Politics-Induced Trade Fragmentation*

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Abstract

We study the global trade effects of political fragmentation. We first empirically estimate that increases in the political distance between two countries have negative effects on their bilateral trade. When a hegemon is involved, trade decreases more with political distance, and also increases with the political distance with the opposing hegemon. A quantitative model of trade and politics that replicates these empirical findings indicates that political fragmentation leads to lower aggregate trade flows, with greater concentration of trade within politically aligned blocks.

Keywords: International trade, geopolitics, hegemonic power, trade policy.

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1. Introduction

In recent decades, the international political landscape has become increasingly fragmented. National leaders are aligning more strongly with–or distancing themselves from–their counterparts in other nations. An implication of this is that trade policy is now often determined bilaterally, leading to heterogeneous treatments depending on political proximity. Notable examples of this trend include Trump's tariff increases targeting countries with left-leaning leaders while granting exceptions to right-leaning ones, as well as the Western-led trade sanctions on Russia, which China did not follow. This evolving landscape raises critical questions about its economic implications: How does political fragmentation reshape global trade flows? What role do the most powerful nations play in shaping this new trade order?

In this paper, we address these questions using an approach that combines an empirical analysis of the effect of political proximity on trade flows, with a quantitative model of global trade and politics. Our analysis indicates that political fragmentation leads to a quantitatively important fragmentation of trade, especially when powerful nations, or "hegemons," are involved. We first estimate that increases in the political distance between two countries have negative effects on their bilateral trade. When a hegemon is involved, trade decreases more with political distance, and also increases with the political distance with the opposing hegemon. Our quantitative analysis indicates that political fragmentation leads to depressed global trade with greater concentration of trade within politically aligned blocks.

The paper begins by constructing a measure of bilateral political distance that summarizes the differences in the policy stance of the ruling parties of countries regarding a variety of relevant topics. We obtain this variable for a panel of 122 countries during the 1970-2019 period. We then estimate the effect of changes in political distance on bilateral trade. Using an instrumental variables approach that exploits variation in political distance during close elections, we estimate that a one-standard-deviation increase in political distance leads to a reduction in bilateral trade flows of 6%. The effects on trade are gradual and take up to 10 years to realize in full.

We then analyze whether trade flows that involve a global hegemon–i.e., the US and

China post-2000s, and the US and the Soviet Union prior to the 1990s–respond differently to changes in political distance. We estimate an additional hegemonic effect of political distance on trade, by which trade involving a hegemon decreases more with bilateral distance and also increases when the political distance with the opposing hegemon increases. The effects are economically large: the responsiveness of trade flows doubles relative to the baseline estimates when we incorporate the additional hegemonic effects. We also find that most of the additional hegemonic effect operates through changes in the hegemons' imports.

Motivated by the empirical findings, we then develop a quantitative model of trade and politics. We introduce hegemons with geopolitical considerations, as in Clayton, Maggiori and Schreger (2023), and a notion of political distance into a canonical trade framework with differentiated goods, as in Eaton and Kortum (2002). Hegemons choose bilateral tariffs to maximize a combination of the economic utility of its consumers and a geopolitical preference that is increasing in the number of countries that identify with them. Following the literature on identity and politics (e.g., Shayo, 2009), we assume countries identify with one of the hegemons, and the likelihood of identifying with a certain hegemon is increasing in the bilateral gains of trade and decreasing in the bilateral political distance. Bilateral political distance affects economic activity through two channels. First, a lower political distance it reduces bilateral trade costs and thereby increases trade. Second, a lower political distance with a particular hegemon increases the likelihood that a country identifies with that hegemon, which induces the hegemon to lower tariffs with that country, thereby also increasing trade. Through these two channels, the model can account for the relationships between political distance and trade flows that we document in the data.

We then use a calibrated version of our model to quantify the general equilibrium of political fragmentation. We calibrate the model so that it can quantitatively reproduce the estimated relationships between political distance and trade flows. To study the effects of political fragmentation, we use k-means clustering to partition countries into two political blocks, with the two hegemons, the US and China, endogenously sorted into different groups. We consider political fragmentation as an increase of one standard deviation in the distance between hegemons, and a retrenchment of the countries in each group towards their hege-

mon so that the total cross-sectional variance of political distance remains unchanged. Our quantitative analysis of political fragmentation reveals two key takeaways. First, political fragmentation leads to depressed and fragmented international trade. While within-block trade increases by 1%, trade across blocks contracts by 2%. In the aggregate, trade flows decrease by 0.2%. An important driver of these results is trade between hegemons, which drops significantly. Second, there are important general equilibrium effects by which the trade reconfiguration leads to movements in economic activity and income, which further exacerbate the fragmentation of trade beyond their partial equilibrium effects.

