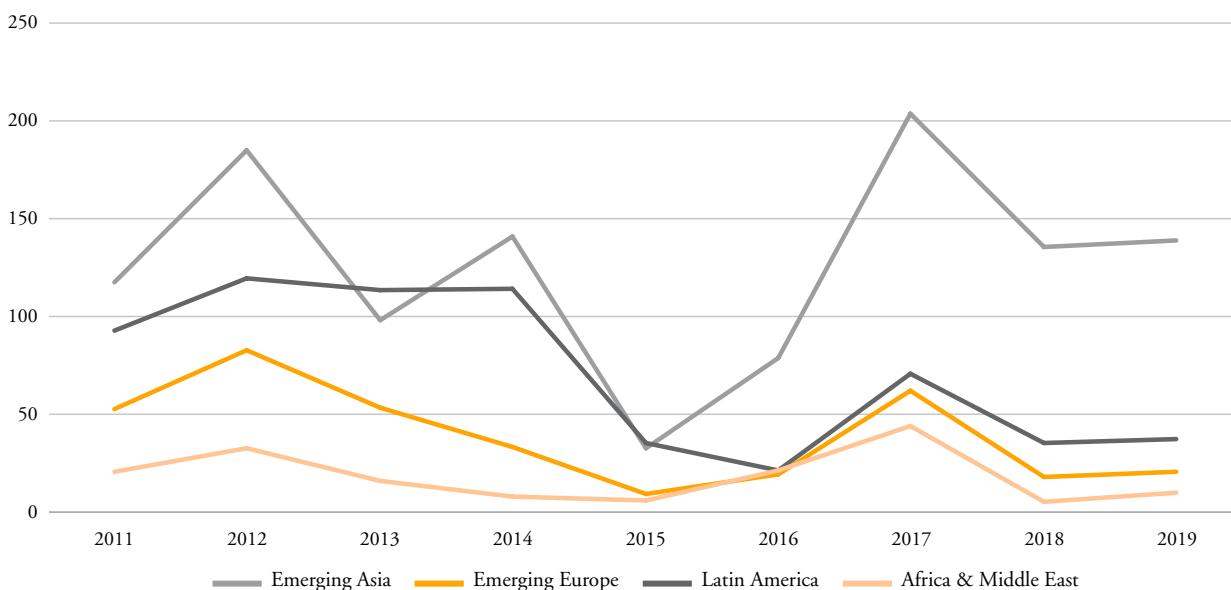
Source: IIF, Natixis.

