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Strategic FDI responses to geopolitical uncertainty

International Business
Bachelor's thesis

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Bachelor's thesis**Subject:** International Business**Author:** Annika Rönkkö**Title:** Strategic FDI responses to geopolitical uncertainty**Supervisor:** D.Sc. Johanna Raitis**Number of pages:** 29 pages +1**Date:** 25.5.2026**Abstract**

The international business landscape has changed significantly over the past decade. A sequence of major geopolitical shocks, namely Brexit, the US–China trade war, the COVID-19 pandemic, and Russia's invasion of Ukraine, has collectively weakened global economic integration and increased uncertainty in the international investment environment. This thesis examines how growing geopolitical uncertainty reshapes the foreign direct investment (FDI) environment and the strategies multinational enterprises (MNEs) use to navigate it.

The geopolitical shocks of the past decade have accelerated protectionism and geoeconomic fragmentation, driving a decline in global FDI flows and eroding the rules-based international trading system. In response, MNEs have adopted three key strategies. First, foreign divestment has increased significantly, and is increasingly treated as a proactive strategic tool rather than a sign of failure. Second, MNEs are reallocating investments through reshoring and nearshoring to reduce supply chain vulnerability. Third, and most notably, friendshoring has emerged as an increasingly significant reallocation strategy, redirecting investments toward geopolitically trusted nations rather than simply shortening supply chains.

The central finding of this thesis is that geopolitical uncertainty has not only reduced global investment flows but also fragmented them. Geopolitical alignment has overtaken geographic distance as a key driver of investment decisions, with FDI between geopolitically aligned countries now being more than twice as likely as without geopolitical considerations. As a result, MNEs have shifted from efficiency-driven strategies toward strategies that prioritize resilience and geopolitical security.

Keywords: geopolitical uncertainty, foreign direct investment, geoeconomic fragmentation, friendshoring

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Tiivistelmä

Kansainvälisen liiketoiminnan toimintaympäristö on muuttunut merkittävästi viimeisen vuosikymmenen aikana. Merkittävät geopoliittiset shokit, Brexit, Yhdysvaltain ja Kiinan välinen kauppasota, COVID-19 pandemia sekä Venäjän hyökkäys Ukrainaan, ovat yhdessä heikentäneet globaalia taloudellista integraatiota ja lisänneet epävarmuutta kansainvälisten investointien toimintaympäristössä. Tässä tutkielmassa tarkastellaan, miten kasvava geopoliittinen epävarmuus muuttaa ulkomaisten suorien investointien (FDI) ympäristöä sekä strategioita, joilla monikansalliset yritykset vastaavat tähän muutokseen.

Nämä shokit ovat kiihdyttäneet protektionismia ja geotaloudellista pirstoutumista, vähentäneet globaaleja FDI virtoja sekä horjuttaneet sääntöpohjaista kansainvälistä kauppajärjestelmää. Vastauksena tähän monikansalliset yritykset ovat omaksuneet kolme keskeistä investointistrategiaa. Ulkomaiset divestoinnit ovat lisääntyneet merkittävästi, ja niitä käytetään yhä enemmän proaktiivisena strategiana eikä epäonnistumisena. Samalla yritykset uudelleensijoittavat investointejaan reshoring- ja nearshoring-strategioiden avulla toimitusketjunsä haavoittuvuuden vähentämiseksi. Erityisen keskeisenä strategiana friendshoring suuntaa investointeja geopoliittisesti luotettaviin maihin toimitusketjunsä lyhentämisen sijaan.

Tutkielman keskeisin löydös on, että geopoliittinen epävarmuus ei ole ainoastaan johtanut globaalien investointien vähentymiseen vaan myös ennen kaikkea niiden pirstaloitumiseen. Geopoliittinen linjautuminen on syrjäyttänyt maantieteellisen etäisyyden keskeisenä FDI-päätöksiä ohjaavana tekijänä, ja investoinnit geopoliittisesti linjautuneiden maiden välillä ovat yli kaksi kertaa todennäköisempiä kuin ne olisivat ilman geopoliittisiä tekijöitä. Tämän seurauksena monikansalliset yritykset priorisoivat kriisinkestävyyttä ja geopoliittista turvallisuutta yhä enemmän kuin kustannustehokkuutta.

Avainsanat: geopoliittinen epävarmuus, suorat ulkomaiset investoinnit, geotaloudellinen pirstaloituminen, friendshoring

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1 Introduction

Over the past decade, the landscape of international business has undergone a fundamental shift. United Nations Conference on Trade and Development described the beginning of the 2020s as “a perfect storm” for global order and business (UNCTAD 2020, 120-121). We have seen a pandemic, many disruptions in the global value chain, wars and other conflicts, and a slowdown in global economic integration marked by trade wars and rising economic nationalism (Ahn et al. 2023, 91; Contractor et al. 2025, 1, 3).

These geopolitical uncertainties have contributed to the drop of global FDI flows as demonstrated in Figure 1. These flows have experienced major volatility in the recent decade, with the steepest drop in 2020. This represents a decrease of 35% from 2019, dropping nearly 20% lower than during the 2009 financial crisis. This continued an existing downward trend in which global flows had already declined by 25% from their latest peak in 2015. In 2021 investment flows rose sharply but then fell again by 12% in 2022 and by 11% in 2024, showing a steady decline in global investment flows. (UNCTAD, 2020, 11; 2021, 10; 2022, 2; 2023, 3; 2025, 7.) Rising geopolitical uncertainty and protectionism are weakening investor confidence resulting in the restructuring of the global investment landscape (Contractor et al. 2025, 1).

