



2025 Trade and development report

Chapter I

Current trends and challenges in the global economy

KEY FINDINGS

- ▶ An increasingly challenging external environment clouds prospects for the global economy. Global growth will decelerate to 2.6 per cent in 2025, down from 2.9 per cent in 2024. Economic expansion in developing economies is projected to stay at 4.3 per cent in 2025.
- ▶ The slowdown expected in the aftermath of frontloaded imports will spill into 2026, weighing on growth. Despite potential gains from new technologies like artificial intelligence, global growth is projected to remain subdued in 2026, at 2.6 per cent. Growth in developing economies is expected to slow marginally to 4.2 per cent in 2026.
- ▶ Deterioration in the international environment affects the global South through trade and financial channels. Increased financial volatility due to sudden policy swings leads to greater instability in capital flows and exchange rates, impacting international financing conditions.
- ▶ Recent volatility in international financial markets has spurred anomalous movements in the prices of safe-haven assets. It remains to be seen whether atypical trajectories in past months correspond to cyclical factors or reflect a more significant long-term erosion in the perception of these assets.



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Policy takeaways

- ▶ **A key factor in reducing exposure to shifts in trade policy is the diversification of export markets through deepening regional integration.** Regional initiatives can also serve to diversify productive structures, preventing excessive reliance on particular exports and individual markets, and providing a bridge to global trade integration based on higher value-added goods.
- ▶ **Combining national and coordinated international actions would be most effective in addressing global imbalances.** It would also limit negative fallout from required macroeconomic adjustments, domestically and globally.
- ▶ Where fiscal pressures constrain critically needed public spending and investments, particularly amid increasing debt-servicing costs and waning external financing, **governments can look to boost public resources through enhanced and more efficient frameworks of domestic revenue mobilization and curbing tax and regulatory arbitrage.**
- ▶ **Alternative arrangements that can provide countries with more options for the settlement of international trade and financial transactions are increasingly discussed as resilience-enhancing measures.** While such efforts could pave a way towards a more diversified international monetary architecture, institutional costs of these initiatives are high and risks of financial fragmentation cannot be overlooked.
- ▶ **Multilateral cooperation and coordinated policymaking are imperative** to avert economic fragmentation, revitalize and sustain long-term development, and tackle global challenges such as rising inequality and climate change.



A. Global economic outlook

1. Introduction

The year 2025 has been defined by protracted and system-wide uncertainty over trade policy shifts and geoeconomic challenges. Even as international policy discussions tend to focus on tariffs, the impact of the current reset goes beyond trade.

International trade is deeply embedded in the global financial system: over 90 per cent of world trade depends on international banking and financial infrastructure. Yet trade and finance are organized according to different systemic principles. Notwithstanding current tensions over tariffs, around 72 per cent of global trade flows continue to be governed by WTO most favoured nations terms (WTO, 2025). Global finance, in contrast, is embedded in long-established market practices and conventions, networks of regulatory arbitrage and standard-setting functions delegated to private authorities.

In the short run, this interdependence can help avoid fracture and provide an effective signal for policy recalibration, as happened, for instance, in April 2025. Over the long-run, the disparity between the rules-based matrix of global trade and the centralized global finance system manifests a deeper imbalance in the global economy.

Although the imbalance between trade and financial architecture has a long gestation, it tests global economic resilience at a time of fading trust in multilateralism, polarization and slowing economic growth. It is particularly damaging to smaller and vulnerable developing economies which are asymmetrically affected by tariff escalation and face mounting debt service costs and climate crises.

2. From subdued to faltering global growth

The ongoing reset of trade policy norms points to a deeper transformation of the global economy, a transition marked by uncertainty and geoeconomic challenges. Both factors amplify the effects of the absence of reliable drivers of growth. Subdued investment spending – aside from outlays concentrated in certain sectors, such as artificial intelligence technologies – as well as debt overhangs and constrained public spending persist in many countries. These factors weigh on growth prospects already weakened by shocks in recent years.

Consequently, global growth is projected to decelerate to 2.6 per cent in 2025, down from 2.9 per cent in 2024. The rate of expansion is 0.4 percentage points below the pre-pandemic average (2016–2019), which was already subpar (figure I.1). UNCTAD foresees the muted global growth dynamic to persist in 2026, at 2.6 per cent, as economies seek to adjust to the evolving external environment.

The current reset goes beyond trade.

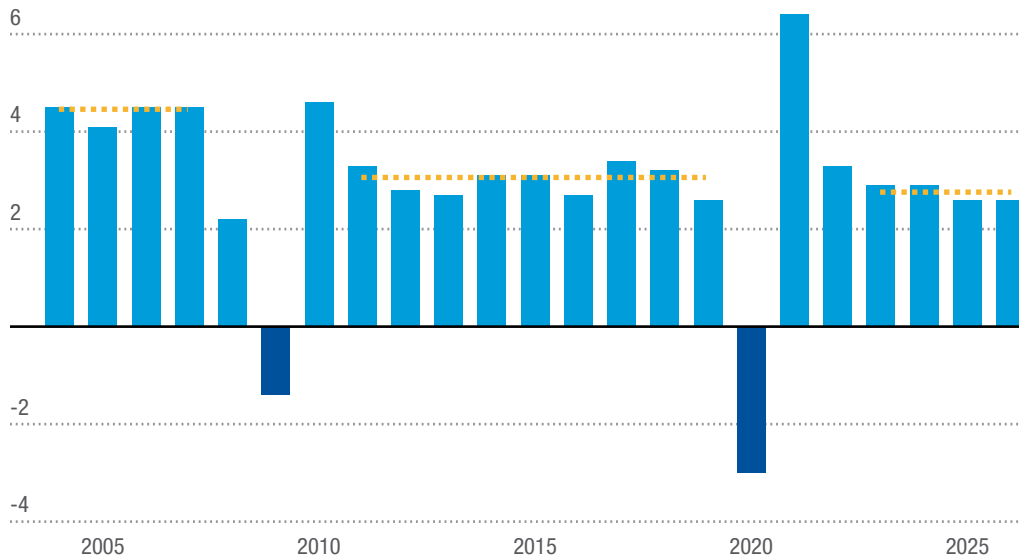
For 2025, UNCTAD estimates a further deterioration in already subdued global growth.





Figure I.1
Faltering global growth shows no signs of picking up in the near term

Global output growth, 2004–2026
(Percentage)



Source: Table I.1.

Note: Output growth is based on GDP at constant 2015 prices (market exchange rates). Yellow dashed lines denote average annual growth rates for 2004–2007, 2011–2019 and 2023–2026. Data for 2025 and 2026 are projections.

Resilience in economic growth numbers observed in early 2025 reflects dynamism in certain sectors and more transitory forces. Strong investment and accelerating deployment of artificial intelligence technologies has boosted economic activity and prospects. At the same time, a notable frontloading of imports and purchases in anticipation of tariff measures – as firms and consumers brought forward purchases to get ahead of increased costs from importing goods – provided a significant albeit temporary support to growth trajectories in the first two quarters of 2025.

Frontloading had a transitory positive impact on outward trade flows to the United States and on production levels, which were ramped up to meet the fleeting uptick in demand for certain goods. The subsequent drop-off, however, will likely negate some of the initial positive impetus from brought forward flows and purchases. As a result, market resilience during the first

half of 2025 may give way to a weakening in activity that will be more clearly reflected in subsequent quarterly data releases.

For its part, the impact of trade policy shifts on global value chains is ongoing and not yet fully internalized. Still, the vulnerabilities of these production processes to sudden shifts in trade policy are evident. Likely disruptions to cross-border production lines will inevitably hurt economic activity. Economies dependent on value chains linked to the United States are particularly exposed to fallout from trade policy shifts.

The policy volatility accompanying these shifts has also hampered growth. Uncertainty complicates firms' decision-making, impacting business spending and capital expenditure as companies delay investment and hiring decisions amid a likely reconfiguration of supply chains. Recent studies have demonstrated that elevated policy uncertainty, particularly around

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Heightened levels of uncertainty have hampered growth.

UNCTAD foresees global growth to remain subdued in 2026, at 2.6 per cent.

trade, tends to coincide with downturns in exports, investment spending and aggregate economic activity (Caldara et al., 2020).

Looking forward, the internalization of trade policy shifts undertaken during 2025 is expected to bring some degree of clarity to the international policy environment in 2026. Yet disruptions and dislocations in international production processes and increasing economic fragmentation stemming from these shifts could continue to temper any potential rebound in global economic activity. Moreover, the expected deceleration in activity after the frontloading of imports and purchases will spill over into next year, further dragging

on growth numbers. The prospect of a positive impetus from investments in new technologies – most notably generative artificial intelligence – will not be sufficient to offset the deterioration in the global economic environment. UNCTAD foresees global growth to remain subdued in 2026, at 2.6 per cent.



Table I.1
World output growth, 1991–2026

GDP growth rates
(Annual percentage change)

Country groups	1991– 1999 ^a	2000– 2009 ^a	2010– 2014 ^a	2015– 2019 ^a	2020	2021	2022	2023	2024	2025 ^b	2026 ^b
World	2.9	3.4	3.2	3.1	-3.0	6.4	3.3	2.8	2.9	2.6	2.6
► Africa	2.3	5.6	2.9	2.8	-3.9	3.9	4.0	3.2	3.2	3.7	4.1
South Africa	2.7	4.0	2.5	1.1	-6.2	4.9	2.1	0.8	0.5	0.9	1.3
► North Africa (incl. South Sudan)	2.6	5.3	-1.8	3.8	-4.8	4.5	3.5	2.3	1.5	3.9	4.2
► Sub-Saharan Africa (excl. South Africa and South Sudan)	1.9	6.5	6.2	2.8	-2.9	3.4	4.8	4.2	4.6	4.2	4.5
► America	3.4	2.5	2.5	2.0	-3.4	6.3	2.9	2.7	2.6	1.8	1.6
► Latin America and the Caribbean	3.3	3.4	3.4	0.0	-7.3	7.1	4.2	2.2	2.2	2.1	2.1
Mexico	3.1	1.7	3.0	1.7	-8.4	6.0	3.7	3.3	1.4	0.8	1.4
► Central America (excl. Mexico) and Caribbean	2.8	4.4	3.6	3.0	-8.8	8.7	4.9	2.9	2.8	2.6	2.8
► South America	3.4	3.9	3.5	-0.9	-6.6	7.3	4.3	1.6	2.4	2.5	2.2
Argentina	4.6	3.8	2.7	-0.3	-9.9	10.4	6.0	-1.9	-1.3	4.0	3.2
Brazil	2.9	3.6	3.2	-0.4	-3.3	4.8	3.0	3.2	3.4	2.1	2.0
► Northern America	3.4	2.3	2.2	2.5	-2.4	6.1	2.6	2.8	2.7	1.7	1.5
Canada	2.8	2.3	2.6	2.0	-5.0	6.0	4.2	1.5	1.6	1.1	1.0
United States	3.5	2.3	2.2	2.5	-2.2	6.1	2.5	2.9	2.8	1.8	1.5
► Asia (excl. Cyprus)	4.4	5.6	5.7	4.8	-0.9	6.8	3.7	4.3	4.0	4.0	3.9
► Central Asia	-4.4	8.1	6.7	4.0	-0.3	5.8	4.6	5.8	5.7	5.9	5.4
► East Asia	4.4	5.6	5.8	4.8	0.4	6.9	2.4	4.1	3.8	3.9	3.6
China	11.0	10.6	8.6	6.7	2.2	8.4	3.0	5.2	5.0	5.0	4.6
Japan	1.2	0.9	1.4	0.9	-4.2	2.7	0.9	1.2	0.1	0.9	0.8
Republic of Korea	6.8	4.9	3.7	3.1	-0.7	4.6	2.7	1.6	2.0	0.8	1.0
► South Asia	5.0	6.6	5.5	6.1	-3.7	8.1	5.9	7.0	5.7	5.3	5.5
India	5.9	7.2	6.6	7.0	-5.9	9.4	7.0	8.8	6.7	6.4	6.4
► South-East Asia	5.3	5.5	5.7	5.0	-3.7	3.8	5.6	4.0	4.8	4.2	4.3
Indonesia	4.8	5.2	5.8	5.1	-2.1	3.7	5.3	5.1	5.0	5.0	4.9
► Western Asia (excl. Cyprus)	4.3	5.1	5.6	2.9	-3.4	7.2	7.3	2.5	2.2	3.1	3.7
Saudi Arabia	2.2	4.3	6.1	2.3	-3.8	6.5	12.0	0.5	2.0	3.6	3.8
Türkiye	3.9	5.0	7.6	4.3	1.9	11.4	5.5	5.1	3.2	3.3	3.5
► Europe (incl. Cyprus)	1.4	2.2	1.2	2.1	-5.7	6.5	3.2	0.7	1.4	1.3	1.3
Russian Federation	-5.9	6.2	3.1	1.2	-2.7	5.9	-1.2	4.1	4.3	1.0	0.6
United Kingdom	2.6	2.1	1.8	2.1	-10.0	8.5	5.1	0.3	1.1	1.2	1.3
► European Union	1.9	1.8	0.8	2.2	-5.5	6.4	3.6	0.4	1.1	1.3	1.4
► Euro area	1.9	1.7	0.6	2.0	-6.0	6.4	3.6	0.4	0.9	1.1	1.2
France	1.9	1.7	1.2	1.5	-7.4	6.9	2.7	1.4	1.2	0.6	1.0
Germany	1.5	1.0	2.0	1.8	-3.8	3.9	1.8	-0.9	-0.5	0.2	1.0
Italy	1.5	0.7	-0.9	1.1	-8.9	8.9	4.8	1.0	0.7	0.6	0.7
► Oceania	3.7	3.2	2.8	2.7	-1.9	5.3	4.1	2.1	0.9	1.6	2.2
Australia	3.7	3.3	2.8	2.5	-2.0	5.4	4.1	2.1	1.0	1.7	2.2
► Developed countries	2.3	2.2	1.8	2.2	-3.9	5.9	2.8	1.7	1.8	1.4	1.4
► Developing countries	4.9	6.4	5.9	4.4	-1.7	7.2	4.1	4.4	4.3	4.3	4.2

Sources: UNCTAD based on United Nations, Department of Economic and Social Affairs, National Accounts Main Aggregates database; United Nations, Department of Economic and Social Affairs, World Economic Situation and Prospects, update as of June 2025; Economic Commission for Latin America and the Caribbean, 2025; OECD, 2025; IMF, World Economic Outlook; Economist Intelligence Unit, EIU Viewpoint Data database; JP Morgan, Global Data Watch; and national sources.

