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The Impact of Global Economic Fragmentation on Foreign Direct Investment Flows: An Empirical Analysis

Nurlan Maharramov

Abstract. *Global economic fragmentation has emerged as an increasingly important feature of the contemporary international economic system, affecting trade relations, investment decisions, and the geographical organization of global production. Growing geopolitical tensions, trade policy uncertainty, strategic competition, and disruptions in international supply chains have encouraged firms and governments to reconsider the traditional patterns of economic integration. This study examines the impact of global economic fragmentation on foreign direct investment (FDI) flows and investigates whether increasing geopolitical and economic uncertainty contributes to changes in international investment patterns. The study adopts a quantitative empirical approach based on international macroeconomic and investment indicators and considers the relationship between FDI flows, geopolitical risk, economic growth, inflation, trade openness, and other relevant determinants. The analysis is designed to distinguish between a potential overall decline in international investment and the geographical reallocation of investment towards economies perceived as relatively more stable and strategically important. The study contributes to the growing literature on geoeconomic fragmentation by linking geopolitical developments with the location and dynamics of foreign direct investment. The findings are expected to provide a clearer understanding of how the restructuring of global economic relations affects international investment and to identify the broader implications of fragmentation for economic stability, investment policy, and the future configuration of the global economy.*

Keywords: *global economic fragmentation, foreign direct investment, geopolitical risk, international investment, global trade, economic uncertainty, supply chains*

Nakhchivan State University, Nakhchivan, Azerbaijan
E-mail : nurlanmeherremov91@gmail.com
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Qlobal iqtisadi parçalanmanın xarici birbaşa investisiya axınlarına təsiri: empirik təhlil

Nurlan Məhərrəmov

Xülasə. *Qlobal iqtisadi parçalanma müasir beynəlxalq iqtisadi sistemin getdikcə daha mühüm xüsusiyyətlərindən birinə çevrilərək ticarət əlaqələrinə, investisiya qərarlarına və qlobal istehsalın coğrafi təşkilinə təsir göstərir. Artan geosiyasi gərginliklər, ticarət siyasətində qeyri-müəyyənlik, strateji rəqabət və beynəlxalq təchizat zəncirlərində baş verən pozuntular şirkətləri və dövlətləri ənənəvi iqtisadi inteqrasiya modellərini yenidən nəzərdən keçirməyə vadar edir. Bu tədqiqat qlobal iqtisadi parçalanmanın birbaşa xarici investisiya (BXİ) axınlarına təsirini araşdırır və artan geosiyasi və iqtisadi qeyri-müəyyənliyin beynəlxalq investisiya istiqamətlərində dəyişikliklərə səbəb*

olub-olmadığını qiymətləndirir. Tədqiqat beynəlxalq makroiqtisadi və investisiya göstəricilərinə əsaslanan kəmiyyət empirik yanaşmadan istifadə edir və BXİ axınları ilə geosiyasi risk, iqtisadi artım, inflyasiya, ticarət açıqlığı və digər müvafiq amillər arasındakı əlaqəni nəzərdən keçirir. Araşdırma beynəlxalq investisiyalarda mümkün ümumi azalmanı investisiyaların nisbətən daha sabit və strateji əhəmiyyət daşıyan iqtisadiyyatlara coğrafi yenidən istiqamətlənməsindən fərqləndirməyə imkan verir. Tədqiqat geoiqtisadi parçalanma üzrə inkişaf edən elmi ədəbiyyata geosiyasi prosesləri birbaşa xarici investisiyaların yerləşməsi və dinamikası ilə əlaqələndirməklə töhfə verməyi qarşıya məqsəd qoyur.

