



2026 Trade and development report

Chapter II

Selective fragmentation: The new geography of trade

KEY FINDINGS

- ▶ Global trade remains resilient, but its geography is being selectively reorganized. Bilateral trade relationships and production corridors are shifting without a generalized retreat from global integration.
- ▶ Market access is becoming more differentiated and policy dependent. Trading-partner- and sector-specific requirements increasingly shape participation, particularly in technologically advanced and strategically sensitive sectors where geoeconomic factors matter most.
- ▶ Developing countries will be affected unevenly by trade reconfiguration. Some may emerge as alternative suppliers or intermediary hubs, but realizing and sustaining these gains will require stronger productive, regulatory and institutional capabilities.



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Policy takeaways

- ▶ **Coordinate trade policies to prevent fragmentation from deepening trade asymmetries.** Governments are increasingly using trade policy to pursue supply-chain resilience, industrial competitiveness, energy transition, technological leadership and national security. Sought through unilateral, discriminatory or weakly coordinated instruments, these objectives can weaken trade predictability, raise trade costs and reinforce existing asymmetries, especially for smaller exporters and least developed countries.
- ▶ **Assess emerging trade opportunities in light of geoeconomic shifts and factors shaping supply-chain resilience.** Trade reconfiguration may create new entry points for some developing economies as alternative suppliers, production locations or connector economies. Trade opportunities will depend not only on conventional productive capacities, however, but also on geoeconomic positioning, perceived reliability, policy stability and exposure to trade restrictions. These factors are especially important in strategic and technologically advanced sectors.
- ▶ **Preserve development safeguards in multilateral trade cooperation.** The World Trade Organization (WTO) remains essential for transparency, predictability, non-discrimination and baseline disciplines. But its role should adapt to emerging trade policy areas such as industrial policy, economic security, climate measures and digital regulation. Preserving non-discrimination and special and differential treatment, while strengthening capacity-building and the participation of developing countries in rule-shaping, is essential to making policy space and market access mutually reinforcing.
- ▶ **Strengthen regional and South–South cooperation as a complement to multilateral rules.** Where WTO-wide agreement remains difficult, developing countries should use open, development-oriented regional and South–South arrangements to improve market access, simplify rules of origin, improve trade facilitation and strengthen their collective bargaining power. These arrangements should remain transparent and interoperable so that they support, rather than deepen, fragmentation.
- ▶ **Strengthen capabilities to meet increasingly complex market access conditions.** Developing countries need targeted support for standards infrastructure, certification, traceability, digital customs systems and regulatory compliance. Without such capabilities, firms may be excluded from trade opportunities not because they lack competitiveness in price or quality, but because they cannot effectively comply with environmental, labour, security or origin requirements.

A. Introduction

This chapter examines the forces, policy instruments and trade implications associated with the shift in the global trading system from a broad-based model of multilateral integration towards a more selective, fragmented and politically conditioned form of trade governance.

Cross-border exchange requires shared expectations about how governments will treat internationally traded goods and services. International trade depends on rules that define market access, limit discrimination, clarify procedures, discipline subsidies and provide mechanisms for resolving disputes. Without commonly agreed rules, trade is vulnerable to abrupt policy changes, political pressure and power asymmetries. The multilateral trading system of the 1990s and 2000s broadly reflected this logic, providing a relatively stable framework for deeper economic integration, the expansion of global value chains and the growth of international trade. Yet even during this period of heightened multilateral cooperation, important development concerns remained unresolved. Many developing countries continued to face structural barriers to market access, limited productive capacities and persistent difficulties in capturing greater value from global trade (UNCTAD, 2018).

Geoeconomic competition increasingly shifts trade policy priorities toward technology, energy transition, critical inputs and advanced manufacturing

Over the past decade, deeper structural changes in trade policymaking have compounded the limitations of this earlier model of integration. Geoeconomic competition has intensified the use of trade policy for strategic purposes, especially in sectors linked to technology, the energy transition, critical inputs and advanced manufacturing. At the same time, governments are increasingly deploying trade-related measures to support industrial transformation, strengthen resilience and pursue regulatory objectives. Together, these dynamics have made it more difficult for multilateral trade rules to absorb policy tensions, sustain coordination and support convergence around shared disciplines.

These shifts reflect tensions created by the success of earlier phases of globalization. Lower trade costs, technological change and rules-based integration enabled deeper specialization, expanded global value chains and generated substantial efficiency gains. Yet they also increased concentration in some production networks and created new forms of dependence on a limited number of suppliers, technologies, inputs and markets. Today, interdependence is increasingly viewed as a source of strategic exposure, although it can still foster significant efficiency gains.



This changing perception has strengthened support for diversification, industrial policy and supply chain security, while making it harder for the multilateral trading system to manage tensions, update rules and maintain consensus. Policy discretion now plays a larger role in determining market access, investment and participation in global value chains. Looking ahead, the forces driving trade policy fragmentation are likely to remain a defining feature of the global trading system.

The key challenge is to prevent trade fragmentation from undermining growth, structural transformation and sustainable

development. This requires adapting multilateral cooperation to more diverse national priorities while preserving core principles such as non-discrimination, transparency, predictability, rules-based discipline and special treatment for developing countries. More flexible, development-oriented cooperation is also needed to address specific policy challenges and avoid a situation where greater policy discretion deepens fragmentation or exclusion. Developing countries should be able to participate effectively in drafting the rules, regulations and institutions that will affect their future trade and development.

Developing countries must be able to participate in drafting the rules affecting their future trade and development

B. Trade policy fragmentation: Causes and dynamics

Since the creation of the post-1945 economic order, multilateral trade governance has rested on non-discrimination, reciprocity and rules-based cooperation. These rules help limit protectionism and policies that shift domestic costs onto trading partners (Bagwell and Staiger, 1999 and 2002). The most-favoured nation principle reduces discrimination and the risk of competing trade blocs, while common disciplines improve regulatory compatibility and

lower transaction costs (Hoekman and Kostecki, 2009). For smaller economies, multilateralism also reduces power asymmetries by providing legal predictability, dispute settlement mechanisms and access to concessions negotiated by larger economies (Jackson, 1997). Together, these features supported the integration of developing countries, the expansion of global value chains and rapid trade growth from the 1990s to the early 2010s.



Increasingly, governments view trade policy as an instrument for achieving broader strategic objectives

Market access depends on competitiveness and firms' ability to navigate trade policies and regulatory divergence

Over the past decade, global trade and trade policymaking have undergone a marked structural transformation. Escalating geopolitical tensions, concerns over economic resilience, renewed industrial policy activism and the proliferation of regulations linked to environmental objectives, technological competition, labour standards and national security have altered the policy environment (Baldwin, 2022; Evenett and Fritz, 2024). Increasingly, governments view trade policy not merely as a mechanism for promoting efficiency and securing market access but as an instrument for achieving broader strategic objectives, including technological leadership, supply chain security, climate transition and economic resilience (WTO, 2023).

For developing countries, the key question is whether this transformation will make participation in international trade more conditional and uneven. Market access increasingly depends not only on price, productivity and production capacity but also on firms' ability to navigate trade policy changes and diverging regulatory requirements. These changes may create opportunities to attract investment, diversify exports and become alternative suppliers in reconfigured value chains. They may also raise entry costs and uncertainty for countries and firms with limited institutional, productive or compliance capacity, reinforcing unequal access to trade opportunities. Fragmentation reflects the interaction of several mutually reinforcing drivers, summarized in table II.1 and examined below.



 **Table II.1**
Drivers of trade policy fragmentation

Driver	Core mechanism	Main policy manifestations	Contribution to fragmentation
Political economy and geoeconomic changes	Trade policy reflects domestic political incentives, organized interests and geoeconomic competition rather than aggregate welfare alone. International competition can intensify lobbying by allowing sectoral interests to be framed as national competitiveness, resilience or security concerns.	Sectoral protection, subsidies, export controls, investment screening, national security restrictions, strategic trade measures.	Shifts trade policy away from universal market access towards country-specific, sector-specific and security-oriented interventions. This increases discrimination among trading partners and encourages reciprocal policy responses.
Domestic incentives for industrial support	Governments increasingly use trade and industrial policy to secure resilience, employment, technological leadership and future comparative advantage.	Local content requirements, procurement preferences, green subsidies, semiconductor support, critical minerals strategies, strategic sector investment incentives.	Makes trade policy increasingly subordinate to national industrial strategies. As governments target similar strategic sectors, subsidy races, retaliatory measures and regulatory divergence become more likely.
Global value chains, rebalancing efficiency and risk	Firms reassess efficiency-oriented globalization in response to supply chain disruptions, policy uncertainty, automation and changing production technologies.	Geoeconomic supply diversification, regionalization, automation-enabled relocation, artificial intelligence-enabled supply chain management.	Weakens globally integrated production networks organized largely around cost differentials. Integration becomes more selective and conditional, depending increasingly on perceived geoeconomic risk, regulatory compatibility, security relationships and policy stability.
Use of trade policy for non-trade objectives	Governments increasingly use trade policy to advance socioeconomic and public policy objectives, including climate, labour, human rights, sustainability and corporate accountability goals.	Carbon border measures; supply chain due diligence laws; labour-related restrictions; sustainability standards; labour provisions; environment, social and governance-linked market access conditions.	Creates differentiated regulatory conditions for market access. Countries vary in standards, enforcement capacity and definitions of acceptable production practices, increasing compliance costs and regulatory divergence.
Weakening multilateralism and reduced constraints on intervention	The multilateral system is not only affected by the above drivers; its weakening also reduces the constraints that previously limited unilateral or discriminatory action.	WTO rule-making stagnation, weakened dispute settlement, greater reliance on unilateral measures, preferential agreements, plurilateral initiatives.	Functions as an enabling condition for fragmentation. As common rules become less able to absorb policy tensions and sustain convergence, governments have greater space to act outside shared disciplines, making fragmentation self-reinforcing.

Source: UNCTAD.

1. Political economy and geoeconomic changes

Political economy and geoeconomic changes are intertwined sources of trade policy fragmentation. At the domestic level, trade policy is shaped by interest groups, distributional pressures, domestic priorities and political demands for greater control over economic outcomes. At the international level, these pressures are increasingly reinforced by strategic competition among major economies. Three interrelated factors are particularly important: political dynamics, the erosion of the political consensus supporting globalization, and growing links between trade policy and security concerns in strategic sectors.

a) Political dynamics

The political economy literature has long emphasized that trade policy outcomes reflect domestic political incentives rather than purely aggregate welfare considerations (Grossman and Helpman, 1994). Contemporary international competition can intensify this dynamic. Claims of unfair foreign support may provide domestic firms with a justification for mobilizing political support, allowing sectoral interests to be framed as national competitiveness or strategic resilience concerns. Once governments respond with supportive measures or trade restrictions, trading partners may adopt similar measures, creating a self-reinforcing cycle of domestic advocacy for policy intervention, contributing to greater policy fragmentation.

b) The erosion of the political consensus supporting globalization

Many current tensions reflect the failure of earlier globalization frameworks to integrate social, environmental and distributional concerns into trade governance, treating them instead as issues for later domestic policy action (Rodrik, 2024). Deep integration can also constrain national

sovereignty and democratic choice, particularly when international commitments limit regulation, redistribution or social protection. Moreover, as globalization has produced uneven and persistent outcomes across workers, sectors and regions, public support for trade liberalization has weakened in many instances (UNCTAD, 2019). The revival of industrial policy, reshoring and trade restrictions can therefore be seen as an effort to restore policy autonomy in response to discontent with inequality, deindustrialization, job insecurity and strategic dependence (UNCTAD, 2024b).

c) Geoeconomic competition and strategic sectors

These domestic political dynamics are reinforced by geoeconomic competition. Trade policy is increasingly intertwined with strategic industrial considerations, especially in sectors such as semiconductors, critical minerals, energy technologies, telecommunications infrastructure and advanced manufacturing. Governments now frequently justify export controls, investment screening, subsidies and trade restrictions on national security or resilience grounds (UNCTAD, 2026a). This securitization of economic policy expands the scope of industrial policy interventions and shifts trade policy away from universal market access towards country-specific, sector-specific and security-oriented measures, thereby contributing to fragmentation (UNCTAD, 2025a).