LAS CLAVES DE LA GLOBALIZACIÓN 4.0

Chart 4

Total Portfolio Flows into Emerging Markets by region

USD bn

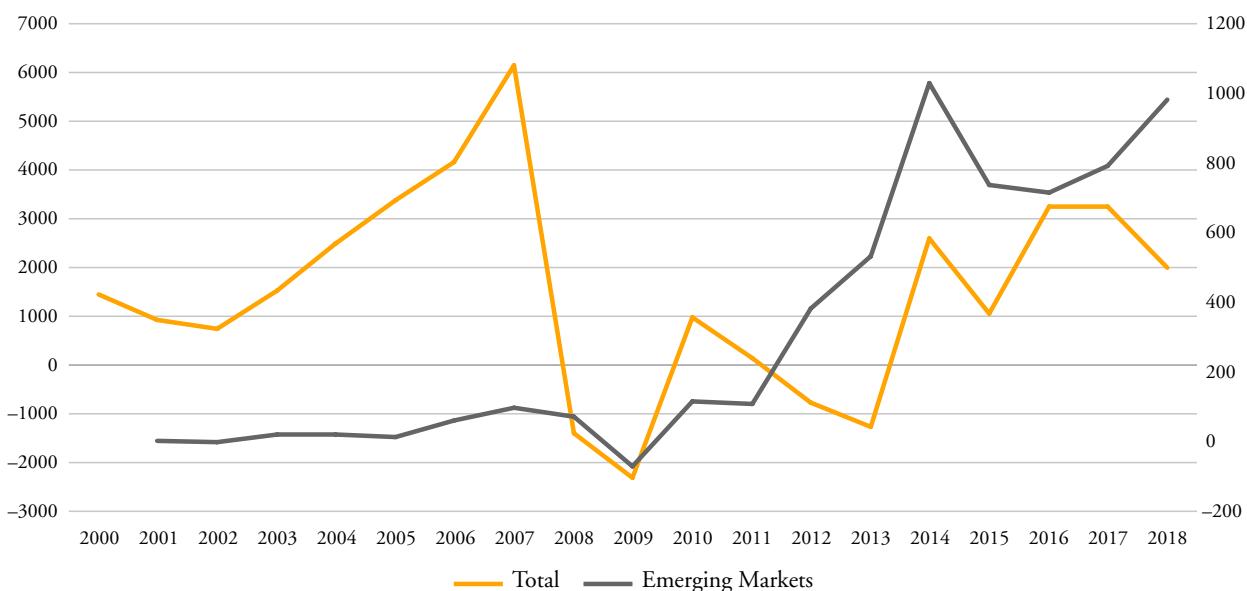


Source: IIF, Natixis.

Chart 5

Global banking flow

USD bn

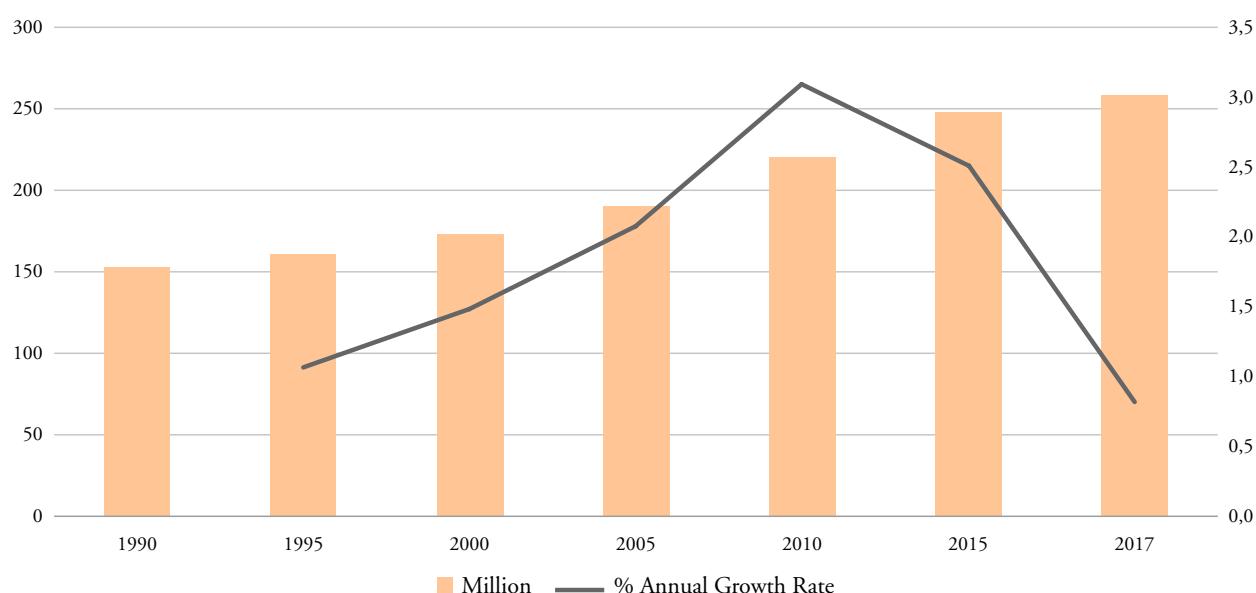


Source: BIS, Natixis.

(*) EM gauged based on available data, including Brazil, Chile, China, Hong Kong, Indonesia, India, South Korea, Macao, Mexico, Philippines, Russia, Singapore, Turkey and South Africa.

