

The Challenges of Global Economic Fragmentation and Capital Flows

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Abstract

This paper provides a comprehensive analysis of the effects of escalating geopolitical tensions and economic fragmentation on global capital flows. It examines international trade encompassing goods and services and discusses the potential repercussions of a deceleration in world trade growth. Additionally, the study investigates trends in foreign direct investment (FDI) and its cross-border movements. By scrutinizing the scope and dynamics of international capital flows, the paper assesses both the short- and long-term implications of the geopolitical landscape on these flows. The findings indicate that increasing trade tensions and heightened uncertainties can substantially impact global economic growth as well as international capital allocations. The paper also analyses the impact of geopolitical tensions on the international monetary system. It also addresses the growing application of artificial intelligence within financial and capital market operations, suggesting that it may lead to higher market correlation, the potential distortion of asset prices, and an increased likelihood of herding behavior among investors.

Keywords: Capital flows, global fragmentation, FDI, trade, artificial intelligence.

1. Introduction

After the outbreak of the global financial crisis (GFC), the real growth of world trade in goods and services slowed down, with no lasting recovery recorded. The slowdown in world trade in recent years has been accompanied by the growth of protectionism. Rising tensions between the world's leading trade rivals have paved the way for a tariff war with no end in sight. Geo-economic realignments after Russia's invasion of Ukraine are ongoing. The rise of trade protectionism not only leads to the restructuring of global value chains but also increases uncertainties in the world economy. Risk-return relationships change rapidly due to the sudden introduction of tariffs. The COVID-19 pandemic has fueled the process of nearshoring, which has paved the way for the reshaping of global value chains. Geopolitical divisions in the world have fueled the disintegration of the global financial market. The net inflow of FDI to global Gross Domestic Product (GDP) is in significant decline. This trend particularly affects developed countries and emerging markets.

The use of various trade and financial sanctions has diminished the effectiveness of the international financial system and created uncertainty for companies and banks regarding cross-border transactions. This fragmentation in the global payment system could further exacerbate the division of international trade and cross-border capital flows. This paper examines current global capital movements and connects them to the trends of geo-economic fragmentation (GEF) in international trade. The central argument is that ongoing fragmentation in the international financial system may heighten trade tensions and potentially lead to the formation of trade blocs around the world. The research is based on data from the Bank for International Settlements, the International Monetary Fund, and other relevant studies.

2. Slowdown of World Trade and International Flow of Capital

From the late 1980s until the outbreak of the 2008 GFC, world trade experienced moderate growth that significantly lagged behind the expansion of global GDP. The integration of financial and commodity markets has improved the efficiency of capital allocation, while technological advancements have facilitated the dissemination of innovations across the global

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economy through FDI. In contrast, although world trade has been recovering slowly since the GFC, FDI as a percentage of GDP has shown a downward trend (Figure 1). The escalation of trade and geopolitical tensions indicates a potential further slowdown in world trade, a trend that began prior to the implementation of recent US tariffs. The disintegration of global value chains, along with sluggish economic growth worldwide, is adversely affecting the outlook for world trade growth. Additionally, the benefits of trade liberalization achieved during the Uruguay Round of trade negotiations appear to have been largely exhausted, while the significance of non-tariff measures and trade policy interventions has increased notably. Industrial policies are costly and can lead to misallocation of resources (Ilyina, Pazarbasioglu, and Ruta, 2024). A poorly designed industrial policy can reduce domestic welfare (Hodge et al., 2024).