Note: The composition of the five geographical regions follows the M49 standard of the United Nations Statistics Division. The distinction between developed and developing countries is based on the updated M49 classification of May 2022. Calculations for country aggregates are based on GDP at constant 2015 dollars (market exchange rates).

^a Average.

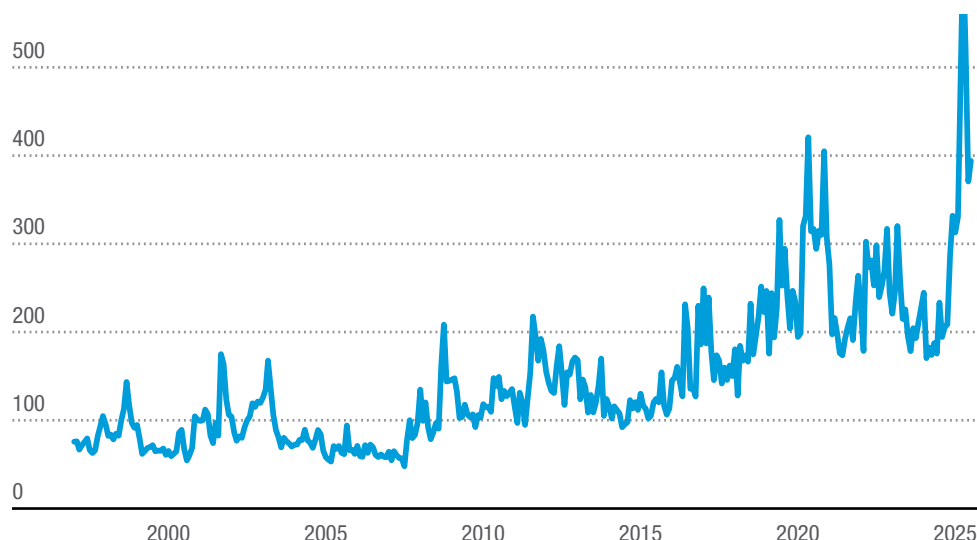
^b Projection.

While policy uncertainty has dropped from unprecedented highs in early April 2025, it nevertheless prevails at historically high

levels. This reflects continuing volatility regarding, although not limited to, future shifts in trade policy (figure I.2).

Figure I.2
While descending from unprecedented highs, policy uncertainty remains elevated

Global economic policy uncertainty index
(Index numbers, average 1997–2014 = 100)



Source: Davis (2016) with updated data from <https://www.policyuncertainty.com>.

Note: The index is calculated monthly based on three underlying components: the newspaper coverage of policy-related economic uncertainty, data from the United States, Congressional Budget Office, and data from the Federal Reserve Bank of Philadelphia's Survey of Professional Forecasters.

The tariff rates that took effect on 7 August have brought greater clarity to the new trading scenario. Yet the potential for further rate adjustments – due to subsequent bilateral agreements, commitments in agreements that affect spending and investments, and the imposition of higher tariffs based on other considerations (as for Brazil, Canada and India) – suggests that

while policy uncertainty has decreased, it will remain elevated and continue to weigh on firms' spending and investment decisions. Prolonged policy uncertainty will likely magnify associated negative effects on trade flows, capital expenditure and overall economic activity, and reverberate in increasingly volatile financial markets.

3. A generalized downturn affects everyone

The downturn in growth prospects cuts across countries. The direct impact of trade measures, along with their

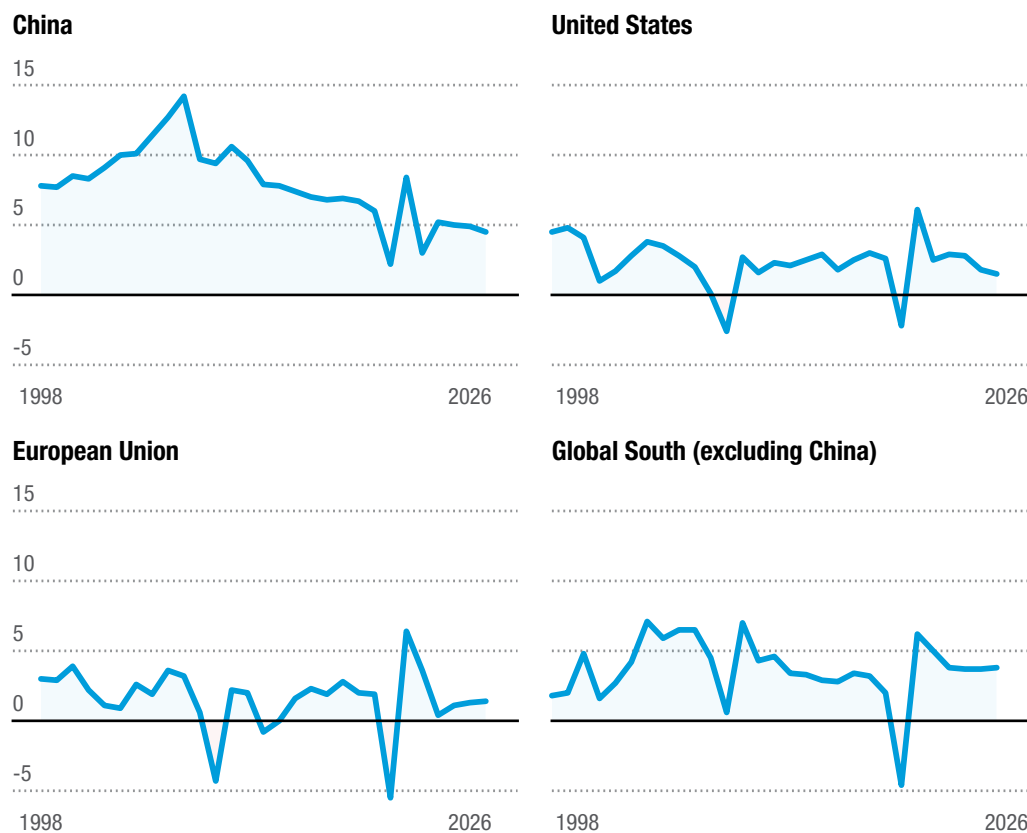
indirect effects through trade linkages and elevated policy ambiguity, has led to a general deterioration in the global environment. Certain regions and countries are, nevertheless, more vulnerable to the adverse international context than others.

The downturn in growth prospects cuts across countries.



Figure I.3 Deterioration in the policy environment is affecting growth dynamics across the globe

Real GDP growth, selected economies, 1998–2026
(Percentage)



Source: Table I.1.

Note: Output growth is based on GDP at constant 2015 prices (market exchange rates). Data for 2025 and 2026 are projections.

In the United States, economic activity is expected to slow as increased tariff rates on supply chains have a detrimental impact on industrial sectors and the services sectors that depend on them. Ongoing policy uncertainty continues to weigh on investment and private consumption (Londono et al., 2025). On the positive side, equity markets have rebounded from

outsized losses in April while investments driven by artificial intelligence have proven particularly strong. These positive trends do not compensate, however, for the shortfall in consumption and other investment spending. UNCTAD expects the United States economy to register a substantial deceleration, expanding by 1.8 and 1.5 per cent in 2025 and 2026, respectively.

Excluding China, growth in developing economies is projected to stay at 3.7 per cent in 2025; and to rise marginally to 3.8 per cent in 2026.



China's rapid diversification of export markets has helped to buttress the expansion in activity.

Among low-income countries, 35 of 68 are currently in or at high risk of debt distress.

Debt defaults have historically led to outsized, long-lasting consequences that hamper any subsequent recovery.

In the European Union, growth is projected to remain sluggish. Despite reaching a deal with the United States to set tariffs for the bloc's exports at 15 per cent – a significant improvement over the initial reciprocal tariff rate – trade frictions could dampen growth prospects. While the agreed baseline tariff rate provides some policy clarity, the prospect of new sectoral tariffs and potential exceptions could keep policy uncertainty high and hinder business investment. Ongoing monetary loosening will likely help ease credit conditions and boost private consumption. A significant expansionary pivot in Germany's fiscal stance may provide some growth impetus, although this will not fully offset the deterioration in the external environment. UNCTAD anticipates ongoing subdued growth in the European Union, with expansions of 1.3 and 1.4 per cent in 2025 and 2026, respectively.

In China, solid economic growth occurred at the beginning of 2025. In the latter part of the year, however, increased bilateral tariff rates have become a drag on output growth. A rapid diversification in export markets as exporters reroute goods shipments to alternative markets; expansionary fiscal policy focused on subsidies for consumption goods, transfers to households and increased outlays for infrastructure; and monetary loosening have all buttressed the expansion in activity. UNCTAD expects the growth rate to remain steady at 5.0 per cent in 2025, before moderating to 4.6 per cent in 2026.

In the rest of the global South, a challenging external environment complicates the outlook. The deterioration in the international environment affects developing economies

through both trade and financial channels (chapter II). Policy shifts reverberate in increasingly volatile international financial markets, leading to greater instability in capital flows and exchange rates and impacting international financing conditions.

Developing countries are particularly susceptible to movements in these variables, especially those with high external financing and refinancing needs and those with elevated external debt burdens. According to the most recent International Monetary Fund (IMF) debt sustainability analysis, more than half of low-income countries – 35 of 68 – are currently in debt distress or at high risk of debt distress (IMF, 2025a). Debt defaults have historically led to outsized, long-lasting reductions in output; a lack of access to international capital markets; and sharp increases in borrowing costs that hamper any subsequent economic recovery.

UNCTAD expects moderate growth in the global South in 2025, with many developing regions experiencing a decline relative to 2024 (table I.1). Excluding China, growth in developing economies on aggregate is expected to remain at 3.7 per cent in 2025 before rising marginally to 3.8 per cent in 2026 (figure I.3).

Amid the subdued global growth outlook, the developing economies of the global South are expected to contribute the lion's share of global economic expansion in 2025, contributing just under 70 per cent of global output growth (table I.2).





Table I.2
Developing regions of the global South are main contributors to global growth

Relative contribution to global growth
(Percentage)

	1995	2000	2005	2010	2015	2019	2024	2025 ^a	2026 ^a
▶ Africa	2.1	2.3	4.7	4.5	3.7	3.3	3.6	4.6	5.2
▶ Americas	29.3	34.6	33.5	26.1	23.3	23.5	29.1	21.9	19.4
▶ Northern America (excl. Mexico)	26.8	28.6	25.5	16.5	23.3	25.0	24.3	17.0	14.4
▶ Latin America and the Caribbean	2.5	6.0	8.0	9.6	0.0	-1.5	4.8	4.9	5.0
▶ Asia	43.9	31.5	42.3	53.7	55.7	54.7	55.6	61.4	62.2
▶ Central Asia	-0.6	0.4	0.6	0.6	0.4	0.9	0.9	1.1	1.1
▶ East Asia	29.5	20.2	27.2	36.3	37.2	38.6	35.3	39.3	37.5
▶ South Asia	4.9	3.4	5.6	7.1	7.8	6.6	10.2	10.4	11.6
▶ South-East Asia	6.2	3.1	3.6	5.2	5.1	6.1	6.1	5.9	6.2
▶ Western Asia	3.9	4.4	5.3	4.5	5.2	2.5	3.1	4.7	5.8
▶ Europe	22.8	30.4	18.1	14.6	15.5	17.0	11.1	10.9	11.6
▶ European Union	21.4	20.4	10.5	9.7	13.7	12.7	6.2	7.9	8.5
▶ Other European economies	1.4	10.0	7.6	4.9	1.8	4.3	4.9	3.0	3.1
▶ Oceania	1.9	1.4	1.4	1.1	1.7	1.6	0.6	1.1	1.6

Source: UNCTAD.