2. Domestic incentives for industrial policy intervention

The second driver of trade policy fragmentation is the renewed centrality of government intervention in support of productive activity (Evenett et al., 2024). From a development perspective, the return of industrial policy should not be understood only as a departure from market-oriented trade governance. Industrial policy has

The revival of industrial policy, reshoring and trade restrictions can be seen as an effort to restore policy autonomy in response to discontent



long been central to debates on structural transformation, productive capacity-building, technological upgrading and economic diversification (chapter III). Historically, one of its main justifications was the infant industry argument: temporary support could help emerging sectors develop capacities, achieve scale, absorb learning costs and become internationally competitive. In this sense, industrial policy remains an important instrument for countries seeking to move into higher-productivity activities and strengthen domestic linkages.

In the current context, however, the rationale for industrial policy has broadened. Modern industrial policy increasingly seeks to shape future comparative advantage by supporting innovation, technological upgrading and strategic production capacities, including by addressing market failures, coordination problems, learning spillovers and the requirements of structural transformation (Juhasz et al., 2024). Financial crises, the pandemic and geopolitical factors have further expanded its role: industrial policy is now used not only to promote development but also, through trade policy instruments, to reduce strategic dependencies, strengthen supply chain resilience, and safeguard access to critical goods and technologies.

The renewed use of industrial policy has important implications for trade governance. Developed and emerging developing economies can often draw on larger fiscal resources, deeper capital markets, stronger technological capabilities and greater institutional capacity to support strategic sectors. Many developing countries face tighter financing constraints and more limited capacity to design, implement and monitor comparable measures. As a result, formally available policy space may not translate into an equal ability to pursue industrial transformation. Large-scale support in major economies can redirect investment, alter competitive conditions and narrow the development options available elsewhere. This asymmetry reinforces the need for common, development-sensitive trade disciplines that preserve industrial policy

flexibility while limiting measures that impose disproportionate costs on trading partners.

3. Global value chains: Rebalancing efficiency and risk

The third driver of trade fragmentation concerns global value chain participation. Increasingly, this is determined by a broader set of considerations than cost efficiency alone. Firms and governments now place greater weight on supply chain resilience, regulatory compliance, security relationships and geoeconomic compatibility when deciding where to source, invest in and locate production.

The expansion of global value chains during the late twentieth and early twenty-first centuries was enabled by declining trade costs, advances in information and communication technologies, and firm strategies focused on efficiency and cost minimization (Baldwin, 2016). In the current geoeconomic context, firms are reassessing their exposure to supply chain risks and seeking greater resilience, encouraging supplier diversification, regionalization and enhanced reliance on jurisdictions perceived as less vulnerable to abrupt policy shifts (Crowe and Rawdanowicz, 2023).

Technological change is reinforcing this shift: automation, artificial intelligence and digital technologies reduce the importance of labour cost differences in offshoring decisions (Artuc et al., 2018). Resilience and policy risk management make regulatory compatibility, security ties and predictable rules more important in sourcing and investment decisions.

4. Use of trade policy for non-trade objectives

The fourth driver of trade policy fragmentation is the growing use of trade policy to pursue socioeconomic and domestic policy objectives. Earlier liberalization largely treated environmental

Financial crises, pandemics and geopolitical tensions have made economic security a central objective of industrial policy alongside development

Supply chain resilience concerns encourage diversification, regionalization and reliance on jurisdictions perceived as safer



Governments have increasingly responded to the social and environmental costs of globalization through trade policy

protection, labour standards, inequality and corporate accountability as separate domestic concerns. As the social and environmental costs of globalization have become more visible, governments have increasingly incorporated these issues into trade policy. Evidence of concentrated labour market losses has strengthened demands for rules that address inequality, employment security and social protection (Autor et al., 2013). Climate and accountability concerns have increased support for environmental standards and responsible business conduct (UNCTAD, 2024a).

Issues advancing faster than multilateral rule-making have pushed governments towards unilateral measures, preferential agreements and plurilateral initiatives

These measures may help sustain domestic support for open trade by addressing concerns previously treated as external to the trading system. Rather than simply representing protectionist departures from liberalization, they may reflect efforts to align trade with domestic social contracts, climate commitments, and expectations of fairness and accountability (Rodrik, 2025). As these objectives are pursued through differing national and regional rules, however, trade becomes less centred on uniform liberalization and more shaped by regulatory compatibility, social conditionality and contested public policy goals, thereby contributing to fragmentation.

5. Weakening multilateralism and reduced constraints on intervention

The weakening of the multilateral trading system is both a driver and consequence of trade policy fragmentation. Geopolitical factors, industrial policy, global value chain restructuring and new socioeconomic objectives are placing growing strain on existing rules. Although WTO continues to provide core principles, transparency, monitoring and baseline legal disciplines, its capacity to update rules, build consensus and manage emerging tensions has weakened. Issues such as industrial subsidies, climate measures, digital trade, supply chain security and national security restrictions have advanced faster than multilateral rule-making, pushing governments towards unilateral measures, preferential agreements and plurilateral initiatives.

This dynamic makes fragmentation self-reinforcing. Weaker reliance on common rules reduces constraints on discriminatory action, while such action further erodes multilateral cooperation (Hoekman and Sabel, 2021). The multilateral system is therefore best understood not as an independent source of fragmentation but as a constraint on fragmentation, one whose effectiveness has weakened over time.

C. Trade policy instruments behind fragmentation

Recent evidence suggests a structural intensification of trade policy activity. The Trade Policy Activity Index points to an increase since 2017, indicating a wider use of trade policy instruments and stronger interconnections among them (figure II.1).

WTO trade monitoring also shows a sharp increase in the value of trade affected by new trade and trade-related measures in 2024–2025, including measures justified on national and economic security grounds.

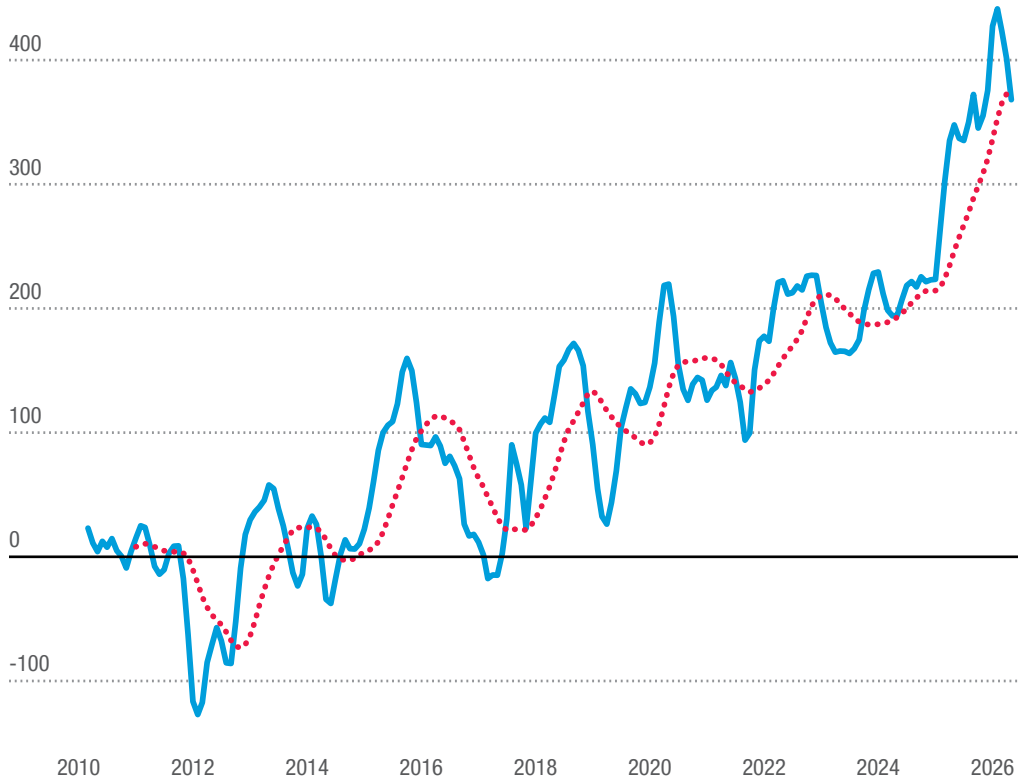




Figure II.1

Trade policy activity has increased over the last decade

Trade Policy Activity Index
(Average in 2010–2011=0)



Source: Centorrino et al. (2025).

Note: The dotted line represents the 12-month moving average. The Trade Policy Activity Index summarizes the common intensity of global trade policy changes, including facilitating measures and restrictive or potentially distortive measures such as tariffs, import and export restrictions, trade remedies, customs reforms, local content requirements, export controls and subsidies. The index is normalized so that average activity in 2010–2011 equals zero; positive (negative) values indicate activity above (below) that reference level. Values are expressed in index points and should not be interpreted as percentage changes.

This expansion reflects a broader change in the purpose of trade policy. It is no longer used primarily to protect domestic producers from foreign competition but increasingly to pursue industrial competitiveness, geoeconomic positioning, supply chain resilience, climate objectives, technological leadership and national security. Fragmentation therefore concerns not only whether measures restrict imports but also how they shape firms'

ability to trade, source inputs, invest, qualify for support and access markets. Traditional market access measures remain important but are increasingly embedded in broader policy packages combining industrial support, regulatory requirements, security controls, environmental conditions and preferential rules. Table II.2 summarizes the main instruments that operationalize fragmentation.

Traditional market access measures remain important but are increasingly embedded in broader policy packages



Table II.2
Trade policy instruments and channels of fragmentation

Instrument group	Main policy forms	Fragmentation channel	Operational and structural challenges
Market access instruments	Tariffs, tariff quotas, trade remedies and partner-specific duties.	Differentiate access by product or partner and redirect sourcing.	Input costs, tariff classification, diversion and retaliation risk.
Regulatory and compliance instruments	Regulations, TBT/SPS measures and conformity assessment.	Create market-specific entry conditions, often behind the border.	Documentation, testing, certification and compliance costs.
Preferential access and origin rules	Rules of origin, regional value content thresholds and tariff shift rules.	Encourage intra-bloc sourcing and supply chain governance.	Origin documentation, supplier tracing and exclusion risk.
Government support and production location instruments	Subsidies, tax credits, procurement preferences, local content requirements and reshoring incentives.	Condition support or market opportunities on production location or sourcing.	Eligibility rules, reporting burdens, relocation pressures and fiscal asymmetries.
Security, technology and strategic control instruments	Export controls, investment screening, procurement exclusions and cybersecurity requirements.	Separate markets by geoeconomic compatibility and strategic sensitivity.	Licensing, end-use checks, legal risk and policy uncertainty.
Institutional and regulatory architecture	Deep regional trade agreements, plurilateral initiatives, WTO+ and WTO-X provisions, digital rules and regulatory cooperation.	Create differentiated rule systems for members and outsiders.	Multiple regimes, regulatory divergence and rule-taker costs.
Socioenvironmental conditionality	Carbon measures, due diligence laws, labour-related restrictions, deforestation rules and green procurement.	Condition market access on production methods and certification capabilities.	Carbon data, audits, geolocation evidence and capacity constraints.

Source: UNCTAD.

