International Commentary — September 2, 2025

The Global Economic Impact of a U.S.-China Bipolar World

Summary

We have long argued that the world economy is the second era of deglobalization. This time, deglobalization is driven by a fragmenting of the global economy with tensions between the United States and China at the helm. We also hold the view that with the U.S. and China on opposite sides of the economic and geopolitical spectrum, countries around the world will have to pick a side: align with the U.S. or align with China. In this report, we update our fragmentation framework to get a sense of how countries could indeed align in the context of ongoing U.S.-China competition. We also update our work on how fragmentation can impact the global economy and result in downward pressure building on global growth.

Economist(s)

Brendan McKenna
International Economist | Wells Fargo Economics
Brendan.McKenna@wellsfargo.com | 212-214-5637

The Global Economic Impact of Bipolar Trade Fragmentation

Our favorite theme—at least global theme—to discuss is the fragmenting of the global economy. Also known simply as "fragmentation." For clarity, when we say "fragmentation" we are referring to the global economy breaking into separate and independent blocs of nations. Rather than one cohesive and integrated global economy, countries with similar views on geopolitics, foreign policy and domestic economic policy—among other considerations—form distinct blocs of nations. Over time, nations look to sever relationships with countries in opposing blocs. Cross-bloc trade is diminished, or even eliminated, cross-bloc capital flows cease, while broader financial and geopolitical relationships are eventually ended. Our main approach to fragmentation is predicated on the fracturing of relations between the United States and China. The U.S.-China relationship has unquestionably worsened over the years, and despite more recent trade truce agreements and a lowering of tariff rates, cooperation, in the broadest sense of the term, between the world's largest economies has receded sharply. Going forward, we would expect the U.S. and China to reduce dependencies rather than pursue deeper integration. Taking fragmenting U.S.-China relations a step further, with the U.S. and China the largest economic powerhouses in the world, and also two of the most influential geopolitical actors, we have argued that countries around the world will likely have to choose a side. Does a nation want to be economically and geopolitical aligned with the United States? Or on the other hand, does a nation prefer strategic alignment with China? Select nations can pursue neutrality, but for the large majority of nations having a relationship with the U.S. and China might not be tenable. As nations determine their respective allegiances, the global economy can fragment into two blocs: a U.S.-led bloc and a second bloc led by China.

We have uncovered tentative evidence to suggest a U.S. bloc and a China bloc are being formed. In fact, blocs may be in the process of being formed for close to a decade. However, the global economy is still far from full fragmentation. We also wonder if countries have even made firm and final decisions in regard to whether to align with the U.S. or China, especially given rapid trade policy changes and pace of geopolitical disruption permeating across the global economy. Nevertheless, we updated our fragmentation framework to get a sense of how countries ***could*** align should fragmentation materialize, and also for the global economic impact of a fragmented global economy. As a reminder, our fragmentation framework is centered around economic and geopolitical indicators we believe could be critical inputs into a nation's decision-making process for strategic alignment. We did, however, make modest adjustments to the indicators in our framework. In our 2023 version, we included whether a country participated in the U.S. Build Back Better World (B3W), a counter program to China's Belt & Road Initiative (BRI) under the Biden administration. Political turnover in the U.S. led us to remove B3W participation from the framework. While we have always included whether a country was signed up for China's BRI in our framework, we adjusted our framework to also now reflect the magnitude of participation (i.e., how much estimated BRI investment a country has received). Our new framework to determine potential U.S. or China alignment now includes