^a Projection.

Developing economies in Asia (excluding China) are projected to see a slowdown in growth, to 3.8 per cent in 2025, and to pick up to 4.0 per cent in 2026. Economic performance in South-East Asia is particularly impacted by trade shifts. On the brighter side, the economy of India continues to exhibit strong growth amid

continued robust public spending and private investment outlays. Western Asia is also projected to see a pickup in growth, to 3.1 per cent in 2025 and 3.7 per cent in 2026, on the back of increasing oil output agreed by OPEC+ countries as well as dynamism in specific non-oil sectors.



In Latin America and the Caribbean, growth is expected to remain relatively weak, at 2.1 per cent in 2025 and 2026. The region's exports are especially affected by trade measures in their principal destination markets, while elevated borrowing costs are weighing on domestic consumption and investment spending in several countries.

In Africa, growth is estimated at 3.7 per cent in 2025 and 4.1 per cent in 2026. A few African economies are experiencing rapid economic development, but a combination of global factors and idiosyncratic domestic conditions holds back the regional aggregate. Cuts to official development assistance are expected to have an outsized impact on the most vulnerable economies in the region, while the expiration of the African Growth and Opportunity Act is likely to have similarly negative consequences for affected countries. Section B provides a more detailed analysis of growth dynamics at the regional and country level.

4. Diverging monetary policy paths add to volatility in international markets

Dramatic policy shifts and the unconventional manner in which these have been implemented have heightened volatility in international markets in 2025. Diverging monetary policy paths in major developed economies exacerbate this effect, amplifying swings in exchange rates and capital flows, among other variables.

In the United States, ambiguity surrounding policy decisions and an uptick in inflation led the Federal Reserve to pause its monetary loosening cycle during the first half of 2025. It subsequently resumed its loosening with two 25 basis-point cuts

in September and October, respectively, amid signs of a weakening labour market. The pace of monetary loosening has, nevertheless, been significantly slower than anticipated when the current loosening cycle began in September 2024.

In Japan, re-emerging inflationary pressures have prompted the Central Bank to begin tightening policy, with a 25-basis-point increase earlier in 2025, after decades of extremely loose monetary conditions.

In the euro area, the European Central Bank continued its loosening cycle in 2025, reducing its key policy rates four times during the first half of the year, by a cumulative 100 basis points. The Bank of England cut its official bank rate three times, by 75 basis points in total.

Despite the reduction in policy rates by other major central banks, while the Federal Reserve held its rate unchanged during the first half of 2025, the dollar depreciated notably. Through the first nine months of the year, it fell 12 and 7 per cent against the euro and pound sterling, respectively. Moreover, its value declined substantially against a broad index of currencies (7 per cent) as well as specifically against a basket of advanced (9 per cent) and emerging (5 per cent) economy currencies (figure I.4). The trajectory in exchange rates relative to the dollar may reflect broader shifts in the perception of safe assets internationally (section C).

Diverging monetary policy paths in the major developed economies adds to volatility in exchange rates and capital flows.

The dollar declined in value against a broad index of currencies.



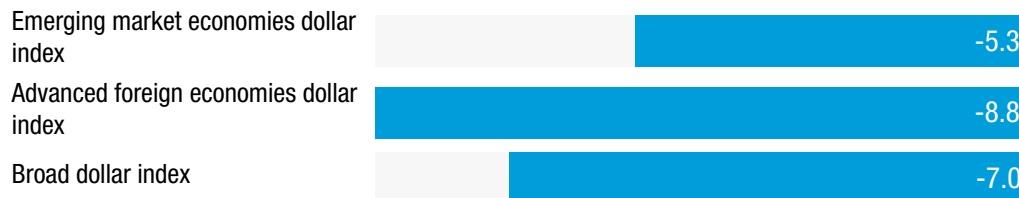


Figure I.4

The dollar depreciated notably against a broad array of currencies in 2025

Evolution of broad, emerging market economies and advanced foreign economies dollar indices, 1 January – 30 September 2025

(Percentage)



Source: UNCTAD based on data from the Federal Reserve Bank of St. Louis.

Notes: A negative (positive) value corresponds to a depreciation (appreciation) of the dollar. The displayed dollar indices refer to a weighted average of the dollar against the currencies of a broad group of major trading partners, advanced foreign economies and emerging market economies.

5. International credit conditions remain tight

Ongoing tight macrofinancial conditions internationally continue to hinder global growth prospects. Although financial markets have partly recovered from April's turmoil, bond yield volatility remains elevated (figure I.5).

Higher yields can indicate an improved outlook for economic growth. However, the uptick in government bond yields has been principally driven by increased uncertainty pushing up term premia, or the amount by which the yield on a long-term bond exceeds that on shorter-term bonds, reflecting the amount investors expect to be compensated for lending for longer periods. Concerns around public debt trajectories are also in play. For example in the United States with the passage of renewed tax cuts¹ and in the United Kingdom.

The direct impact of rising government bond yields on debt-servicing costs is particularly worrisome given elevated public debt levels. Increased bond yields do not immediately translate into higher government interest payments. But this does occur over time as existing bonds mature and are refinanced by issuing new bonds at prevailing yields.

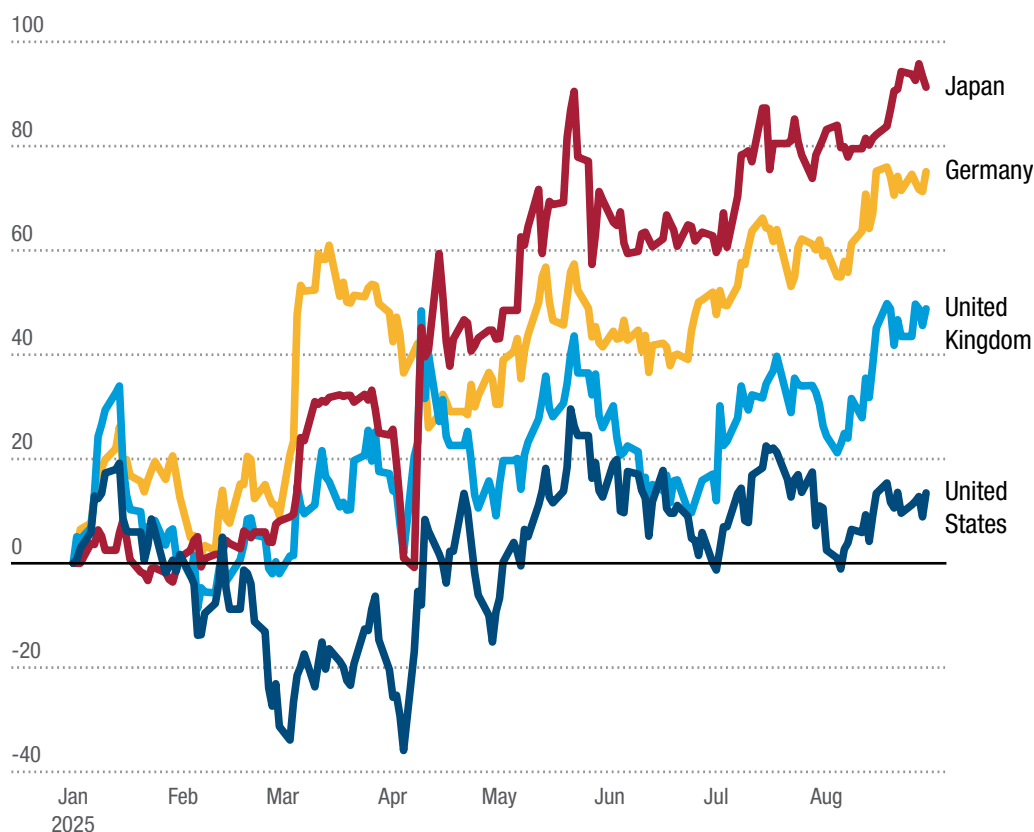
Ongoing tight macrofinancial conditions internationally hinder global growth prospects.

¹ The White House (2025). President Trump's One Big Beautiful Bill Is Now the Law. 4 July.



Figure I.5
Increases in long-term government bond yields in developed economies reflect tight macrofinancial conditions

Change in 30-year government bond yields since 1 January 2025
(Basis points)



Source: UNCTAD based on the LSEG Workspace.

Increased bond yields in major developed economies put upward pressure on global interest rates.

The indirect impact is equally troublesome. Increased bond yields in the major developed economies put upward pressure on global interest rates. Tight international financial conditions, in turn, strain public finances in developing countries, many of which will soon need to refinance significant shares of outstanding debt. While the depreciation of the dollar during 2025 has provided some reprieve in this regard, the upward trajectory of bond

yields nevertheless marks a concerning trend. Moreover, government bond markets play a key role in broader capital markets, serving as the foundation for a range of other financing vehicles that directly influence the borrowing costs of businesses and households.

6. Policy responses

In the current environment, proactive policy action is crucial to shield economies from the adverse effects of current shifts and an unpredictable international landscape. It must also lift economies out of their low-growth malaise.

Where fiscal pressures constrain critically needed public spending and investments, particularly amid increasing debt-servicing costs and waning external financing, governments can look to boost public resources through enhanced and more efficient frameworks of domestic revenue mobilization. Failure to meet growing public investment needs is likely to have long-lasting detrimental impacts on growth and development prospects (UNCTAD, 2024b), while unaddressed public spending constraints severely limit the capacity to enact countercyclical policies to manage demand shocks (UNCTAD, 2024b).

Internationally, regulatory arbitrage – including tax avoidance, base erosion and profit shifting, particularly by larger corporations – continues to drain fiscal revenues from developing countries and can undermine financial stability (chapter III). Greater international tax cooperation is vital to address these harmful practices (UNCTAD, 2019). Increased concessional financing is needed to support development objectives, particularly in the most vulnerable developing countries. Coordinated global policy actions – encompassing concessional financing and debt relief – are critical to mitigate growing financing vulnerabilities.

A key factor in reducing exposure to prevailing trade shifts is through deepening regional integration and export diversification (chapter IV). When a country's exports have multiple destination markets, businesses can more easily adapt to shifts or downturns in one market by redirecting outward flows to others (UNCTAD, 2025c).

Recently, China rerouted exports to alternative markets amid tariff escalation with the United States (UNCTAD, 2025c). This suggests that market diversification can cushion the impact of sudden shifts in any individual market on revenues and production.

Regional initiatives can help diversify productive structures and prevent excessive reliance on particular products – as well as any individual export destination market – while providing a potential bridge to global trade integration based on higher value-added goods (UNCTAD, 2025e). In parallel, strategies beyond manufacturing-led exports, particularly those that seek to create quality jobs in the services sectors, including non-tradable services, can also provide a complementary development path and reduce exposure to external dynamics (UNCTAD, 2024b).

Multilateral institutions are crucial in mitigating the potentially negative spillover effects of policy decisions in one country on others. More generally, multilateral cooperation and coordinated policies are needed now more than ever to avert economic fragmentation, revitalize and sustain long-term growth, and tackle global challenges.

Proactive policy action is crucial in shielding economies from the adverse effects of current shifts.

Failure to meet growing public investment needs is likely to have long-lasting detrimental impacts on growth and development prospects.



B. Regional trends

The Americas

The **United States** economy is navigating a complex and somewhat fragile landscape. Since early 2025, the Government has embarked on policy initiatives to decisively recalibrate national priorities.

This is reshaping domestic and external dynamics. While certain policy intentions are clearly articulated, their long-term macroeconomic impact remains contingent on dynamic global responses and domestic adjustments still underway. It is therefore premature to draw conclusions about its economic trajectory in the medium-term. The recent shutdown of the federal government further blurred the picture as several data releases were delayed, including third quarter GDP. With these caveats in mind, annual GDP is expected to grow by 1.8 per cent in 2025 and 1.5 per cent in 2026.

Looking back at the first half of 2025, output growth recovered at an annualized rate of 3.8 per cent during the second quarter, after contracting by 0.6 per cent in the first quarter. Large swings in trade data distorted these trajectories as significant frontloading took place following tariff announcements in the first semester. On the expenditure side, improvement in the GDP headline figure in the second quarter primarily reflected decreased imports and a moderate rebound in consumer spending, although this mostly corresponded to the highest income deciles. These positive contributions were offset by declining investment and exports. More granular indicators suggested that the economy had been losing steam in the third quarter of 2025. The growth of the labour supply slowed even as the unemployment rate remained stable.

On inflation, momentum in reducing wage and price growth to levels compatible with Federal Reserve objectives has faltered in recent months. Nevertheless, having paused rate cuts during the first half of 2025, the Federal Reserve resumed its monetary loosening with two 25 basis-point cuts in September and October, respectively, amid signs of a weakening labour market.