Chart 6

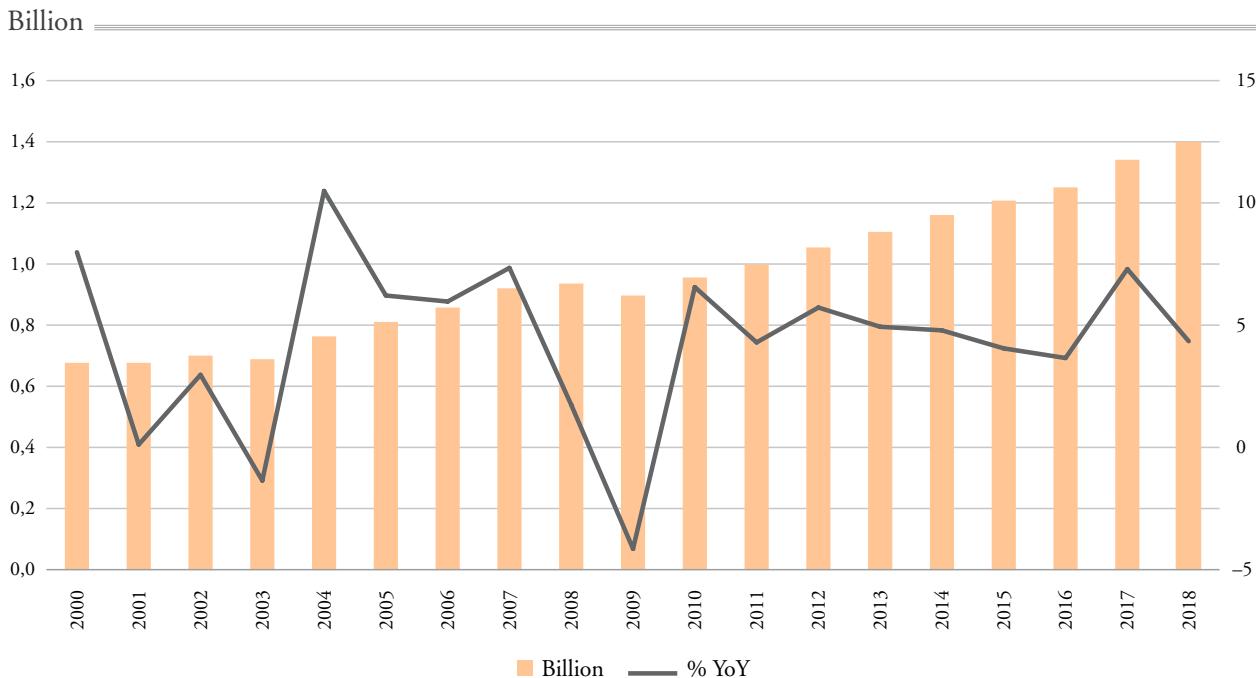
International migrant stock



Source: UN, Natixis.