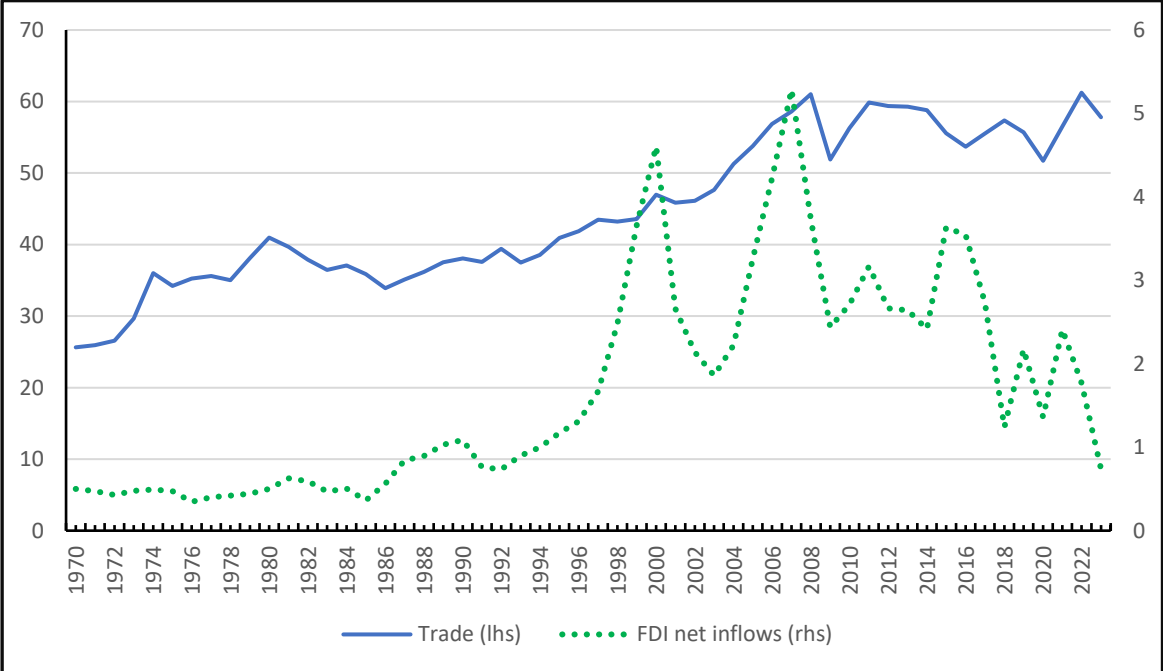


Figure 1: Global trade and FDI (% of global GDP)

Note: Trade: sum of global exports and imports of goods and services.

Source: BIS (2025, Graph 8.C., p. 18).

The recent deceleration in global trade has led to a resurgence of protectionism. The United States has exacerbated this situation by implementing elevated tariffs on imports, justifying these actions on the grounds of reducing bilateral trade deficits and restoring previously relocated production to domestic shores. Although the primary objective of these tariffs is to enhance domestic employment within the United States, empirical evidence suggests that trade balances do not respond appreciably to the imposition or removal of tariffs (BIS, 2025). Boehm et al. (2023) calculated that the elasticity of tariff-exclusive trade flows is -0.76 in the short run, and approximately -2.25 in the long run. Therefore, it is a low value of long-term elasticity, where it takes 7 to 10 years to converge to the long run.

Instead of relying on import tariffs, a comprehensive approach utilizing both fiscal and structural policies would be more effective in mitigating trade imbalances (BIS, 2025, box A, p. 15). Empirical evidence shows that a reduction in fiscal deficits by 1 percentage point as a share of GDP has historically been associated with a reduction in trade deficits by 0.3 to 0.5 percentage points of GDP (BIS, 2025, Box A, p. 16). The escalation of input costs and punitive tariffs has effectively nullified the positive impacts on employment (Flaen and Pierce, 2024; Steil and Della Rocca, 2020). GEF incentivizes nations to strengthen regional integration. For

example, GEF impedes the advancement of Central and Eastern European countries within the framework of global value chains. Although the interdependence between these countries and those in Western Europe mitigates the risk of substantial capital outflows, GEF complicates efforts to diminish their structural dependence. Consequently, these nations remain constrained to regional supply chains (Boguslawski, 2025, p. 14).

The decline in net inflows of FDI poses a significant threat to the economic growth of emerging markets, as FDI serves as a vital engine for this growth. Furthermore, FDI contributes to the transfer of knowledge and technology to these countries. Traditional viewpoints assert that the presence of FDI within a domestic economy facilitates the dissemination of management expertise to local firms that act as suppliers to foreign investors (Javorcik, 2004). By engaging with foreign investors, domestic companies are able to enhance their presence in international markets and increase their export activity. Through the utilization of investors' distribution networks, domestic firms can expand their export portfolios and achieve deeper integration into global value chains (Cheng et al., 2015). Consequently, a reduction in FDI flows will yield profound implications for the economic development of emerging markets. The ability of countries to use the positive externalities of FDI depends on their absorptive capacity (Alfaro et al., 2004; Qju et al., 2023).

Countries that are reliant on export-dependent growth are experiencing a restricted inflow of knowledge, which poses a significant threat to their competitive edge in global markets. The rise of trade protectionism is disrupting global value chains and generating considerable uncertainty within the economy. This heightened uncertainty acts as a deterrent to foreign investment in developing countries and emerging markets. Extended periods of protectionism increase the likelihood that a growing proportion of imports from foreign companies' subsidiaries will be subjected to tariffs and trade restrictions. Consequently, this situation not only postpones investment initiatives in developing countries and emerging markets but also raises the possibility that companies may consider relocating their investments back to their countries of origin. Caldara et al. (2020) estimated that trade uncertainty reduced US investment by approximately 1.5 percent in 2018. Uncertainty reduces consumer demand and income by reducing investment and discouraging trade (Handley and Limão, 2017).

The unexpected introduction of higher tariffs changes the risk-return relationship, leading to a decrease in global FDI volume.