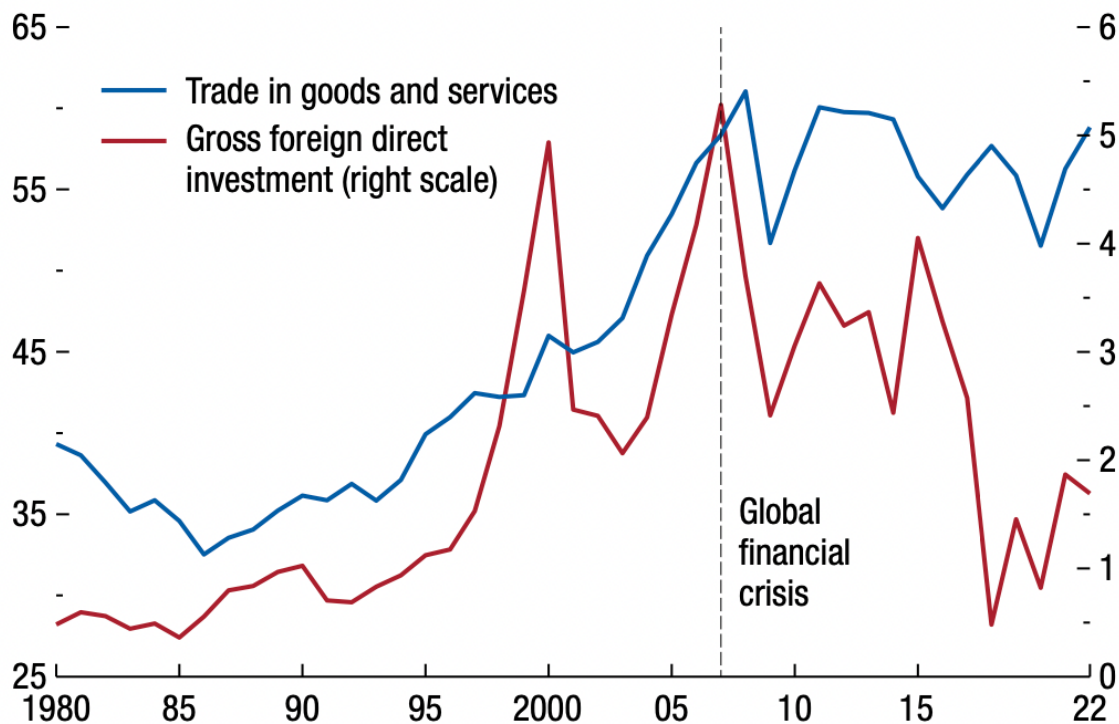


Figure 1 FDI declines with geopolitical shocks (% of GDP) (Ahn et al. 2023, 92)

As shown in Figure 1, the FDI flows have recovered gradually from the 2020 drop, but the investment landscape has transformed in the process. For so long multinational enterprises (MNEs) have sought cost reduction and efficiency from their foreign direct investments (FDI), often located in developing markets with economical labor and production costs. However, in the recent years we have seen a change in the foreign investment motives and strategies. (Nguyễn 2023, 14574-14576; Contractor et al. 2025, 1.) The era of efficient globalization has been replaced by security-oriented business strategies (Contractor et al. 2025, 1). Multinational enterprises have to navigate this complex business environment, evidently leading to changes in their strategies and priorities (Nguyễn 2023, 14574).

These themes have become more relevant than ever in today's volatile global landscape. In 2026 both the World Economic Forum and the Munich Security Conference affirmed that the traditional rules-based international order has shifted toward a highly competitive and fragmented world (Bostenaru 2026; World Economic Forum 2026). Today, geoeconomic confrontation and armed conflicts, particularly in Ukraine, have become the primary drivers of global risk, leading to disruptions in the global economy, increased protectionism and the weaponization of economic tools (World Economic Forum 2026).

Antràs (2020) suggests that the current shift in the FDI environment can be mirrored to previous historical periods of deglobalization. This shows that the current unraveling of global relations is not an isolated event, on the contrary, it can be seen as a repeating pattern, which helps to better anticipate the long-term consequences of this shift. The Interwar Period of the 20th century provides the most relevant historical comparison, as it was characterized by a transition from global integration to a turbulent and fragmented world. The similarities to today are clear. Much like the Interwar Period, the 2020s have been shaped by a global pandemic and severe economic disruptions. This pattern suggests that vast disruptions to global order and economic stability leads to distrust and a reduction in economic integration.

Foreign direct investments are a key part of international business and they have traditionally been widely studied, especially the firm-level factors (Sethuram & Gaur 2024, 1038, 1042). However, the external factors, such as geopolitical factors, are still understudied according to many IB scholars. (Nguyễn 2023, 14562; Yu & Wang 2023, 2.) As geopolitical factors are increasingly affecting the global investment landscape (Yu & Wang 2023, 1), it is extremely important to study their effects on a major part of international business, FDI's.

The aim of this thesis is to examine how increasing geopolitical uncertainty reshapes the foreign direct investment (FDI) environment and the strategies behind investment decisions.

To address this aim, the following sub-questions will be discussed:

- How has growing geopolitical uncertainty changed the FDI environment?
- How do MNEs strategically respond to this transformed environment?

These sub-questions provide a structure for the thesis. Chapter 2 discusses how geopolitical uncertainty has transformed the global FDI environment, focusing first on the key shocks and drivers of this change and then on describing the changed environment, especially on the rise of geopolitically driven protectionism. Chapter 3 examines how multinational enterprises respond to this transformed environment. It first analyzes market exits and foreign divestments driven by the change in the environment, and then explores how MNEs reallocate investments through strategies such as reshoring, nearshoring, and especially friendshoring.

2 The changing FDI landscape under geopolitical uncertainty

2.1 Key geopolitical shocks driving the change

The global investment landscape has witnessed a significant transformation during the past decade. Major geopolitical events, especially Brexit, US–China trade war, the COVID-19 pandemic and Russia's invasion of Ukraine, have acted as drivers of this change fundamentally reforming the global business environment (Yu & Wang, 2023, 1; Contractor et al. 2025, 3).

2.1.1 Brexit

The United Kingdom's withdrawal from the European Union and shift in U.S. trade policy following President Trump's election in 2016 can be seen as some of the first significant turning points in the international business environment since the 2008 financial crisis (Contractor et al. 2025, 3). The UK's decision to leave the European Union in 2016, also known as Brexit, was a major shock that caught global markets by surprise as most polls predicted the UK to stay. However, when the final vote on 23rd of June in referendum turned on behalf of leaving, the surprise outcome created uncertainty for international business. The surprise result in the referendum was largely driven by the bold promises of the "Vote Leave campaign". (Hassan et al. 2023, 435.) The Leave campaign's slogan "Take Back Control" was rooted in a perceived loss of sovereignty, which resonated particularly strongly in a country with Britain's imperial history (Bachmann & Sidaway 2016, 48). It was based on confident promises of regulatory freedom, reduction of government expenses, and the unprecedented ease of the trade negotiations with the EU. (Hassan et al. 2023, 435).

However, in practice, these promises proved to be largely unrealistic. Instead of a quick or easy separation, Brexit increased uncertainty for firms all over the world (Hill et al. 2019, 58). The risks were most severe for firms with close geographic and trade links to the UK. Unsurprisingly, British and Irish firms faced the highest levels of risk, but EU members, such as the Netherlands, Denmark, and Belgium were also affected significantly. Even beyond Europe, highly linked economies, like the United States and Australia, experienced elevated uncertainty. (Hassan et al. 2024, 424–425.) The impact was particularly strong for larger companies that are more vulnerable to political uncertainty, like those highly dependent on global supply chains, those operating in highly regulated sectors, and firms with greater investment opportunities. These firms experienced significant negative effects on their growth and investment decisions. (Hill et al. 2019, 59; Hassan et al. 2024, 455.)