Note: SPS: sanitary and phytosanitary; TBT: technical barriers to trade. WTO+ provisions concern areas subject to some form of commitment in WTO agreements. They reconfirm existing commitments and include additional obligations. WTO-X provisions cover areas outside the current mandate of WTO.

The key challenge of trade policy is to design measures safeguarding resilience, sustainability and security while minimizing uncertainty and exclusion

The growing use of overlapping trade policy instruments is making trade integration increasingly complex, including in services (box II.1). Firms must not only compete efficiently but also comply with rules of origin, environmental and labour standards, local content requirements, cybersecurity rules, and other regulations. These overlapping and evolving requirements raise participation costs. They may favour larger firms and countries with stronger institutions, and reduce certainty around future market

access (UNCTAD, 2026b). Moreover, the risk of abrupt policy changes raises the risk premium associated with trade, increasing operating costs and weakening the competitiveness of smaller and less diversified firms and economies (United Nations, 2026). The central challenge is therefore to design measures to pursue resilience, sustainability and security in ways that minimize unnecessary uncertainty and avoid making trade more exclusionary.



Box II.1

Trade in services: The risk of policy fragmentation

Services trade provides an important development opportunity for developing countries. It can support diversification by expanding direct services exports, increasing the services content embodied in manufactured goods and agricultural exports, and helping firms move into higher-value segments of value chains. Realizing these gains, however, depends not only on market access but also on regulatory conditions that allow services suppliers to operate, move data, establish commercial presence and deliver services across borders. Trade policy can support this process through stronger competition in backbone services, commercial presence abroad, the temporary movement of professionals, lower administrative and regulatory trade costs, and regulatory cooperation. Where these rules evolve unevenly across jurisdictions, however, services trade may become increasingly fragmented.

This risk is particularly visible in digitally deliverable services. Digitalization expands cross-border services trade. It enables goods and services to be bundled more closely, including through software, digital content, connected devices and cloud-based services. Yet the multilateral framework has not fully adapted to these changes. Under the WTO Work Programme on Electronic Commerce, the classification of digitally delivered products remains unresolved, while discussions on the moratorium on customs duties on electronic transmissions address only one part of the policy environment. The moratorium historically supported predictability for digital delivery models but did not cover many regulatory measures shaping market access and competition. Following the failure of WTO members to achieve consensus at the 14th Ministerial Conference, the long-standing multilateral moratorium officially expired on March 30, 2026. This post-moratorium landscape shifts digital trade governance from a unified standard to a fragmented regime, forcing developing economies to balance digital industrial policy space and domestic revenue generation against the rising threat of localized digital trade barriers.

Fragmentation may arise from divergent rules on data governance, cybersecurity, investment screening, digital infrastructure, privacy, professional mobility and recognition of qualifications. These rules are often designed to pursue important public policy objectives, including data protection, national security and critical infrastructure resilience. Differences in design and implementation, however, can raise compliance costs, restrict cross-border delivery and create market-specific conditions that are difficult for smaller firms and most developing country suppliers to meet.

Trade agreements increasingly address digital trade, telecommunications, data flows, digital transactions and the temporary movement of natural persons. These provisions can support “servicification” but may also contribute to fragmentation if they generate competing regulatory models or de facto standards negotiated by limited groups of countries. For developing countries, the central challenge is to design services-related rules that support diversification rather than creating new barriers linked to regulatory capacity, digital infrastructure and data governance. A development-oriented approach should combine market access with regulatory cooperation, interoperability, transparency, capacity-building and meaningful participation in emerging services and digital trade rules.

Source: UNCTAD (2026c and 2026d).



The appeal of tariffs lies in their administrative simplicity and political visibility

1. Market access and compliance instruments

a) Import restrictions: Tariffs and trade remedies

Import restrictions, such as tariffs and quotas, remain the most visible market access instrument. Although their use declined during earlier globalization, recent years have seen the renewed use of tariffs,

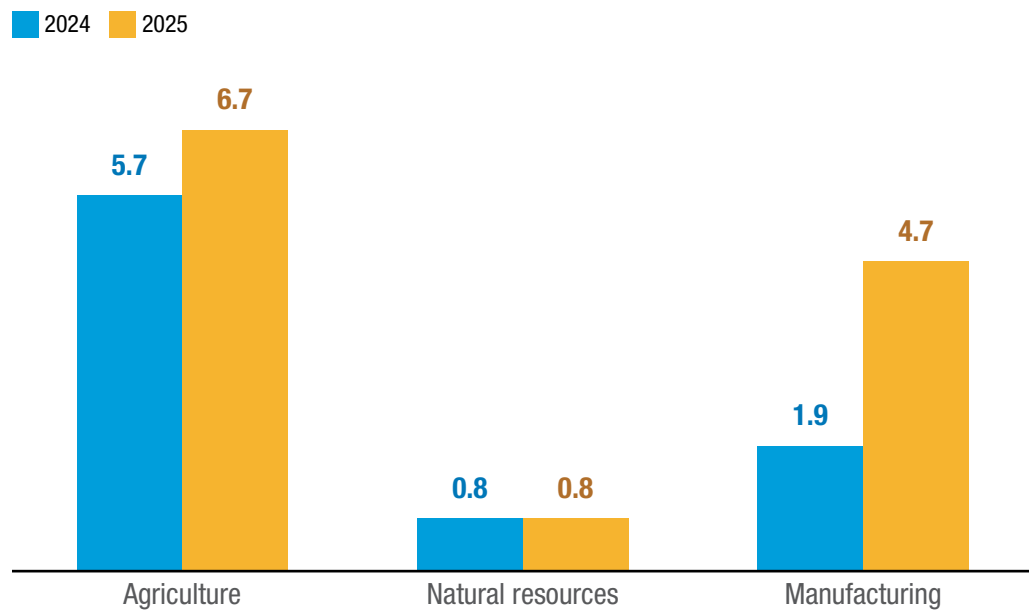
especially as bargaining tools, defensive instruments and geopolitical signals. This became more evident in 2025 when the global average tariff rose, particularly in manufacturing, reflecting increases introduced by a major economy (figure II.2). Tariffs have been used in disputes over technology, industrial capacity, labour practices, migration, national security and trade imbalances. Their appeal lies in their administrative simplicity and political visibility.



Figure II.2

The average global tariff rose significantly in 2025, especially in manufacturing

Trade-weighted average tariff on global trade
(Per cent)



Source: UNCTAD based on the TRAINS database.

The effects of tariffs are rarely confined to the targeted product or sector. In a very integrated global economy, tariffs on intermediate inputs often raise costs for downstream firms, encourage trade

diversion and create incentives to redesign sourcing patterns (box II.2). Tariff changes can fragment trade as firms reorganize supply chains around preferential, exempted or lower-risk jurisdictions (WTO et al., 2025).





Box II.2

Unilateral preferential schemes and trade policy uncertainty

Trade policy fragmentation affects developing countries not only through new restrictions but also through the weakening of predictable preferential market access. Non-reciprocal trade preferences have long supported export growth, industrialization and participation in global value chains, particularly in the least developed countries. By granting duty-free or reduced tariff access to major markets, these schemes have facilitated the integration of otherwise marginalized developing economies into global markets and helped offset competitiveness constraints in sectors such as apparel, footwear and processed food products. As preferential access is central to export competitiveness for many beneficiary countries, however, uncertainty surrounding these arrangements can be particularly damaging.

Since non-reciprocal preferences are unilateral arrangements, they can be modified, suspended or withdrawn more easily than negotiated reciprocal commitments. In a more fragmented policy environment, this creates an additional source of uncertainty for countries whose firms, investors and supply chains have developed around unilateral preferential access. Recent developments illustrate this risk. The expiration or non-renewal of major preference schemes, together with the increasing use of unilateral tariffs, have abruptly raised the applied tariffs faced by vulnerable exporters. The impact is likely to be greatest where countries are highly dependent on a single preference-granting market, have concentrated export structures, or export manufactured or agricultural goods facing high most-favoured nation tariffs. Historical experience suggests that the loss of preferences and even heightened uncertainty about preference eligibility can reduce exports, weaken investor confidence, disrupt value chains and slow diversification.

Preference erosion and trade preference uncertainties represent a specific development channel of fragmentation. Over the past 45 years, exports from the least developed countries grew much faster during periods of low trade policy uncertainty and geopolitical tension (7.6 per cent) than during high-uncertainty periods (2.4 per cent). Similarly, foreign direct investment (FDI) inflows to the least developed countries rose by 11.3 per cent annually during 1994–2014 but declined by 1.2 per cent a year from 2015 to 2023 as uncertainty increased.

Global trade fragmentation could further change the terms on which vulnerable economies participate in global trade. As market access becomes less predictable, multilateral responses should seek to preserve the development value of preference schemes while making them more stable, transparent and predictable. This requires a renewed framework or coordinated dialogue between preference-granting and preference-receiving economies, so that trade relationships, production capacities and investment flows built under preferential arrangements are not abruptly undermined.

Source: UNCTAD (2025b).



Measures designed to protect consumers increasingly serve to differentiate between suppliers

b) Regulatory requirements

Non-tariff measures, particularly technical barriers to trade (TBT) and sanitary and phytosanitary (SPS) measures, are increasingly behind trade fragmentation. TBT and SPS measures are central to modern trade because they determine whether products can legally enter a market, even

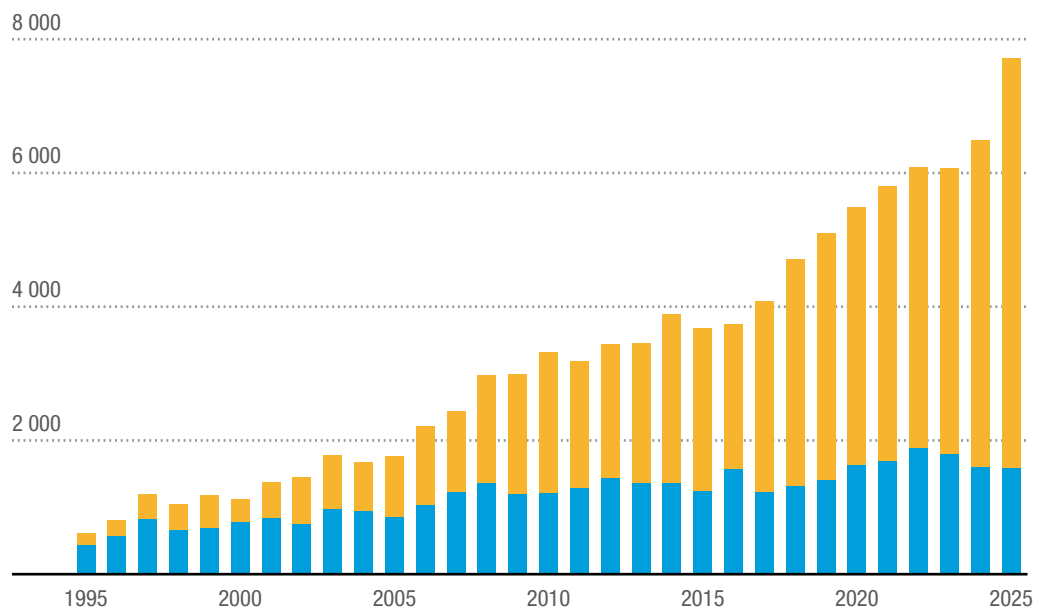
when tariffs are low. Their expansion reflects the spread of regulatory requirements, including among developing economies (figure II.3). Many non-tariff measures serve public policy objectives, including consumer protection and compliance with health, safety and environmental standards. Their growing scope and complexity, however, also make them powerful instruments of differentiation.



