

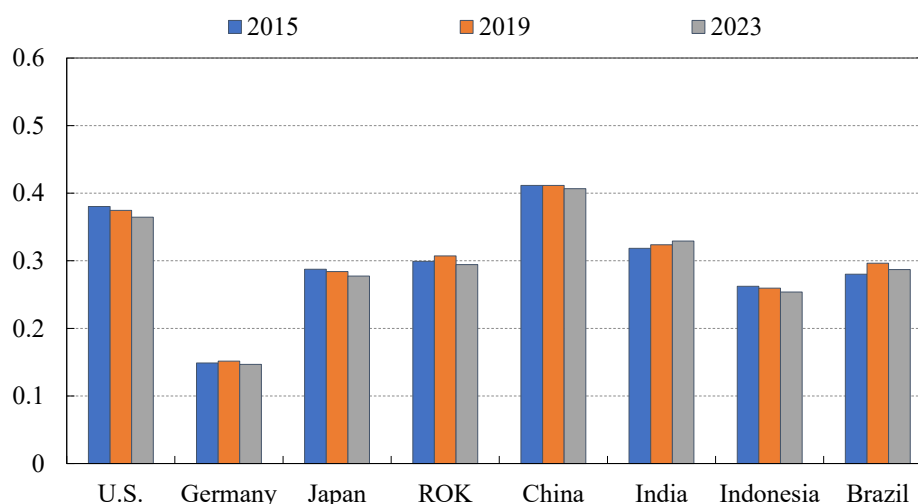
Section 2 Impact on world trade

The previous section pointed out Western countries' widening geopolitical distance from China, but their relationships with countries other than China have also changed to some degree and the change may be producing effects on cross-border corporate activity, including trade transactions. Therefore, this section analyzes how major countries' trading partner countries can be geopolitically positioned and how de-risking of supply chains is actually affecting which countries and regions.

First, in order to grasp an overview of major countries' trade and geopolitical distances, let us look at "trade-based geopolitical distance." Each country's trade-based geopolitical distance is calculated by weight-averaging its geopolitical distances with other countries around the world by trade share. If a country's trade with a geopolitically close country increases relatively, its trade-based geopolitical distance decreases, while growth in trade with a geopolitically distant country leads to an increase in the trade-based geopolitical distance. As a result, if de-risking is affecting trade relationships, it is assumed that the trade-based geopolitical distance will move toward zero.

Figure I-4-2-1 shows major countries' trade-based geopolitical distances, calculated based on the average geopolitical distances for 2022-2023, the most recent two-year period for which data is available. Although the values for the United States and Japan declined, the margin of decline is very small, so the effects of de-risking on the whole of trade are not necessarily clear.