Economic indicators

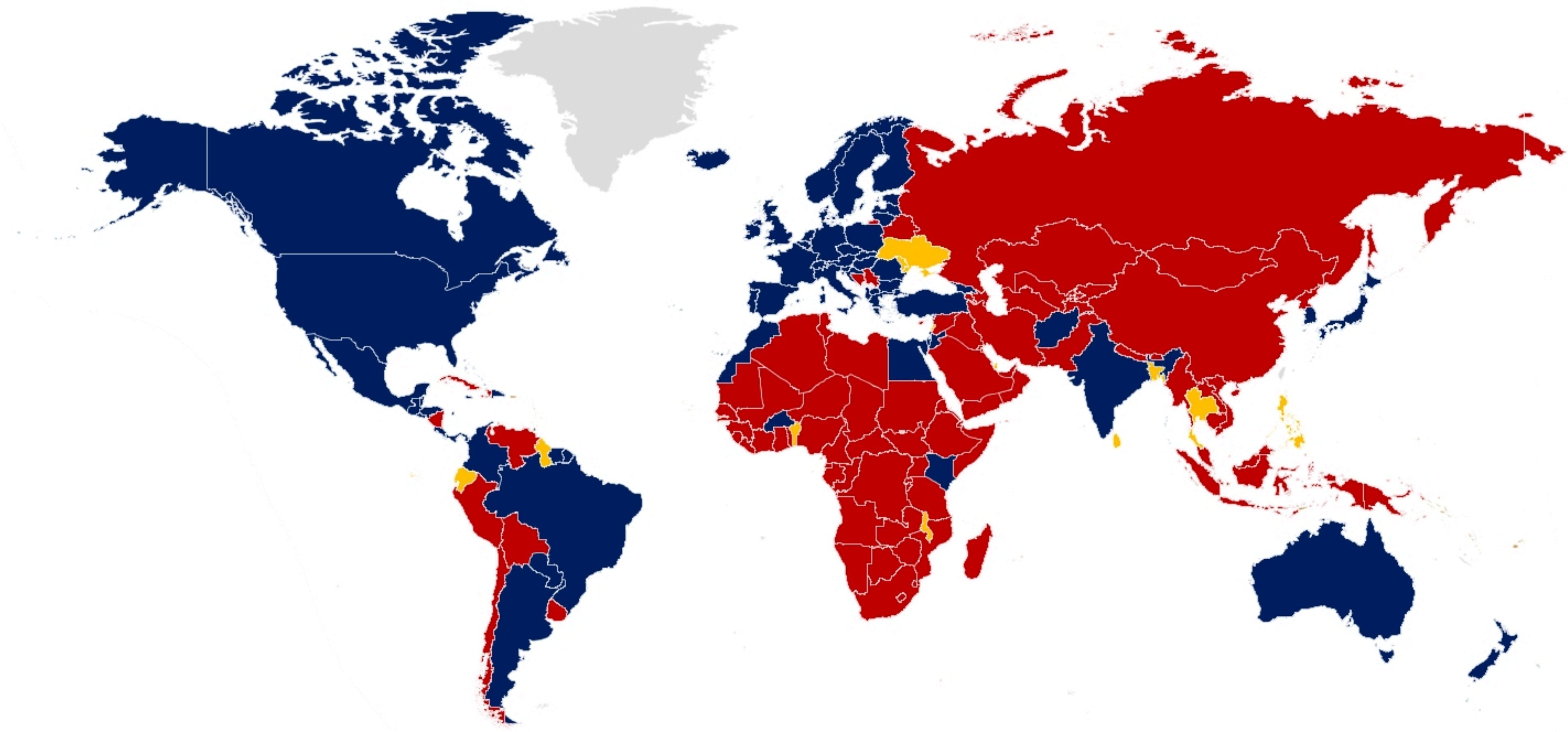
- Trade relationship with the U.S. and China
- Participation in China's Belt & Road Initiative

Geopolitical indicators

- National security alliance membership
- United Nations General Assembly voting alignment

The framework also allows for the possibility of a country to adopt neutrality, and while a balanced relationship might still be untenable over the long term, for now, our framework is built to include countries that show no discernible allegiance to the U.S. or to China. Figure 1 shows the latest update for how fragmentation could unfold. Countries in dark blue, according to our framework could align with the United States, those in red with China, and the select few in orange are the nations our framework identify as neutral. At a high level, fragmentation is likely to take place between advanced and developing economies. Most of the G10, based on our metrics, would opt for allegiance with the U.S., while nations across Asia and Africa could choose alignment with China. According to our framework, Latin America, thematically, is most split as neither the U.S. nor China is dominant in the region. Perhaps going forward, Latin America will be a battleground for the U.S. and China to accumulate allies and influence.

