

The Macroeconomic Effects of Deglobalisation



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Abstract

We assess the macroeconomic impact of two structural deglobalisation scenarios: 1) rising barriers to trade between regions and 2) stronger home bias (a higher preference for domestic products). Our simulations show that deglobalisation significantly reduces trade and economic activity in major economies, such as the euro area and the US, while raising inflation during the transition period. The more open and integrated an economy, the stronger the impact. A stronger home bias decreases global trade and increases inflation, while the effects on individual regions depend crucially on the home bias dynamics of their trade partners. Lower global integration changes the balance between external and domestic shocks, making domestic drivers more prominent. It also weakens structural trends such as the ‘globalisation of inflation’.

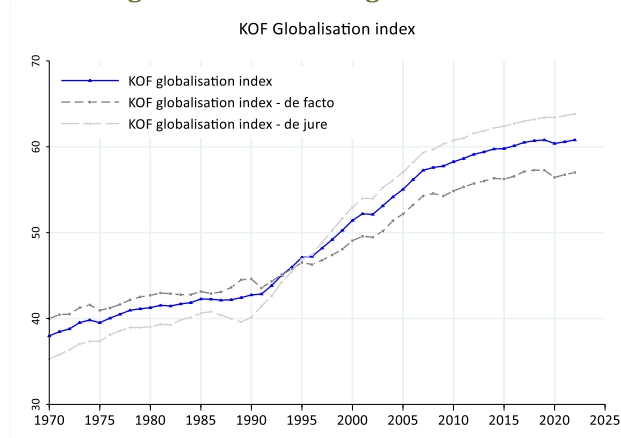
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Deglobalisation: not there yet, but not implausible

Following decades of rising global economic integration, globalisation faces increasing threats. These threats are arising in the form of growing physical and security threats to trade, but also from an apparent diminishing political appetite for further integration in some parts of the world. Using a multi country estimated macroeconomic model, we assess how longer-term deglobalisation trends, could affect growth, inflation, and economic stability in the euro area. Our results show that fragmentation is costly: it lowers output, raises inflation, and makes economies more exposed to domestic shocks. The analysis thus goes beyond current developments in trade policy, notably the broad-based imposition of tariffs by the US.

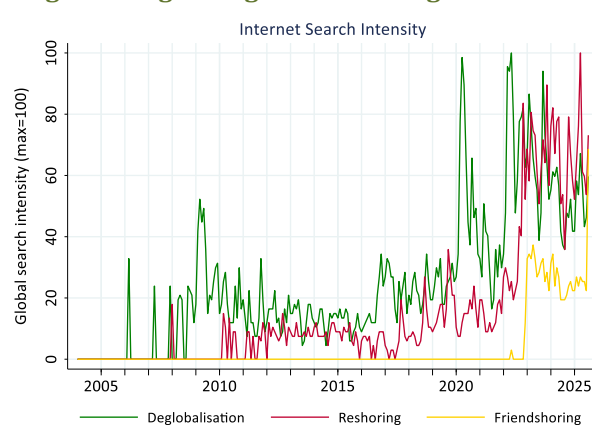
While the evidence, at least until 2024, points to stagnation in global integration, rather than to a retreat (Figure 1), there are growing indications of incipient fragmentation and regional realignment in goods trade, portfolio flows and bilateral investments (e.g. Gopinath et al., 2025). With growing talk of deglobalisation, fragmentation and related terms (Figure 2), prospects of a further departure from the hitherto dominating policy premise that international economic integration, embedded in a rules-based framework, is in any economy's self-interest, constitute plausible scenarios.

Figure 1. The state of globalisation



Note: The KOF Globalisation Index is a composite index, which measures the economic, social and political dimensions of globalisation. The de facto globalisation index measures actual international flows and activities, while the de jure globalisation index measures policies and conditions that, in principle, enable, facilitate and foster flows and activities. Source: Gygli et al 2019.