Figure II.3
Regulations are increasingly central to world trade

Use of SPS and TBT by developed and developing countries
(Number of notifications per year)

■ Developing countries
■ Developed countries



Source: UNCTAD, WTO and International Trade Centre.

c) Rules of origin and preferential access requirements

Rules of origin are an important but often overlooked source of fragmentation. In preferential trade agreements, they determine whether products qualify for tariff preferences. Their significance has grown as such agreements have proliferated. In complex manufacturing,

requirements such as regional value content thresholds or specific production processes can shift sourcing towards suppliers within the trade bloc rather than the most efficient global producers. Rules of origin can support regional integration and supply chain governance; they also increase administrative costs and may burden smaller firms struggling to source qualifying inputs or document compliance.



2. Government support

a) Subsidies and industrial support

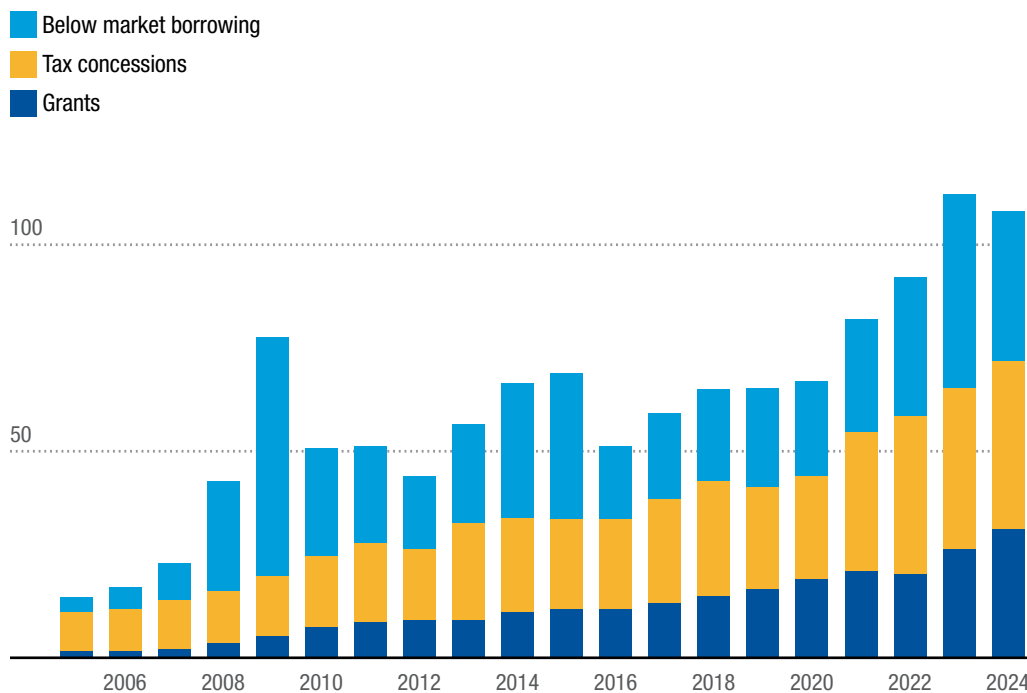
A second group of instruments shapes both market access and the location and

competitiveness of production. These include subsidies, tax credits, state aid, concessional finance, public guarantees, procurement preferences, reshoring incentives and manufacturing mandates. Their use has expanded with the revival of industrial policy and growing support for strategic sectors (figure II.4).

Industrial support can deepen fragmentation when eligibility depends on production location, input origin or firm nationality

Figure II.4
Industrial subsidies reached their highest levels in 2023 and 2024

Global industrial subsidies in 15 key sectors, by type of subsidy
(Billions of dollars)



Source: UNCTAD based on the OECD MAGIC database of industrial subsidies.

Note: The 15 key sectors are: aerospace and defence; aluminium; automobiles; cement and other building materials; chemicals; fertilizers; glass, ceramics and refractories; heavy machinery; semiconductors; shipbuilding; solar photovoltaic cells and modules; steel; telecommunications network equipment; rolling stock and signalling; and wind turbines. Data are based on 525 of the largest manufacturing groups globally (including Chinese and other non-OECD companies).

Industrial support can address market failures, promote innovation, accelerate the green transition and build productive capacity. Yet it can also deepen fragmentation when eligibility depends on production location, input origin or firm nationality. These effects can induce competing subsidies, trade remedies, local content requirements and other measures.

b) Local content requirements and domestic preference rules

Local content requirements and domestic preference rules reinforce fragmentation by linking access to subsidies, procurement, tax incentives or markets to the use of domestic inputs, labour or production. Common in sectors such as renewable

A development asymmetry results when large economies can use fiscal support and market size to attract investment and supply chains

energy, electric vehicles, defence, pharmaceuticals, infrastructure and digital technologies, these measures are often justified by employment, resilience, technological upgrading or national security. They can discriminate against foreign suppliers and redirect production, however, according to policy boundaries rather than efficiency. They also risk creating a development asymmetry: large economies can use fiscal support and market size to attract investment and supply chains, while smaller and poorer countries often lack comparable resources (UNCTAD, 2026e).

3. Security, technology and strategic control instruments

A third group of instruments concerns security, technology and strategic control, including export controls, investment screening, procurement exclusions, cybersecurity requirements, technology restrictions and end-use monitoring. Their deployment has expanded as trade policy has become more closely tied to national security and geopolitical competition (chapter III).

These measures are particularly fragmenting because they differentiate trade not only by product but also by partner, ownership, end-use and perceived strategic risk.

Security-related restrictions in strategic sectors increase trade dependency on relationships and licensing, raising policy risks

They can restrict access to sensitive technologies, limit foreign participation in strategic sectors, exclude firms from procurement, and disrupt established trade and financial relationships. Although often justified by security concerns in sectors such as semiconductors, telecommunications, critical minerals, artificial intelligence, defence and advanced manufacturing, they also make trade increasingly dependent on established commercial relationships and licensing decisions, while raising legal and policy hazards. Firms may redesign supply chains not only to reduce costs but also to limit exposure to geoeconomic risk.

4. Institutional and regulatory fragmentation beyond WTO

A further source of fragmentation is the changing institutional architecture of trade governance. As multilateral rule-making has struggled to address new policy issues, governance has shifted towards bilateral, regional and megaregional agreements (figure II.5). These arrangements increasingly cover investment, services, procurement, standards, labour, the environment, digital trade, subsidies and regulatory cooperation. They may reduce uncertainty among members but also create differentiated rule systems that disadvantage outsiders.

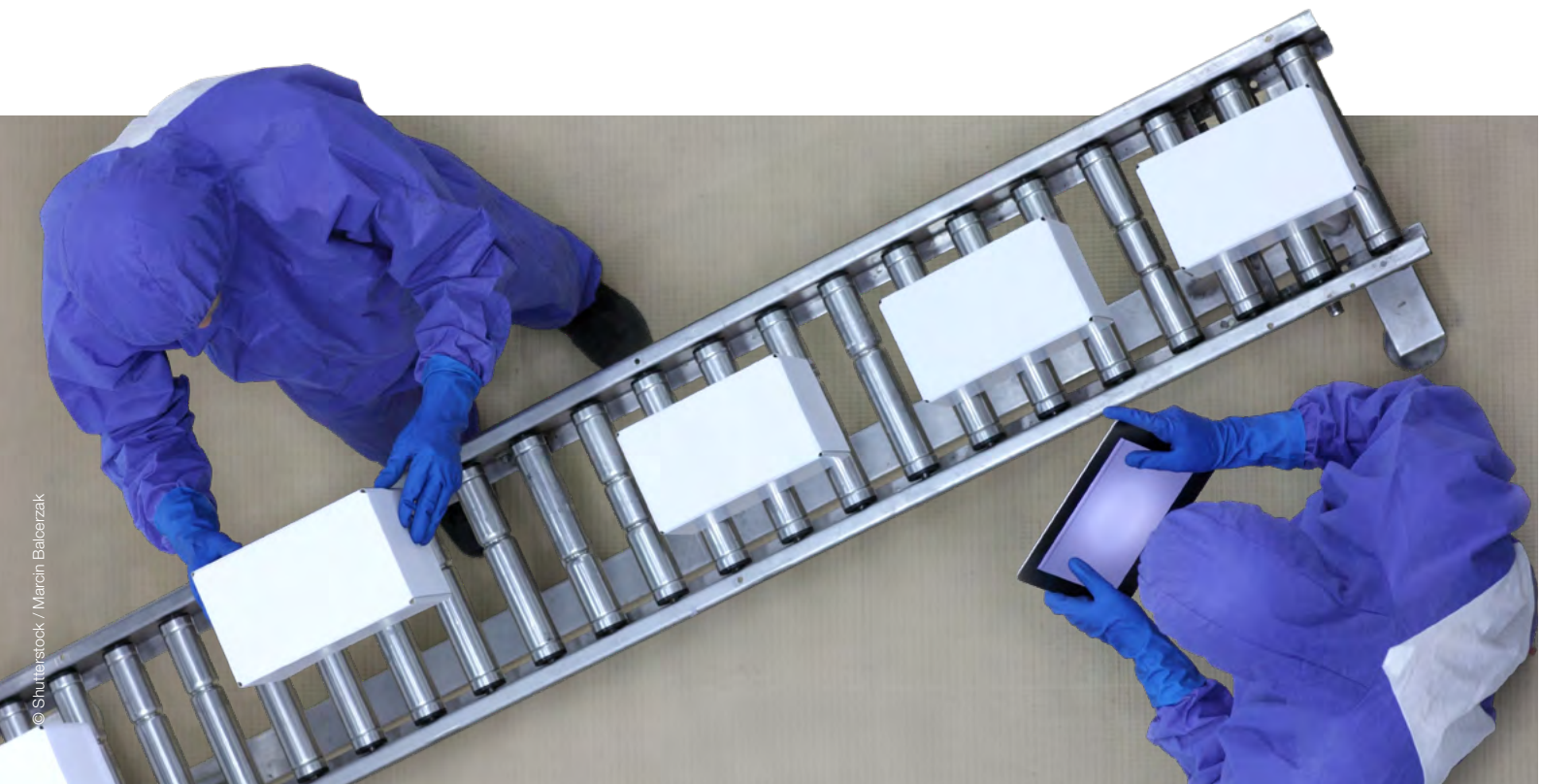
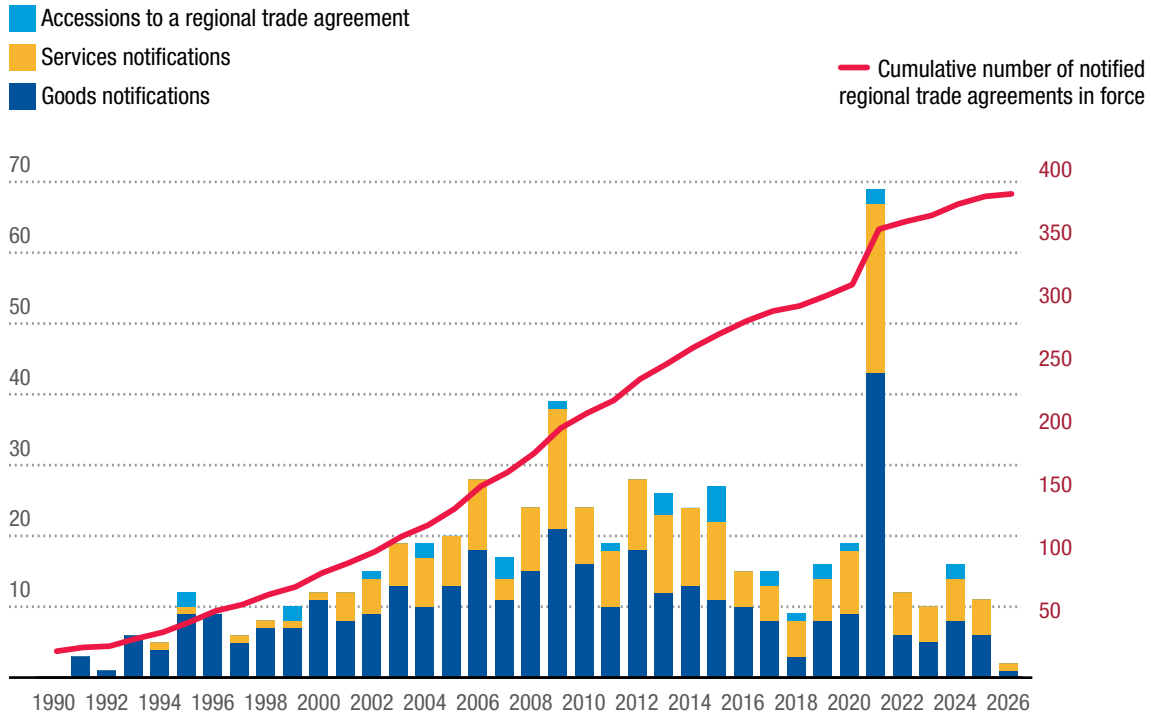




Figure II.5

Regional trade agreements have multiplied and become deeper

Regional trade agreement notifications and agreements in force
(Number notified to WTO)



Source: UNCTAD based on the WTO RTAIS database.