The effects were high even prior to the UK's formal withdrawal in January 2020, as Brexit affected firm behaviour primarily through heightened uncertainty rather than through concrete changes. Firms' decisions were thus driven more by the anticipation of risk than by its actual realization. As more information about the conditions of the UK's withdrawal became available, the focus shifted increasingly toward potential supply chain disruptions. (Hassan et al. 2024, 416, 424–426.) As a result, Brexit set a precedent of a growing trend where nations increasingly prefer national sovereignty over the benefits of economical and regional integration, such as the EU (Contractor et al. 2025, 3).

2.1.2 US–China Trade war

The trade conflict between the United States and China originated on March 22, 2018, when the United States imposed tariffs on Chinese imports. According to the Trump administration this move was driven by questions over intellectual property and trade secrets as well as concerns over the Chinese government support for domestic companies. The United States viewed these policies as unfair as they gave Chinese industries unjust advantages in the global market. (Peng et al. 2025, 1678.) Between 2018 and 2019, the conflict escalated through three major rounds of reciprocal tariffs, resulting in a sharp increase in tariff levels, for example the average tariff on Chinese imports rose from 2.6% to 16.6% (Peng et al. 2025, 1678; Fajgelbaum et al. 2020, 2). They targeted a wide range of goods, including steel, aluminum, and crude oil, collectively affecting around 450 billion U.S dollars worth of trade (Fajgelbaum et al. 2024, 295; Peng et al. 2025, 1678). Coincidentally, global FDI inflows declined by 13 percent in the same year (Nguyễn 2023, 14567).

In early 2020, the "Phase One" trade agreement was signed, and the next round of tariffs were cancelled. While the agreement prevented further escalation and led to the removal of most tariffs, the tensions between the two superpowers continued. This tension transformed into technological competition, as the US introduced strict export restrictions on semiconductors and other strategic technologies, later maintained and expanded by the Biden administration. These measures were also intended to decouple strategic supply chains from China, for example through alliances with other major Asian markets. (Ahn et al. 2023, 107–108.) Similar measures have been adopted across other major economies as well, including the EU and China (Kim et al. 2021, 211; Ahn et al. 2023, 108).

At the same time, the US began to erode the rules-based international trading system (Mariotti 2023, 232). By obstructing new appointments to the WTO Appellate Body, the US left the organization without a functioning mechanism to resolve trade disputes, whilst WTO also ruled several of

its trade actions inconsistent with international trade rules by the WTO (Ahn et al. 2023, 108). The trade war diminished the previously thriving trend of lowering barriers in cross-border business, catalyzing deglobalization (Fajgelbaum et al. 2024, 295). A WTO analysis confirms that the resulting rise in policy uncertainty led to substantial reductions in both exports and investment between the two countries (Ahn & Lee 2021, 182).

These trade tensions are still visible today, as the global investment landscape remains defined by tariffs and high policy uncertainty (Contractor et al. 2025, 9). In 2025, the US significantly expanded these measures, applying a baseline 10 percent tariff to numerous countries and even more to China. These ongoing negotiations and the resulting instability are forcing firms to constantly adjust their international trade strategies. (UNCTAD 2025, 14.)

2.1.3 Covid-19 pandemic

In early 2020, the international business environment faced a third major shock, the Covid-19 pandemic. The outbreak began in China in late 2019 and already by March 2020 it had been officially declared as a pandemic (Antràs 2020, 38–39). According to Gereffi (2020) the pandemic stood out as an exceptionally powerful shock that acted as a wakeup call to the fragility of pre-pandemic global value chains (GVCs), which had become heavily concentrated in only some parts of the world, particularly China (Gereffi et al. 2021, 514–516; Niu et al. 2025, 1025; Gopalan & Reddy 2025, 2360).

As governments responded by shutting down borders and implementing protective measures, it exposed the vulnerability of this concentration leading to severe disruptions in global integration and supply chains (Bellucci & Rungi 2023, 978). This led to a pause in economic activity in most of the world's key economies for months, resulting in a drastic drop in global FDI flows and a sharp rise in unemployment and public debt (Nguyễn 2023, 14567–14568; Gereffi 2020, 288). Unlike previous disruptions, which had usually been limited to certain suppliers or regions, the pandemic affected essentially the entire global supply base at once, leaving firms with almost no alternative sourcing options as lockdowns spread across the world (Niu et al. 2025, 1029).

In addition, many other logistical bottlenecks and disruptions occurred at the time, including the Suez Canal blockage and the container crises, causing critical shortages further enflamed by surging inflation (Niu et al. 2025, 1026). The severe semiconductor shortage also illustrated how easily highly concentrated production can be paralyzed (Lan et al. 2022, 102.). These disruptions collectively forced firms to re-evaluate the vulnerabilities of their value chains (Ahn & Lee 2021, 182).

The consequences were visible. For example, in the US, UK, Germany, Italy and France, 94 percent of companies reported pandemic related supply chain disruptions, with approximately 20 percent reporting severe disruptions. These disruptions were not distributed evenly across industries, with critical sectors being hit the hardest. (Allianz Research 2020, 4). Global FDI flows were also affected, declining by almost 20 percent between 2020 and 2022 compared to the pre-pandemic time (Ahn et al. 2023, 95). In addition, the pandemic exposed acute vulnerabilities in global health security, as the production of some crucial equipment, such as face masks, had become heavily concentrated in China, leading to critical shortages during a pandemic (Gereffi 2020, 293). The pandemic also exposed institutional vulnerabilities. The US withdrew from the WHO at the height of the crisis, and China failed to co-operate sufficiently and share critical information, complicating the efforts to implement preventive global measures in time (Kornprobst & Paul 2021, 1312).

2.1.4 The Russia–Ukraine war

As the global economy was still recovering from the pandemic, the world was shaken by another geopolitical shock as Russia invaded Ukraine on 24th of February 2022 (Deberge 2023, 1). This conflict greatly impacted the global business environment by driving up oil and food prices, which consequently increased operating costs for firms and reduced the purchasing power of affected markets (Nguyễn 2023, 14568). The destruction of critical infrastructure, including the Nord Stream gas pipeline and the Crimean bridge, further heightened geopolitical uncertainty and disrupted supply chains (Yu & Wang 2023, 1; Niu et al. 2025, 1026).