Figure I-4-2-1. Trade-based geopolitical distance in major countries

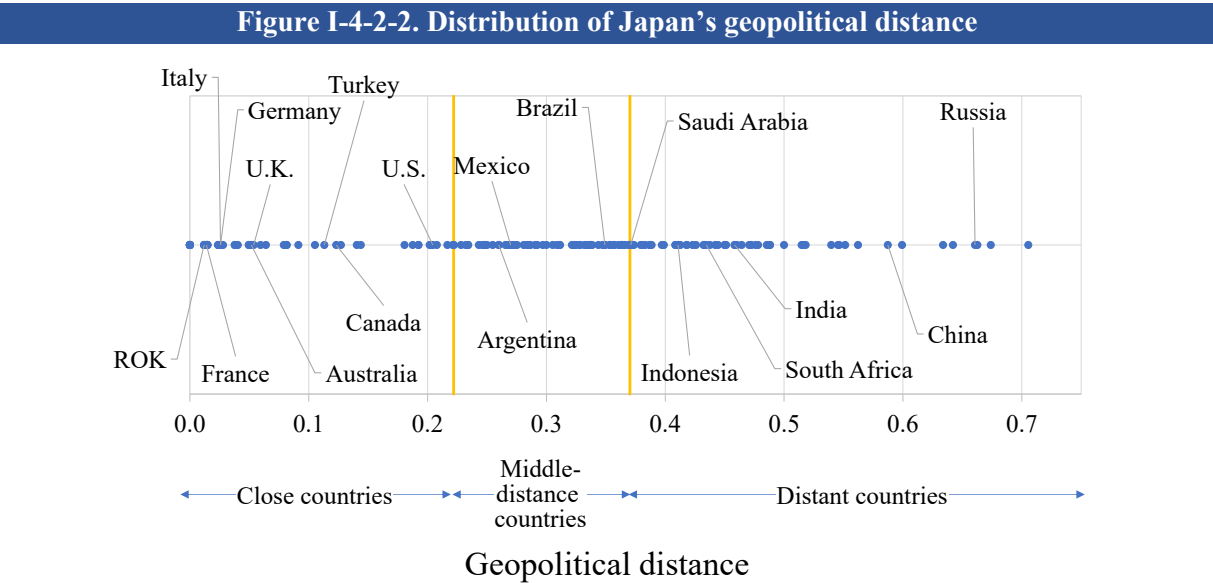


Note: This figure shows each country's geopolitical distance (2022–2023 average) from all other countries, in which the geopolitical distance is calculated by weight-averaging each year's share of trade value.

Sources: *UNGA-DM Database* (University of Geneva) and the United Nations Digital Library as for UN voting data, the U.S. Department of State as for data falling under the "important issues," UN Comtrade as for data on trade values.

Given that trade-based geopolitical distance is computed through weight-averaging, even if a country’s trade with geopolitically close countries increases, the distance calculated may remain unchanged if trade with other countries also increases. Therefore, instead of looking merely at the weight-averaged numbers, let us analyze the trade trends of major countries by examining their trade with partner countries as classified into three groups: (i) geopolitically close countries, (ii) geopolitically middle-distance countries, and (iii) geopolitically distant countries. The three-group classification was adopted because, just as the distances from the United States or from China vary widely across countries as described in the previous section, the distance from other countries is presumed to differ widely and because distinguishing merely between geopolitically close and distant countries is insufficient to capture the diversity of relationships.

For each country, the values of geopolitical distances from all other countries were calculated and were used to sort those other countries: countries were assigned to Group (i) (“close countries” group) when the value calculated was in the bottom third of all values calculated, to Group (iii) (“distant countries” group) when the value calculated was in the top third, and to Group (ii) (“middle-distance countries” group) when the value calculated was in the middle third. Figure I-4-2-2 shows Japan’s trade partner countries thus classified. Western countries were assigned to the “close countries” group, Central and South American countries to the “middle-distance countries” group, and China and Russia, among other countries, to the “distant countries” group.



Note: This figure shows Japan’s geopolitical distance from other countries (2022–2023 average), classifying these countries into three groups by closeness and arranging them in a line. The labeled countries refer to G20 countries.

Sources: *UNGA-DM Database* (University of Geneva) and the United Nations Digital Library as for UN voting data, the U.S. Department of State as for data falling under the “important issues.”

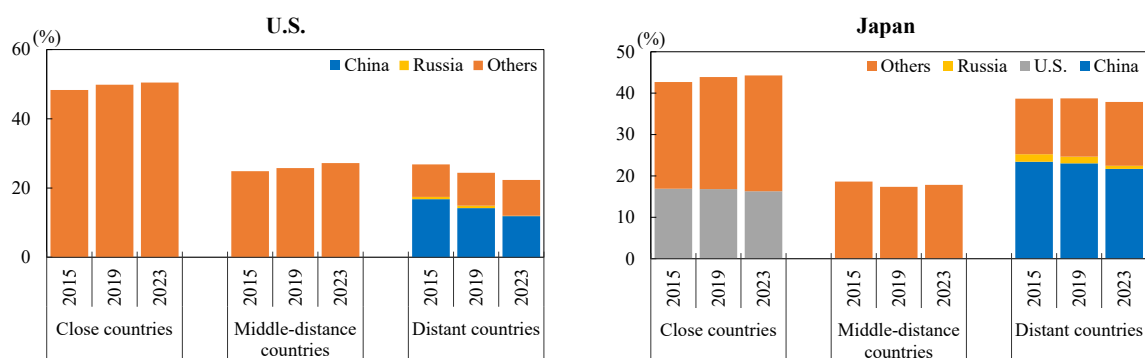
Similar classification was made with respect to trade partner countries of other major countries, and Figure I-4-2-3 shows changes in the shares of the groups in each major country's overall trade.