Concerns about the United States fiscal deficit – which is about 6 to 7 per cent of GDP, a historically high figure outside a recession – are growing in financial markets. This has begun to drive up yields on longer-maturity Treasuries and could lead to a reassessment of their safe-haven status, prompting further bearish sentiments on the dollar and threatening global financial stability.

In **Canada**, trade tensions have put the economy on a lower growth path for the coming years as evolving trade relations are expected to fundamentally reshape the Canadian economy.² GDP is projected to grow by 1.1 per cent in 2025 and 1.0 per cent in 2026, with risks tilted to the downside. During the first half of 2025, GDP contracted by 1.6 per cent in the second quarter after recording 2.2 per cent growth during the first quarter, amid a temporary surge in exports in anticipation of increased tariffs. During the second half of 2025 and in 2026, economic activity is expected to recover albeit at a very modest pace.

Mexico is estimated to register sluggish growth of 0.8 per cent in 2025, after a subdued expansion of 1.4 per cent in 2024. A 25 per cent tariff on Mexican goods to the United States – excluding goods under the United States–Mexico–Canada Agreement – has had a substantial impact on the

² Bank of Canada (2025) Monetary Policy Report – October 2025.



country's critically important export sector. Given that the United States accounts for approximately 80 per cent of Mexican goods exports, and that half of these goods do not fall under the Agreement, the tariffs represent a significant strain on growth prospects. Ongoing uncertainty regarding future tariff rates weighs on investment and business spending, and has prompted slowing industrial production and subdued household consumption. A more accommodative monetary policy stance is largely offset by a restrictive fiscal stance, which is tempering the growth outlook. For 2026, growth is projected to pick up moderately but remain subdued, at 1.4 per cent, amid challenging external conditions.

Economic recovery is expected in **Argentina** after two consecutive years of contractions. The economy is estimated to expand by 4.0 per cent in 2025. The rebound in the first half of 2025 was driven by a recovery in private consumption due to improving real wages and an uptick in investment spending amid easing domestic credit conditions. Strong performance by the extractive mining and energy sectors helped boost exports and overall economic activity. However, a sharp weakening of the peso in September and significant depletion of foreign exchange reserves amid efforts to support the currency's value dampened the growth momentum observed in the first half of 2025. The provision of external financial support – most notably the establishment of a 20 billion dollar swap line with the United States – served to partially calm markets. The Government's aggressive cutting of public outlays including sharp cuts to public works projects, may also continue to constrain activity amid already difficult socioeconomic conditions, with poverty affecting over 30 per cent of the population in the first semester of 2025 (INDEC, 2025). In 2026, growth is projected to decelerate to 3.2 per cent as an increasingly difficult external environment and slowing growth in some of the country's main export markets hamper a more dynamic expansion.

In **Brazil**, growth is estimated to slow to 2.1 per cent in 2025 compared to 3.4 per cent in 2024. A more restrictive monetary policy and high borrowing costs, which will likely depress domestic consumption and investment spending, and an increasingly unfavourable external environment are largely responsible for the more subdued expansion. An ongoing expansionary fiscal stance could help to buttress growth. The decision by the United States Administration to impose a 50 per cent tariff on Brazil's goods exports – with the notable exclusion of the energy and aviation sectors – is expected to have an impact on the economy and specifically on the value of the Brazilian real, although exports to the United States only account for 12 per cent of the country's total goods exports. Growth is projected to remain stable at 2.0 per cent in 2026, with the prospect of a less restrictive monetary stance helping to ease credit conditions and boost domestic consumption and investment spending.

European Union

In the economies of the European Union, growth is expected to remain relatively weak at 1.3 per cent in 2025. The deal between the United States and European Union setting tariffs on the bloc's exports at 15 per cent was an improvement over earlier announcements of much higher rates. It brought greater policy certainty to the trading relationship. Nevertheless, the 15 per cent blanket tariff rate and a higher 50 per cent rate on exports of metals are a significant setback from prior trading arrangements. A more complicated external environment will likely hamper growth. Accommodative monetary policy conditions – the European Central Bank continues to reduce its key policy rates – could help shore up private consumption and investment. Economic growth is projected to reach 1.4 per cent in 2026 as domestic demand strengthens amid ongoing monetary easing and lower borrowing costs.



Economic expansion in **France** is estimated to decelerate from 1.2 per cent in 2024 to 0.6 per cent in 2025. Tariffs could hold back export growth as well as private investment spending. The easing of monetary policy may help to buoy consumer spending amid lower borrowing costs. While economic growth was higher than expected in the first half of 2025, this was largely driven by accumulating inventories, implying a probable softening in growth during the latter part of the year. In 2026, growth is projected to rise moderately to 1.0 per cent as further monetary easing encourages private spending.

In **Germany**, growth is estimated to return to positive territory, reaching 0.2 per cent in 2025 after a 0.5 per cent contraction in 2024. A substantial trade surplus with the United States makes the German economy particularly exposed to fallout from higher tariff rates. A transitory boost to the economy from frontloading export orders at the beginning of the year will likely fade. Growth may slow significantly in the second half of 2025 as exports and investment spending wane. On the positive side, reforms to fiscal rules that previously constrained public spending, particularly on infrastructure, could facilitate greater public outlays and buttress growth. In 2026, growth is projected at 1.0 per cent, as infrastructure spending boosts investment and growth, and easing monetary conditions support household spending.

Economic expansion in **Italy** is estimated to remain steady at 0.6 per cent in 2025, compared to 0.7 per cent in 2024. The Italian economy is similarly exposed to the tariff hikes as it runs a significant trade surplus with the United States, its largest non-European Union export market. The unfavourable external environment will likely dampen investment. But easing borrowing costs from looser monetary policy could support a more dynamic expansion in private consumption, further aided by lower inflationary pressures that could bolster household disposable incomes. In 2026, growth is projected at 0.7 per cent as

ongoing monetary easing produces a steady expansion in household consumption.

United Kingdom

Growth in the **United Kingdom** is estimated to remain almost constant at 1.2 per cent in 2025. The United Kingdom was among the first countries to reach a tariff deal with the United States, which fixed a blanket higher rate of 10 per cent. Despite the predominance of the United Kingdom's services exports – which are unaffected by tariff increases – the higher rate may still weigh on the country's goods exports and hamper economic growth. While a strong expansion in activity took place at the beginning of the year, this corresponded mostly to the frontloading of exports to the United States in anticipation of tariff hikes. The outlook for the remainder of the year is one of slowing growth amid increasing energy costs and inflation that may offset the positive boost to household demand from continued monetary easing. UNCTAD expects growth to rise marginally in 2026, to 1.3 per cent, as a series of large-scale public investment projects – focused on green energy technologies, infrastructure and residential construction – stimulate economic activity. A projected easing in inflation along with reduced interest rates could support greater household consumption.

Russian Federation

The economy of the **Russian Federation** is expected to see a sharp deceleration. After expanding by 4.3 per cent in 2024, growth is expected to decelerate to 1.0 per cent in 2025 and 0.6 per cent in 2026. Falling oil prices, external trade and financial restrictions, and policy uncertainty amplify pressures on growth. The central bank has lowered its key policy rate from 21 to 17 per cent, but credit conditions remain tight. Inflation hovers around 9 per cent, over double the 4 per cent target. Unemployment is low at around 2.3 per cent, primarily due to labour shortages, but wage growth has lagged



inflation, weakening consumption. In some industries, such as transport, construction, retail trade and real estate, the slowdown is acute propelling higher numbers of corporate and debt restructurings as well as rising unemployment. While central bank interventions and fiscal inflows strengthened the rouble early in 2025, a modest decline is expected later in the year. Coupled with low growth, rising military expenditure, sectoral adjustments and declining oil prices, the budget deficit is projected to be 2.5 to 2.7 per cent of GDP.

East Asia

China is estimated to achieve its growth target of 5.0 per cent in 2025, building on strong growth in the first three quarters. Better-than-expected performance is generally attributed to two factors.

First, anticipating external challenges, China announced expansionary policies before the tariff shocks. In fiscal policy, the Government increased the ratio between the budget deficit and GDP from 3 to 4 per cent. It also announced RMB 1.3 trillion of ultra-long special treasury bonds to support consumption and national strategic projects; RMB 500 billion in special treasury bonds to replenish the capital of large State-owned commercial banks; and RMB 4.4 trillion in local government special-purpose bonds. In monetary policy, the Central Bank deployed policy measures comprising further cuts to the policy rate (10 basis points), a reserve requirement ratio (50 basis points), structural policy tool rates (25 basis points), mortgage rates (25 basis points), and structural loan support to science, technology and innovation, services and agriculture. With proactive policy measures, consumption grew by 5 per cent.

Second, merchandise exports have proven resilient amid tariff shocks. Despite a 9.9 per cent decline in goods exports to the United States in the first half of 2025, trade flows to other countries, notably to ASEAN countries, Africa and Central Asia have grown rapidly. Along with the

effects of frontloading, these flows enabled overall exports to increase by 7.1 per cent over the first three quarters of 2025. The bilateral summit between China and the United States in October resulted in a one-year suspension of specified tariffs and export control measures, providing some stability to the bilateral trading relations.

Some risks remain, including ongoing tariff tensions. Domestically, the real estate market remains vulnerable and continued to weigh on growth through the third quarter of 2025. While manufacturing output growth was robust (6.8 per cent), investment slowed in the third quarter and the purchasing managers' index for the sector has been below 50 per cent since April. Finally, consumer price indices remained negative during the first three quarters of the year, at -0.1 per cent, pointing to constraints on domestic consumption despite 4.5 per cent growth in this period.

Growth in the **Republic of Korea** is estimated to reach only 0.8 per cent in 2025. Weak performance in the first two quarters came on the back of falling private consumption, reduced investment in construction, and lower exports. Economic activity is expected to expand faster in the second half of the year supported by monetary and fiscal policy measures. The Central Bank has cut interest rates by a cumulative 100 basis points since October 2024. The Government approved a KRW 13.8 trillion supplementary budget in May and plans to inject another KRW 20 trillion. Inflation is expected to remain stable at 2.0 per cent, as upward pressures from processed food and services prices are offset by weak demand and declining global oil prices. The labour market has shown resilience, with the unemployment rate shrinking to 2.6 per cent in June.

On 31 July 2025, the Republic of Korea and the United States reached a trade agreement. Under the new terms, general exports to the United States will face a 15 per cent tariff. Automobiles have a globally standardized tariff of 25 per cent, while steel, aluminium and copper are at

50 per cent. Although these rates remain elevated, the agreement provides greater predictability and reduces uncertainty, offering some relief to exporters. Economic growth is projected at 1.0 per cent in 2026.

The economy of **Japan** is estimated to expand by 0.9 per cent in 2025, reflecting the impact of weakening global growth and import tariffs in the United States. Japan's economy is highly export-oriented; export revenues accounted for roughly 17 per cent of GDP in 2024. The United States is the single largest destination market. Motor vehicle exports to the United States declined sharply during the second and third quarters, although a trade deal negotiated in July saw Japan pledge a \$550 billion package of investments and loans to the United States in exchange for a reduction in tariffs on automobile imports. Lower public sector expenditure has been a drag on growth over the first half of the year, and in October, the newly elected Prime Minister announced an economic stimulus package that is expected to expand local government grants, with a focus on small and medium-sized companies, and investments in growth sectors such as artificial intelligence and semiconductors. In monetary policy, the Central Bank has deferred further increases to the short-term policy target rate, currently at 0.5 per cent, after hikes in 2025 put Japanese interest rates above zero for the first time in many years. Rates are still far lower than in most other advanced economies. Economic growth is projected at 0.8 per cent in 2026.

expenditure, easing financing conditions and declining inflation. In fiscal policy, the Government planned a public deficit of 4.4 per cent of GDP over the current fiscal year, amid tax cuts and corporate tax rebates. In August, S&P Global upgraded the sovereign credit rating from “BBB-” to “BBB”, citing robust fundamentals, disciplined fiscal governance, improved policy frameworks and market dynamism. This upgrade is likely to bolster investor confidence and burgeoning transnational corporate investment plans, although tariff policy changes could temper enthusiasm. In monetary policy, the Reserve Bank of India initiated cuts to the repo rate in 2025; it remained unchanged at 6.5 per cent for several years before being cut by 100 basis points between February and October. Inflation is likely to hover around 4 per cent in 2025, well within the Reserve Bank's target band of 2 to 6 per cent. Externally, its relatively low ratio of goods exports to GDP limits the exposure of India to global trade effects. Tariffs imposed by the United States, however, could have an impact on critical manufacturing sectors, such as apparel and electronics, potentially shaving up to 0.3 percentage points from GDP growth. Capital markets have exhibited resilience as domestic institutional investors have compensated for most foreign outflows, significantly reducing their disruptive impact. The economy is projected to grow by 6.4 per cent in 2026, supported by continued public spending, private investment and a weakening dollar alleviating its trade deficit.