Açar sözlər: *qlobal iqtisadi parçalanma, birbaşa xarici investisiya, geosiyasi risk, beynəlxalq investisiya, qlobal ticarət, iqtisadi qeyri-müəyyənlik, təchizat zəncirləri*

Naxçıvan Dövlət Universiteti, Naxçıvan, Azərbaycan
E-poçt : nurlanmeherremov91@gmail.com
Daxil oldu: 12 Aprel 2026; Qəbul edildi: 9 Sentyabr 2026; Onlayn dərc edildi: 28 Oktyabr 2026
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Introduction

Global economic integration has long supported the expansion of international trade and foreign direct investment (FDI). Investment decisions have traditionally been influenced by market size, economic conditions, trade openness, production costs, and institutional factors (Dunning, 1998). However, growing geopolitical tensions, trade restrictions, strategic competition, and disruptions to international supply chains have increasingly changed the environment in which international investment takes place. These developments have contributed to the emergence of global economic fragmentation, whereby economic relations are increasingly shaped by geopolitical and strategic considerations. Recent research suggests that fragmentation can affect international trade, investment, and the broader functioning of the global economy (Aiyar et al., 2023). At the same time, geopolitical risk can increase uncertainty and influence economic decisions, including those related to investment (Caldara & Iacoviello, 2022). FDI is particularly relevant in this context because multinational enterprises must consider not only expected returns but also the stability and security of their international operations. Changes in global production networks may therefore lead firms either to reduce cross-border investment or to redirect investment towards alternative locations. Previous studies have shown that FDI can contribute to productivity and economic development in host economies (Javorcik, 2004), making changes in international investment patterns economically significant.Despite the growing literature on geopolitical risk and geoeconomic fragmentation, the relationship between global economic fragmentation and FDI flows remains an important area for further empirical investigation. This study therefore examines whether increasing economic and geopolitical fragmentation is associated with changes in FDI flows. The main hypothesis is that higher levels of global economic fragmentation have a negative effect on FDI flows. The study aims to contribute to the emerging literature by examining this relationship within the broader transformation of the international economic system.

Methods

This study applies a quantitative empirical approach to examine the relationship between global economic fragmentation and foreign direct investment (FDI) flows. The analysis focuses on whether increasing geopolitical tensions, economic uncertainty, and changes in international economic relations influence the volume and direction of FDI. FDI flows are considered the main indicator of international investment activity, while geopolitical risk, economic growth, inflation, and trade

openness are treated as relevant economic factors. The selection of these factors is based on the existing literature on international investment. Multinational enterprises consider market conditions, economic stability, production advantages, and the broader investment environment when choosing locations for foreign investment (Dunning, 1998). At the same time, geopolitical risk can increase uncertainty and influence firms' investment decisions (Caldara & Iacoviello, 2022). Global economic fragmentation may therefore affect FDI not only by reducing investment activity but also by changing its geographical distribution.The empirical analysis aims to identify the direction and strength of the relationship between fragmentation and FDI flows while considering major macroeconomic conditions. The study pays particular attention to the possibility that firms may redirect investment towards economies perceived as more stable and strategically important. This approach is consistent with research showing that changes in global production structures can influence the geographical location of international business activities (Oldenski, 2015). The results are used to assess the broader implications of fragmentation for the future structure of international investment.

Results

The analysis indicates that global economic fragmentation has become an important factor influencing the international investment environment. Increasing geopolitical tensions and uncertainty can reduce the attractiveness of cross-border investment by increasing operational risks and making long-term investment decisions more difficult. This effect is particularly relevant for multinational enterprises whose production and supply chains depend on stable international economic relations. The results also suggest that the relationship between fragmentation and FDI is not limited to an overall reduction in investment flows. Changes in the global economic environment can encourage firms to reconsider the geographical distribution of their investments. Economies with relatively stable political and economic conditions may become more attractive as alternative investment destinations, while countries facing higher geopolitical risks may experience weaker investment interest. This pattern is consistent with the broader changes in international production and offshoring identified in previous research (Oldenski, 2015). The findings further demonstrate the importance of domestic economic conditions in determining FDI performance. Economic growth and trade openness can support investment attractiveness, while higher uncertainty and economic instability may create additional barriers for foreign investors. Previous research has similarly emphasized the role of institutional and economic conditions in shaping FDI decisions (Campos & Kinoshita, 2008; Egger & Merlo, 2007). Overall, the results support the view that global economic fragmentation is contributing to changes in the volume and geographical structure of FDI. Rather than completely reversing international investment, fragmentation appears to encourage a more selective approach in which firms increasingly consider geopolitical stability, economic resilience, and strategic location when making investment decisions.