Between 2009 and 2023, newly implemented restrictions on the importation of goods and services from developed countries to emerging economies increased at an average rate of 8% per annum. The coverage of these restrictions regarding imports from emerging economies rose significantly, escalating from approximately 5% in 2009 to 62% in 2023 (BIS, 2025, p. 20). Consequently, there has been a notable decline in outward FDI from the developed nations that adopted these measures. The diminished inflow of FDI into emerging economies adversely impacts their potential for economic growth. This trend suggests that the continued growth of trade protectionism is likely to yield increasingly detrimental effects on emerging markets. A slowdown in their economic growth further reduces their opportunities to bridge the gap with the economic development of developed countries.

3. Trade Restrictions and the Financial System

In addition to its positive aspects, financial integration has also exposed certain vulnerabilities. In the aftermath of the terrorist attacks on September 11, 2001, the United States began to utilize its financial system as a significant instrument of economic power. This financial infrastructure was transformed into a mechanism for advancing both domestic and foreign policy objectives. Such initiatives include the imposition of sanctions designed to protect the interests of the sanctioning country. The dollar's status as the world's reserve currency has facilitated the United

States in pursuing its foreign policy objectives through these sanctions. In the context of Russia's invasion of Ukraine in 2022, sanctions were again employed to achieve specific foreign policy aims (Figure 2). Additionally, the United States, the European Union, and their allies collectively froze approximately \$300 billion in international reserves belonging to the Russian central bank. Furthermore, the financial market infrastructure was leveraged to exclude Russian financial institutions from the global financial system, thereby restricting their access to international capital markets. In this way, the global financial system has been utilized to advance targeted objectives.

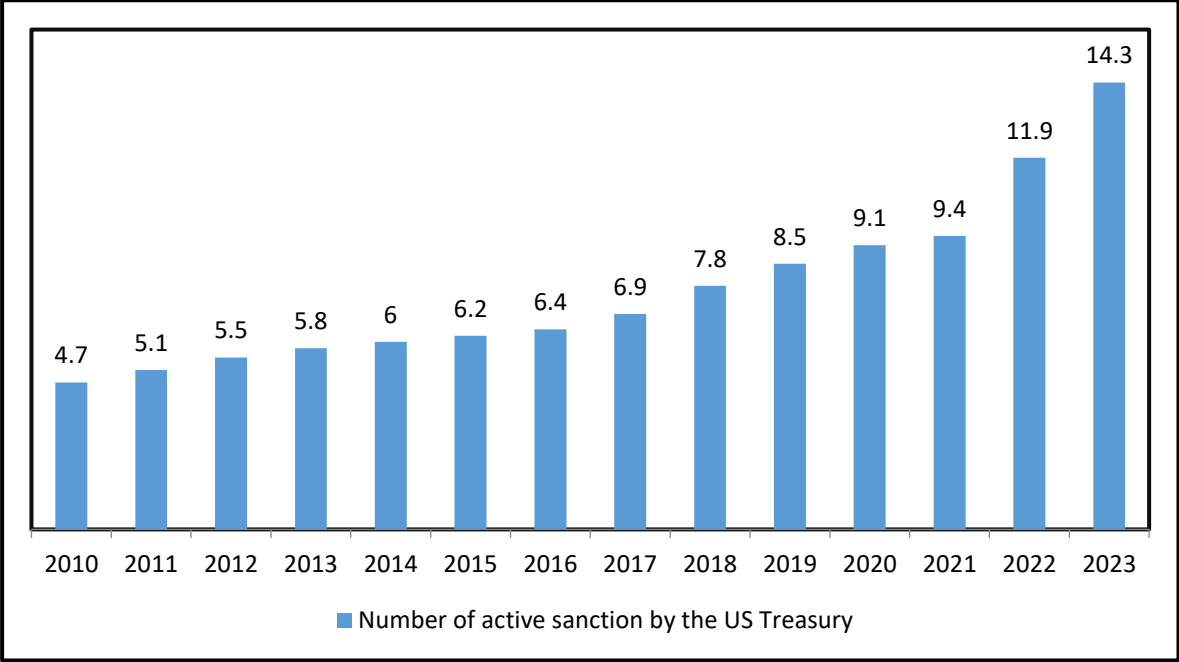


Figure 2: Number of active sanctions by US Treasury, 2010-2023, in thousands

Note: Between 2010 and 2017, the number of sanctions increased at an average rate of 6%. From 2017 to 2021, the growth rate averaged 8%. In 2022-2023, the growth rate was 23%.

Source: Oliver Wyman Forum x NYSE CEO Survey 2024. Oliver Wyman Forum analysis. According to: World Economic Forum (2025, Figure 5, p. 14).

