

THE END OF SOVEREIGNTY?

Globalization, nationalism and the implications for institutional investors

Never before in history have people, information and capital moved across borders at the speed, frequency and volume we see today. In PGIM's latest white paper, we take a closer look at the escalating tussle between globalization and nationalism, the implications this could have for global financial markets, and how long-term investors may best position themselves to navigate these uncertain times.

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GLOBALIZATION AT THE SPEED OF LIGHT

70 of the top 100 global "economies" are now multinationals¹

40% of the revenues of firms in the S&P 500 and 50% MSCI Europe Company Sales are from outside the Eurozone.²



Global connectivity has unlocked access to human capital

Interregional migrants have increased by over 50% since 1995³

50%



Cross-border investment assets

Since the 2008 financial crisis, aggregate cross-border capital flows into G20 countries have rebalanced, driving the stock of cross-border financial assets to an all-time peak⁴

20% of GDP in 1835 → **30%** of GDP in 1950 → **~400%** of GDP today⁵

The evolution of multinational firms

Global supply chains account for nearly 80% of global trade and 1 out of 5 jobs⁶



Countries are knit together by a web of digital infrastructure



1.1 million kilometers of undersea internet cables Enough to circle the globe 28 times⁷

THE NATION-STATE STRIKES BACK

The momentum behind global integration and the "borderless" challenges this has created is seen as a threat to state sovereignty – and nation-states are taking a variety of actions to wrest back control.

3 POTENTIAL RESPONSES TO MONITOR

1 A populist backlash in developed markets potentially threatens the agreements global trade is built on

5x Support for populist parties in countries with at least one populist party has increased fivefold since 1965⁸



25% Tariffs directly targeting China imposed by the U.S. on 1,300 items were announced in March 2018⁹

13% Restructuring of H-1B visas representing approximately 13% of all jobs in the U.S. tech industry¹⁰

2 Crackdown on cyberspace and the media

25 Countries have blocked social media communication apps in 2017, including China, Brazil, India, Indonesia and Malaysia¹¹



3 "Carrots-and-sticks" approach to encourage the return of the "local" multinational

\$2tr US Tax Cuts and Jobs Act shifted taxation on accumulated foreign earnings – potentially leading to up to \$2 trillion of repatriated capital¹²

5 KEY INVESTMENT IMPLICATIONS

The escalating tussle between globalization and nationalism could have significant implications for global markets. As a result, institutional investors may want to consider rethinking their investment approach across 5 primary areas.

- 1 Decrease reliance on top-down country-level factors**, which have a diminishing role in driving equity, real estate and corporate debt returns.
- 2 Apply a global framework for all investment decisions**, given the increasing importance of cross-country spillover effects in driving asset prices.
- 3 Ensure developed market political risk is embedded** in in-house and third-party manager investment decisions.
- 4 Position the portfolio** for greater volatility and political uncertainty.
- 5 Recognize that in an era of diminished sovereign influence, asset owners will increasingly be called upon to act as agents of change on global challenges.**

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12. "United States tax act could lead to repatriation of \$2 trillion of overseas investment", United Nations Conference on Trade and Development, February 5, 2018. <<http://unctad.org/en/pages/PressRelease.aspx?OriginalVersionID=447>>

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