Related Literature. [Incomplete] Our paper relates to various strands of the literature. First, a rising body of research studies the connection between international trade and politics. One body of research analyzes how bilateral trade can enhance political alignment and give rise to international power (see, e.g., Kleinman, Liu and Redding, 2024; Liu and Yang, 2024). Another stand of this literature studies the interaction between trade, conflicts and war (see, e.g., Martin, Mayer and Thoenig, 2008; Mansfield, 2021; Thoenig, 2023). A more recent related body of work analyzes how trade and financial linkages respond to geopolitical tensions and economic security considerations (see, e.g., Gopinath, Gourinchas, Presbitero and Topalova, 2025; Aiyar and Ohnsorge, 2024), and its implications for stabilization policy (Di Giovanni, Kalemli-Özcan, Silva and Yildirim, 2024). We contribute to this literature by analyzing how international political fragmentation can reshape global trade using a quantitative model of trade and politics.

Second, our paper contributes to the raising literature that studies international political economy and economic policy (see, Hirschman, 1958, for a seminal contribution). Clayton *et al.* (2023) develop a theoretical framework for analyzing how countries use their economic power to achieve their geopolitical and economic goals. Related work has studied the role of hegemonic powers in globalization and economic fragmentation (see, e.g. Clayton, Maggiori and Schreger, 2024; Broner, Martin, Meyer and Trebesch, 2024). Our work builds on these recent advances, and contributes to this strand of literature by estimating an additional hegemonic effect that plays a first-order effect on the global reconfiguration of trade in

response to political fragmentation. In doing so, we also build on the theoretical frameworks from a related literature on identity politics (see, e.g., Shayo, 2009; Grossman and Helpman, 2021).

The rest of the paper is organized as follows. Section 2 presents the empirical analysis of the effects of bilateral political distance on trade, highlighting the special role of hegemonic powers; Section 3 presents a quantitative model of trade and politics and assesses the effects of political fragmentation on global trade; Section 4 concludes.

2. Empirical Analysis

2.1. Data Description

This section describes the data used to construct the main variables used in our empirical analysis: the bilateral political distance, a measure of close elections and trade flows. Appendix A provides further details on these data and describes the additional variables used in the empirical analysis.

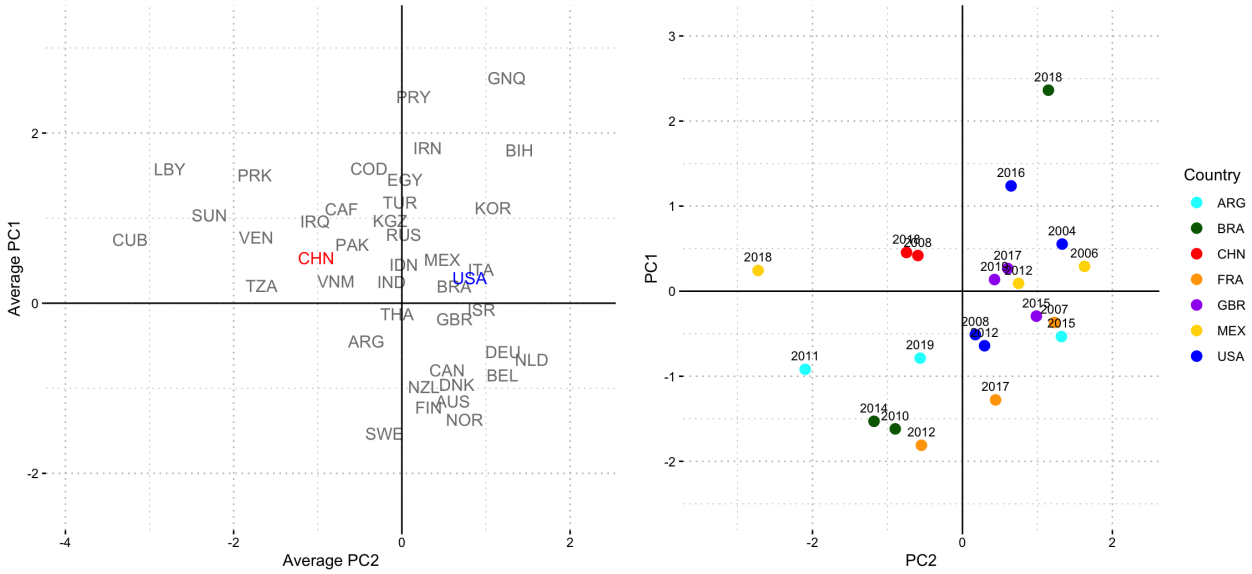
Our measure of political distance is constructed using the V-Dem Dataset. This is a panel dataset that reports a variety of indicators related to democracy and politics. We use a set of indicators that report the policy stance of the ruling political parties on fifteen different policy issues, which cover minority rights, cultural diversity, political pluralism, economic policy, among others. These data is available for an unbalanced panel of 169 countries for the 1970-2019 period. For each of the policy issues, the dataset assigns a numerical rating that reflects how in favor/against the political party is regarding a particular policy stance. We summarize the information of the fifteen policy issues with their first two principal components. The first component has large loadings on minority rights, cultural diversity and political pluralism, and thereby summarizes the stance regarding social and democracy issues. The second component has large loadings on economic policy, welfare state, and populism, and thereby summarizes the stance on the economy and welfare. These two principal components jointly explain more than half of the total variance of the fifteen