Figure 2 illustrates the expanding influence of United States sanctions, which have emerged as a substantial impediment to the international movement of capital. In the wake of Russia's invasion of Ukraine, there has been a pronounced decline in cross-border banking and portfolio investments directed towards Russia and its allies. The findings from empirical research employing gravity models, as presented by Catalán et al. (2024, p. 12), demonstrate that an increase in geopolitical distance between the capital-exporting nation, the United States, and the capital-receiving nation, China, by one standard deviation—which aligns with the disparity in voting these countries in the United Nations since 2016—corresponds to a reduction of approximately 25 percent in allocations to portfolios of stocks and bonds. Furthermore, financial fragmentation has the potential to directly and indirectly affect the real economy, leading to a reinforcement of real and financial channels (IMF, 2023).

The escalating geopolitical tensions are likely to result in pronounced alterations in international capital flows. Such changes may elevate the financing costs for banks operating in numerous developing countries and emerging markets, thereby leading to a decline in profitability and a reduction in lending activities directed toward the real sector. The limited capacity of these nations to absorb resultant shocks exacerbates their vulnerability. Banks that are well-capitalized are generally less susceptible to these shocks; conversely, those that are

less capitalized in developing and emerging markets experience a more pronounced increase in borrowing costs. Therefore, it is imperative for these institutions to enhance their capital buffers. Should these tensions persist, the fragmentation of cross-border capital flows has the potential to diminish the diversification of cross-border risk, while simultaneously increasing macro-financial volatility.

GEF, in conjunction with financial sanctions and the exclusion of Russian banks from the SWIFT system as a response to the Russian invasion of Ukraine, poses a significant risk of exacerbating the fragmentation of the international payment system. There is a growing desire among various countries to reduce their reliance on existing international financial infrastructure and associated standards. The migration of trade and financial transactions away from the US dollar towards alternative currencies has been motivated by both economic imperatives and geopolitical considerations. Many nations are concerned that they may be subjected to sanctions limiting their banking operations and complicating international payment processes, leading them to seek alternative solutions. The potential establishment of new payment systems may diminish overall efficiency and elevate transaction costs. Consequently, the fragmentation of the global payment system may further contribute to the disintegration of trade and capital flows.

4. Integration and Disintegration of the Global Financial Market

During the 1980s and 1990s, the processes of financial deregulation and innovation were instrumental in facilitating the global integration of capital markets. The substantial expansion of the derivatives market significantly improved cross-border capital mobility (Rogoff, 2003). The bond market's value experienced notable growth, increasing from \$260 billion in 1982—equivalent to 3% of the annual GDP of industrialized nations—to approximately \$1.4 trillion by the end of 1990, which represented 8% of their annual GDP (IMF, 1992, June 15). Cross-border bank lending also saw considerable expansion during the 1970s, accompanied by a rise in stock market turnover. However, a decline in bank lending was observed in the early 1980s due to emerging challenges associated with servicing the debts of developing countries. This resulted in sovereign borrowers increasingly relying on bond markets to secure financing. Concurrently, many countries categorized as emerging markets transitioned away from development strategies centered on import substitution, opting instead for approaches that prioritized export-driven economic growth. This shift contributed to a deeper integration of financial markets and international trade (Calomiris and Neal, 2013).

Technological advancements have significantly facilitated the integration of financial markets. The rise of electronic trading platforms and the Internet has markedly accelerated trading activities, resulting in a decrease in the costs associated with international financial transactions. The establishment of the World Trade Organization (WTO) in 1995 provided a robust institutional framework for the development of a global trade system, which further reinforced the processes of financial integration. In the eurozone, the introduction of the euro as a common currency has notably strengthened these integration efforts. Furthermore, the liberalization and globalization of financial markets have substantially contributed to the growth of FDI, which escalated from 0.5% of global GDP in 1970 to 5.28% of global GDP by 2007 (World Bank Group, 2025). However, the collapse of the real estate market in the United States in 2007 precipitated a global financial crisis, thereby revealing the inherent risks associated with financial integration. This provided validation for the thesis that financial integration can amplify the transmission of crises between nations (Devereux & Yu, 2020). To ensure the integrity of the international financial system, regulatory coordination was enhanced through the establishment of the Basel Committee on Banking Supervision (BCBS). This initiative aims to foster improved oversight and cooperation among banking authorities globally.

Despite leaving the Bretton Woods monetary system, the United States dollar has preserved its critical role as the principal reserve currency within the international monetary framework. The 2008 GFC underscored the vulnerabilities that countries experience due to their reliance on the US dollar. Such dependence engenders uncertainty about the potential fluctuations in US monetary policy, which may significantly impact global liquidity. Additionally, variability in the dollar's exchange rate further compounds this uncertainty. The dominance of the dollar can be attributed to the robust nature of the American economy and its pivotal influence on the development of international trade, alongside various network effects. Moreover, the capacity to create liquidity through swap arrangements confers a distinct advantage upon the United States, as central banks in other nations regard these mechanisms as a safeguard against potential banking system illiquidity. The euro has struggled to expand its share in international financial transactions, whereas the ascent of the Chinese yuan has been limited due to the absence of full convertibility and capital account regulations. Although there is a discernible trend towards decreasing the proportion of the US dollar in global foreign exchange reserves, the prevailing confidence in the US currency, coupled with the government's commitment to fulfilling its debt obligations, continues to uphold the dollar's predominant position in the international monetary system (Figure 3).