Figure 1

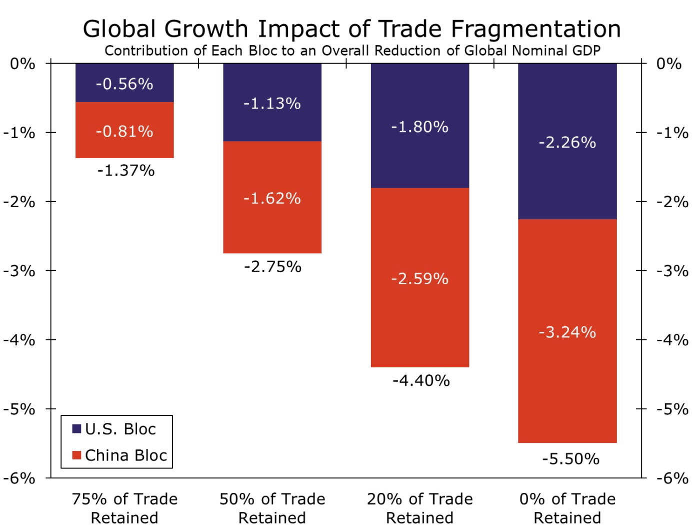


Source: Wells Fargo Economics

With an updated sense for how the world could fracture, we can also update our estimate of how fragmentation could affect the global economy. Trade relationships between countries around the world are under the most scrutiny at the current juncture, so in that sense, assessing the global economic impact of fragmentation through the trade channel is still most appropriate. In reality, linkages between countries run much deeper than purely trade. In a full fragmentation scenario, cross-bloc foreign direct investment, portfolio flows, technology sharing, intelligence sharing, flow of people, etc., may also end. While trade disruptions will have an impact on the global economy—as we will show—the elimination of all linkages between nations in opposing blocs would compound the global economic impact of fragmentation. But for trade, we simulate a scenario where nations in opposing blocs stop trading with each other. For example, our framework suggests Panama would align with the United States and South Africa would align with China. In our simulations, we assume Panama and South Africa, by being in opposing blocs, cease all trade with each other. Elimination of the Panama-South Africa trade relationship may not happen all at once, but nevertheless cross-bloc trade flow between these nations are ultimately halted over a longer period of time. Our simulations also assume that neutral countries, such as Ukraine, continue to trade with countries in both blocs. Using the Panama and South Africa example, we simulate a scenario where Ukraine maintains its bilateral trade relationship with both Panama and South Africa. Under those central assumptions, we simulated scenarios where every country in a bloc stops trade activity with nations in the rival bloc, while all neutral nations maintain trade relations with both blocs.

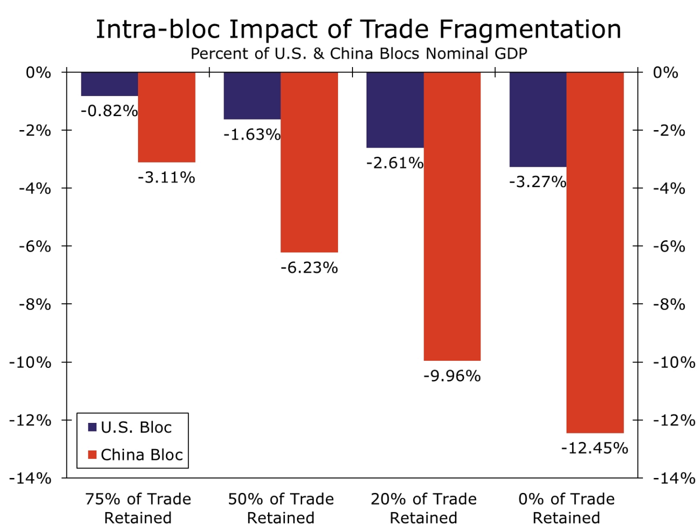
In the simulation where all cross-bloc trade ceases to exist, the global economy could lose 5.5% of nominal GDP (Figure 2). From a trade perspective, this full trade fragmentation simulation is the worst-case scenario. Of course, in the context of fragmentation and reduced cross-bloc trade flows, new intra-bloc trade relationships could be formed as nations look to replace former trading partners. Cross-bloc trade could also be severely diminished, but continue at a substantially reduced level. To account for the possibility of new intra-bloc relations being formed, or where some cross-bloc trade continues, we also simulated scenarios where 20%, 50% and 75% of lost cross-bloc trade is retained. In the scenario where 20% of trade is retained, the global economy loses 4.4% of nominal GDP. If 50% of trade is preserved, 2.75% of nominal GDP is lost; and even in our most optimistic simulation where 75% of trade is retained via these channels, the global economy still loses 1.37% of global nominal output. We also took our analysis a step further to identify the magnitude of contribution from each bloc to reduced global nominal GDP. Our analysis reveals that China bloc nations account for the majority of reduced global nominal GDP. The takeaway there is that nations in the China bloc are not as economically diversified relative to U.S. bloc countries. China bloc countries are more reliant on trade, and in particular, trade with the United States, and removing a key trading partner(s) puts a dent in China bloc economic output. We can see this dynamic also on display in Figure 3, where we calculated the potential lost output of each bloc from trade fragmentation. The China bloc loses significantly more output relative to the U.S. bloc, punctuating how dependent these nations are on trade.