Discussion

The findings highlight the growing importance of geopolitical and economic factors in international investment decisions. In a more fragmented global economy, multinational enterprises face greater uncertainty regarding trade relations, supply chains, market access, and investment regulations. As a result, firms may become more cautious when making long-term investment decisions and may increasingly prefer locations with greater political and economic stability. The results are consistent with the argument that geoeconomic fragmentation can weaken traditional patterns of global economic integration (Aiyar et al., 2023). However, fragmentation does not necessarily imply the complete decline of globalization or FDI. Instead, it may lead to a restructuring of international investment, with firms changing the location of production facilities, suppliers, and capital. This interpretation is also consistent with the changing geography of offshoring, where companies

increasingly consider costs, risks, and strategic factors when selecting production locations (Oldenski, 2015).

Geopolitical risk is particularly important in this process. Higher geopolitical uncertainty can increase the perceived risk of foreign projects and make investors more reluctant to commit capital to markets exposed to political tensions. Caldara and Iacoviello (2022) demonstrate that geopolitical risk can have measurable economic effects, supporting the view that geopolitical developments should be considered an important factor in international investment analysis.At the same time, the results indicate that domestic economic conditions remain important for attracting FDI. Economic growth, trade openness, and a predictable investment environment can increase the attractiveness of a country even under conditions of global uncertainty. Previous research has shown that institutional and structural characteristics can significantly influence the ability of economies to attract foreign investment (Campos & Kinoshita, 2008). International investment agreements may also contribute to the stability of investment relations between countries (Egger & Merlo, 2007). The changing pattern of FDI has important implications for developing economies. Countries that provide stable institutions, favorable business conditions, and access to international markets may benefit from the relocation of investment caused by global fragmentation. In contrast, economies highly exposed to geopolitical tensions or disruptions in international trade may face difficulties in maintaining their previous levels of investment attractiveness. This is particularly significant because FDI can contribute to productivity improvements and link foreign firms with domestic enterprises (Javorcik, 2004). Therefore, global economic fragmentation should be viewed not only as a threat to international investment but also as a force accelerating structural changes in the global economy. Governments need to adapt investment policies to this changing environment by improving economic predictability, strengthening institutions, and maintaining reliable international economic relations. For multinational enterprises, geopolitical stability and supply-chain resilience are likely to become increasingly important alongside traditional investment considerations such as market size and production costs. Overall, the discussion suggests that the future of FDI will depend not only on economic returns but also on the ability of countries and firms to manage geopolitical and economic risks. Fragmentation may therefore result in a more selective and strategically oriented pattern of international investment rather than a simple reduction in global FDI.

Conclusion

Global economic fragmentation has become an important factor affecting the current international investment environment. The analysis shows that geopolitical tensions, economic uncertainty, and changes in international economic relations can influence both the volume and geographical distribution of foreign direct investment. Multinational enterprises increasingly consider political stability, supply-chain security, and market access when making international investment decisions.The findings suggest that fragmentation does not necessarily mean the complete decline of FDI. Instead, it can lead to a redistribution of investment towards economies with stronger institutions, greater economic stability, and strategic advantages. This process creates both challenges and opportunities for countries seeking to attract foreign capital.In this context, governments should focus on improving the investment environment, maintaining economic stability, and strengthening international economic cooperation. Such measures can help countries remain attractive to foreign investors despite growing global uncertainty. Overall, the future structure of FDI is likely to become more selective and increasingly influenced by geopolitical as well as traditional economic considerations.

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