South Asia

Economic activity across the region remains dynamic and driven by its largest economy, India. Complex debt dynamics burden smaller economies, such as Bangladesh, Pakistan and Sri Lanka, which struggle under IMF programmes. **India** has been the world's fastest-growing major economy since 2021. Economic activity is estimated to expand by 6.4 per cent in 2025 through continued elevated public capital

South-East Asia

Economic expansion in **Indonesia** is estimated at 5.0 per cent in 2025. The economy registered 5.0 per cent growth in the first three quarters of the year, driven primarily by exports and domestic consumption. The three largest exports destinations for Indonesia continue to be China (23.3 per cent of total exports), the United States (11.5 per cent) and India (7.0 per cent). Government spending contracted slightly in the wake of the 2024 election



but returned to positive growth in the third quarter of 2025. The government has revised the fiscal deficit to GDP ratio up to 2.8 per cent. This should enable funding for a new stimulus package and measures to offset external uncertainties. The manufacturing sector has seen increasingly strong growth in recent months, indicating ongoing expansion, while the services sectors registered similarly robust activity. The growth momentum is expected to persist through 2025. In monetary policy, amid low inflation, the Bank of Indonesia has cut its policy rate five times since September 2024, totalling 125 basis points, amid manageable inflationary pressures. Indonesia submitted its initial memorandum on its accession to the Organisation for Economic Co-operation and Development (OECD) in June, which is likely to lead to broader policy reforms. Economic growth is projected to remain robust at 4.9 per cent in 2026.

Western Asia

Western Asia grew more rapidly in 2025 despite lower oil prices and geopolitical tensions across the region. **Saudi Arabia** is estimated to grow at 3.6 per cent in 2025 on the back of increasing oil output agreed by the Organization of the Petroleum Exporting Countries plus allied non-OPEC countries (OPEC+) and a dynamic non-oil sector. The country continues to rely on its Vision 2030 diversification strategy, even though several major projects, such as Neom, were scaled down, reflecting cost pressures, lower oil prices and slowing oil revenue growth. The Saudi economy is projected to expand by 3.8 per cent in 2026, though the region and oil prices remain particularly volatile.

Türkiye is undergoing stabilization and is estimated to grow by 3.3 per cent in 2025, supported by more cautious monetary policy, public spending and external demand boosted by a competitive exchange rate. Annual inflation has declined but remains elevated, hovering above 30 per cent in September. This crimps private consumption and investment. GDP is projected to expand

by 3.5 per cent in 2026 amid possible fiscal stimulus before the 2028 election.

Africa

Economic activities across the continent are projected to grow by 3.7 per cent in 2025 amid considerable uncertainty. This rate, partly resulting from low base effects in some large African economies, is largely insufficient to support sizeable progress on the Sustainable Development Goals. A few African economies are experiencing rapid economic development, but a confluence of global factors and idiosyncratic domestic conditions holds back the aggregate. While exports of hydrocarbons and many other primary commodities are expected to remain relatively immune to United States trade policy, which primarily targets manufacturing, a challenging global macroeconomic environment will likely depress growth. Moreover, the introduction of new tariffs on African countries and the expiration of the African Growth and Opportunity Act at the end of September could hinder their structural transformation. Prospects for 2026 remain subdued. The appreciation of many currencies coupled with slowing inflation rates throughout the region may be a boon, improving current account balances and allowing central banks to shift towards more accommodative stances. This trend has started, but several central banks remain cautious.

In **South Africa**, which is among the region's three largest economies, recent data reveal persistent supply-side problems, including logistics. These continued to hamper growth in the first half of 2025. Business and consumer confidence declined amid uncertainty. Ongoing structural reforms, however, are expected to gradually support economic activities in the coming years, with GDP growth increasing gradually, albeit only to a feeble rate of about 2 per cent.

In **Nigeria**, the National Bureau of Statistics in mid-2025 rebased GDP to 2019. This showed that the economy is 35 per cent



larger than initially estimated under the prior 2010 base year. The revision changed historical data for both the country and the African continent. Recent data point to improved economic activities in several key sectors, resulting in higher net capital inflows, increased earnings from greater crude oil production, rising non-oil exports and a significant reduction in aggregate imports. The renewed push to expand the country's free zones ecosystem also supported this development. In parallel, the Government's ambition to step up infrastructure development, including new roads, will also have positive spillovers to the wider economy once it reaches broadscale realization.

In **Egypt**, improved economic conditions following macroeconomic instability (2022–2024) led to year-on-year growth of 4.5 to 5 per cent during the first half of 2025. A solid recovery in non-oil manufacturing activity and significant activity in the tourism and telecommunication sectors supported this development. On the expenditure side, increased private investment coupled with improved net exports boosted aggregate demand. Despite a recent decline, inflation is persistently high, although private consumption is expected to remain robust. Fixed investment is poised to strengthen, owing partly to large foreign-led projects in real estate as well as the ongoing transformative high-speed railway project.

In the rest of Africa, economies characterized by resource abundance and strong commodity exports are expected to maintain momentum amid intensified competition for strategic natural assets. Yet triggering positive spillovers to other economic sectors and the general population remains a challenge. The adverse impact of elevated public debt levels – particularly in countries with limited fiscal space – still looms (UNCTAD, 2025d). This financial pressure is poised to dampen investment and growth prospects while constraining policy flexibility. Additional vulnerabilities stem from geopolitical tensions, especially in

the Sahel, and episodes of civil unrest which can disrupt economic activity. The former also contributes together with climate variability and extreme weather events to aggravated food insecurity; 31 African countries still require external assistance for food (FAO, 2025).

Oceania

The economy of **Australia** is estimated to expand by 1.7 per cent in 2025. Its growth trajectory is tempered by the broader global context, with weaker global and national demand amid increased uncertainty due to trade tensions. Fiscal policy measures, including public investment, continue to be important support for the domestic economy, helping to offset a decline in private demand as business and consumer confidence soften. The economy has limited direct exposure to trade tariffs. It is nonetheless at risk indirectly if the Chinese economy slows and reduces demand for Australia's commodity exports.

In monetary policy, the Reserve Bank surprised markets by choosing not to continue lowering interest rates at its latest meeting in July, holding the base rate at 3.85 per cent. This is nonetheless the lowest level for the last two years. A rise in unemployment to over 4 per cent signals a cooling job market.

Severe weather events have impacted critical sectors of the economy, including mining, tourism and shipping, with uncertain implications for costs and prices. The Reserve Bank recently changed regulations on surcharges on credit and debit cards and interbank charges. This could potentially save consumers and businesses more than AUD 1 billion dollars and nudge demand without lowering the cost of credit. Growth is expected to increase to 2.2 per cent in 2026, supported by recovering domestic consumption and continued strength in public demand.



C. The role of the dollar in the global economy

1. Introduction

The central role of the United States dollar in the international monetary and financial system has endured through recent decades despite profound transformations in the global economy. Through this period, the dollar's centrality has been underpinned by strong network effects and complementarities among its different functions in global trade and international financial transactions, in international reserve holdings, as a benchmark for exchange rate stabilization, and in the unmatched depth, liquidity and perceived safety of United States assets. While some recent developments have spurred debates about the future role of the dollar, its functions as the global financial anchor are deeply embedded in trade and financial networks (chapter IV).

The dollar saw a gradual rise as the global reserve currency. During the 1920s and 1930s, it gained prominence as the pound sterling declined in international trade (Chitu et al., 2014). After the Second World War, the Bretton Woods Agreement pegged the dollar to gold and required countries to ensure convertibility to the dollar at a pre-determined rate. This fixed exchange rate regime lasted nearly three decades. In 1971, the United States suspended dollar–gold convertibility, ushering in free-floating currencies and unrestricted capital flows. Despite this, the dollar's dominance continued, shaping international liquidity and credit conditions (Tooze, 2021). The emergence of the euro and China's global economic rise coexisted with the dollar's centrality, which was further reinforced by the expansion of global finance and financialization (chapter IV). These transformations cemented the dollar as the

primary global currency, underscoring its enduring influence on the world economy and position as the global financial anchor (Eichengreen, 2021, 2025).

Some developments in 2025 have reignited long-running debates in economic history and globalization about the role of the dollar in international monetary order and the global hierarchy of currencies. The following section examines key recent trends in the macroeconomic context. Chapter IV discusses the dollar-anchored financial system and the global South.

2. The enduring centrality of the dollar

The various complementary uses of the dollar, along with associated network effects and jointly reinforcing dynamics between trade and finance, have underpinned the currency's dominant position in recent decades. For example, its prevalent use in trade invoicing can incentivize companies and households to hold dollar-denominated assets as a store of value (IMF, 2025b). In turn, high demand for dollar deposits has depressed associated interest rates, favourably impacting terms for dollar-denominated borrowing and encouraging companies and households to assume dollar-denominated liabilities. The dollar's dominance in international transactions has induced central banks to seek to minimize movements of their respective currencies against the dollar (IMF, 2025b). The resulting greater stability in the dollar exchange rate and increased liquidity in capital markets reinforced reliance on the dollar in trade invoicing and debt issuances.

The dollar's centrality has been underpinned by strong network effects and complementarities among its different uses.

Despite the restructuring of the Bretton Woods system, the centrality of the dollar endured.



The dominance of offshore dollar financing underpins the international transmission of the Federal Reserve's monetary policy.

The dollar's role as the global reserve currency appears to be evolving; its weight in international reserves has declined significantly since 2000.

The centrality of the dollar in the bulk of its functions— as a currency for foreign bank loans and deposits, foreign exchange transactions and global payments; an invoicing and settlement currency for international trade; and a global investment asset – has remained largely intact (chapter IV). The share of the dollar in these different areas has remained relatively stable since 2000. The dollar currently accounts for 89 per cent of all global foreign exchange trades (BIS, 2025),³ approximately half of all international trade⁴ and about half of the total value of global payments processed through the SWIFT network (United States of America, Federal Reserve, 2025).

More than 60 per cent of the \$30.8 trillion in outstanding international debt securities is denominated in dollars.⁵ This preponderance of offshore dollar financing reflects the dollar's status as the primary funding currency in global markets and underpins the international transmission of the Federal Reserve's monetary policy, which continues to shape the global financial cycle (chapter II).

Yet some shifts away from dollar centrality are now palpable, most notably in its status as the global reserve currency. The share of dollars in the basket of currencies making up the allocated official foreign exchange reserves of central banks across the globe – the total size of which stands at \$11.5 trillion – has been in decline since 2000 (figure I.6). This trend points to a greater diversification of currencies in international reserves, indicating a strategy to reduce excessive exposure to the dollar.

³ Data remain the latest available as of August 2025.

⁴ Based on data summarized in United States of America, Federal Reserve, 2025.

⁵ BIS International Debt Securities Statistics, July 2025.





Figure I.6

The dollar has seen a notable decline in its share of central banks' foreign exchange reserves

Change in share of foreign currency reserves, first quarter of 2000 – fourth quarter of 2024
(Percentage points)



Source: UNCTAD based on data from the IMF Currency Composition of Official Foreign Exchange Reserves (COFER).

The apparent divergence in trends between the dollar's role as a reserve asset for monetary authorities and its ongoing centrality in other international functions can appear puzzling. This is particularly so given the assumed complementarities between these different functions (Gopinath and Stein, 2021).

Diverging trajectories indicate an apparent misalignment between the new strategic treatment of the dollar by State actors, and the established practices of private markets that is sufficient to offset these complementarities (chapter IV). The liquidity, scale and perceived safety of dollar-based assets have continued to be defining factors for the sector. At the same time, monetary authorities have increasingly prioritized other considerations, including geopolitical factors, in determining the composition of reserve holdings (Eichengreen, 2025).

Based on these trends, the dollar's central role in the international monetary system is likely to endure for the majority of its functions, with only a gradual ongoing decline in its role as the global reserve currency. However, while the dollar's share of official foreign exchange reserves has declined markedly, this has not been mirrored by the commensurate ascent of any single alternative currency (figure I.7).

Rather, the lower share of the dollar is reflected in an increasing share of an array of other currencies that, while growing, still only each account for a marginal share of the foreign currency holdings of monetary authorities. In other words, despite its notable decline, the dollar continues to account for a far greater share of central banks' reserve assets than any other currency. While the move away from the dollar in official foreign exchange reserves is clear, no indication exists of another currency as a potential replacement.

Diverging trajectories indicate an apparent misalignment between the new strategic treatment of the dollar by State actors, and the established practices of private markets.

The decline in the dollar's share of international reserves has not been mirrored by the ascent of any single alternative currency.