Figure 2



Source: IMF, Bloomberg Finance L.P. and Wells Fargo Economics

Figure 3



Source: IMF, Bloomberg Finance L.P. and Wells Fargo Economics

One final takeaway we make from this analysis: No matter if a country is diversified, overly reliant on trade, or somewhere in between, no country nor bloc of countries gains economic output in any fragmentation scenario.

In the next iteration of our fragmentation reports, we plan to examine an even more fragmented global economy. Rather than an economy fractured along U.S. and China lines, we will run the same analysis but for a tri-polar world with three blocs of nations. Those blocs will still include a U.S. bloc and China bloc, but we will also introduce a Europe bloc. Over the past eight months, Eurozone and broader European Union nations seem to be looking more inward and becoming self-reliant, both from an economic and geopolitical perspective. Not long ago, we performed a similar analysis where a tri-polar world forms and each bloc of nations applies tariffs to each other. The coming report and analysis will be similar to this report, but with a bit of a different perspective attached. Keep an eye out for that publication in the coming weeks.

In the meantime, for additional background on fragmentation, below are links to prior reports focused on the theme.

The World Cleaving into Trade Blocs: Economic Effects of Deglobalization (June 2025)

Strategic Implications of "Liberation Day" (April 2025)

Trump 2.0 & Rising Restrictive Global Trade Policy (February 2025)

The Geopolitical Influence on Global Trade (July 2024)

The Rise of Deglobalization: Part III: Examining a Fragmented Global Economy With No Neutral Nations (December 2023)

Middle East Travel Takeaways (November 2023)

The Rise of Deglobalization: Part II: Geopolitics are Dividing the World and Global Growth is at Risk (October 2023)

Israel-Gaza Conflict Views & Potential Implications (October 2023)

The Rise of Deglobalization: Part I (September 2023)

Subscription Information

To subscribe please visit: www.wellsfargo.com/economicsemail

Via The Bloomberg Professional Services at WFRE

Economics Group

Tim Quinlan	Senior Economist	704-410-3283	Tim.Quinlan@wellsfargo.com
Sam Bullard	Senior Economist	704-410-3280	Sam.Bullard@wellsfargo.com
Nick Bennenbroek	International Economist	212-214-5636	Nicholas.Bennenbroek@wellsfargo.com
Sarah House	Senior Economist	704-410-3282	Sarah.House@wellsfargo.com
Azhar Iqbal	Econometrician	212-214-2029	Azhar.Iqbal@wellsfargo.com
Charlie Dougherty	Senior Economist	212-214-8984	Charles.Dougherty@wellsfargo.com
Michael Pugliese	Senior Economist	212-214-5058	Michael.D.Pugliese@wellsfargo.com
Brendan McKenna	International Economist	212-214-5637	Brendan.Mckenna@wellsfargo.com
Jackie Benson	Economist	704-410-4468	Jackie.Benson@wellsfargo.com
Shannon Grein	Economist	704-410-0369	Shannon.Grein@wellsfargo.com
Nicole Cervi	Economist	704-410-3059	Nicole.Cervi@wellsfargo.com
Delaney Conner	Economic Analyst	704-374-2150	Delaney.Conner@wellsfargo.com
Ali Hajibeigi	Economic Analyst	212-214-8253	Ali.Hajibeigi@wellsfargo.com
Azhin Abdulkarim	Economic Analyst	212-214-5154	Azhin.Abdulkarim@wellsfargo.com
Anagha Sridharan	Economic Analyst	704-410-6212	Anagha.Sridharan@wellsfargo.com
Andrew Thompson	Economic Analyst	704-410-2911	Andrew.L.Thompson@wellsfargo.com
Coren Miller	Administrative Assistant	704-410-6010	Coren.Miller@wellsfargo.com

Required Disclosures