Figure 2. A growing interest in deglobalisation



Note: The graph shows the global internet search-intensity for the listed topics. The peak search-intensity is set to 100. Source: Google Trends.

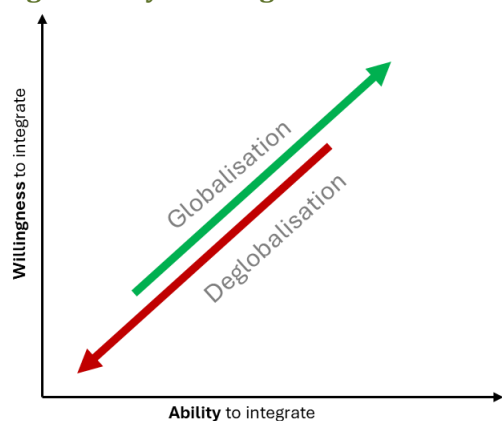
(De)globalisation = (in)ability + (un)willingness to integrate

We characterise globalisation as an outcome of two main sets of drivers, namely the *ability* and the *willingness* of countries to integrate (see Figure 3). “Ability” reflects how easy it is to trade — for example depending on transport costs, the logistics, or the operation of global supply chains. “Willingness” reflects policy choices and public attitudes towards openness. The period of “hyperglobalisation” (Antràs, 2020), which stretched from the mid-1980s to the time of Global Financial Crisis, combined both: a greater ability to integrate due to faster and cheaper international transport, while progress in information and communication technology facilitated international production and the reliance on a rapidly expanding global labour force. The willingness to integrate, meanwhile, was exemplified by trade liberalisation and the widespread conviction that an open and rules-based trade system would bring benefits. Deglobalisation, by contrast, occurs when either or both forces reverse, i.e. when physical or policy barriers rise, or when economies turn inward.

Accordingly, we frame deglobalisation as a reversal along either of these two dimensions. For our analysis, this translates into two deglobalisation scenarios (Figure 4): 1) exogenous disruptions to regions’ ability to trade with each other, typically against their will, as captured by higher trade costs, and 2) greater self-chosen inward orientation of individual regions, as reflected in a higher home bias. Both scenarios are visible today: physical obstacles to trade have been multiplying (e.g. COVID-19 pandemic, climate-related disruptions, conflicts along trade routes), while events such as Brexit or the recent US withdrawal from several intergovernmental organisations illustrate a faltering appetite for global integration in some regions.

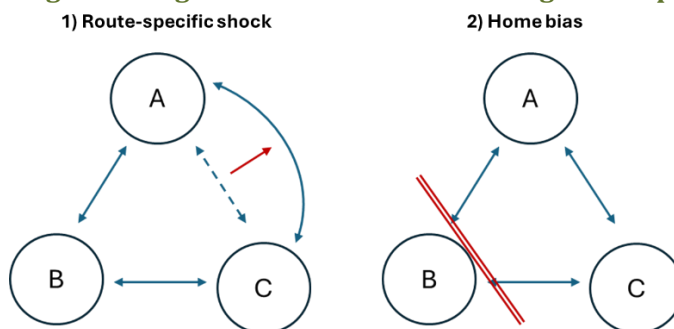
Our exercise consists in assessing the macroeconomic impact and transmission mechanisms of these two deglobalisation scenarios (see Buelens et al., 2025). For this, we use the European Commission’s GM model (Cardani et al., 2023), an estimated global dynamic general equilibrium framework, that considers three regions, namely the euro area (EA), the US, and the rest of the world (RoW).

Figure 3. Stylised deglobalisation forces



Note: The figure illustrates the intensity of globalisation as a function of economies’ ability and willingness to integrate.

Figure 4. Deglobalisation forces in a 3-region setup



Note: The illustrations represent our two deglobalisation narratives. In the left panel, a route specific shock is represented as an increase in the distance between A and C, while the distances A-B and B-C remain unchanged. In the right panel, region B’s home bias increases resulting in greater isolation from region A and region C’s exporters.