Beyond the immediate armed conflict, the invasion also triggered a wave of "economic warfare", such as the extensive Western sanctions and Russian countersanctions that complicated the operations of multinational companies (DeBerge 2023, 1). For instance, by 2023 the over 40 countries, mostly in the EU and G7 members, had already implemented several sanction packages, steadily raising the cost and risk of doing business in Russia (Evenett & Pisani 2023, 512, 514)

The war has also redirected FDI. While the risk of investments has considerably increased in the directly affected regions, FDI has also increasingly shifted toward securing critical industries, such as food and renewable energy. (Nguyễn 2023, 14568.). This ongoing conflict is still creating uncertainty for the political and economic environment today (Bostenaru 2026).

2.2 The rise of protectionism and geoeconomic fragmentation

Together, these geopolitical shocks have driven a resurgence of protectionism and economic nationalism, challenged the international order and driven a shift toward deglobalization and geoeconomic

fragmentation (Ahn et al. 2023, 91; Yu & Wang 2023, 1). According to Mariotti (2023), this current era of protectionism was triggered by the 2008 financial crisis and fueled by series of geopolitical shocks since then. A newer term, global protectionism, has been coined to describe protectionism in the 21st century. It extends beyond traditional trade barriers, such as tariffs, to include for example FDI, offshoring and the movement of capital and people. Relatedly, economic nationalism is a broader concept in which countries use their economies to promote domestic interests and strengthen their geopolitical position through more than solely defensive ways. (Enderwick 2011, 326; Mariotti 2023, 231–232.) Protectionism can thus be seen as one of the instruments within economic nationalism.

The UK's withdrawal from the EU proved to be an early sign of this trend (Contractor et al. 2025, 3). The desire to reassert national control that had driven Brexit was also visible in the rise of Trump's support in the US and the revival of right-wing parties across Europe and other advanced economies (Bachmann & Sidaway 2016, 48). As a result, economic nationalism gained popularity across the world, for example in Turkey, Hungary, the United States, and China (Contractor et al. 2025, 3). The pandemic fueled this trend even further, as lockdowns pushed governments to turn inward and adopt increasingly protective measures (Nguyễn 2023, 14562).

A good example of such economic nationalism is Donald Trump's "America First" ideology and the protectionist policies that accompanied it, such as the Tax Cuts and Jobs Act (TCJA), the Creating Helpful Incentives to Produce Semiconductors (CHIPS) Act and the America First Investment Policy, which encouraged domestic production and reshoring of supply chains (Nguyễn 2023, 14565–14567; UNCTAD 2025, 15). The Biden administration continued along the same path by forming strategic alliances with, for example, the EU, Japan, the UK, and Australia, aiming to create economically integrated blocs among key allies. Similarly, the EU pushed for the European CHIPS acts, while China also started to reduce its dependence on foreign markets by prioritizing domestic markets and regional supply chains. Thereby, countries have started dismantling the trade regulations originally built to enable global integration, replacing them with policies that prioritize national security (Ahn & Lee 2021, 182; Ahn et al. 2023, 92; Aiyar et al. 2024, 2.)

Deepened supply chain and national security concerns have driven governments, especially in developed economies, to implement stricter FDI screening in sectors perceived as important for national and economical security (Contractor et al. 2025, 4; UNCTAD 2025, 96). For instance, the US

has tightened investment screening and implemented so called “Outbound Rules” to limit investment flows to “countries of concern”, like China. Similarly, the EU has implemented member-state screening for critical technologies including AI and semiconductors. (Contractor et al. 2025, 4.)

This new rise of protectionism has further accelerated deglobalization and geoeconomic fragmentation, referring to a decline in global economic integration (Ahn et al. 2023, 91; Peng et al. 2025, 1676). The erosion of the rules-based trading system reinforced this shift. As multilateral institutions, like WTO, faced growing legitimacy challenges and international cooperation trembled during the pandemic, countries increasingly turned toward unilateralism, in addition, the IMF and the World Bank also faced growing disagreements over governance and conditionality, with China promoting alternative global institutions in response. (Mariotti 2023, 232; Kornprobst & Paul 2021, 1312.) The pandemic further exposed the fragility of multilateral cooperation, as Chinas actions and the US withdrawal from the WHO weakened the international co-operation at a critical moment (Kornprobst & Paul 2021, 1312). Together, these developments made the international investment environment significantly less predictable, increasing uncertainty and erosion of global co-operation (Contractor et al. 2025, 2).

As a result, global value chains are steadily becoming more regional and fragmented (Yücesan 2025, 2). For example, during the pandemic, firms responded to the heightened uncertainty by expanding their supplier networks (Niu et al. 2025, 1029). As a result, FDI has become more fragmented as well with protectionist policies deepening deglobalization (Kornprobst & Paul 2021, 1306, 1311). This has long-lasting consequences, with some estimates suggesting that sustained fragmentation could reduce global output by as much as 2 percent (Aiyar et al. 2024, 11; Ahn et al. 2023, 94).

However, the extent of deglobalization remains debated. While these tensions have clearly driven a reorganization of global flows, Fajgelbaum et al. (2024) note that several third-party countries, such as Vietnam, actually increased their exports in tariff-targeted products, suggesting that the US–China trade war acted more as a driver toward global reorganization rather than true deglobalization. Similarly, Freund et al. (2024) suggest that deglobalization had not been reached yet, at least as of 2022, as US imports remained nearly 40 percent above pre-pandemic levels. Views on the extent of global uncoupling remain divided as well, with some researchers arguing that the depth of global economic interdependence makes a full disintegration unlikely (Ahn & Lee, 2021, 182).

3 MNE responses to the transformed environment

This shift in international business environment has made investors more cautious making geopolitical aspects an increasingly central part of FDI strategies (Ahn et al. 2023, 97). Now, companies are increasingly prioritizing geopolitical considerations over than mere cost-efficiency leading to a shift in the allocation of foreign direct investment (Nguyễn 2023, 14562; Deng et al. 2025, 2).