Note: The figure for 2026 includes only notifications received by June.

This fragmentation is reflected in WTO+ provisions, which deepen commitments in areas already covered by WTO rules, and WTO-X provisions, which extend cooperation into areas not fully covered by existing multilateral disciplines such as data governance, cybersecurity, labour, the environment, investment screening and digital trade. When negotiated outside the multilateral framework, these rules can produce overlapping regulatory regimes. Most developing countries and small firms may face higher compliance costs while having limited influence over standards set elsewhere, reinforcing the divide between rule-makers and rule-takers.

5. Socioenvironmental conditionality

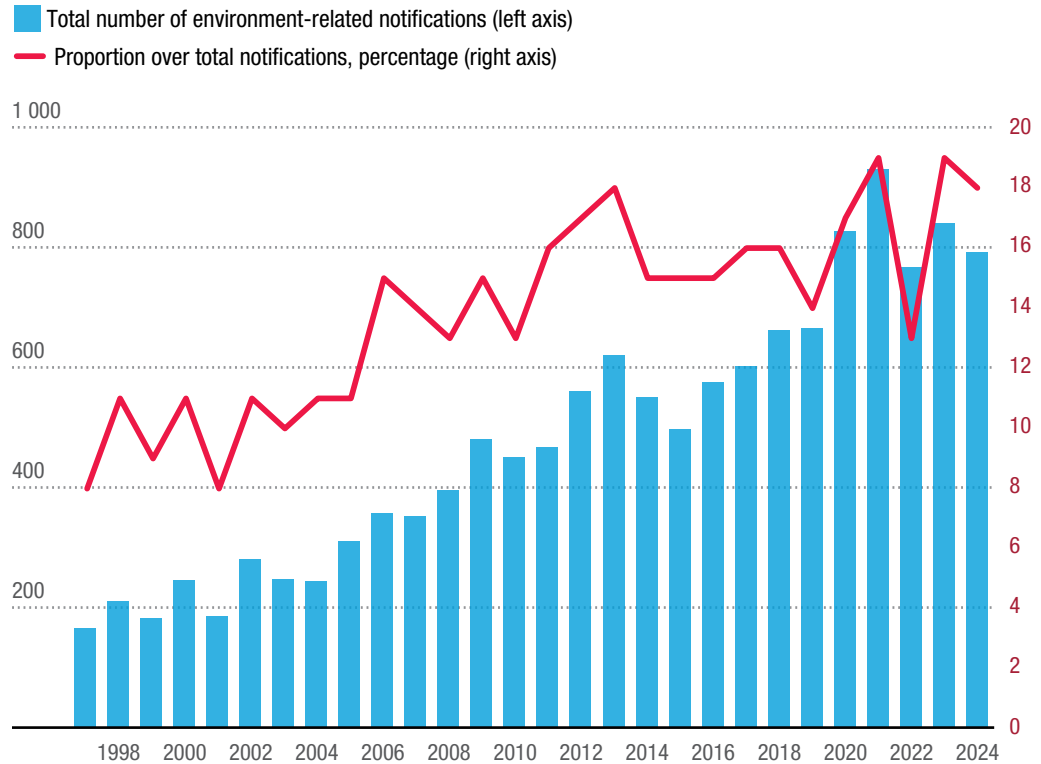
A final group of instruments concerns the socioenvironmental dimension of trade policy. The growing recognition of trade's social and environmental implications has spurred the increasing incorporation of climate, labour, human rights and supply chain due diligence requirements into trade agreements and domestic legislation with cross-border effects on trade and global supply chains (World Bank, 2020a). Examples include carbon border measures, labour-related import restrictions, deforestation-free supply chain rules, battery sustainability standards, corporate due diligence obligations and green public procurement. This trend is reflected in the rising number of environment-related notifications submitted to WTO (figure II.6).

Developing countries may face higher compliance costs with limited influence over standards set elsewhere



Figure II.6 Environment-related measures affecting trade are on the rise

Environment-related measures notified to WTO
(Number of notifications and share of total notifications)



Source: UNCTAD based on WTO Environmental database.

Managing sustainability and development tensions requires transition periods, technical assistance, mutual recognition and capacity-building

The design, implementation and verification of these measures determine their fragmenting effects. Differences in carbon accounting, due diligence obligations, traceability rules, audit standards and definitions of acceptable production practices mean that market access increasingly depends on exporters' ability to provide market-specific evidence of compliance. Because many compliance costs are fixed, they weigh more heavily on smaller firms and on many exporters from developing countries, especially where certification systems, data infrastructure

and traceability mechanisms remain weak. Firms may be excluded not because their production is non-compliant but because they cannot document compliance in the required form. The key development challenge is to avoid creating unnecessary barriers while pursuing sustainability objectives. This may call for measures such as transition periods, technical assistance, mutual recognition, interoperable reporting systems, and support for domestic certification and traceability capacity.

D. Changing trade patterns and geoeconomic shifts

This section examines whether rising policy intervention is already reshaping global trade flows. The evidence points not to generalized deglobalization but to a selective reorientation. Aggregate trade remains resilient, while bilateral relationships, strategic sectors and production corridors are increasingly shaped by geoeconomic considerations.

1. Trade resilience amid volatility and unequal outcomes

The historical resilience of trade openness through repeated systemic shocks suggests that current tensions are reshaping the geography and organization of trade rather than producing a generalized reversal of global integration. Despite intensifying trade policy fragmentation, global trade

continues to expand. Goods and services trade reached about \$33 trillion in 2024 and exceeded \$35 trillion in 2025, with merchandise trade surpassing \$26 trillion in 2025 and services trade rising above \$9 trillion (figure II.7). During the first half of 2026, it continued to grow (chapter I).

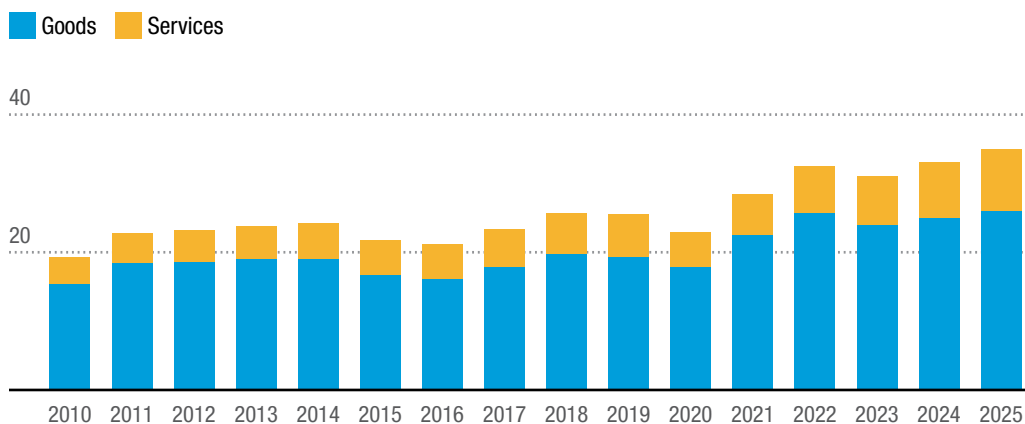
Trade resilience at the aggregate level conceals important changes in the geography, sectoral composition and organization of trade. Since 2021, the concentration of bilateral trade flows – which is highly sensitive to developments in the largest bilateral trade relationships – appears to have declined, suggesting a relative weakening or rebalancing of the largest trade links (figure II.8). At the same time, the Gini coefficient of the distribution of bilateral trade flows – which is most sensitive to changes in the middle of the distribution – has increased, reflecting growing trade asymmetries internationally.¹

Geoeconomic factors are reshaping the geography and organization of trade rather than reversing globalization



Figure II.7
Global trade in goods and services continues to expand

Trade in goods and services
(Trillions of current dollars)



Source: UNCTADStat.

¹ A similar pattern is visible in international investment, where recent growth has been concentrated in a relatively narrow group of economies and sectors, limiting development impact (UNCTAD, 2026a).



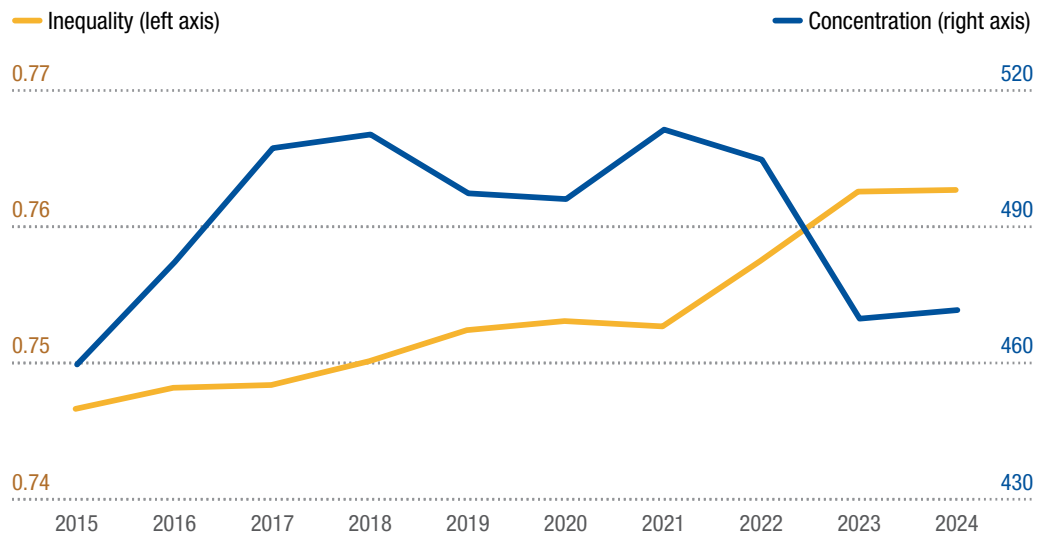
Taken together, these trends suggest that fragmentation is neither simply reducing trade nor dispersing it evenly across partners. Instead, large

trade relationships are losing weight, selected corridors are expanding and smaller trade links are languishing.



Figure II.8 Trade fragmentation is uneven, driven by shifts in concentration and distribution

Gini and Herfindahl-Hirschman concentration indices for global trade
(Index numbers)



Large relationships are losing weight, selected corridors are expanding and smaller links are languishing

Source: UNCTAD based on United Nations Comtrade database.

Note: Inequality refers to the Gini coefficient; concentration is captured by the Herfindahl-Hirschman index. Both indices are based on the dollar values of bilateral merchandise trade flows, aggregated across products at the country-pair level.