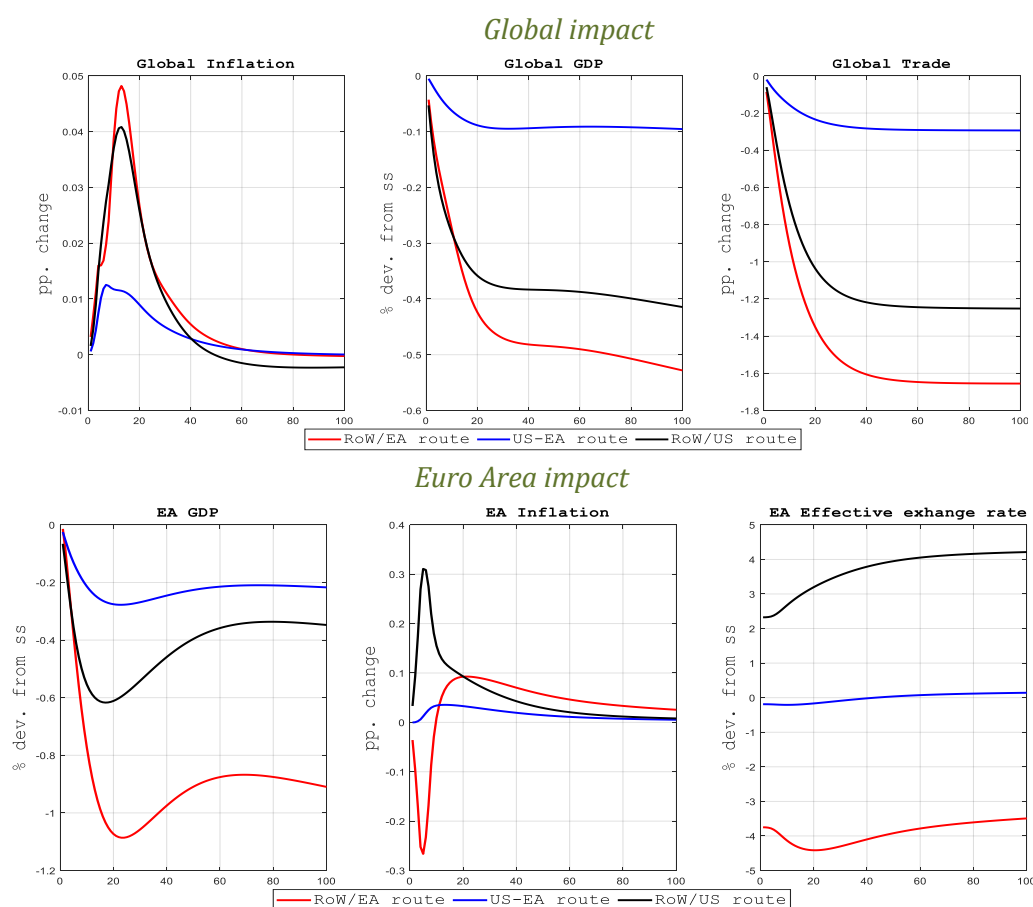
Our results show that the two deglobalisation mechanisms considered impose significant costs, in terms of output, on the global economy and its individual regions. The transition dynamics towards the new steady state are typically stagflationary and are often characterised by substantial exchange rate fluctuations.

The impact of route-specific physical trade constraints

We simulate a gradual increase of trade costs of 10% in the long-run across key inter-regional trade routes: EA-RoW, EA-US, and US-RoW. The effect of a simultaneous persistent disruption on all trade routes is stagflationary in the transition, with global GDP and the global trade-to-GDP ratio contracting to a lower steady state, while inflation gradually falls back to central banks' inflation targets.