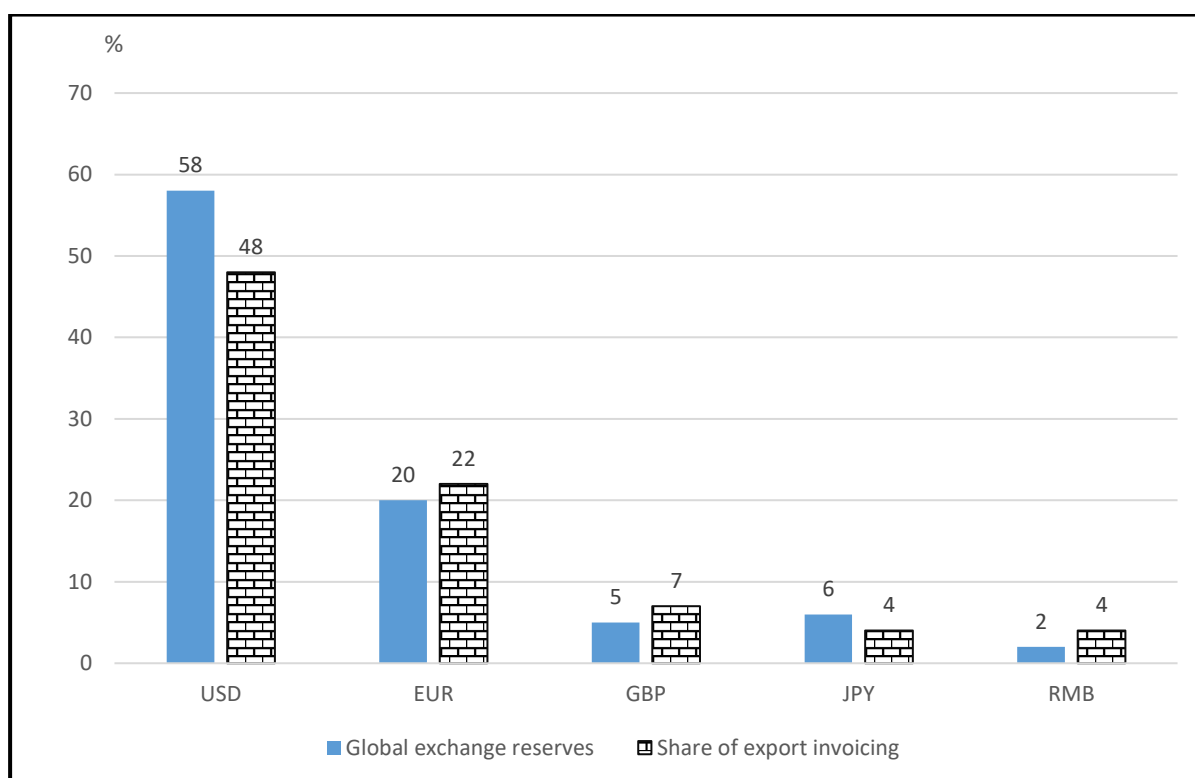


Figure 3: Currency share of global reserves and global export invoicing, 2024 (in %)

Source: World Economic Forum (2025, Figure 4, p. 12).

As of the end of 2024, the United States dollar constituted 58 percent of global foreign exchange reserves, a decrease from 65 percent recorded ten years earlier. Concurrently, the share of the US Treasury bond held by foreign investors has experienced a significant decline, falling from 50 percent in 2014 to approximately one-third at present. However, the proportion of global exports invoiced in US dollars stands at around 48 percent, which is considerably greater than the percentage of US exports relative to total global exports. This disparity underscores the dollar's function as a global vehicle currency and emphasizes its predominant role in the invoicing of international trade. In comparison, the euro, which accounts for approximately 22

percent, represents less than half of the dollar's share. Furthermore, the dollar retains its position as the leading currency in foreign exchange trading. In the currency structure for one-day trading on the foreign exchange market in 2022, the United States dollar accounted for 88% of transactions, establishing its dominance. This was followed by the euro, which represented 31%, the Japanese yen at 17%, the British pound at 13%, and the Chinese yuan at 7%. (BIS, 2022, p. 7.) It is important to note that the sum of shares of individual currencies equals 200%, as each transaction involves the exchange of two currencies.