2. Trade patterns, geographic distance and geoeconomic compatibility

The recent reorganization of global trade has followed geoeconomic rather than purely geographic patterns. Geographic factors, such as physical distance and associated transport and logistics costs, remain important in global value chain sourcing decisions.

They must still be considered alongside differences in production capacities, specialization and costs across the global economy. But geoeconomic compatibility, which concerns potential exposure to policy shifts, is increasingly important as firms seek to mitigate policy risks and trade restrictions.²

Figure II.9 shows that the trade-weighted geographic distance of global trade increased from 2015 to 2025, alongside a rise in geoeconomic compatibility.³

² Geoeconomic tensions are also selectively reallocating greenfield FDI across sectors and destinations, rather than reversing cross-border investment (Avendano et al., 2026).

³ Geographic distance is measured as the bilateral trade-weighted average geodesic (great circle) distance, in kilometres, between countries' capitals. Geoeconomic compatibility is proxied by similarity in United Nations General Assembly voting patterns (Bailey et al., 2017). This index is a statistical measure developed by independent academic researchers using publicly available UN General Assembly voting records; it does not constitute a UN classification, position or assessment of Member States.



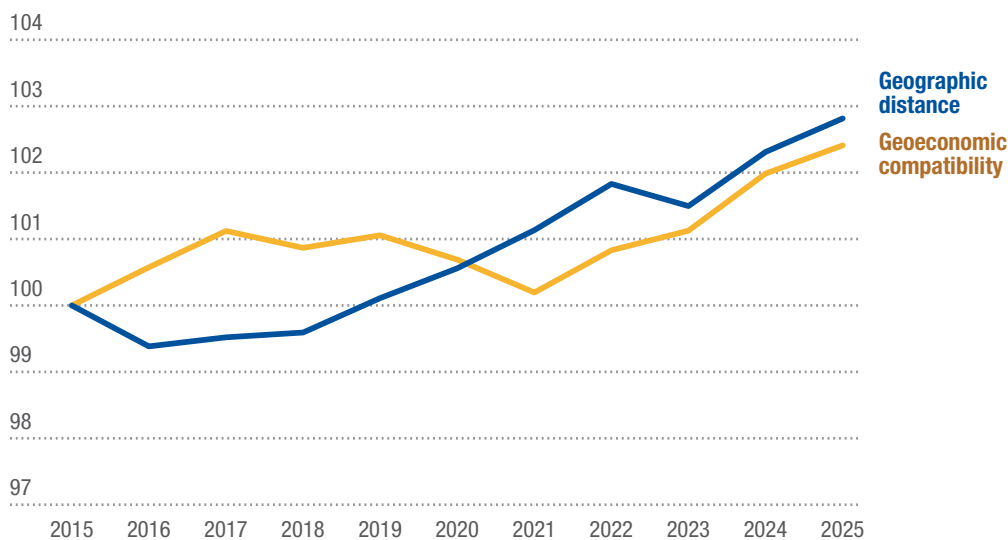
This indicates that firms continue to rely on distant suppliers, where cost, scale or specialization advantages remain strong, while using alternative hubs and intermediary economies to manage strategic exposure. The literature points not to straightforward regionalization or nearshoring but to trade becoming more geoeconomically filtered

while remaining geographically dispersed (Blanga-Gubbay and Rubinova, 2024; Campos et al., 2024). This pattern is consistent with firms strengthening resilience within existing production networks through supplier diversification, greater redundancy and the selective relocation of activities, rather than through widespread nearshoring.

Trade is being filtered by geoeconomics while remaining geographically dispersed

Figure II.9 Global trade, still geographically dispersed, is increasingly geoeconomically filtered

Geographic distance and geoeconomic compatibility indices
(Index numbers, 2015 = 100)



Source: UNCTAD based on United Nations Comtrade database.

Note: Geographic distance is measured as the bilateral trade-weighted average geodesic (great circle) distance, in kilometres, between countries' capitals. Geoeconomic compatibility is proxied by similarity in United Nations General Assembly voting patterns (Bailey et al., 2017).

Recent changes across major trade corridors reinforce this interpretation (table II.3). Between 2019 and 2024, trade expanded across most major relationships, despite the pandemic, logistics disruptions and growing strategic competition. China–United States integration weakened but remained substantial, while developing economies recorded relatively strong trade growth. The 2024–2025 pattern shows a sharper reorientation.

Trade between China and the United States fell by more than 20 per cent. As China's imports from the United States

and Europe weakened, its links with the rest of East Asia continued to expand. Europe remained connected to both the transatlantic economy and Asian production networks. The rest of East Asia emerged as a major beneficiary, with strong growth in trade involving China and North America. This is consistent with firms diversifying assembly, sourcing and logistics across the region while continuing to rely on China-centred inputs and industrial capacities.

Other developing economies present a less favourable picture. Trade among them grew in nominal terms by around

Developments show selective reorientation around strategic relationships, regional systems, intermediary hubs and separated trade blocs

8 per cent annually between 2019 and 2024 but increased by only about 2.5 per cent in 2025. In comparison, global merchandise trade expanded by approximately 7 per cent. The trade dynamism of other developing economies, therefore, became more dependent on links with the major economic poles than on stronger integration among themselves.

Taken together, these developments do not yet indicate the formation of fully separated trade blocs. They instead point to selective reorientation around strategic relationships, regional production systems and intermediary hubs. The structure of interdependence is changing even as global trade growth remains widespread.



Table II.3
Global trade is reorganizing along selective bilateral lines

Growth in imports and exports between 2019 and 2025, selected flows
(Annual percentage change)

Annual growth 2019–2024 (importer)	Exporter						Average growth in imports
	China	Rest of East Asia	Europe	United States	Rest of North America	Other developing economies	
China		4.0	1.9	6.1	7.8	7.3	4.8
Rest of East Asia	5.3	4.9	1.9	3.5	3.5	4.1	4.4
Europe	6.4	3.2	4.3	5.6	3.8	2.0	4.2
United States	2.1	8.8	5.6		6.2	5.6	5.9
Rest of North America	8.2	7.9	4.9	4.4	4.8	9.1	5.7
Other developing economies	11.7	4.8	3.2	3.6	2.0	8.1	6.7
Average growth in exports	6.7	5.1	4.1	4.5	5.7	5.7	

Annual growth 2024–2025 (importer)	Exporter						Average growth in imports
	China	Rest of East Asia	Europe	United States	Rest of North America	Other developing economies	
China		6.3	-4.0	-20.1	-0.8	1.4	1.5
Rest of East Asia	12.8	13.5	5.9	8.0	18.9	0.5	10.4
Europe	11.6	11.9	7.9	19.8	20.2	5.8	9.0
United States	-24.3	23.3	11.4		0.5	4.6	4.9
Rest of North America	1.6	32.2	3.3	-3.5	9.2	6.1	3.4
Other developing economies	11.1	9.9	5.5	10.8	11.0	2.4	6.7
Average growth in exports	6.3	13.5	7.3	5.5	3.3	3.0	

Source: UNCTAD based on United Nations Comtrade database.

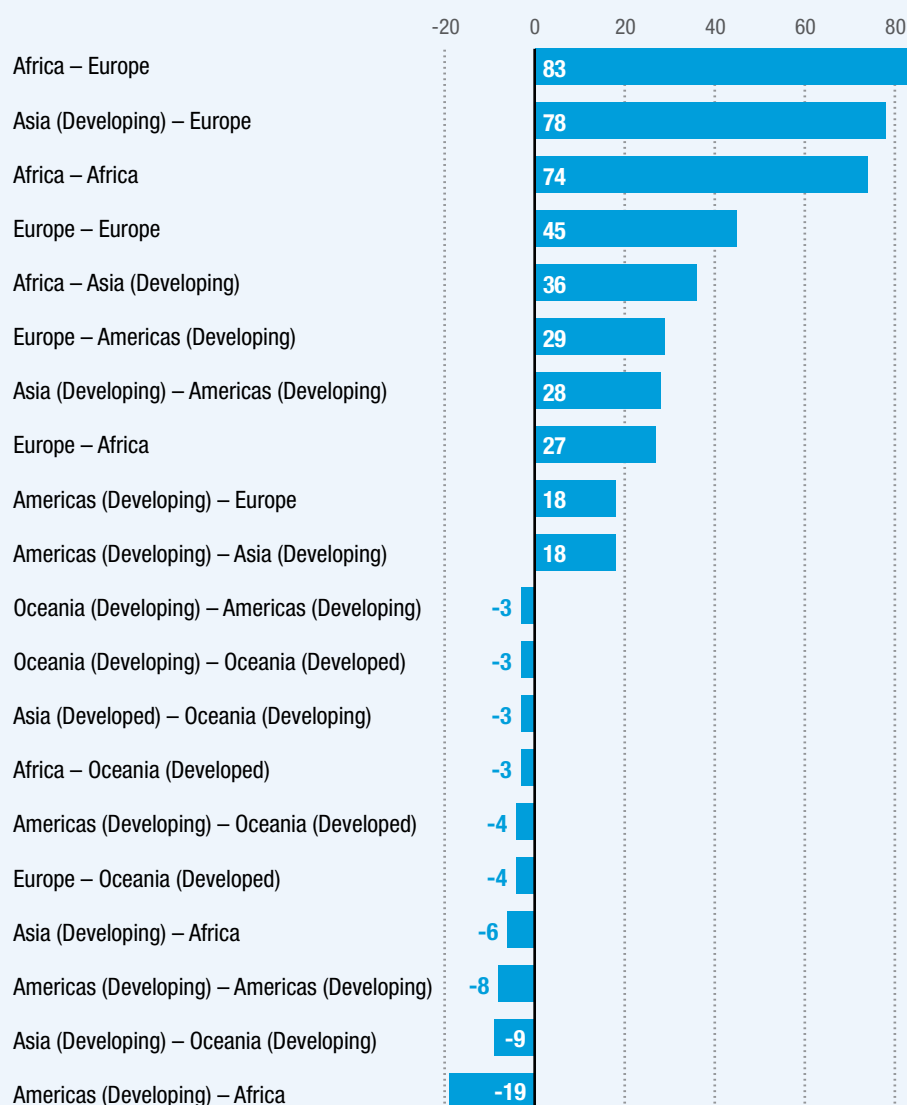


Box II.3 Trade reconfiguration at the extensive margin

Trade fragmentation is not only influencing changes in trade values among existing partners. It also affects the creation and disappearance of bilateral trade relationships. This margin is important because trade expansion depends not only on increasing exports within existing relationships but also on the ability of countries and firms to enter new markets, diversify partners and sustain newly established trade links.

Box figure II.3.1 Trade reconfiguration is creating and erasing export partnerships

Top 10 increases and decreases in active bilateral merchandise export relationships by regional corridor, 2019–2025
(Change in the number of active bilateral export flows)



Source: UNCTAD based on UNCTADStat.

Note: Positive values indicate newly created bilateral export relationships; negative values indicate discontinued bilateral export relationships. Corridor labels are presented as exporter–importer. Active bilateral merchandise flows are defined as flows larger than \$1 million.

Export promotion,
market
information,
export finance and
support for
smaller firms can
help transform
new bilateral links
into long-term
partnerships

Box figure II.3.1 shows that the period 2019–2025 was characterized by considerable churn in merchandise trade partnerships. The largest increases were concentrated in export relationships involving developing Asia, particularly exports to Europe. Africa recorded substantial growth in new relationships, notably with Europe and within the region. This suggests that developing Asian economies found new opportunities, particularly where countries and firms could reposition within changing value chains. At the same time, some partnerships disappeared, especially across more peripheral or lower-density trade links.