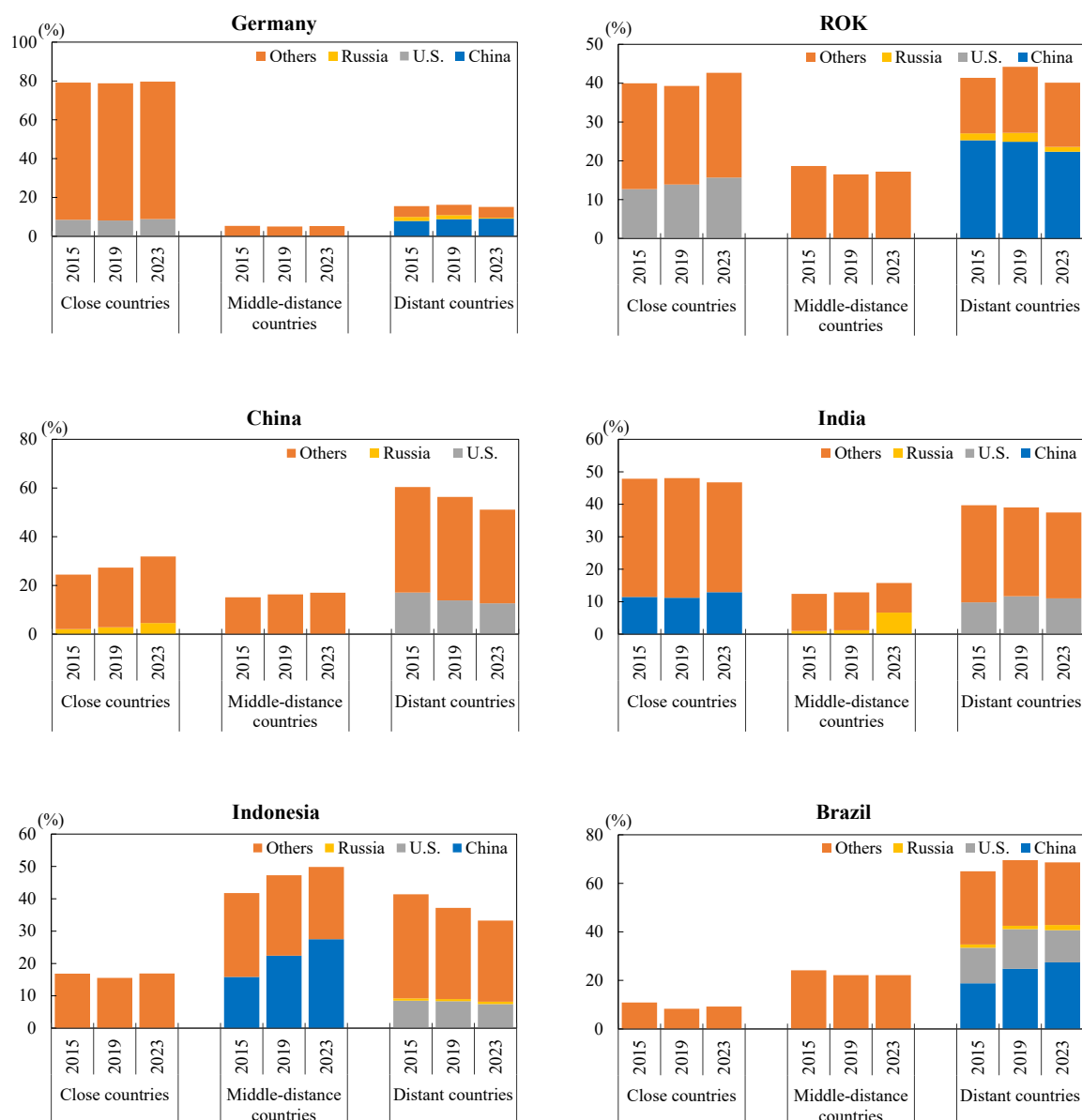
In the case of the United States, while trade with geopolitically close countries and with middle-distance countries increased, the share of trade with distant countries declined. This suggests that trade with China, a geopolitically distant country, decreased due to de-risking. However, this does not necessarily mean that only “friend-shoring,” which refers to building supply chains among allied or friendly countries, increased. In the cases of Japan and the ROK as well, trade with “close countries” increased, but these two countries did not reduce trade with China as much as the United States did, so the progress in de-risking was limited. In the meantime, in the case of Germany, trade with other EU member countries, classified as “close countries,” accounts for most of overall trade, so no pronounced trend can be observed.