3.1 Foreign divestment as a strategic response to geopolitical risk

There are multiple conflicting definitions of foreign divestment (FD) in IB literature and hence Sethuram & Gaur (2024) have suggested broader and more comprehensive definition: “the voluntary or forced reversal or undoing of the initial FDI decision, whether this is partial or complete, and a de-merger or de-investment.”. The exit strategies range from total withdrawals from the market to more subtle approaches, partial exits. Partial exits, for example reducing or freezing operations in the host country, allow a company to maintain some operations or the possibility for re-entering the market while simultaneously reducing the risk. (Dai et al. 2023, 1093; DeBerge 2023, 2.) In a total withdrawal, the firm ceases all operations in the host country (Meyer & Estrin 2023, 4.) Choosing between these strategies depends on whether the company wants to keep the option of returning later or if it needs to withdraw immediately to minimize risks. For example, in response to the Russia-Ukraine war, firms exited Russia in varying degrees from total withdrawal to only delaying new operations (DeBerge 2023, 2).

Current research shows a link between rising geopolitical uncertainty and the increase in foreign divestment (Nguyen et al. 2022, 679). According to a survey conducted by Deloitte the number of divestitures doubled in just a year from 2020 to 2021. This spike in global divestment can be seen to be the result of major global shocks, such as the war in Ukraine, Covid-19 pandemic, all of which factor to the fragmentation of the global business world. (Deloitte 2022; Sethuram & Gaur 2024, 1039.) This shift is further accelerated by home country protectionist policies that encourage firms to localize their operations, which frequently results in host countries experiencing significant withdrawals of foreign investment (Peng et al. 2025, 1677).

A major driver for these exit decisions is political friction, which according to Nguyen et al. (2022), provides a more comprehensive assessment of the actual impact on a firm than political distance alone, as it accounts for firm-level factors as well. Political friction essentially refers to the tension an MNE faces when operating within the host country’s political environment. It incorporates several levels of misalignment, including political distance between home and host countries, such as

differences in stability, regime type and institutions, as well as the level of the firm's interaction with those differences in practice. When firm's interaction and the political distance is high, the friction also increases and vice versa. (Nguyen et al. 2022, 676, 679, 482.)

While political friction measures the actual tension experienced by the firm, geopolitical risk increases this friction (DeBerge 2023, 1). Geopolitical risk consists of three types of risks: political, such as conflicts, economic, such as protectionism, regulation, and trade frictions, and natural, for instance tsunamis (Yu & Wang 2023, 2). This thesis will focus on the first two as natural aspects are not relevant for the subject. Political friction increases the likelihood of FD as it creates high risks and barriers, such as higher adaptation costs, making it harder for multinational enterprises to remain in certain markets (Nguyen et al. 2022, 680). According to Altiner & Bozkurt's (2023, 1303) study, one percent increase in geopolitical risk decreases FDI inflows by approximately 0.8 percent. As this friction increases even further, for instance in a case of a conflict, the pressure to exit the market rises (Nguyen et al. 2022, 687).

Recent geopolitical shocks have steered companies to reassess their heavily concentrated networks and accelerated the fragmentation of supply chains by reshoring investments out of China (UNCTAD, 2020, 38). For instance, the tariff barriers introduced during the US–China trade war prompted many international companies to relocate their operations. Consequently, regions heavily exposed to US tariffs saw a significant rise in firm exits, with MNEs such as Samsung withdrawing from China in response to rising expenses. (Peng et al. 2025, 1676, 1678, 1688.) FDI inflows to and from China illustrate the effects of this trend. While Asia, in its entirety, has seen its market share of FDI shrink, the decline in both inward and outward FDI in China has been much more severe than the regional average. For instance, US investment into China dropped far more than the global average while remaining significantly more stable, and even growing, in other regions, like emerging Europe. (Ahn et al. 2023, 95.)

The rise of divestments can also be seen particularly clearly in the Russian invasion of Ukraine. By late 2022, between 5 and 13 percent of companies from EU and G7 countries had divested at least one of their business stakes in Russia (Evenett & Pisani 2023, 512–513). MNEs have faced intense pressure to exit the Russian market, demonstrating how high political friction significantly increases the likelihood of divestment. Growing geopolitical uncertainty thus force companies to reconsider how they balance social concerns and traditional business goals. (Mol et al. 2023, 2; Nguyen et al. 2022, 679.)

In IB literature, divestments have traditionally been seen as failures or at most reactive strategies. Sethuram & Gaur (2024), however, argue that rather than being treated solely as a failure, FD should be better understood as a strategic reaction to rising geopolitical risks and frictions between home and host countries. For example, in a 2019 survey over 80 percent of companies now use divestment as a proactive strategy to reorganize their operations rather than seeing it as a failure (Ernst & Young 2019; Sethuram & Gaur 2024, 1042).

3.2 Reallocation as response to geopolitical uncertainty

The rise in global divestments shows an ongoing reconfiguration of the investment landscape. Although divestments doubled in 2022, total FDI flows decreased by only 12% (Deloitte 2022; UNCTAD 2023, 3), suggesting that MNEs are reorganizing their investments rather than merely withdrawing them. In the past, companies moved production abroad (offshoring) mainly to maximize the cost-efficiency of their operations, but they are now shifting their focus toward global supply chain security in response to geopolitical shocks that exposed their fragility (Nguyễn 2023, 14576; Deng et al. 2025, 2). Consequently, firms are reallocating their investments by moving operations back home, to neighbouring markets, or toward geopolitically aligned partners (Aiyar et al. 2024, 2).

Reshoring, also known as backshoring, is the most discussed reallocation strategy in IB literature. It refers to relocating FDI back to the MNE's home country by closing down foreign operations and replacing them with domestic ones. (Bellucci & Rungi, 2023, 978; Deng et al. 2025, 2.) Companies often choose this strategy to gain better control over their supply chains, reduce transportation time and costs, while also catering to a rising demand for local production. Additionally, the cost gap between home and foreign markets is shrinking due to increased competition and decreasing wage disparities. (Yücesan 2025, 2.) Besides, the growing risk of intellectual property theft has further reduced the appeal for offshoring. (Deng et al. 2025, 2).

Alongside reshoring, nearshoring has also gained popularity. It refers to a strategy where production is moved to a country that is physically closer to the home country or the final market. (Yücesan 2025, 2.) Both strategies shorten the supply chains, making them less vulnerable to cross-border disruptions and geopolitical shocks (Nguyễn 2023, 14568; UNCTAD 2021, 173). This has become increasingly important as rising uncertainty has pushed MNEs to build greater resilience (Bellucci & Rungi 2023, 978; Deng et al. 2025, 2). Consequently, MNE's interest in reshoring has grown significantly, as seen in Figure 2.