The increasing public debt in the United States prompts a critical examination of its sustainability. This trend may diminish confidence in the dollar and potentially strengthen the roles of alternative currencies within the realm of international finance. Furthermore, the advent of digital currencies could facilitate the diversification of foreign exchange reserves. Recent observations suggest a growing trend towards increasing the proportion of gold within total reserves. A study conducted by Arslanalp et al. (2023) reveals that central banks in emerging markets are particularly active in this diversification effort, prioritizing a higher share of gold. This phenomenon is also evident among countries that are subject to sanctions imposed by the issuers of reserve currencies.

The current state of the world economy has generated a range of perspectives regarding the potential peak of globalization, with the future remaining uncertain. An increasing number of studies indicate a projected decline in global trade volume, suggesting that the process of "deglobalization" may have commenced, as evidenced by a reduction in cross-border capital flows. Conversely, there exists the possibility of the emergence of competitive blocs within the global economy. The decrease in the dollar's share of global foreign exchange reserves—from 71% in 1999 to an anticipated 58% by 2024—reflects significant transformations in the international financial architecture (Tran, 2024). The disruption caused by the COVID-19 pandemic, coupled with subsequent interruptions in supply chains, has compelled developed nations to adopt industrial policies aimed at stabilizing their domestic economies. Furthermore, the imposition of sanctions against Russia has exacerbated the geo-economic fragmentation of the world economy, indicating the onset of a dismantling of the previously integrated financial system (Gopinath, 2024). Consequently, the geo-economic approach is gaining increasing significance for participants within the global financial system. However, this process carries risks, particularly regarding the potential redirection of cross-border capital flows, along with a trend towards the particularization of financial regulation.

Objectives that are vital to national interests are pursued through the implementation of industrial policy (Feingold and Torkington, 2024). Measures enacted by nations, including export controls, customs duties, and investment restrictions, are often driven by the necessity to protect these interests. Nevertheless, such measures can result in increased costs and may lead to inefficient restructuring of investment portfolios and supply chains, potentially exacerbating global price increases. Additionally, obstacles within foreign exchange markets, as well as in cross-border transactions and investment flows, can adversely affect the liquidity of the global financial system (Avdjiev et al., 2020). Research conducted by the International Monetary Fund (IMF) in 2024 indicates that significant escalations in geopolitical tensions between countries can lead to a reduction of approximately 15% in bilateral cross-border portfolio and banking allocations. Another study by the IMF (2025) underscores that major geopolitical risk events could adversely impact the stability of both banking and non-banking financial institutions, thereby posing potential risks to macro-financial stability.

A significant deterioration in global financial conditions has the potential to precipitate a balance of payments crisis in smaller nations that possess limited access to international capital markets. A decline in raw material prices may serve as an indicator of an impending recession,

resulting in reduced import demand from countries reliant on these commodities. Consequently, this would lead to a decrease in export revenues for raw material exporters and exacerbate the challenges faced by highly indebted nations. Countries with substantial refinancing requirements may encounter rising interest rates. Furthermore, initiatives undertaken by central banks to stabilize inflation expectations could result in tightened financial conditions, thereby complicating the operational landscape for financial institutions (Bergant et al., 2025).

The 2008 GFC instigated two interconnected structural changes within the global financial system. Firstly, the emphasis of financial intermediation transitioned from extending loans to private borrowers toward the acquisition of government bonds. Secondly, non-bank financial institutions (NBFIs) emerged as the primary actors in the financing landscape. A pivotal component of the global financial system in the aftermath of the 2008 GFC is the portfolio manager, whose role involves the investment in government bonds (Figure 4).

