Box 2: Geopolitical risk and global value chain fragmentation

The Covid-19 pandemic, the war in Ukraine and recent disruptions in the Red Sea have highlighted the vulnerabilities associated with global supply chains that have become increasingly concentrated in recent decades, most notably supply shortages and rapid price spikes.

More fundamentally, it is evident that national and economic security considerations are re-shaping industrial policies in some advanced economies – with activity pivoting towards domestic production ('re-shoring'), shortening of supply chains ('near-shoring') or favouring strategic allies in production location decisions ('friend-shoring'). These evolving industrial strategies are especially prevalent in technologies that are critical to the climate and digital transitions.^

In short, priorities are shifting from strategies geared around *efficiency* of production (or, in economic terms, from production based on comparative advantage) towards strategies geared around *security* of production.

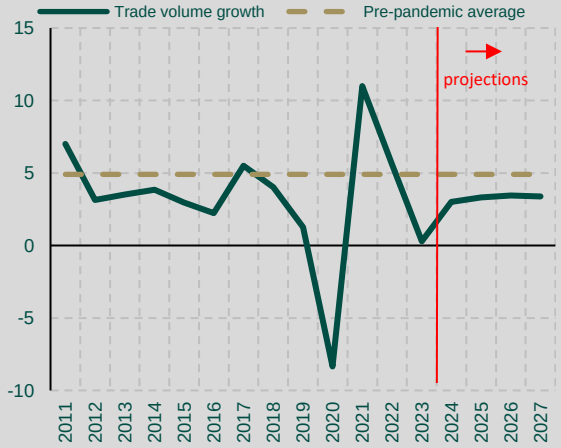
These developments are overlapping with historically weak global trade growth: global trade stood at just over 60 per cent of GDP in 2022, effectively the same level as in 2008 (to put this into perspective, global trade as a share of GDP had increased by 20 percentage points in the previous two decades).

Last year, global trade is estimated to have grown by less than 1 per cent, well below the pre-pandemic long-run average growth rate of almost 5 per cent; the IMF is projecting relatively muted growth in the years ahead, with trade distortions and geo-economic fragmentation expected to weigh on global trade (**figure 5A**).

Moreover, recent years have seen a sharp increase in the number of trade restrictions being imposed: according to *Global Trade Alert*, more than 3,000 new restrictions on trade were introduced last year, around five times the annual average in the decade leading up to the pandemic. The IMF estimates that that trade fragmentation could reduce global GDP by between 0.3 and 2.3 per cent in the long-run, with estimates increasing to 7 per cent if adjustment costs are assumed to be greater.^^

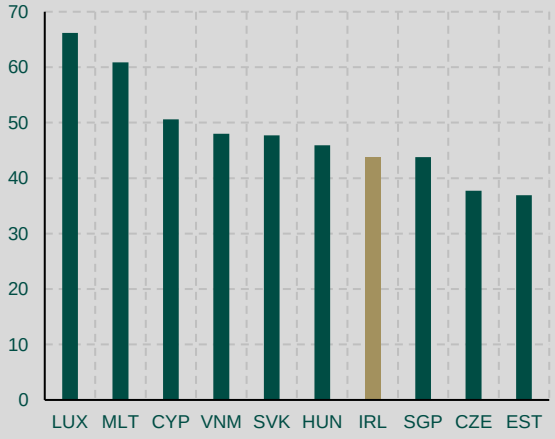
Figure 5: Trade and global value chain integration

A: IMF world trade volume forecast, per cent



Source: IMF World Economic Outlook April 2024

B: Backward participation in GVCs in 2020, per cent



Note: measured as the value of imported intermediate goods and services embodied in exports, as a share of total exports. Figures refer to top ten countries.
Source: OECD TiVA database

Developments in global trade are of particular importance for Ireland, given the highly globalised nature of the economy. In contrast to wider developments, Ireland's trade as a share of GDP has continued to increase in recent years, reaching more than 230 per cent in 2023. The Irish economy is also highly integrated into global value chains, with more than 40 per cent of gross exports' content originating abroad (**figure 5B**).

Against this backdrop, an intensification of trade fragmentation or de-globalisation would pose a significant risk to Irish exports, with knock-on implications for employment and tax receipts. Forthcoming analysis will explore the impacts of a slowdown in world trade on the Irish economy.^^^

^ See *EU Industrial Policy and Potential Implications for Ireland, Economic Insights –April 2024*, available at: https://www.gov.ie/en/publication/fdbbf-economic-insights-volume-2-2024/
^^ https://www.imf.org/en/Publications/WP/Issues/2023/03/24/Fragmentation-in-Global-Trade-Accounting-for-Commodities-531327
^^^ Research as part of the Department's Joint Research Programme with the ESRI.