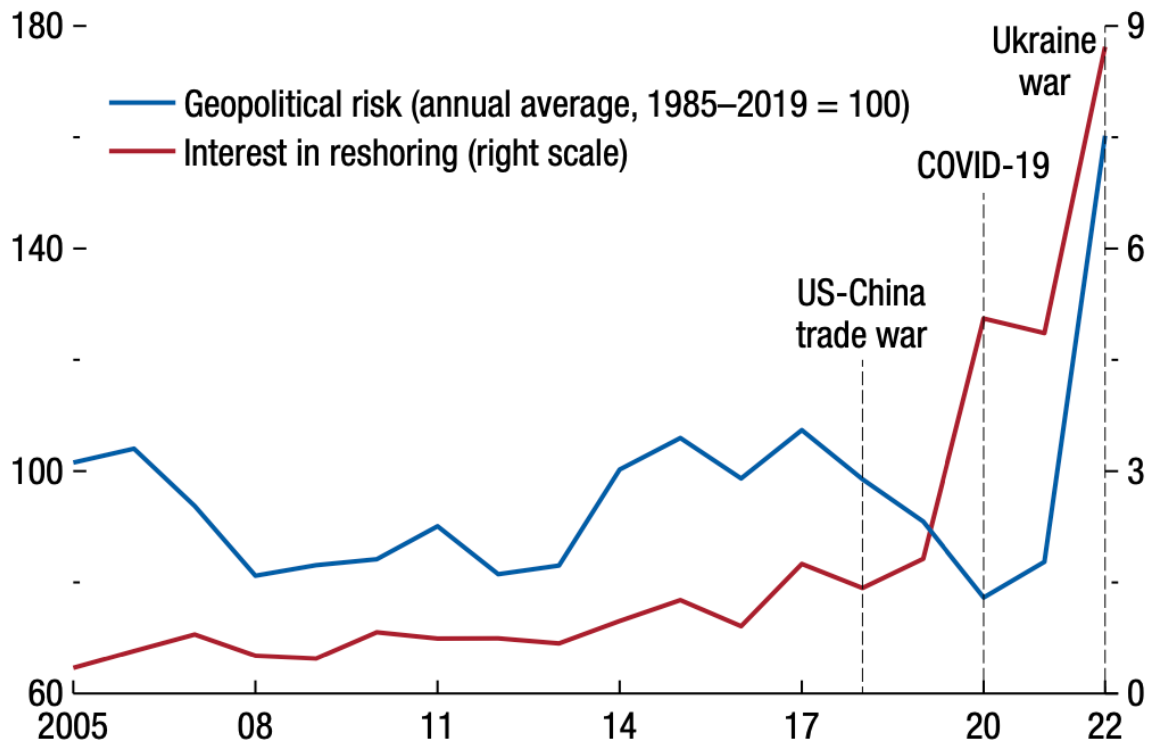


Figure 2 Geopolitical risk and mentions of reshoring and friendshoring (Ahn et al. 2023, 92)

Figure 2 shows an overall upward trend in both geopolitical risk and reshoring, especially in the 2020s. The interest in reshoring accelerated after the trade war between the United States and China. During this period, the US Reshoring Index reached record levels as many companies sought to avoid the heavy tariffs by shifting investments away from China (Kim et al. 2021, 211; Nguyễn 2023, 14567). Accordingly, 59 percent of companies that reshored in 2018–2019 were returning from China (Nguyễn 2023 14566–14567).

The trend received another push after the Covid-19 pandemic revealed the vulnerability of global supply chains. The measured geopolitical risk was relatively low at the beginning of the pandemic, also seen in Figure 2, but as the world began to recover from the initial shock, it became clear that supply chains needed restructuring to better withstand future disruptions (Bellucci & Rungi 2023, 978). For example, the critical shortage of semiconductors further increased pleas for both reshoring and a fundamental increase in supply chain resilience (Lan et al. 2022, 102). Many US firms responded by shifting their production toward neighbouring regions, such as North and Central America (Niu et al. 2025, 1029). The geopolitical risk index caught up with the reshoring trend later, and both have reached record highs in the 2020s as the pandemic progressed and another shock, Russian invasion of Ukraine, occurred (Figure 2).

Government-implemented protectionist policies have reinforced this development by creating financial motivations for firms to reshore back to the home country. For example, the CHIPS Act has driven a considerable increase in domestic investment in the semiconductor and electronics industries (Deng et al. 2025, 2), the America First Investment Policy seeks to boost domestic manufacturing while encouraging the reshoring of supply chains (UNCTAD 2025, 15), and the TCJA has encouraged domestic investment through tax benefits and encouraging the repatriation of foreign capital (Nguyễn 2023, 14566). Similarly, the European Chips Act, seeks to influence the production and sourcing strategies of MNEs (Aiyar et al. 2024, 2).

This aligns with a 2020 survey of 260 global value chain leaders, which confirms that companies are actively rearranging their operations in response to geopolitical uncertainty. The results show that one-third of supply chain managers had already started or planned to move production out of China by 2020 to build more resilient supply chains and reduce the risk of disruptions caused by global shocks. In 2022, they created a new survey of over 400 leaders. It showed that in just two years 74% had altered the size or location of their supply chain networks, and over half had increased their total amount of locations, making the supply chains more geographically fragmented. These changes were conducted in response to sustainable development goals, rising inflation, new national industrial policies and, of course, disruptions caused by COVID-19 pandemic. (Nguyễn 2023, 14571.)

A similar survey of over a thousand executives from major Western economies was conducted in late 2020. It shows that MNEs prefer regional fragmentation over reshoring production back home. While more than half planned to change suppliers in the near future, they preferred practical alternatives as one third considered markets where they already had strong partnerships, and only one fifth considered switching to domestic suppliers. When it came to relocating subsidiaries, less than 15% wanted to return to their home country. Instead, about 30% preferred nearshoring to neighbouring markets, particularly those within the same trade agreement or customs union. (Allianz Research 2020, 2). Reorganizing the value chains also makes them less vulnerable against future disruptions, and 40 percent of companies already reported making changes to their supply chains in 2020. (Allianz Research, 2020, 4).

3.3 Friendshoring as a key reallocation strategy

While reshoring and nearshoring aim to secure supply chains and investments by shortening the physical distance, many MNEs are opting to seek security by investing in countries that they consider “trusted” (Deng et al, 2025, 1). This strategy, known as friendshoring, involves relocating

supply chains to countries that are considered politically aligned and therefore “friendly” (Bellucci & Rungi, 2023). This approach aims to mitigate risks by ensuring that supply chains, especially in critical sectors, are not reliant on “unfriendly” nations with conflicting political interests. Unlike reshoring, friendshoring still allows firms to leverage the foreign market advantages while simultaneously prioritizing supply chain security and building resilience over economic efficiency. (Deng et al. 2025, 1, 11.)