The policy implication is that fragmentation should be assessed not only through aggregate trade values but also through its effects on the formation and durability of trade relationships. For developing countries, the challenge is to capture new opportunities created by reconfiguration while reducing the risk that emerging partnerships remain shallow and short-lived. In this context, export promotion, market information, export finance and support for smaller firms can help transform new bilateral links into more durable trade relationships. Monitoring the extensive margin can therefore provide an early indication of whether trade reconfiguration is supporting diversification or reinforcing exclusion.

Geoeconomic
filtering matters
least for
standardized
goods – and most
where technology,
intellectual
property and
strategic
competition
converge

3. Technological content of trade and strategic products

Trade fragmentation is not uniform across sectors. Geoeconomic considerations, for instance, are less likely to matter for low-technology, standardized products. They

are more likely to apply to technologically advanced or strategically sensitive goods, where specialized production capacities and security concerns play greater roles. Table II.4 examines changes between 2019 and 2024 across manufacturing categories classified by technological content as well as selected groups of strategic and sensitive products.⁴



⁴ The technological content of products is measured by the PRODY index. It assigns each product an income-based score according to the per capita income of the countries that export it, weighted by the product's importance in each country's export basket.



Table II.4
Trade patterns evolved differently by technology level and for critical products

Change in selected indicators between 2019 and 2024
(Percentage change, except for changes in the Herfindahl–Hirschman and Gini indices)

	Geographic distance	Goeconomic compatibility	Global reallocation of market shares	Change in trade concentration (Herfindahl–Hirschman)	Change in trade inequality (Gini)
Manufacturing, very low tech	-2.6	-3.3	10.5	7.9	0.014
Manufacturing, low tech	2.5	-0.2	6.8	8.6	0.007
Manufacturing, high tech	3.7	1.2	6.5	9.3	0.005
Manufacturing, very high tech	3.6	2.4	6.1	-4.4	0.005
Strategic goods	4.6	4.9	7.2	-3.2	0.003
Common high-priority goods	3.6	28.9	6.7	2.4	0.004
Critical supply chain goods	2.6	6.3	7.4	0.5	0.000

Source: UNCTAD based on United Nations Comtrade database.

Note: The technological content of products is measured by the PRODY index. Strategic goods are identified using the European Commission Joint Research Centre's Strategic Trade Atlas; common high-priority goods are based on the February 2024 Common High-Priority Items List; and critical supply chain goods are based on the United States Department of Commerce's Draft Harmonized System Code List of Critical Supply Chains.

The results provide little evidence of a generalized shortening of manufacturing supply chains. Geographic distance increased in low-, high-, and very high-technology manufacturing and declined only for very low-technology products. Strategic and sensitive goods also continued to rely on geographically dispersed production networks.

The more significant change is the growing role of goeconomic factors. The importance of goeconomic compatibility strengthened with technological intensity and was most pronounced for strategic goods. This points to a selective reorganization of global trade: goeconomic pressures are filtering trade most strongly in products linked to technology, security and strategic dependence. These products are more exposed to export controls,

investment screening, industrial policy, and supply chain risks, while access to suppliers, technologies, standards and critical inputs increasingly depends on long-term reliability as well as cost and efficiency.

Market shares have also shifted across manufacturing sectors. But this has not produced a more even distribution of trade opportunities. Concentration increased in very low-, low-, and high-technology manufacturing, while trade inequality rose across all technological categories. For developing countries, this may create additional barriers to entering higher-value segments of global value chains as trade in advanced and sensitive products becomes increasingly organized around a narrower group of trade partners perceived as more reliable in terms of supply security and policy risk.

Goeconomic pressures filter trade flows most strongly in products associated with technology, security and strategic dependencies



4. Regional trade agreements

Stronger regional trade growth may reflect both trade agreements and geoeconomic compatibility

Regional trade agreements provide an institutional lens through which to assess trade reconfiguration. Shallow agreements generally focus on tariff preferences and basic market access commitments. Their disciplines are therefore concentrated mainly at the border, reducing the direct costs of trade without substantially harmonizing or coordinating domestic regulatory frameworks. Deep agreements also cover services, investment, standards, procurement, digital trade, regulatory cooperation and dispute settlement.

By addressing these “behind-the-border” policies and reducing regulatory and institutional frictions, deep agreements can support closer and more complex forms of economic integration. They may therefore provide a stronger framework for integrated production networks and more predictable trade relationships.

From 2019 to 2024, aggregate trade among regional trade agreement partners grew only slightly faster than trade among countries without such an agreement. Regional trade agreement membership alone therefore does not explain the broader pattern of trade reconfiguration. The differences are clearer in manufacturing, where trade growth was generally stronger among partners in deep regional agreements than among countries without agreements or in shallow arrangements (figure II.10). This pattern applies across technological categories, suggesting that deep agreements support manufacturing trade broadly by reducing uncertainty, improving regulatory compatibility and facilitating cross-border production.

The association is also relatively strong for selected strategic products. These goods are particularly sensitive to policy risk, export controls, security concerns and the need for reliable supply chains. Countries participating in deep agreements may already share closer institutional, regulatory or geoeconomic relationships, however. Stronger trade growth may therefore reflect both the effects of the agreements and the geoeconomic factors that encouraged countries to negotiate them.

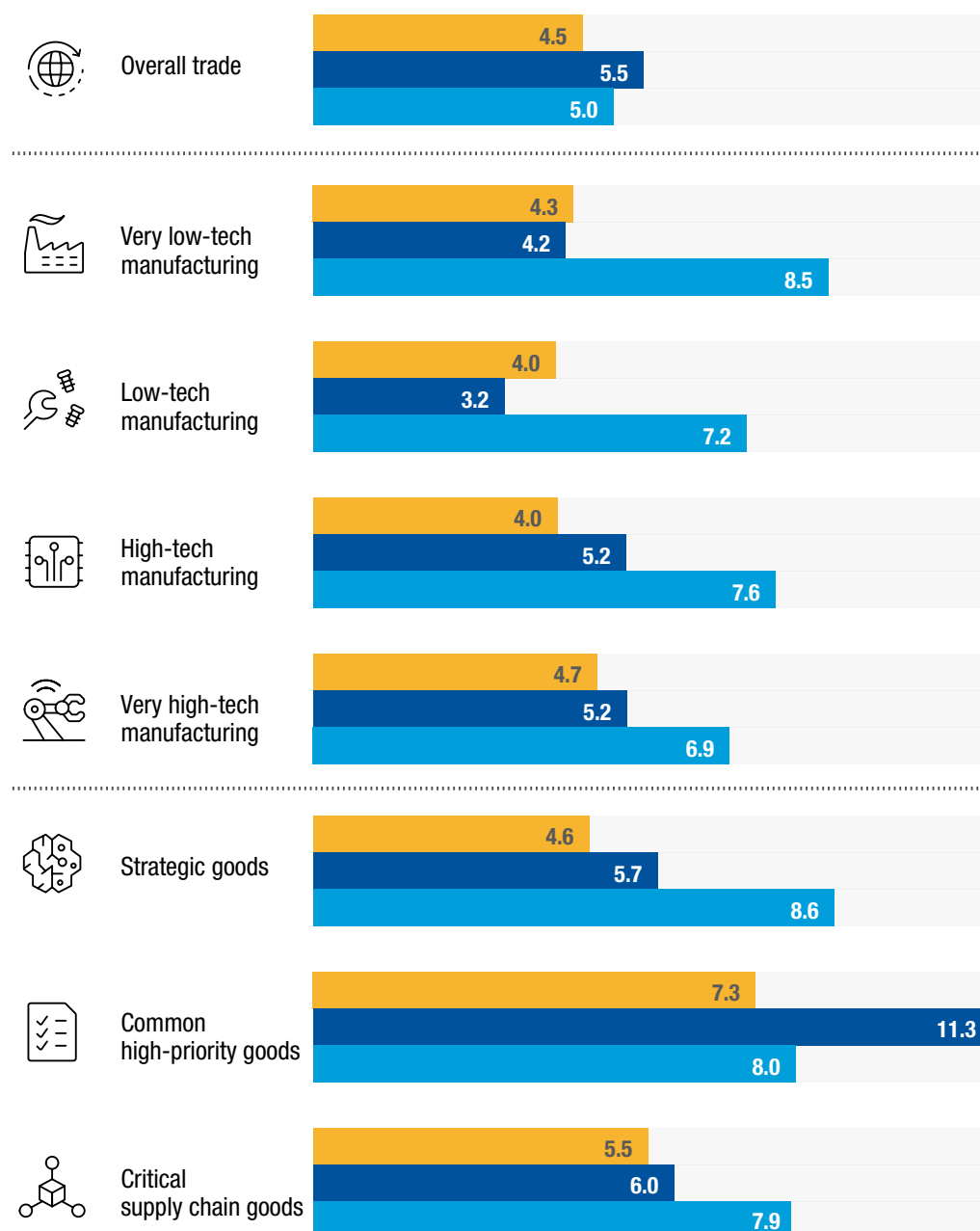
Overall, regional trade agreements facilitate some forms of trade reconfiguration, particularly in manufacturing and selected strategic goods, but do not fully explain recent changes in global trade. The generally stronger performance of trade within deep agreements points to the importance of institutional depth, regulatory compatibility and established commercial relationships, rather than formal agreement membership alone.



Figure II.10 Regional trade agreements broadly support growth in manufacturing trade

Growth in overall trade and within regional trade agreements, 2019–2024, by technological intensity and strategic product group
(Annual percentage change)

- Outside regional trade agreements
- Within shallow regional trade agreements
- Within deep regional trade agreements



Source: UNCTAD based on United Nations Comtrade database.

Note: The technological content of products is measured by the PRODY index. Strategic goods are identified using the European Commission Joint Research Centre's Strategic Trade Atlas; common high-priority goods are based on the February 2024 Common High-Priority Items List; critical supply chain goods are based on the United States Department of Commerce's Draft Harmonized System Code List of Critical Supply Chains.

E. Policy implications: Managing fragmentation while preserving development opportunities

The policy challenge is to accommodate governments' growing demand for flexibility in trade policy while preserving trade and development opportunities, particularly for developing countries

Current trade policy dynamics are best understood less as a retreat from international economic integration than as a shift towards more flexible, conditional and politically mediated integration. Although its full trade and development implications remain uncertain, this shift is likely to produce selective and uneven outcomes, both across countries and among firms. Differences in market access conditions, including applied tariffs, preference margins, rules of origin and exposure to trade remedies, will shape which countries, sectors and firms are able to benefit – and which risk losing market share or being excluded from emerging trade opportunities. Beyond market access conditions, outcomes will also depend on geoeconomic positioning and on how trading partners use trade policy to pursue broader strategic, industrial and environmental objectives.

For the multilateral trading system, the central challenge is to accommodate governments' growing demand for flexibility in trade policy while preserving trade and development opportunities, particularly for developing countries. As government priorities have evolved, trade policy is increasingly expected to support not only market integration, but also resilience, industrial upgrading, energy transition,

technological capacity and national security. This broader agenda also raises questions about how existing multilateral frameworks can accommodate policy areas in which negotiated outcomes have proved difficult to achieve. Where multilateral agreement within WTO remains difficult, developing countries may need complementary pathways to support trade integration and diversification. These arrangements should not be viewed as substitutes for multilateralism but as complementary mechanisms to help maintain development opportunities, while WTO continues to provide the core framework for transparency, non-discrimination and baseline disciplines.

The absence of common rules in emerging trade-related policy areas can itself tighten development policy space. Developing countries may be less formally constrained by multilateral disciplines but, in practice, more exposed to standards and conditions set elsewhere, particularly as trade governance shifts towards bilateral, regional and plurilateral arrangements. The challenge is therefore not only to preserve policy space, but also to uphold the meaningful participation of developing countries in shaping rules determining market access and value chain participation (box II.4).⁵

⁵ For instance, a recent proposal by the Least Developed Countries Group emphasizes that meaningful participation requires not only formal inclusion but also timely access to information, manageable negotiating processes, and a substantive role in agenda-setting and rule-shaping (WTO, 2026).