The mechanism is similar when considering persistent cost disruptions on any of the three bilateral trade routes individually (Figure 5). However, the global impact of route-specific trade disruptions is uneven and depends on the size and global value chain integration of the regions connected by the specific route. Given the size of the respective regions and their trade-openness (RoW is the largest bloc in our model, EA is the most open region), a disruption of the EA-RoW route has the biggest effect on the world economy. Meanwhile, a similar disruption of the EA-US route has milder effects on the global (and EA) economy, reflecting both their lower combined size relative to the other regional pairs, and the low degree of trade openness of the US. The exchange rate and inflation dynamics depend crucially on the bilateral trade route that is being disrupted. Specifically, in the case of the EA-RoW route, EA inflation decreases in the short-run due to a large appreciation of the euro vis-à-vis the US dollar, which causes a shift of EA imports from RoW towards the US, reducing the overall import prices of the EA. As we show in the paper, the magnitude of the impact crucially depends on regions' ease to switch the origin of their imports, and their ease to replace imports by domestically produced goods.

Figure 5. Bilateral trade route disruptions

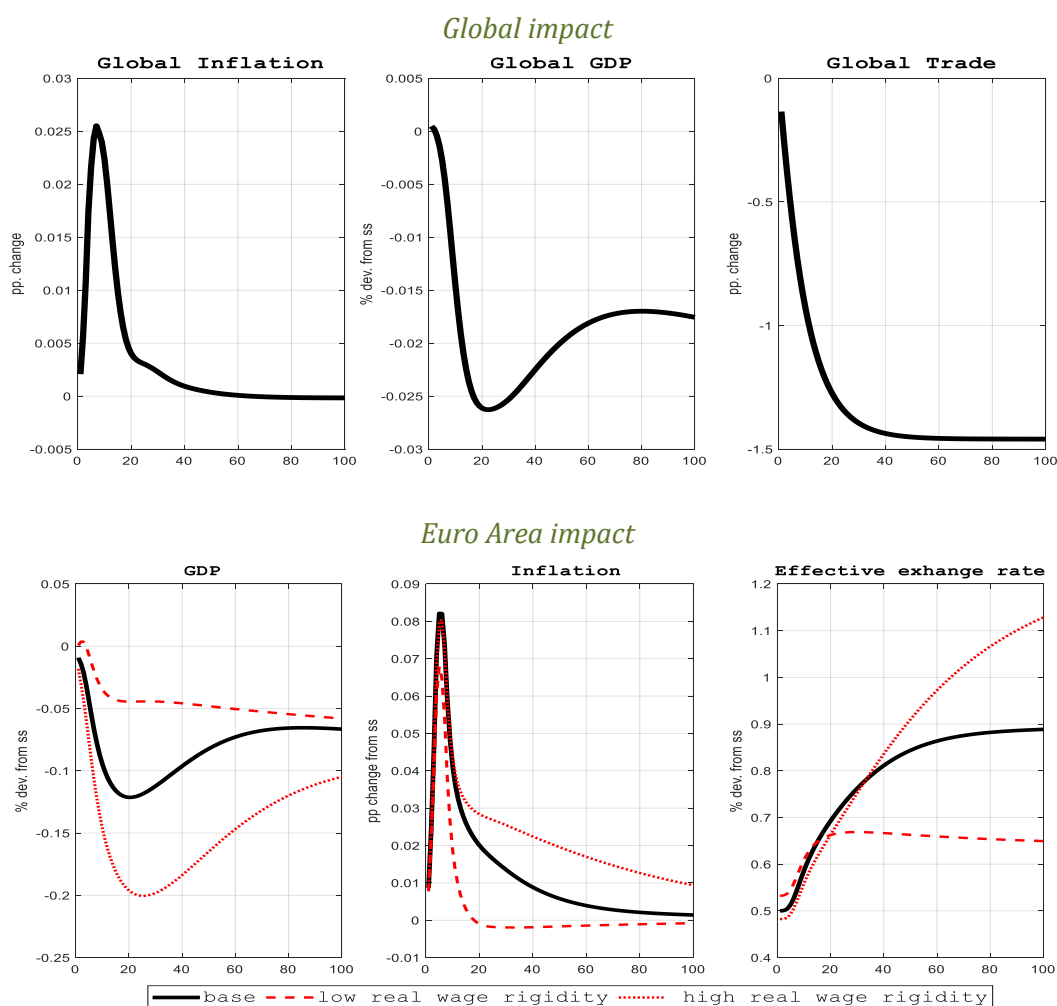


Note: The Impulse Response Functions shown correspond to different scenarios. Each scenario represents a friction on a given bilateral trade route and is the combination of two symmetric and simultaneous shocks affecting the bilateral export sector of each of the two regions that are connected by it. For example, the “US/EA route” corresponds to a shock increasing export prices from EA to US in combination with a shock increasing export prices from US to EA by the same proportion. A decrease (increase) in the exchange rate denotes an appreciation (depreciation) of the euro. Periods are quarters.

The impact of a stronger home bias and costs of shifting preferences

The increase in a region's home bias is modelled as a permanent shift in demand preferences. The change in preferences lowers its trade openness and affects the production of all final demand categories. Figure 6 (upper panel) shows the impact of a global increase in the home bias, resulting from simultaneous preference shifts in all regions. In the new steady state, output is permanently lower, despite the initial drop being partially mitigated by the gradual substitution of exports with domestic production.

Figure 6. Global Home bias shock



Note: The Impulse Response Functions in the upper panel correspond to a scenario in which the home bias increases in all three regions. A decrease (increase) in the exchange rate denotes an appreciation (depreciation) of the euro. The lower panel shows the impact of a global home bias shock on the EA for different degrees of real wage rigidity. Periods are quarters.