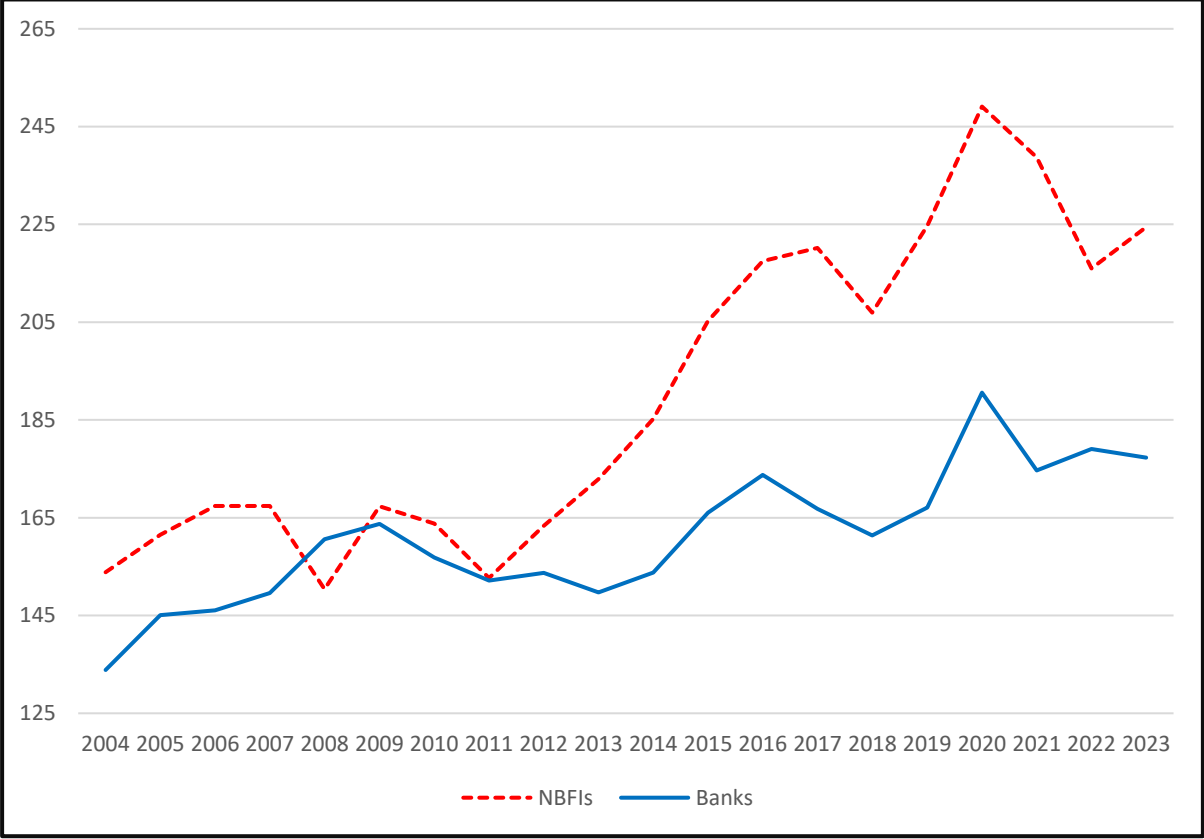


Figure 4: Total global financial assets as a percentage of global GDP

Source: BIS (2025, Graph 2, p. 49).

Figure 4 illustrates the enhanced role of collective investment funds and long-term institutional investors within the primary bond markets. Between 2009 and 2023, the share of NBFIs within the global financial system has increased significantly more than the share of total assets held by banks. These structural changes have resulted in alterations to cross-border capital flows, particularly in the context of cross-border credit flows. Prior to the GFC, international capital flows were predominantly mediated by banks, whose cross-border activities contributed to the spillover effects of financial conditions. In this framework, fluctuations in the indebtedness of global banks represented potential sources of risk. However, in the aftermath of the GFC, the emphasis of international financial intermediation has shifted toward international portfolio investments in global bond markets. This transition has been facilitated by expansionary fiscal

policies and a marked increase in the issuance of government bonds. The growing engagement of NBFIs in financial activities has led to greater currency diversification within their portfolios. This trend has been supported by the expansion of foreign exchange (FX) swap markets, which enable investment managers to invest on a global scale while employing instruments to hedge against currency risk. As a result, financial shocks are now transmitted more effectively across borders. Cross-border transfer of financial conditions is not only registered in small open economies, but can also be observed in large developed countries. Unconventional monetary policy shocks in the Eurozone appear to have hit the balance sheets of NBFIs more than the balance sheets of banks (see Holm-Hadulla et al., 2023).

The domestic conditions anticipated for the implementation of the planned monetary policy are subject to potential changes. Consequently, the execution of domestic monetary policy becomes increasingly complex. A thorough understanding of the nature of global spillovers is vital for the effective calibration of domestic monetary policy. Additionally, fluctuations in global financial conditions pose challenges to the autonomy of monetary policy (IMF, 2020). To strengthen the monitoring and supervision of global financial markets, the intensification of cooperation among central banks will be of paramount importance in the future. Such collaboration will facilitate the harmonization of policies and mitigate undesirable consequences. The evolving role of NBFIs in linking global financial markets represents a new challenge for financial stability. Therefore, the enhancement and application of regulatory standards are essential to bolster the resilience of the financial system.

The alleviation of ongoing geo-economic tensions has the potential to moderate inflation expectations and redirect available resources toward productive endeavors. The economic ramifications of a wartime environment are significant. Research indicates that the "war tax" on economic growth may reach as high as 30% of GDP, contributing to inflationary growth by approximately 15% (Federle et al., 2024), with neighboring countries experiencing the most pronounced impacts. The cessation of hostilities and the renewal of cooperation between nations would likely facilitate the growth of global GDP and international trade, thereby exerting a beneficial influence on the global financial system.