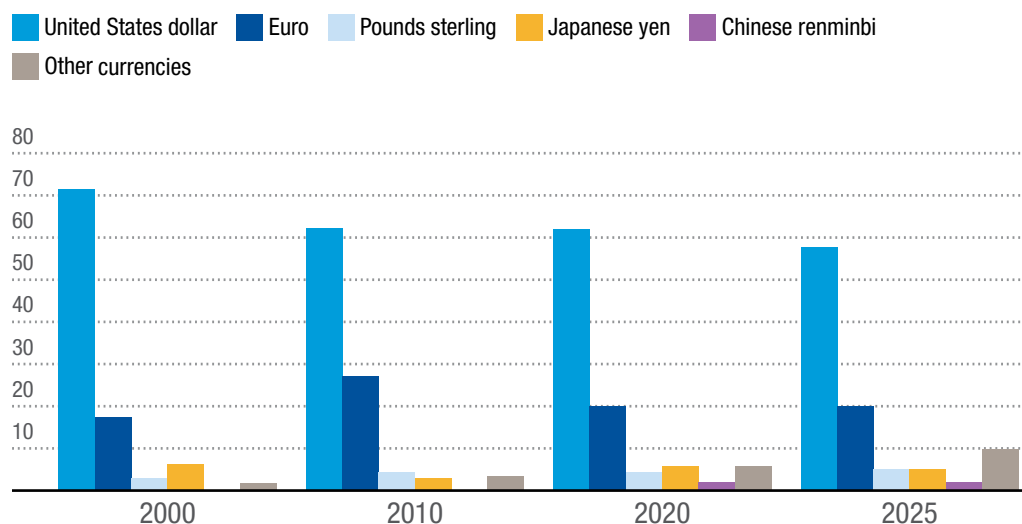




Figure I.7

The decline of the dollar in foreign exchange reserves is not mirrored by the ascent of any single alternative currency

Share of total allocated foreign currency reserves
(Percentage)



Source: UNCTAD based on IMF COFER.

Note: 2025 refers to the first quarter of 2025.

Importantly, the data and analysis presented above corresponds to foreign currency reserves and, by definition, excludes monetary gold. Despite its distinct characteristics as an asset class – as well as the fact that it is not issued by a monetary authority and therefore does not confer specific benefits to a particular issuing country – gold has nevertheless gained renewed prominence as a central bank reserve asset.

Indeed, the market value share of monetary gold in central bank total reserves surpassed 20 per cent at the end of 2024 and continued to rise in 2025 (figure I.8A). Gold has now superseded the euro as the second largest central bank reserve asset. While the vast bulk of this upswing corresponds to price effects, volumes have also registered sustained, albeit far more moderate, increases (figure I.8B). Ongoing

demand for gold from monetary authorities is principally born out of diversification strategies to guard against economic risks, such as inflation and cyclical downturns, as well as geopolitical considerations (ECB, 2025). The sustained demand for gold could add further weight to the potential softening demand for the dollar as a reserve asset. Nevertheless, as noted previously, the dollar's predominance in this regard persists.

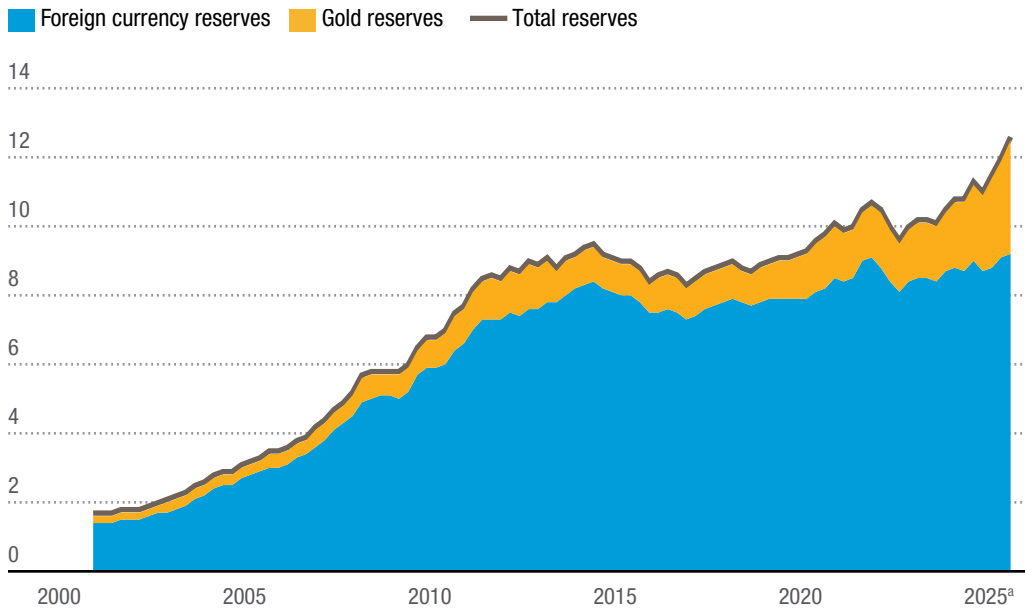




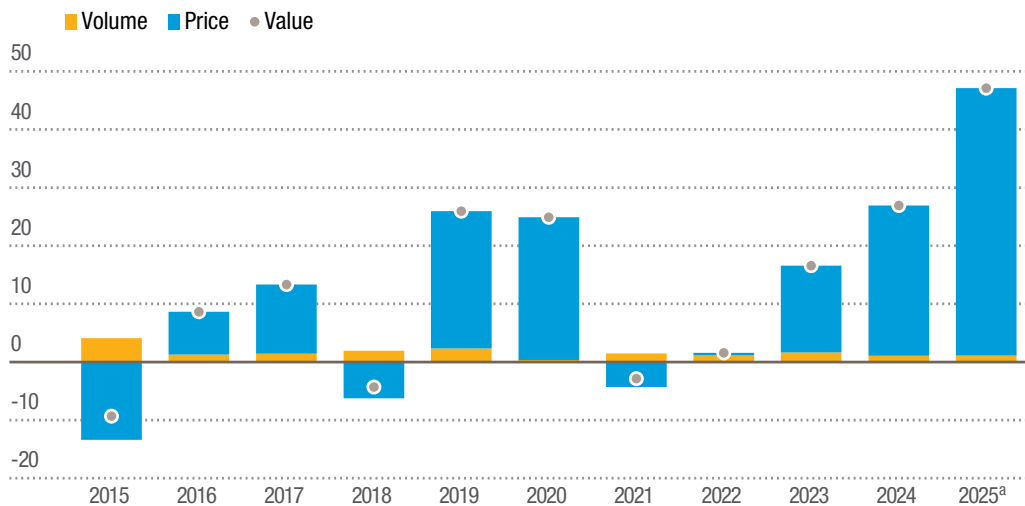
Figure I.8

Rising share of gold in central bank total reserves, as surging gold price drives up market value

A. Foreign currency and monetary gold reserves held by central banks globally
(Trillions of dollars)



B. Change in market value of central bank monetary gold reserves decomposed by volume and price effects
(Percentage)



Source: UNCTAD based on data from World Gold Council.

^a Corresponds to third quarter.



3. The benefits and drawbacks of dollar centrality

The dollar's dominant international status embeds a premium in United States assets that reduces borrowing costs.

The central role of the dollar in global trade and finance has long been viewed as affording a strategic advantage to the United States. The dollar's dominant international status embeds a premium in United States assets that reduces the country's borrowing costs – evidenced by the so-called “convenience yield” enjoyed by dollar-denominated bonds issued by the public or private sector (Jian et al., 2019). This suggests a higher return on

the country's external assets than on its external liabilities as well as a significant relaxation of its external constraints (Gourinchas and Rey, 2007 and 2022).

The higher return is reflected in the fact that despite its outsized and growing negative net international investment position – which corresponds to the gap between the stock of foreign assets owned by United States residents and the stock of assets within the United States owned by non-residents – the net returns from these assets and liabilities, shown by the primary account balance of the current account, have been mostly positive in recent years (figure I.9).



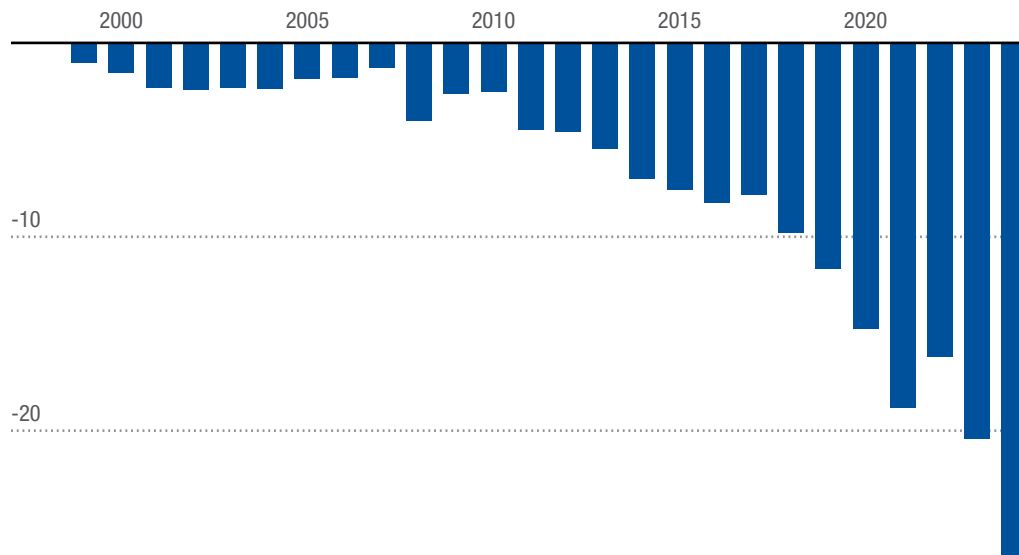


Figure I.9

Despite mounting net claims on United States assets held by non-residents, resulting income flows remain fairly balanced

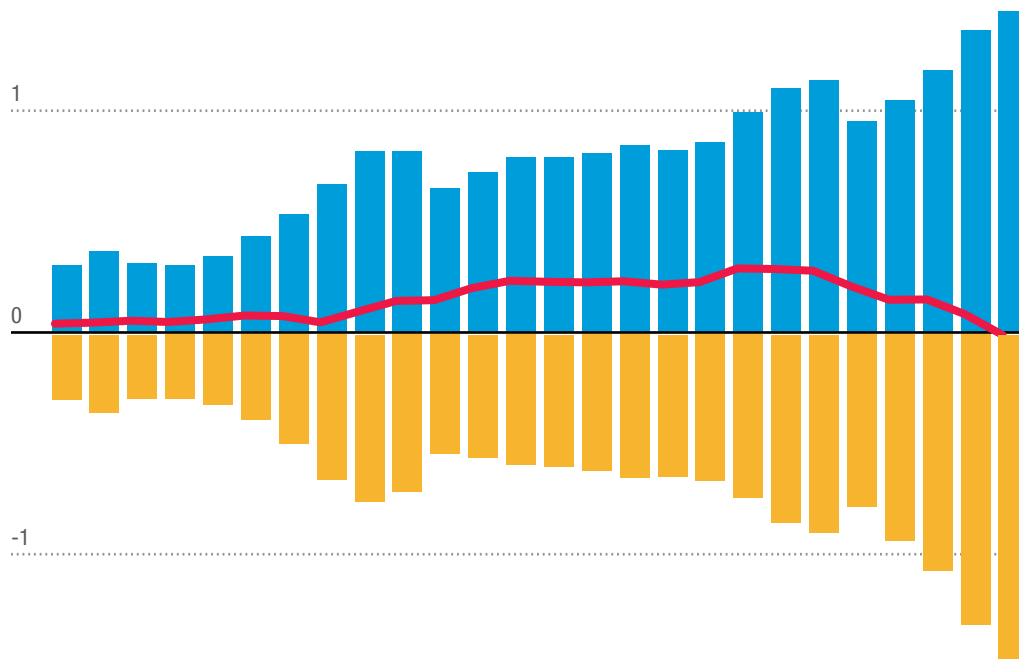
Net international investment position and primary income account of the balance of payments, United States, 1999–2024
(Trillions of dollars)

A. Net international investment position



B. Primary income account

■ Primary income receipts ■ Primary income payments — Primary income account balance



Source: UNCTAD based on data from United States Bureau of Economic Analysis.



An appreciation of the dollar puts upward pressure on the servicing costs of dollar-denominated external debts.

The recent trajectory of United States assets indicates weakening demand for them, precisely when the reverse would be the norm.

Given that the bulk of official dollar reserves are held in United States Treasuries (Bertaut et al., 2025), additional demand for these assets due to the dollar's reserve currency status has enabled Treasuries to command exceptionally lower yields than comparable instruments (Jian et al., 2019). This has reduced the funding costs of the United States Government by a significant margin. While estimates of this lower cost vary, recent research points to a differential of up to 120 basis points between the yields on "safe" AAA corporate bonds and Treasuries (Szoke et al., 2024).

The dollar's central role in international markets supports its historic safe-haven status. At times of economic or financial turmoil – even when it has originated within the United States economy, as in the global financial crisis of 2008 – financial capital tends to flow into the dollar and United States assets. International investors typically withdraw funds from riskier assets and channel them towards those perceived as safe, the so-called "flight to safety" (Baele et al., 2014). This tends to have a stabilizing effect on the United States economy and its financial markets at times of elevated volatility and shocks (Noeth and Sengupta, 2010).

The potential for high exposure to the dollar in global markets can, however, complicate international transactions in other sets of countries. This is particularly the case for developing countries, where governments and companies often use non-domestic currencies to conduct basic international transactions. These actors also must often borrow in foreign currencies, generally the dollar, even though they may have limited dollar revenues. This mismatch between the currencies of liabilities and income streams exposes governments and firms to unexpected exchange rate movements. An appreciation of the dollar puts upward pressure on the servicing costs

of dollar-denominated external debts, often bringing up liquidity and solvency issues that would otherwise not be a concern.