Restrictions on trade and investment motivated by national security have risen steadily over the past decade as national security concerns have become a more central part of firms’ decision-making. Relatedly, geopolitical distance, measured by the difference in countries’ voting patterns at the UN General Assembly, has become an increasingly more important factor in FDI decisions than geographic distance, as shown in Figure 3. (Aiyar et al. 2024, 5).

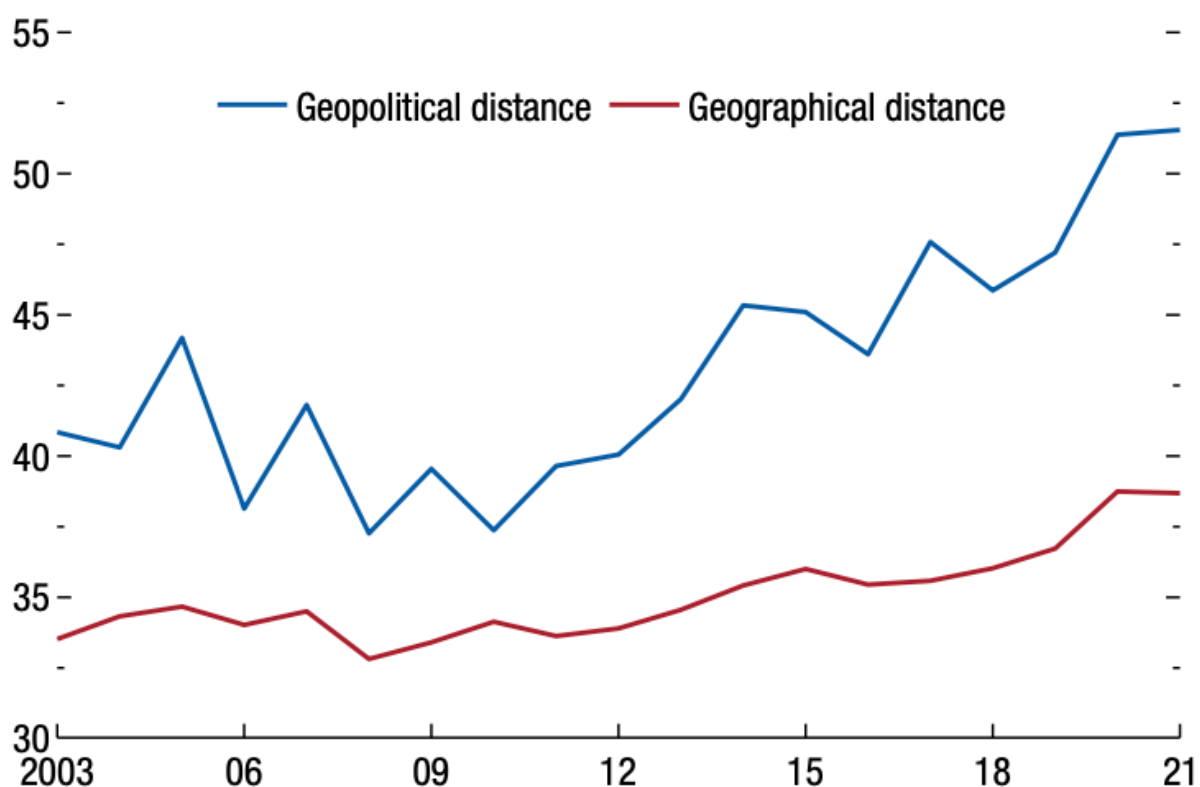


Figure 3 FDI flows between geopolitically and geographically close countries (Ahn et al. 2023, 96)

Yearly share (%) of FDI flows between country pairs in the same distance, geopolitically or geographically, from the US.

As Figure 3 illustrates, FDI flows between geopolitically close countries have grown considerably faster than with geographically close countries, particularly during the past decade. This suggests that geopolitical alignment has overtaken geographic proximity in investment decisions (Aiyar et al.

2024, 5). In fact, the probability of FDI occurring between geopolitically aligned countries is over twice as high as without geopolitical considerations, and this has only grown recently (Aiyar et al. 2024, 11). Correspondingly, investment between geopolitically distant nations, referring to those with conflicting political interests or foreign policies, fell from 23% in 2013 to 13% in 2022 (UNCTAD 2024). Furthermore, investments in geopolitically distant countries, are more likely to be reshored in response to heightened geopolitical uncertainty (Aiyar et al. 2024, 2). As a result, FDI flows are becoming increasingly concentrated within blocs of politically aligned nations (Aiyar et al. 2024, 8).

Again, this strategy is being encouraged by many governments as well. For example, in 2022 the U.S. Treasury Secretary Janet Yellen publicly urged businesses to shift their supply chains toward trusted nations, arguing that allowing other nations to gain control over critical supply chains poses considerable risks to both economic and national security (Deng et al. 2025, 3). Similarly other major economies, including China and the EU, have pursued policies aimed at reducing dependence on geopolitically distant countries (Aiyar et al. 2024, 2).

The importance of geopolitical alignment is emphasized in developing markets, like China, which are particularly susceptible to friendshoring, as they tend to rely heavily on investment from geopolitically distant partners. Accordingly, geopolitical distance is directly linked to a greater probability of FDI relocation. For instance, US FDI flows to geopolitically aligned markets, like Canada and Europe, remained relatively stable, while investment to more geopolitically distant economies, such as China, declined relatively more. (Ahn et al. 2023, 91, 96, 98.) This also varies by sector, with strategic sectors, such as food and transportation, being more exposed to reshoring (Ahn et al. 2023, 110; Aiyar et al. 2024, 2).

Although the term friendshoring was only formally introduced in 2022, the tactic itself had existed earlier under different names. For instance, the term “allied shoring” was used during the pandemic and the US–China trade war had also driven many MNEs to relocate production toward geopolitically aligned countries. Apple, for example, began relocating parts of its supply chains away from China toward more geopolitically aligned nations, particularly Vietnam (Deng et al. 2025, 3).

This is related to a widely known “China+1” strategy, in which MNEs maintain existing operations in China while directing new investments toward geopolitically aligned markets to diversify risk (Nguyễn, 2023 14567). Unlike earlier motivations, which were primarily driven by rising labor costs in China, companies today are increasingly willing to accept higher production costs in markets considered geopolitically safer in order to reduce dependence on China (Deng et al. 2025, 3).