5. Artificial Intelligence (AI) and Its Impact on Financial Markets

The rapid advancement of artificial intelligence (AI) is markedly enhancing the operational efficiency of both financial and non-financial institutions. In contemporary markets, AI plays a pivotal role in automated trading activities within the world's most liquid financial arenas. Organizations are now equipped to swiftly analyze fluctuations in the prices of bonds and other financial instruments, utilizing comprehensive data to bring these prices closer to their intrinsic values. Nonetheless, the deployment of AI carries potential risks to traditional channels of financial stability, including liquidity, leverage, and market interconnectedness. These potential adverse effects have prompted regulatory bodies to adopt a more vigilant approach in monitoring market activities and to implement appropriate regulations aimed at mitigating such risks. A comparable response was observed following the global financial crisis of 2008, which led to enhanced resilience within the financial system. Furthermore, the implementation of AI-driven surveillance technologies for the detection of fraud and other systemic issues is becoming an indispensable tool for regulators seeking to prevent market manipulation.

The widespread adoption of AI for selecting optimal models for trading algorithms, along with the incorporation of extensive data in decision-making processes, presents a significant risk of diminishing the motivation to allocate capital according to alternative models. When all participants in the financial market utilize similar models, this can lead to the convergence of investment strategies among them. Such a scenario may increase market correlation, distorting asset prices and elevating the likelihood of herding behavior. During periods of heightened market stress, a substantial number of participants could simultaneously adopt the same trading

strategy, resulting in increased asset price volatility. These developments could adversely impact global liquidity. In the event of adverse shocks, AI models may advocate for a concurrent rebalancing of portfolios toward safer assets, thereby contributing to a self-fulfilling cycle of asset liquidations (IMF, 2024, p. 93). Moreover, the risks associated with cyber vulnerabilities are escalating. As a result, the responsibility of regulators to leverage the advantages of AI while mitigating potential negative consequences has become increasingly complex and pressing.

6. Conclusion

Since the early 2020s, GEF has been accompanied by a slowdown in global trade growth, a resurgence of protectionist policies, and a growing emphasis on geopolitical blocs that influence trade flows and enforce financial restrictions within the international monetary system. The slowdown in trade was already evident before the United States implemented its recent trade policies. When the U.S. imposed high import tariffs, other countries responded with their tariffs, which further exacerbated the decline in global trade. Tensions escalated following Russia’s invasion of Ukraine, adding complexity to the already strained U.S.-China trade relations. These tensions have intensified amid ongoing global challenges, including those stemming from the COVID-19 pandemic. Additionally, changes brought about by digital innovation and the push for a greener economy have contributed to trade fragmentation. This fragmentation is reflected in a decrease in international capital flows, particularly regarding FDI. In recent years, there has been a notable rise in restrictions and financial sanctions that undermine the integrity of the existing international monetary system.

Although the United States dollar continues to be the predominant reserve currency globally, there is a discernible trend towards diminishing its proportion within the global structure of foreign exchange reserves. In spite of that tendency, thanks to global confidence in the ability of the US government to service its debt, foreign creditors, particularly central banks, continue to invest their foreign exchange reserves in dollar-denominated bonds. Besides, the dollar remains the leading currency for invoicing in international trade, a status that can be attributed both to historical inertia and the efficiency of existing transfer and clearing systems.

The international payment system is currently confronting considerable challenges, particularly the threat of fragmentation. The exclusion of Russian banks from the SWIFT system, following Russia's invasion of Ukraine, has initiated a series of consequences that extend beyond Russia. Consequently, other nations are now contemplating the adoption of alternative international payment systems to mitigate potential future sanctions. This situation has fostered a growing distrust within the international monetary system, especially in light of the freezing of Russian foreign exchange reserves held in Western banks. This event has underscored the inherent risks associated with maintaining reserves in these institutions. Although the partial transition from U.S. dollars to other convertible currencies was primarily motivated by economic factors aimed at enhancing returns, the apprehension regarding the potential blockage of assets has also played a significant role in the restructuring of foreign reserves. In recent years, there has been a notable increase in the proportion of gold reserves within the total foreign exchange reserves of numerous countries, particularly among emerging markets. The potential establishment of new payment systems in regional contexts poses a serious threat to the integrity of the global international payment framework. Additionally, the rise in operational costs stemming from reduced interoperability of these systems could hinder the efficiency of international payments, consequently impacting business profitability adversely.

A deterioration in global financial conditions could significantly intensify the balance of payments challenges encountered by smaller countries, which typically possess limited access to the international capital markets. Furthermore, a potential decline in raw material prices might adversely affect the external positions of exporters of these commodities, resulting in diminished export revenues. Additionally, countries with substantial levels of indebtedness may

experience difficulties in refinancing their external debt, particularly in the context of rising interest rates.

Cooperation among central banks is essential for effectively overseeing the global financial market. By collaborating, these banks can better coordinate their monetary policies and reduce associated costs. As NBFIs become increasingly important in global capital flows, it is vital to strengthen and enforce regulatory standards to maintain the stability of the international financial system. One significant factor driving this enhanced collaboration is the rising influence of artificial intelligence (AI) in the financial sector. Given the potential negative impacts of AI on global liquidity and financial stability, regulators must closely monitor market developments and implement regulations designed to address any emerging challenges.

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