The dollar's central global status reverberates in policy decisions in the United States that tend to have an outsized impact on international monetary conditions (chapter II). Central banks in developing countries find themselves pressured to mimic or follow the Federal Reserve's policy stances, even when domestic macroeconomic fundamentals and trajectories may point to another monetary policy path (UNCTAD, 2024b).

4. Recent developments and the future of the global monetary system

Recent developments have introduced uncertainty around the potentially evolving role of the dollar in the international financial system. The announcement of "reciprocal tariffs" by the United States on 2 April was met by heightened volatility and distress in international financial markets. Such market turmoil invariably translates into a sharp increase in demand for safe-haven assets, which in turn typically leads to falling yields of United States Treasuries as well as an appreciation of the dollar (Gourinchas et al., 2019).

In stark contrast to historical norms, however, a very different trajectory emerged in 2025. The yield on Treasuries increased, widening the spread between them and the sovereign bonds of other major developed economies. The dollar suffered a sharp depreciation (figure I.10).⁶ These trajectories indicate softening demand for United States assets, precisely when the reverse would be the norm.

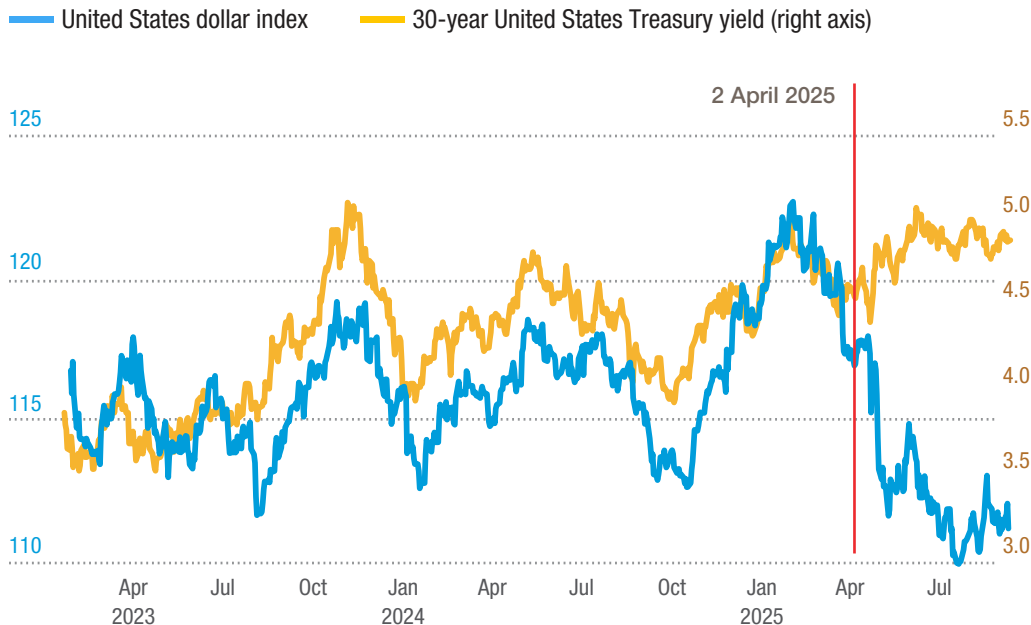
⁶ By the end of August 2025, the 30-year Treasury yield remained 40 basis points above its level at the beginning of April. The dollar's value against a basket of developing economy currencies depreciated 5 per cent in the same period.



Figure I.10

The distress in financial markets in April saw anomalous movements in safe-haven United States assets

Nominal advanced foreign economies dollar index and the market yield on 30-year United States Treasury securities
(Index January 2006 = 100, percentage)



Source: Federal Reserve Bank of St. Louis.

Note: The dollar index corresponds to a weighted average of the foreign exchange value of the dollar against a subset of broad index currencies of advanced foreign economies. Upward (downward) movement of the index indicates an appreciation (depreciation) of the dollar.

The synchronous weakening of Treasuries and the dollar would suggest a decline in the traditional safe-haven status of these assets. The recent trajectory of both has undermined their traditional hedging role in portfolio diversification. Under normal market conditions, the dollar and Treasuries exhibit a reliable negative correlation with equities, as financial capital would typically flow to them during economic stress or market downturns, causing them to appreciate as equities fall. This natural hedge has been a foundation of portfolio construction, allowing investors to mitigate risk. Yet since April 2025, the United States market experienced simultaneous declines across equities, bonds and the dollar.

It remains to be seen whether these anomalous movements correspond to cyclical factors or more significant long-term erosion in the perceived safety of

these assets. A continued and rising positive correlation among dollar assets would indicate that traditional diversification strategies within dollar-denominated portfolios are becoming less effective. It may also suggest an evolving role of the dollar in international markets.

Efforts to establish alternative arrangements for countries to reduce excessive exposure to the dollar could be increasingly important in shaping an evolving international monetary system (box I.1). Although still in early stages, such efforts could, if elaborated, pave the way towards a more diversified international monetary architecture. The institutional costs of such initiatives and required levels of policy coordination, however, are high, and risks of financial fragmentation cannot be overlooked (chapter IV).

It remains to be seen whether anomalous movements correspond to a long-term erosion in the perception of United States assets.



**Box I.1****Initiatives to diversify settlement options for international transactions gain prominence, yet institutional challenges loom large**

There are several initiatives underway that seek to provide more options for the settlement of international trade and financial transactions. The BRICS Plus^a countries have proactively advocated the greater use of national currencies in the invoicing and settlement of trade among member countries – in the context of growing intra-BRICS Plus trade (chapter IV) – thereby aiming to reduce reliance on a single currency.

For cross-border payment systems, the BRICS Plus group has proposed enhancing correspondent relationships among members' own banks to diminish dependence on other correspondent banking systems. Such an alternative would have to be supported by a messaging system akin to the SWIFT system but would be controlled by banks in BRICS Plus countries. The group has begun introducing cross-border payment infrastructure such as BRICS Pay and BRICS Bridge.^b For cross-border investments, it envisages a dedicated platform, BRICS Clear, that could serve as a central securities depository (BRICS, 2024).

In a similar vein, China has developed its own payment system, the Cross-Border Inter-Bank Payment System. It has also struck trading deals with other countries that enable their respective companies to settle trade in domestic currencies. China has extended loans and bilateral currency swap lines in renminbi to central banks in Argentina, Pakistan and other countries to provide an emergency lending function at times of financial distress. Subsequently, use of the renminbi in trade invoicing between China and recipient countries has significantly increased (Benguria and Novy, 2025).

African countries have advanced initiatives such as the Pan-African Payment and Settlement System to facilitate intra- and extraregional trade in local currencies, thereby overcoming issues around access to foreign currencies. Within the Southern African Customs Union, domestic currencies – particularly the South African rand – are increasingly prominent in cross-border trade and financial transactions.

Finally, countries are leveraging digital innovations to transform the mechanisms that underlie international transactions. Emerging technologies such as distributed ledger technology (DLT) and central bank digital currency (CBDC) may be critical going forward. DLT enables the secure and low-cost cross-border transfer of digital assets and payments. For example, the new BRICS Plus international payment systems use DLT for processing international payments, aiming at reducing the need for established international financial intermediaries.

There is potential for countries to share a CBDC, akin to a common currency in a monetary union, or to link the CBDCs of different countries on a single platform. Project mBridge is a collaboration among the central banks of China, Hong Kong Special Administrative Region, Saudi Arabia, Thailand and the United Arab Emirates to link CBDCs so that central and commercial banks of participating countries can carry out transactions with one another on the same platform. Once participating countries have agreed on governance and regulations, such platforms could provide a viable alternative for cross-border transactions (Eichengreen, 2025).

Note:

^a Originally Brazil, Russian Federation, India, China and South Africa; now expanded to include Egypt, Ethiopia, Indonesia, Iran, Saudi Arabia and the United Arab Emirates.

^b BRICS Pay facilitates transactions in domestic currencies and offers a viable alternative to the SWIFT system. BRICS Bridge is a settlement platform to deepen financial integration among BRICS Plus members.

Countries are leveraging digital innovations that could transform international transactions.



D. Global imbalances

1. Introduction

Global trade imbalances have been growing since 2020 and have become central to policy discourse in 2025. Internationally, the imbalances are driven by large economies, partly reflecting internal economic and financial structures, but are also related to long-standing misalignments between the global trade and financial systems (chapter IV). An additional set of factors contributing to imbalances in trade is the shift of the global economy toward a system where complex services, digital and intangible assets play an increasingly central role (WIPO, 2025).

This presents a challenge to many earlier assumptions and models of the global economy, and policy research is yet to address these issues comprehensively. More specifically, while the trade literature has evolved from classical theory of trade in goods to theories of intra-industry trade, and recently to trade in tasks, trade in intangibles has not been fully integrated into the theory of international trade and macroeconomic models. In part, this is due to the lack of a systemic framework, as well as difficulties in data collection (Fu and Ghauri, 2021).

Yet services trade, digital and intangible assets increasingly shape economic trajectories. In goods trade, among large economies, the United States continues to run the largest trade deficit, while China maintains the largest surplus. The European Union recorded a significant trade surplus in 2024. Major deficit countries include India, Japan, and the United Kingdom (figure I.11A).

The picture is partly inverted when services trade balances are considered. The European Union, the United Kingdom, the United States and other advanced economies dominate the large surplus nations. Altogether, developing economies account for less than 30 per cent of all service exports globally and thus are mainly service importers (figure I.11B). The multidimensional nature of global trade and financial imbalances underscores the need for coordinated international policy measures at the multilateral level to address the deepening misalignments.

Services trade, digital and intangible assets increasingly shape economic trajectories.



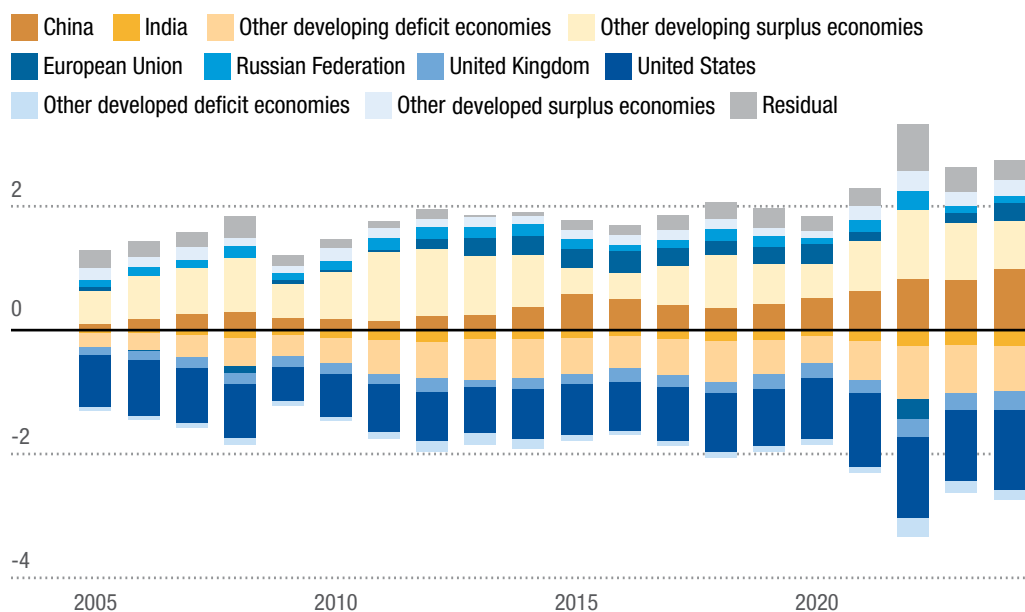


Figure I.11

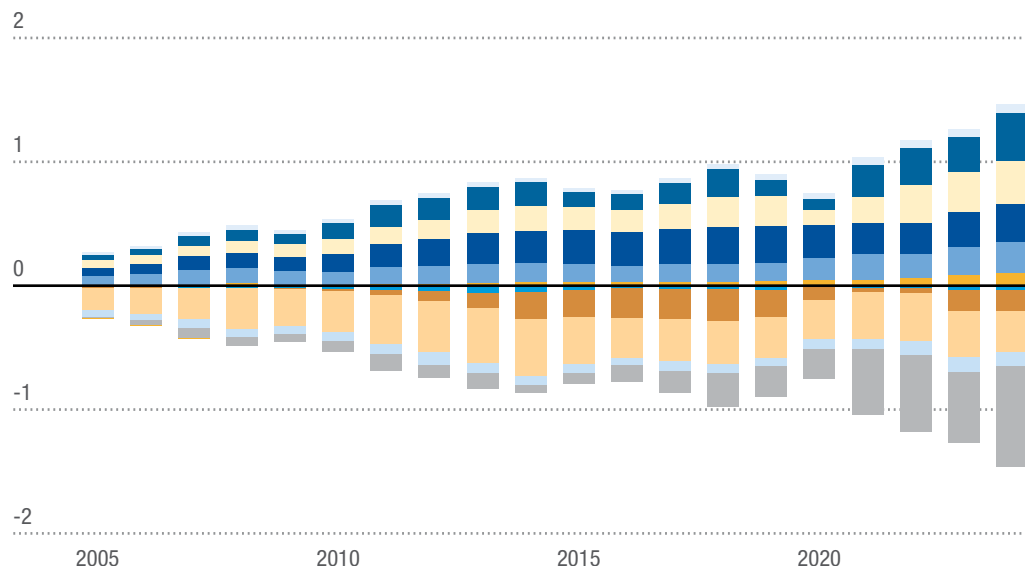
Global trade imbalances have widened in recent years

Nominal contributions to trade balances
(Trillions of dollars)

A. Merchandise goods



B. Services



Source: UNCTAD based on UNCTADstat.