Chart 7

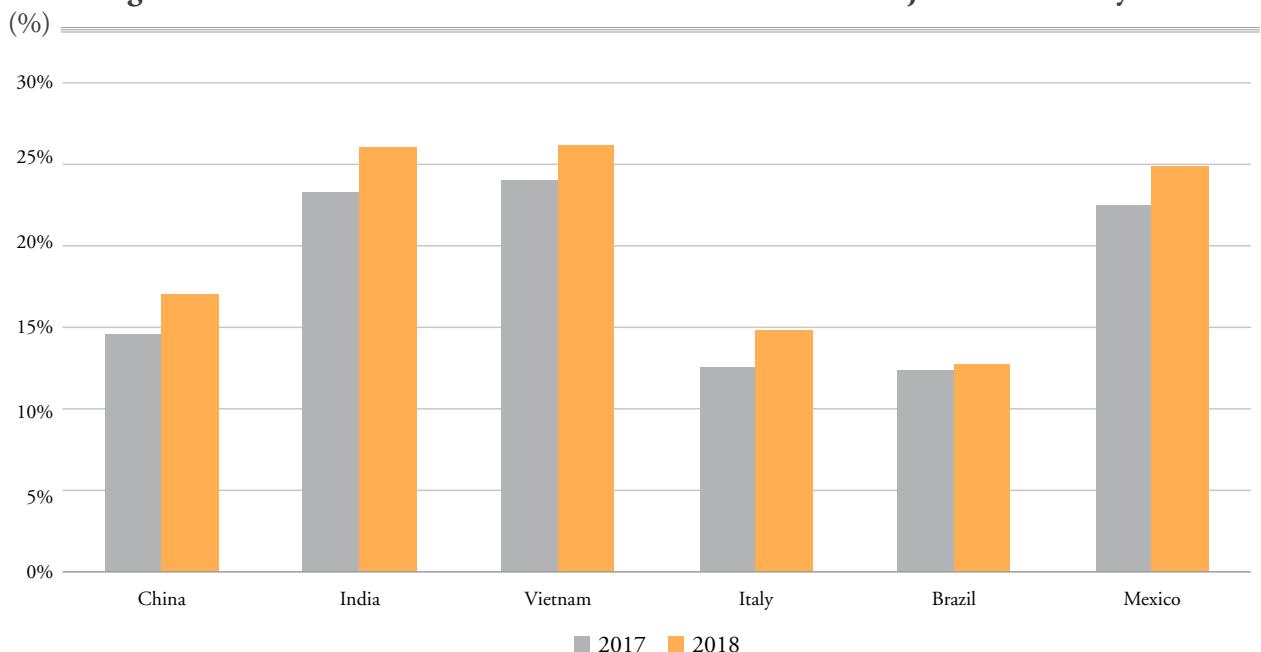
International tourist arrival



Source: UNWTO, Natixis.

Chart 8

Increasing visa refusal rate for tourist and business travelers from major economies by US (%)



Source: US Department of State, Natixis.

The question, thus, is how have we gotten here and what to expect next. One key aspect is the increasingly hostile relation between the two largest economies in the world, namely the US and China. Analyzing the reasons for this and its future consequences can offer some cues as to the potential for additional deglobalization forces. The next section reviews the trade aspects of the US-China strategic competition, followed by a section on other economic aspects as well as a brief account of the implications of the ongoing US-China trade war on the World Trade Organization (WTO) and, thereby, to the further deglobalization of trade.

2. The US-China trade war

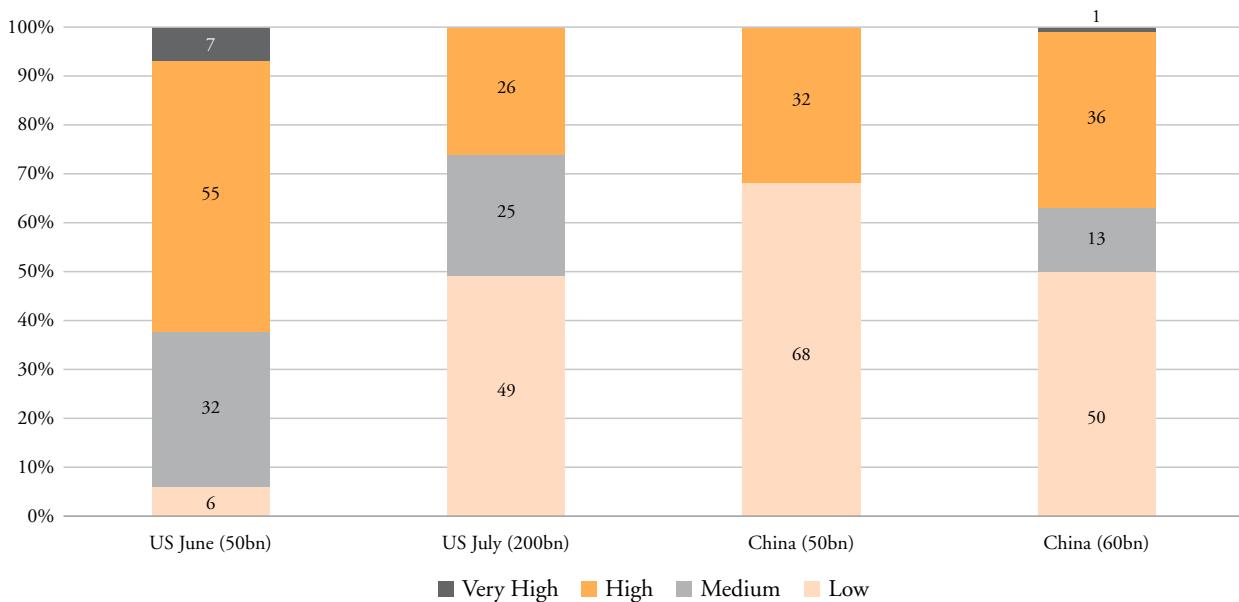
To understand the trade war and its implications, a good starting point is to review the actions taken by both sides so far. From seemingly untargeted measures announced in early February 2018 for solar panels and washing machines, the US has been moving in increasingly targeted direction against China and away from current global status quo. The most ob-

