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# How the Shifting Landscape of Global Trade May Affect Small Developing Economies

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As tensions in global trade continue to intensify, the world finds itself in a period of strategic recalibration. The ongoing economic rivalry between the United States and China—often referred to as the “trade war”—has evolved far beyond tariffs. It now encompasses strategic decoupling, supply chain reconfiguration, technology bans, export controls, and capital flow restrictions. While these maneuvers are framed as geopolitical chess moves between two superpowers, their consequences ripple far beyond the primary actors, often landing most heavily on smaller, developing economies like Cambodia.

At first glance, a global decoupling of supply chains and the weakening of trade ties between major economies might appear to offer new opportunities for low-income countries. Southeast Asia in particular has seen growing interest as an alternative production hub. However, the reality is more complicated. For economies like Cambodia the disruption of global trade norms presents both opportunities and serious risks.

## The Shifting Center of Gravity

The US-China trade war is not a transient event, but part of a larger structural transition. The United States, along with many of its allies, has grown increasingly wary of deep economic integration with China. Tariffs, export bans, and reshoring incentives are aimed not only at curbing Chinese economic expansion but at realigning the geography of production. China, for its part, is doubling down on domestic industrial policy, emphasizing manufacturing self-reliance and high-tech advancement, while seeking new markets to offset declining demand from the West.

In this process of decoupling, global value chains are being reshuffled. Companies—particularly in electronics, textiles, and automotive components—are moving

operations to lower-cost, politically safer destinations. Vietnam, India, Indonesia, and to a lesser extent, Cambodia, are seeing increased investor interest.

On paper, this is good news for Cambodia. The country offers a young labor force, preferential access to Western markets through trade programs like the EU’s “Everything But Arms” (EBA), and low-cost operating conditions. Indeed, some Chinese manufacturers—especially those in garment and footwear sectors—have relocated or expanded to Cambodia to sidestep US and EU tariffs.

## Fragile Gains, Growing Exposure

Yet these potential benefits mask deeper vulnerabilities. Cambodia’s economic model depends heavily on a narrow export base, mainly garments, footwear, bicycles and food products—products deeply embedded in global value chains and sensitive to disruptions in trade policy. While the relocation of manufacturing may generate short-term gains in employment and foreign exchange, it also exposes Cambodia to the very dynamics reshaping global trade.

For instance, as multinational corporations diversify away from China, they also diversify their risk. Cambodia is increasingly seen not as a standalone investment destination, but as part of a “China+1” strategy—an add-on rather than a replacement. This means that Cambodia’s fortunes remain tied to China’s trade policy and economic performance. If China’s exports to the US are curtailed further or if new sanctions emerge, firms in Cambodia operating as part of Chinese value chains may find themselves cut off from their customers or financing.

Moreover, the trade war has accelerated protectionist sentiment in many parts of the world. The United States and the European Union are reconsidering their support for trade preference programs, often citing labor rights, governance, or environmental concerns. Cambodia has already faced partial suspension of its EBA privileges due to human rights concerns. If geopolitical tensions

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continue to rise, countries like Cambodia—perceived as politically aligned with China or lacking leverage in Western diplomacy—could find themselves further marginalized.

### **The Demand Constraint**

At a more structural level, the trade war reflects a broader deficiency in global demand. One reason for the imbalance in global trade is the persistent excess of savings over investment in surplus economies like China, Germany, and Japan. These countries rely heavily on manufacturing-driven growth and run large trade surpluses. Their surplus savings, if not absorbed by productive investment elsewhere, exert downward pressure on global demand.

In the best-case scenario, these surplus savings are directed toward investment in capital-scarce developing economies, helping to fund infrastructure and industrial capacity. However, this requires that the recipient economies—like Cambodia—have the ability to absorb investment productively, manage debt, and sustain rising consumption.

Unfortunately, the current wave of investment in countries like Cambodia is largely geared toward low-wage, low-value-added manufacturing—hardly the kind of transformative, consumption-boosting investment needed to rebalance global demand. Without strong domestic policies that promote wage growth, education, and productivity, these investments risk entrenching a race-to-the-bottom model where development is shallow and vulnerable to external shocks.

### **Financial Fragility and Dollar Dependence**

Another looming risk is financial. As global capital flows shift in response to trade realignment, developing economies often become more exposed to volatile foreign financing. Cambodia is no exception. While the country has benefited from Chinese investment, this has come largely in the form of infrastructure loans and real estate speculation, which may not be sustainable. At the same time, the country remains heavily dollarized, which limits the government's ability to conduct independent monetary policy.

As the trade war depresses global growth and increases volatility in capital markets, small economies like Cambodia may face sudden stops in investment, currency instability, or rising debt burdens. If demand in the West contracts sharply or if global interest rates remain elevated, countries reliant on external capital to finance development could face painful adjustments.

### **The Way Forward**

What can Cambodia—and countries like it—do to mitigate these risks?

First, diversification is key. Cambodia must move beyond garment exports and develop a broader industrial base that includes higher value-added sectors. This requires investment in education, logistics, and institutional quality.

Second, policy autonomy matters. Countries need stronger fiscal tools to support domestic demand and manage external shocks. Reducing dependence on foreign currencies and building credible financial institutions are long-term priorities.

Third, global governance frameworks must be more inclusive. As major economies reshape trade and investment flows, the interests of smaller developing countries must not be overlooked. Institutions like the WTO, IMF, and regional development banks should ensure that these countries are supported—not penalized—during a period of transition.

Finally, the trade war is not a temporary storm to weather—it is a systemic realignment of global economics. For countries like Cambodia, the challenge is not simply to adapt temporarily to shifting trade winds, but to seize the moment to build a more resilient, inclusive, and sustainable growth model.

In sum, the trade war may open doors for smaller economies, but it also presents complex risks. Without thoughtful policy, these opportunities could quickly turn into vulnerabilities. For Cambodia and others, the real challenge is to shape their positions within the new global trade order before it shapes them.