In the case of China, trade with the United States declined, indicating China changed its behavior somewhat in light of the increased risk associated with investments in the United States. However, it has been pointed out that there are indirect imports to the United States by Chinese companies through trade with or investment in third countries, so it is not necessarily clear whether de-risking is making progress. On the other hand, China's deepening trade relationship with Russia may be considered to be a form of friend-shoring.

Among emerging countries, Indonesia's trade with “close countries” remained almost flat, but its trade with “middle-distance countries” increased while its trade with “distant countries” decreased. China accounts for most of Indonesia's trade with “middle-distance countries,” indicating that Indonesia is giving some precedence to economic interests. The situation is similar in the case of India. India is strengthening its trade relationship with Russia, assigned to the “middle distance countries” group, mainly in the energy sector. Finally, in the case of Brazil, the share of trade with geopolitically distant countries grew, a trend not observed in the cases of other major countries. The main factor was, as might be expected, the expansion of trade with China. One presumed reason for the increased trade with China is that the need to be conscious of friend-shoring is relatively low because Brazil's geographical distance from China reduces the risk of its being involved in geopolitical conflict, as the United States, Europe, and Asian countries have been.

Figure I-4-2-3. Changes in the share of trade according to geopolitical distance





Note: In this figure, all trading partner countries are classified into three groups of “close countries,” “middle-distance countries,” and “distant countries” by geopolitical distance (2022–2023 average) to illustrate the share of trade for each group. In calculating the share of trade, trade with certain regions not subject to the calculation of geopolitical distance is excluded, such as Hong Kong, Macau, and Taiwan.

Sources: *UNGA-DM Database* (University of Geneva) and the United Nations Digital Library as for UN voting data, the U.S. Department of State as for data falling under the “important issues,” UN Comtrade as for data on trade values.

The summary of the analysis results presented in this chapter is as follows. In terms of geopolitical distance based on voting behavior at the UN General Assembly, Western countries are relatively close to the United States and are distant from China, while emerging countries in general are more distant from the United States. Even so, at some times, Western countries’ geopolitical distance from the United

States widened depending on the United States' attitude. Among emerging countries, the stance toward the United States or China varied more widely than among Western countries, meaning that emerging countries' geopolitical positions are more diverse.

The analysis of the relationship between geopolitical distance and trade shows that regarding de-risking, which has been attracting attention in recent years, there is no clear evidence that the fragmentation of global trade relationships as a whole or division of global trade into blocs is proceeding. Between the United States and China, which are at the heart of the geopolitical conflicts, there is no doubt that direct trade relationship is declining. However, trade between geopolitically close countries and trade between geopolitically middle-distant countries are also increasing, meaning that it is not friend-shoring alone that is proceeding. Rather, the realignment of supply chains is, in fact, oriented toward diversity. Among Western countries, such as Japan, the ROK, and Germany, the impact of de-risking on the entire trade value is limited for the moment. Indonesia and India are presumed to be maintaining and expanding trade relationships with countries around the world because of the precedence they give to economic interests amid the geopolitical conflicts. There are also some countries, such as Brazil, whose trade relationships with geopolitically distant countries are expanding. As described above, amid the confrontation between the United States and China, de-risking is currently oriented toward the diversification of supply chains, with neither fragmentation of global trade relationships, division of global trade into blocs, nor friend-shoring acting as the main driving force. Of course, that is a trend observed from the perspective of overall trade, so if we look at the current situation on a product-by-product basis, a different trend may become apparent.

Recently, the second Trump administration has introduced tariff measures not only against China but against all countries, and those measures, coupled with the escalating uncertainty, are expected to have a huge impact on the realignment of supply chains, too. It is difficult for the moment to identify or predict the future direction of de-risking by the United States and other countries. It is necessary to keep a close watch over the future course of geopolitical conflicts, countries' trade policies, and the realignment of supply chains by companies while taking into consideration the effects that de-risking has so far had on trade relationships.