vious instance of this was the announcement of 25 percent additional import duties to be applied to \$50 billion equivalents of imported goods from China on the basis of China's infringement of intellectual property rights. More importantly, about two thirds of those import tariffs have been applied since 6 July 2018. The speedy introduction of the announced import tariffs by the US, without allowing much time for negotiation of a deal between China and the US, shows that the US resolution to change global trade flows, at least as far as China is concerned. On that basis, China had no choice but to retaliate with equivalent import tariffs on US goods.

Since then, the list of Chinese imports on which the US is aiming to increase tariffs has expanded to cover an additional \$200 billion of goods. Thanks to a truce reached on the side-lines of the Buenos Aires G20 summit in late 2018, the 25 percent US import tariff on an additional \$200 billion of goods from China was postponed, but it is clear that this was just a truce to buy time for both sides.

Chart 9

A comparison of the US-China targeted products released in June and July
(%)



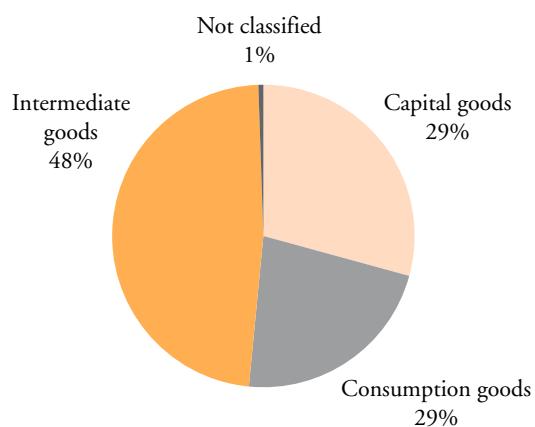
Source: Natixis, USITC, UN Comtrade.

China's ability to retaliate against US trade measures has obviously been more limited, at least on the trade side, because it does not import enough goods from the US to match the US import tariffs. This explains why China's second batch of retaliatory measures was more moderate, at least in size (\$60 billion). Unfortunately, the peace did not sustain as the turning point came in March 2019 when the US raised tariff to 25 percent from 10 percent on the \$200 billion Chinese imports. Ever since then, the market has seen no shortage of hostility such as US's move to place Huawei into its *entity list* in May, banning it from purchasing from US companies and China retaliation to increase tariff on \$60 billion worth of product at 25, 20 and 10 percent respectively in June. Between periods of tension escalation is tentative cooling-off phases, as President Xi and President Trump repeatedly rekindled trade talks before major meetings but subsequently let the market down all of a sudden. The tale of the two went on until almost full tariff coverage of Chinese imports was placed and made pending by President Trump on August 13 followed by declaring China as a currency manipulator. The confrontation

went on as China retaliated with tariff on USD 75 billion worth of US goods on August 23rd and lodged a WTO tariff case against the US on September 2, 2019. Soon however, China and US agreed to 13th

Chart 10

Decomposition of US' imports from China under the 200 billion tariff list



Source: Natixis, USITC.