The scenario of a global increase in home bias assumes an exogenous preference shift without additional economic costs, such as labour market adjustment frictions or reduced competition. In reality, a transition toward stronger domestic preference would likely be accompanied by other structural changes that create efficiency trade-offs.

To capture some of these trade-offs, we consider complementary scenarios in which the stronger home bias interacts with different degrees of real wage rigidity (see lower panel of Figure 6). With rising inflation, lower wage rigidity implies slower nominal wage growth or even a decrease in nominal wages. This increases total hours worked and domestic production, which reduces inflationary pressures and therefore attenuates the contractionary effects of a

global home-bias shock. In the main paper, we also examine how changes in the degree of competition, captured by variations in markups, can further mitigate or amplify the impact of the shock.

Spillovers of external shocks under fragmentation

Finally, we also analyse the implications of deglobalisation on the international transmission of shocks. In a ‘deglobelised’ steady state, characterized by a stronger global home bias, economies are less exposed to foreign shocks, but more vulnerable to domestic ones. In the case of the euro area economy, external shocks produce less volatility in terms of GDP and inflation, and international price level movements are less synchronous. More fragmentation would hence isolate the euro area from foreign shocks, while domestic shocks would conversely become more relevant, as they would be less attenuated by foreign demand. One implication is that structural trends, such as the “globalisation of inflation” observed in recent decades (Borio and Filardo, 2007), may weaken or reverse as a result.

Policy implications

Deglobalisation is costly for all major regions: it lowers output and raises inflation, especially during the adjustment period. Some drivers — such as geopolitical tensions or climate disruptions — are global in nature and can only be mitigated through multilateral cooperation. Maintaining open, rules-based trade remains essential.

From a European perspective, two strategies can limit the costs of fragmentation. First, diversify and deepen trade links — both to avoid overdependence on single partners and to strengthen supply-chain resilience. Second, reinforce domestic sources of growth through innovation, skills, and investment, as outlined in the EU’s *Competitiveness Compass* and recommended in the *Draghi Report* (Draghi, 2024). Our results also suggest that increasing labour market flexibility and increasing domestic competition could help shielding the euro area economy from the effects of global fragmentation. These strategies would allow to continue benefitting from global integration, while building strength at home in view of minimising the impact of external disruptions.

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