Southeast Asian markets have benefited from this strategy as, for example, FDI inflows to Singapore, Thailand, and Vietnam increased significantly in 2024 (UNCTAD 2025, 34). Vietnam, in particular, has benefited from its position as a so-called "connector economy" maintaining a relationship with both the US and China, making it an attractive destination for firms relocating investments away from China (Deng et al. 2025, 4; Wu 2024). However, despite its growing relevance, the consequences of friendshoring and the role of suppliers in the relocation process remain an understudied area in IB literature (Deng et al. 2025, 2).

Conclusions

The aim of this thesis was to examine how increasing geopolitical uncertainty reshapes the foreign direct investment environment and the strategies behind investment decisions. This was addressed through two sub-questions: (1) How has growing geopolitical uncertainty changed the FDI environment? (2) How do MNEs strategically respond to this transformed environment? To address the first sub-question, major geopolitical shocks of the past decade were analyzed alongside the transformation they have driven in the FDI environment. The second sub-question was examined by evaluating key strategic responses MNEs have adopted in response to this transformed environment.

A sequence of major geopolitical shocks, Brexit, the US–China trade war, the COVID-19 pandemic, and the Russia–Ukraine war, has driven the transformation in the FDI environment: Brexit set a precedent for prioritizing national sovereignty over economic integration fueling economic nationalism. The trade war between United States and China introduced extensive trade barriers still visible today, while the COVID-19 pandemic caused global disruption at unprecedented scale and severity, exposing the fragility of heavily concentrated global value chains. Together, these shocks drove firms to reassess their China-centered strategies. The most recent shock, the Russia–Ukraine war, accelerated the fragmentation of FDI through elevated uncertainty.

These shocks have further accelerated the underlying global megatrends, deglobalization and geoeconomic fragmentation, illustrated by rising global protectionism and decline in global investment flows. Governments have responded with increasingly protectionist policies, as seen for example in Donald Trump's "America First" ideology, while multilateral institutions have simultaneously lost legitimacy and global co-operation has weakened in the process. Consequently, FDI has become increasingly fragmented and global supply chains are steadily regionalizing, with estimates suggesting that this could lead to global output decreasing by as much as 2 percent (Ahn et al. 2023).

The main finding of this thesis is that while geopolitical uncertainty has contributed to a decline in global investment flows, the more significant and lasting consequence has been the fragmentation of FDI as MNEs have adapted their investment strategies to emphasize resilience over cost-efficiency. Consequently, geopolitical alignment has overtaken geographic distance as a key driver of investment flows with FDI between geopolitically aligned countries now more than twice as likely

as it would be disregarding geopolitical factors (Aiyar et al. 2024, 11), and investment between geopolitically distant nations having fallen from 23 percent to 13 percent in the past decade or so (UNCTAD 2024).

This has resulted in a restructuring of FDI through three main strategies. Firstly, political friction has become a central factor in divestment decisions, with firms increasingly treating divestment as a proactive strategic reaction to heightened uncertainty rather than a sign of failure. Secondly, MNEs are reorganizing their investments to reduce supply chain vulnerability. While reshoring and nearshoring shorten supply chains to mitigate these risks, though surveys suggest that firms generally prefer regional diversification over returning to home markets. Third, and probably the most noteworthy strategy, friendshoring, has gained popularity in recent years. This strategy emphasizes geopolitical alignment reorienting supply chains toward trusted nations to increase their security rather than simply shortening them.

The consequences of this shift are unevenly distributed as developing economies that rely heavily on investment from geopolitically distant partners face disproportionate exposure to FDI reorientation, while other regions such as Europe have remained relatively more stable. However, some developing countries, such as Vietnam, have emerged as surprising beneficiaries of this by positioning themselves as geopolitically neutral “connector economies” (Deng et al. 2025, 4; Wu 2024). In conclusion, increasing geopolitical uncertainty has fundamentally reshaped both the foreign direct investment environment and the strategies MNEs use to navigate it, deepening the shift from an era of efficient globalization toward one defined by fragmentation, resilience, and geopolitical alignment.

Future research could explore several areas emerging from this analysis. The suppliers’ reaction to firms’ friendshoring decisions calls for further attention (Deng et al. 2025, 2) and as geopolitical uncertainty deepens, further analysis of connector economies, such as Vietnam, would also be an interesting area for future research.

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Appendices

Appendice 1. Declaration of use of Artificial Intelligence

Several AI platforms (ChatGPT, Claude, Volter's AI assistant, Keenious, and Anara) have been used in the planning, writing and revision phases of this thesis. All use has been in line with the University of Turku's academic integrity guidelines. AI was used only as a supportive tool, and all content of the thesis is the author's own. AI was not used to generate theoretical content or conclusions, and all AI's suggestions were critically reviewed and edited before being applied, and all academic sources were read by the author themselves. Examples of the prompts used with each platform are listed below.

ChatGPT (OpenAI)

Phase: Planning

Use: Brainstorming the topic, narrowing the scope, exploring wording alternatives, refining the research questions, and clarifying the typical structure of a bachelor's thesis.

Example prompt (26.1.2026): " I am writing a bachelor's thesis in international business and I am struggling to narrow down my topic. I want to write about geopolitical uncertainty and international business, but the topic feels too broad. Suggest some more focused angles that could work well for a bachelor's level thesis?"

The suggestions were used as inspiration and the final topic, scope, and research questions were determined by the author.

Claude (Anthropic)

Phase: During and after the writing process

Use: Proofreading the text for spelling and grammar, improving fluency, pinpointing repetition, and ensuring a consistent academic tone and terminology throughout the thesis.

Example prompt (5.5.2026): "Review the following chapter for grammar errors, repeated phrases, and inconsistent terminology."

Each correction was checked by the author and applied only when it improved the text without altering meaning.

Volter's AI-assisted search

Phase: Finding sources

Use: Finding relevant academic literature through the University of Turku's library databases.

Example prompt (12.2.2026): "Find articles related to geopolitical risk and foreign divestment."

Keenious

Phase: Finding sources

Use: Finding relevant articles for the thesis and locating additional academic articles based on the existing text.

Example prompt (20.3.2026): " Here is a what I have written about friendshoring. Can you find academic articles that discuss similar themes?"

Anara

Phase: During the writing process

Use: Confirming that the original source texts were interpreted correctly when the wording or argumentation in the source was complex.

Example prompt (26.4.2026): "Based on this article, isn't it accurate to say that political friction increases when both the political distance between the home and host country is large and the firm has high levels of interaction with the host country's political environment, or have I misunderstood?"

The tool was used solely as a comprehension aid and to help with translating some meanings to Finnish. All final conclusions were made by the author.