Note: Residuals reflect challenges in compiling international statistics, including data availability constraints; conceptual and methodological differences; asymmetries between partner countries; reporting time lags; mode of supply estimation; exchange rate and valuation issues; timing and accrual adjustments.

External imbalances are partly driven by internal ones—since external deficits and surpluses mirror gaps between saving and investment rates (UNCTAD, 2025a). Examining how trade policy

shifts and other developments influence domestic saving and investment can provide insights into the overall effects on countries' external balances (box I.2).



Box I.2 External imbalances: a macroeconomic view

National income accounting identities show that the current account balance^a not only equals the difference between receipts and payments of international transactions, but also the difference between domestic saving and investment (Blecker, 2025; Krugman, 1991). Put differently, a current account deficit or surplus does not simply represent an imbalance in external accounts. It also reflects internal imbalances that occur when the domestic investment rate persistently exceeds or falls short of the combined rate of domestic saving by the private and public sectors (see annex I.1 for a detailed explanation).

In countries that operate a current account deficit, the gap between domestic saving and investment is bridged by foreign investment that translates into a surplus in the financial account, which is the flip side of the deficit in the current account (leaving aside the capital account, which relates to capital transfers, e.g., debt forgiveness, and non-produced, non-financial assets, e.g., intellectual property rights). Since net exports and net capital outflows must balance each other, negative net exports (a current account deficit, roughly speaking) are matched by positive net capital inflows. Conversely, in economies that run a current account surplus, the mismatch between internal saving and investment typically translates into financial outflows to the rest of the world that exceed inflows, generating a deficit in the financial account which is the counterpart of the current account surplus.

As an example, the higher investment rate relative to saving in the United States is mirrored by a negative current account balance. In contrast, in Germany, high saving together with declining investment in recent years have been reflected in a widening positive current account balance.

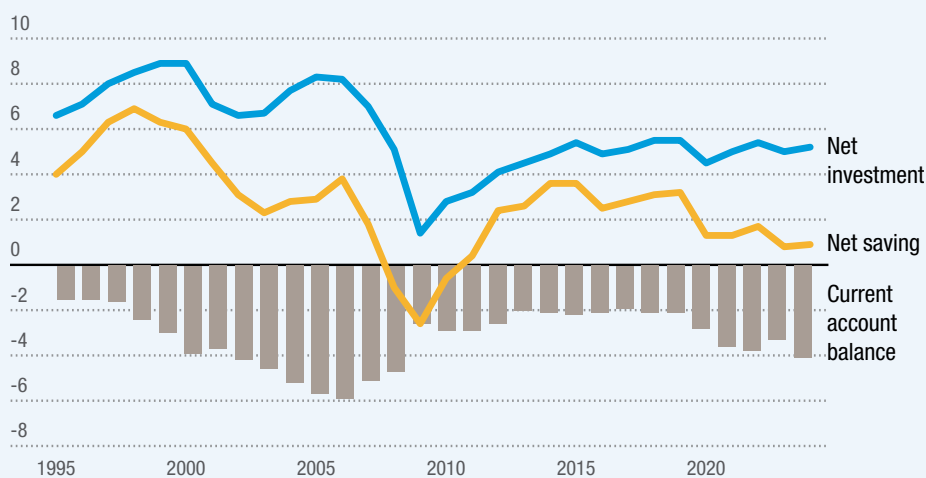
Foreign investments bridge the gap between domestic saving and investment, translating into a surplus in the financial account.

Current account imbalances mirror gaps between domestic saving and investment

Net saving, net investment and current account balance

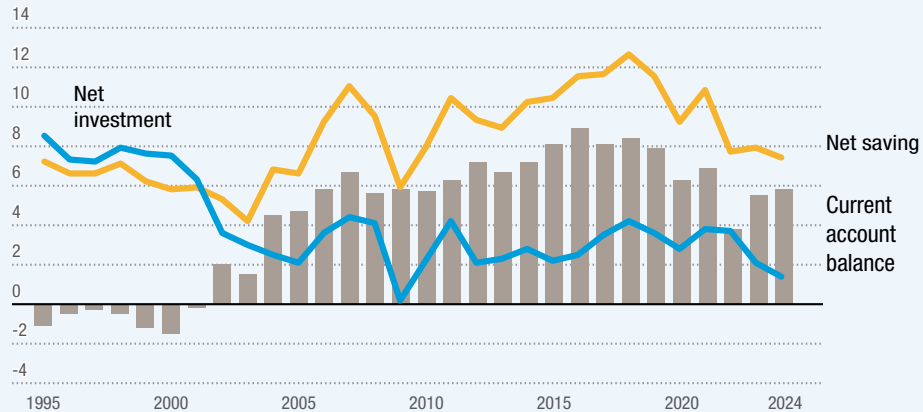
(Percentage of GDP)

A. United States



B. Germany

Current account balance



Source: UNCTAD based on data from the United States Bureau of Economic Analysis and German Statistical Office.

Notes: Net saving is a measure of the saving available for adding to the nation's net stock of fixed assets or for lending to the rest of the world. It equals the sum of personal saving, undistributed corporate profits with inventory valuation and capital consumption adjustments, and net government saving. Net investment corresponds to new capital spending that adds to a country's capital stock, discounting depreciation of existing capital stocks.

Domestic macroeconomic trajectories can therefore be key in assessing countries' external balances. A range of factors – including domestic private demand conditions, fiscal stances, productivity paths, exchange rates, trade policy measures, among others – impact both directly and indirectly saving and investment outcomes that, in turn, underpin the trajectory of external accounts.

Addressing external imbalances

Trade policies such as tariffs are often used to address external imbalances by boosting domestic production and closing gaps between exports and imports. But the overall impact on external balances is ambiguous: literature suggests that tariffs tend to have limited effect on trade deficits, as reduced imports are often offset by reduced exports, with resources diverted from export sectors to meet domestic demand — especially when the economy's full employment is assumed (Furceri et al., 2022; Costinot and Werning, 2025; Baldwin, 2024; UNCTAD, 2025a).

Further, since production processes increasingly involve cross-border supply chains, tariffs can raise the costs of imported inputs for export-oriented manufacturing. In this way, tariffs can effectively act as a tax on exports and imports, leading to net effects on overall external accounts that are uncertain. Tariff imposition is also typically associated with offsetting real exchange rate appreciations (Furceri et al., 2022). This is because reduced demand for imports lowers the supply of a currency to the rest of the world, which in turn pushes up its value vis-à-vis other currencies. The resulting appreciation partially offsets the increased cost of imports due to tariffs. It can also have a detrimental impact on competitiveness, which would dampen exports. However, contrary to assumptions, the dollar registered a notable depreciation between February and June 2025. As outlined previously, this trend responds to distinctive factors that have emerged this year.

The overall impact of tariff measures on aggregate external imbalances can be limited.

In evaluating the potential impact of policy shifts and other relevant developments on external balances, it can be useful to assess the dynamic effects of these changes on saving and investment rates, thereby revealing the final aggregate effects on current account balances. In economies with large and persistent current account deficits, trade policy measures, such as tariffs, can effectively reduce external imbalances through a reduction in investment, primarily by raising costs linked to imported capital goods. However, the positive outcome is accompanied by a negative impact on the wider economy. For their part, tariff receipts are also likely to increase public savings, but this tends to be compensated by concomitant decreases in private savings, often negating the aggregate impact (IMF, 2025b).

Rather, by impacting factors that lie behind domestic imbalances, policy actions can effectively bring about rebalancing in external accounts. Those economies that exhibit external deficits can look to bolster saving. In instances where external deficits are driven by excess dissaving in the public sector, for example, a reorientation of fiscal trajectories towards enhanced domestic public revenue generation can help balance external and internal disparities.

In surplus economies, policy measures that boost domestic demand and limit excess saving – such as more expansive fiscal stances, strengthening of social safety nets, and more active labour market policies that boost labour income and consumption (UNCTAD, 2017, 2019) – can serve to bring external accounts towards balance, as well as leading to positive outcomes in terms of income inequality (UNCTAD, 2024a). Similarly, domestic policies and regulations, particularly regarding the financial sector, can impact saving and investment decisions through their influence on both the conditions and allocation of credit.

Additionally, policymakers can explore alternative avenues to complement more traditional manufacturing-led development models. In the context of already subdued merchandise trade and rapid digital advances, opportunities to generate quality employment in the services sectors, including in non-tradable services, can offer viable development paths that are not as dependent on external demand (UNCTAD, 2024b; Rodrik and Sandhu, 2024; Rodrik and Stiglitz, 2024).

^a The current account comprises the external balances of a country's trade in goods, trade in services, primary income and secondary income.

2. Rebalancing is most effective when achieved through coordinated international actions

Collective and coordinated international actions among countries operating excessively positive and negative external balances can greatly facilitate addressing such imbalances globally. In contrast, the reliance on isolated trade measures to address external imbalances can face limitations in achieving objectives, while potentially risking significant adverse domestic and international economic fallout.

A nuanced approach combining national and coordinated international actions

would be most effective in addressing external imbalances, while limiting negative fallout from macroeconomic adjustments, domestically and globally. Internationally, corrective action demands a multilateral policy response focused on a more coordinated approach to global economic governance (Rodrik, 2025).

A more cooperative approach to policy challenges – for trade, industrial policies and taxation, among others – could minimize potential negative spillover effects and avoid adverse impacts on the most vulnerable economies. Similarly, regional integration initiatives need to incorporate integrated policy mechanisms, spanning trade, financial and macroeconomic priorities.

A nuanced approach combining national and coordinated international actions would be most effective in addressing external imbalances.



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Annex I.1

National accounting identities illustrate the macroeconomic determinants of movements in the current account balance. Starting with the definition of gross national product in period t (GNP_t) as the sum of gross domestic product (Y_t) and net income from abroad, represented by the ex-post return (r_t) on the stock of net foreign assets (B_t):

$$GNP_t = Y_t + r_t B_t$$

A negative value for B_t indicates that the value of outstanding foreign assets owned by domestic residents is less than the value of outstanding domestic assets owned by non-residents.

For its part, equilibrium conditions require that GDP equal the demand for private consumption (C), government spending (G), investment (I) and net demand from abroad (NX), such that:

$$Y_t = C_t + G_t + I_t + NX_t$$

NX is equivalent to the excess of exports over imports, also known as the trade balance.

From these two identities, it follows that the current account (CA), which is conventionally defined as the sum of the trade balance and net income from abroad, can be rewritten as the excess of GNP over the sum of private consumption, government spending and investment, such that:

$$CA_t = NX_t + r_t B_t = GNP_t - (C_t + G_t + I_t)$$

Additionally, by subtracting private consumption (C) and government spending (G) from GNP, we get the total of private and government savings, otherwise known as national savings (S):

$$S_t = GNP_t - (C_t + G_t)$$

As a result, the current account (CA) is also equal to the difference between national savings (S) and investment (I):

$$CA_t = S_t - I_t$$

Defining the current account as the difference between domestic savings and investment helps to explain observed patterns in international capital flows. Savings at time t are equivalent to the change in wealth from the beginning to the end of period t . Since a country's wealth at the beginning of period t is given by the sum of its stock of capital (K_t) and its net assets from abroad B_t , the preceding identity can be rewritten as:

$$CA_t = (B_{t+1} + K_{t+1} - B_t - K_t) - I_t$$

Making use of the capital accumulation equation $K_{t+1} - K_t = I_t$, such that:

$$CA_t = B_{t+1} - B_t$$

This final identity demonstrates that the current account over a period of time t is the change in the value of net assets relative to the rest of the world. A net inflow is registered when the increase in domestic assets held by non-residents exceeds the increase in foreign assets held by domestic residents. This essentially means that if domestic savings are insufficient to finance domestic investment, the excess of investment over savings is financed by savings from abroad. As such, the counterpart of a current account deficit is a financial account surplus, i.e., a net inflow of capital. This outcome increases a country's net borrowing position relative to the rest of the world. On the other hand, if domestic savings are larger than domestic investment, the excess savings will finance investment abroad. The current account surplus will therefore result in a net outflow of capital, which will increase the country's net lending position relative to the rest of the world.