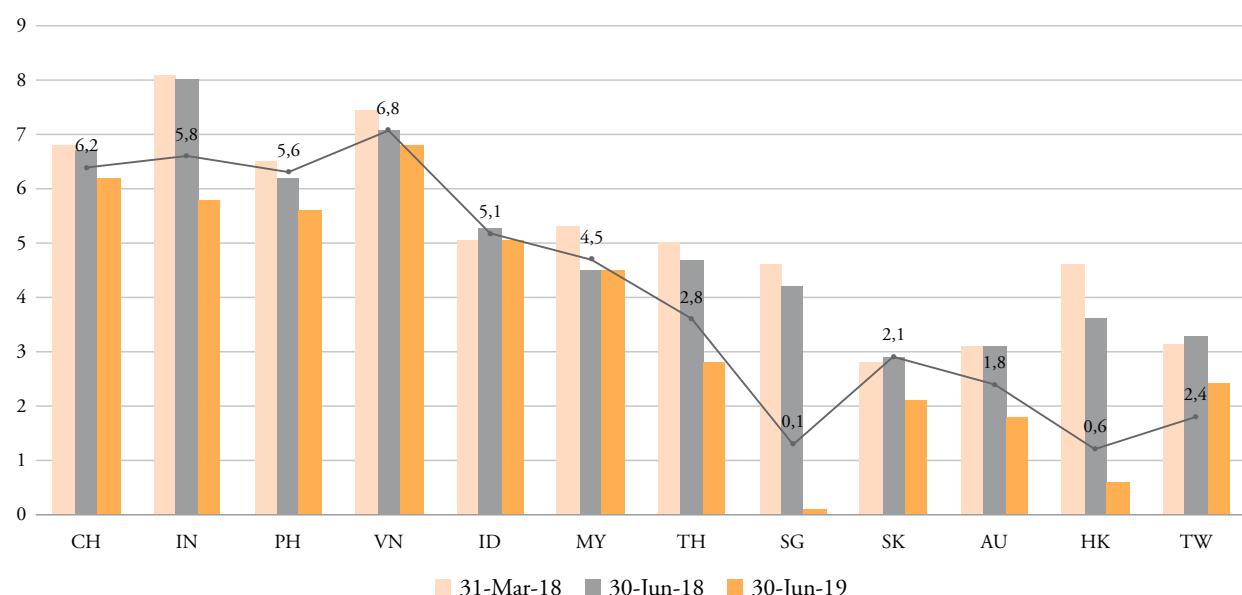
round of trade talks on September 5th and China unveils tariff exemption list for US imports on September 11th, 2019, suggesting a new cooling off period is on the doorstep. As rounds of escalation and de-escalation of trade tension took place, the market seems to gradually adapt to a new norm of hospitality between the two world superpowers. These tariffs and complaints feature the severe confrontation between US and China. Rounds of conflicts and making up seem to be the main theme since early 2018, rapturing global supply chain over and over again.

Arguably, the Sino-US trade war has been a landmark event for deglobalization forces in the realm of trade. In fact, global trade has seen declining since 2018 both in value and volume and there have been relevant disruptions of the global supply chain. The ensuing economic uncertainty has put downward pressure on investment, which has led the International Monetary Fund in its July World Economic Outlook to downgrade the forecast for global growth, but especially for China and Asia (chart 11). Overall, rounds of de-escalation and re-escalation of the US-China trade war have significantly

raised the risk of protectionism, weighing on market sentiment and deteriorating global risk appetite. What's more, in response to heightened geopolitical risk in China and Asia (as expanding sanctions are threatened by the US to be imposed on Vietnam), massive reshoring away from China, and possibly Asia are taking place. This trend is going to significantly distort global trade and capital flows, pushing the global economy further towards the trend of deglobalization.

Apart from the above, following the path of the US, other countries are leveraging protectionism and trade as weapons to achieve unilateral benefits. For example, Japan's recently tightened its export controls on South Korean imports from Japan. Also the US has opened a number of cases against European exports into the US and has even threatened to expand those tariffs to much more relevant sectors, such as the European automobile industry. More generally, the fear exists that other countries may engage in further protectionist measures, introducing a race to the bottom.