Box II.4

An agenda for a rules-based multilateral trading system

Trade policy fragmentation raises a central institutional question: how can the multilateral trading system preserve predictability, non-discrimination and development opportunities when trade measures are increasingly shaped by industrial policy, economic security and selective cooperation?

The WTO Agreements establish a system based on binding market access commitments, reciprocity, non-discrimination through the most-favoured nation principle, transparency and legally enforceable obligations supported by dispute settlement. The functioning of this framework, however, has gradually declined as members have increasingly adopted unilateral, uncoordinated or non-compliant measures. These comprise partner-specific tariffs, security-related restrictions and trade-related industrial policy instruments. Strengthening “the rules-based, non-discriminatory, open, fair, inclusive, equitable and transparent multilateral trading system with the World Trade Organization at its core”, as reaffirmed in the Sevilla Commitment adopted at the Fourth International Conference on Financing for Development in 2025, remains essential for sustainable development.

A priority is to preserve the most-favoured nation principle. By requiring trade advantages granted to one WTO member to be extended to all others, the principle limits discrimination and prevents market access from being determined mainly by bargaining power or geopolitical factors. This is particularly important for developing countries, many of which lack the leverage to negotiate favourable bilateral arrangements with major trading partners due to their smaller market size and weaker bargaining power. Even where enforcement is constrained, most-favoured nation disciplines help preserve predictability, transparency and a degree of protection against arbitrary discrimination.

A second priority is to clarify the relationship between trade rules and economic security. Economic security considerations now cover supply chain resilience, access to strategic technologies and natural resources, critical infrastructure and geopolitical risk. This has encouraged greater use of export controls, investment screening, procurement exclusions and other measures that distinguish trading partners based on perceived strategic risks. Yet the WTO legal architecture has not formally changed to accommodate this shift. Greater transparency, clearer principles for using security-related measures and stronger dialogue among members would help prevent economic security from becoming a broad justification for discretionary or discriminatory restrictions that could ignite a vicious cycle of retaliatory trade restrictions among major economies.

A third priority is to manage plurilateral initiatives so they support the multilateral system. Such initiatives can help willing members advance rule-making where consensus is not yet possible although their systemic effects depend on their design. Open-ended plurilateral agreements extending benefits to all WTO members can support wider liberalization and reduce the risk of exclusion. Closed agreements may deepen cooperation among participants but create differentiated legal regimes and new divisions between rule-makers and rule-takers. From a development perspective, while plurilateral initiatives may offer a pragmatic response to negotiating deadlocks, they remain a second-best solution where multilateral agreement is not yet possible.

Source: United Nations (2026).



Regional trade agreements can provide one such pathway when they expand market scale, reduce trade costs and support regulatory cooperation without becoming exclusionary blocs. From a development perspective, the African Continental Free Trade Area is especially relevant because it links market integration directly to diversification, regional value chain development and poverty reduction. By connecting 1.3 billion people across 55 countries with a combined GDP of \$3.4 trillion, full implementation of the agreement could raise regional income by 7 per cent, or \$450 billion, and lift 30 million people out of extreme poverty by 2035 (World Bank, 2020b).

The Regional Comprehensive Economic Partnership illustrates a different dimension of the same trend: the emergence of large regional agreements that combine market access with broader regulatory disciplines. Bringing together 15 economies accounting for about 30 per cent of global GDP and roughly a third of the world's population, the partnership is expected to boost intraregional exports through tariff concessions. Its provisions on rules of origin, services, investment, e-commerce, customs procedures, standards and trade facilitation show how large regional trade agreements can extend beyond tariff liberalization (UNCTAD, 2021).

The Global System of Trade Preferences among Developing Countries provides a specifically South–South channel. As an interregional agreement for preferential South–South trade liberalization among developing countries, it is legally covered under WTO's 1979 Enabling Clause. Implementation of the São Paulo Round Protocol could generate welfare gains of up to \$27 billion and tariff reductions of at least 20 per cent on about 6,000 products. Yet its trade and development impact would be stronger if tariff preferences were accompanied by simplified rules of origin, digital customs procedures, standards cooperation, trade finance and support for small firms (UNCTAD, 2025c and 2026f).

Softer forms of cooperation can play a complementary role. Asia-Pacific Economic Cooperation (APEC) illustrates how flexible, non-binding regional cooperation can preserve dialogue, support issue-specific coordination and reduce unnecessary regulatory divergence without being presented as a substitute for the multilateral trading system.

A central caveat is that these arrangements should reinforce the multilateral trading system by operating as building blocks for more inclusive integration (box II.5). They are most credible when they expand effective market access, reduce avoidable compliance costs, support productive transformation, preserve policy space and remain compatible with broader multilateral principles, including transparency, non-discrimination, and special and differential treatment. They become more fragmenting when they operate as exclusive arrangements, restrict opportunities for outsiders, generate complex or exclusionary rules of origin or deepen rule-taker dynamics for countries with limited influence over emerging standards.

Overall, the extent to which global trade can continue to support developing countries' development-oriented integration into the global economy will depend on whether governments can make policy flexibility and shared commitments mutually reinforcing rather than opposing objectives. Greater flexibility should be accompanied by safeguards that limit discrimination and uncertainty and prevent adjustment costs from falling disproportionately on countries with less economic power. Preserving an open, inclusive and rules-based trading system will also require greater transparency and coordination in the use of trade measures, together with development-sensitive disciplines, including, where appropriate, special and differential treatment, as well as capacity-building and meaningful participation by developing countries in rule-shaping.





Box II.5

Economic cooperation in Asia and the Pacific amid trade policy fragmentation

In May 2026, the APEC Ministers Responsible for Trade met in Suzhou, China; the heads of international organizations, including UNCTAD and WTO, also participated. The meeting produced two ministerial outcomes: the Suzhou Statement and the APEC Roadmap for Innovative, Competitive and Resilient Services. These indicate that APEC cooperation remains active despite rising trade policy fragmentation.

Established in 1989, APEC is the premier economic forum in Asia and the Pacific. It brings together 21 member economies with widely differing economic sizes, levels of development and strategic interests. While this diversity exposes cooperation within APEC to potential geoeconomic risks, the forum has remained an important platform for dialogue, confidence-building and practical economic cooperation.

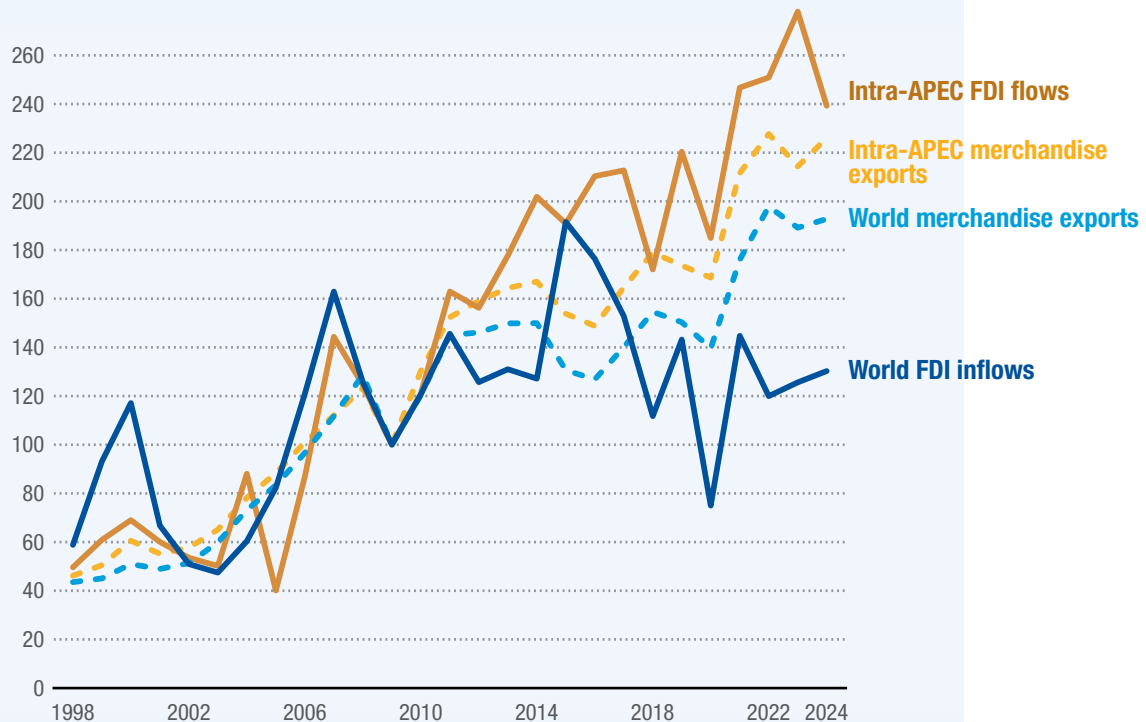
Trade and investment data reflect the resilience of economic integration within the region. From 1998 to 2024, intra-APEC merchandise trade grew at an average annual rate of 6.3 per cent, slightly faster than global merchandise trade, which expanded by 5.9 per cent annually. The difference was more pronounced for FDI. Intra-APEC flows increased by 6.5 per cent annually, compared with 3.1 per cent globally. From 2009 to 2024, global FDI inflows grew by only 1.8 per cent annually; intra-APEC flows rose by 4.6 per cent (box figure II.5.1).



Box figure II.5.1

Intra-APEC trade and FDI flows have remained strong since the 2008 financial crisis

FDI flows and merchandise trade, 1998–2024
(Indices, 2009 = 100)



Source: UNCTAD based on FDI inflow data from UNCTADstat and bilateral FDI statistics.



APEC's continuing relevance rests first on its members' commitment to economic cooperation. In 1994 and 2020, members adopted the Bogor Goals and the Putrajaya Vision 2040, respectively. These frameworks reflect a shared commitment to a free, open, fair, non-discriminatory, transparent and predictable trade and investment environment. Such common objectives have helped sustain the regional cooperation agenda despite growing economic and geopolitical tensions.

A second distinguishing feature is APEC's flexible and pragmatic approach. Cooperation is based on a combination of collective and individual actions, allowing members to work towards shared objectives while retaining substantial policy autonomy. This approach has supported measurable progress. The simple average most-favoured nation tariff applied in the APEC region declined from 13.9 per cent in 1994 to 5.2 per cent in 2019, while the share of tariff lines subject to zero duties nearly doubled over the same period.

APEC has also contributed to regional cooperation by incubating issue-specific initiatives. It has advanced work on information technology, environmental goods, services and digitalization, among other areas. Some initiatives first developed within APEC subsequently informed broader plurilateral or multilateral processes, including the Information Technology Agreement. In 2012, APEC members agreed on a list of 54 environmental goods at the six-digit Harmonized System level.

The private sector has played an important role in shaping APEC's cooperation agenda. Regular dialogue between policymakers and business representatives, including through the APEC Business Advisory Council and the APEC CEO Summit, has helped connect regional initiatives with commercial priorities and implementation challenges.

APEC nevertheless faces important limitations. Trade relations among its members are shaped by overlapping preferential agreements, including megaregional arrangements with substantially overlapping memberships. These "spaghetti bowl" effects can increase transaction costs and complicate regulatory coherence. APEC has provided an important platform for dialogue across these arrangements, although further coordination could help reduce complexity and enhance regulatory coherence.

Overall, APEC complements but does not substitute for the multilateral trading system. Its shared objectives, flexible methods, issue-based initiatives and engagement with the private sector provide a pragmatic model of regional cooperation. In a period of selective fragmentation, such platforms can help preserve dialogue, reduce unnecessary regulatory divergence and support gradual convergence across economies with differing priorities and levels of development.



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