Chart 11
Asia growth slowed across the board



Sources: Natixis, Datastream.

3. From tariffs to other types of protectionism

Apart from trade measures, the US has leveraged several other weapons against China. Most notably, on December 1, 2018 the arrest of Huawei's chief financial officer took place in Canada at the US request, based on a potential breach of sanctions against Iran. This case testifies the US' intention to weaponize its current hegemonic position as a rule setter. As the national champion in China's telecommunication sector, Huawei has attracted multiple restrictions on top of the arrest. For instance, the US has tightened its control over technology transfer into China and, in particular Huawei, by placing this company into the US *entity list*, which effectively forbids US companies to conduct business with this company. In addition, many countries have voiced out concerns of privacy and Chinese spy suspicion for the 5G & smartphone manufacturer to harness its growth and the outlook of China's Information and communications technology development. As such, the sniped Huawei symbolize the deterred process of technology globalization, which will in turn drive fragmentation of investment, manufacturing and employment.

Beyond Huawei, the US administration has conducted a reform of its Committee on Foreign Investment in the United States Committee (CFIUS), with the view of making it easier to blocking an increasing amount of China's M&A into US, especially on the high-end industrial sector. Technology protectionism is actually going beyond the US into other developed countries, especially the European Union, which has finally set up its own investment screening device last April.

Beyond tech protectionism, there seems to be an embryonic move towards financial decoupling due to geopolitical trends. In fact, several Chinese companies including SMIC and Alibaba have announced the voluntarily delisting from US stock exchanges. However, concerns have been raised whether such voluntary delisting may lead to less access to USD issuance and in return shortage of USD liquidity, given the dominance of the US financial system in sourcing greenback financing. In response, China has adopted policies to encourage the funding for tech companies including the launch of SSE STAR Market and

loosening regulations for financing. Such potential financial decoupling deepens concerns over the trend of deglobalization.

4. The demise of the WTO and its implications

The WTO has become increasingly dysfunctional during the last few years and, in particular, since the arrival of President Trump to power. Three main reasons can be identified. First, the increase in membership has brought about heterogeneity as more emerging countries joined the club. This is clearly shown by the lack of agreement on concluding the Doha round of trade liberalisation measures, which launched in 2001. Second, some new members, especially China but also Vietnam, are still state-led planned economies, a model the WTO rules have not been designed for. Third, under the Trump administration, the United States has clearly turned its back on the WTO as an institution that can solve the US's perceived trade problems. A further decision by President Trump that unsettled the global trading community in 2018 was the announcement that (continuing a policy initiated by President Obama) the US would block reappointments to the WTO's appeals panel, on the grounds that the appellate body took too long to reach decisions and tended to overreach. At the time of writing, the appellate body is down to only three members (out of seven) of which two will end their terms in December 2019. If the US administration continues to refuse new appointments, the WTO's dispute settlement mechanism will no longer be able to function. This threat comes two sides: President Trump's profound disdain for multilateralism, and China's state-led system, which is not compatible with the liberal nature of the global trading system and might have weakened the WTO's foundations. China has influenced the WTO's rule setting, which is intended to ensure a level playing field. In fact, it has become increasingly clear that the existing rules governing the WTO cannot adequately control the use of non-market measures designed to favour a specific trading partner (namely China) over others. To this end, several proposals have been made to reform of the WTO, including from the European Union, but none of them can really accommodate both China and the US under the same umbrella. The most

likely scenario is for the WTO to become a zombie institution as the US disengages further. Should this scenario materialize, the pale international negotiation mechanism will become incapable of mediating international trade disputes and building multilateral trust, driving economies to seek their own leverages and solutions.

5. Some tentative conclusions

After decades of increasing globalization both in trade, capital flows but even people to people movements, it seems the trend has turned towards deglobalization. This article shows some evidence of the decrease in merchandise, capital and, to a lesser extent people to people flows. In addition, zooming into trade, the article offers an account of the importance of the strategic competition between the US and China to foster the

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