indicators. We then compute the political distance between a country pair as the Euclidean distance between the two principal components. Appendix A describes in greater detail the construction of this variable.

Panel (a) of Figure 1 shows that there is significant variation in the countries' location regarding the two principal components, with many Western Hemisphere countries locating in the southeast panel, and Eastern Hemisphere countries in the northwest panel. Panel (b) illustrates that there is also important variation within countries across time, associated with alternation of political parties in power. Focusing on the US as an example, there are substantial differences between republican and democratic governments in both principal components. Our analysis exploits variations in changes in bilateral political distance between countries. Appendix Figure A.2 illustrates this type of variation in selected elections of certain countries. Panel (a) reports the change in the bilateral political distance between the US and all other countries when Trump got first elected, with the US moving away from Canada and Europe, and closer to Russia. Panel (b) depicts the Argentinean election of 2015, when Macri was elected, with Argentina moving closer to Europe and the US. Panel (c) depicts the Brazilian election of 2018, when Bolsonaro was elected, with Brazil moving closer to the US. In all of these elections the countries moved significantly in their location of the political landscape, triggering heterogeneous changes in the political distances with other countries.

Another relevant variable that we use for the instrumental variables strategy is an indicator of close elections. To create this indicator we complement our V-Dem data with data on elections from Marx, Pons and Rollet (2022), which collect data on presidential and parliamentary elections from 1946 and 2018 for 201 countries. Finally, our baseline analysis uses data of bilateral trade flows from the IMF, which has the largest coverage of 200 countries during the 1960-2023 period. After merging all the data we obtain a complete dataset covering 122 countries during the 1970-2019 time period.

Figure 1: Political Distance Across Time and Space



(a) Political Distance Across Countries **(b)** Political Distance Across Years

Notes: This figure shows scatter plots of the two principal components of the policy stance of different countries at different points in time. The first principal component (PC1) relates to social and democracy issues. The second principal component (PC2) refers to the economy and welfare. Panel (a) shows the cross-country variation averaging over time, focusing on a subset of countries. Panel (b) shows the time series variation for selected countries. See Appendix A for further details on this variable.

2.2. Political Distance and Bilateral Trade

Gravity regressions In this section we estimate the effect of changes in political distance on trade flows. We start by estimating the following gravity regression:

$$\ln X_{ijt} = \beta PD_{ijt} + \alpha_{ij} + \alpha_{it} + \alpha_{jt} + \zeta' \mathbf{Z}_{ijt} + \varepsilon_{ijt} \tag{1}$$

where X_{ijt} are trade flows from country i to country j in year t; PD_{ijt} is the standardized measure of bilateral political distance; $\alpha_{ij}, \alpha_{it}, \alpha_{jt}$, are origin-destiny, origin-year, and destiny-year fixed effects; Z_{ijt} is a vector of controls, which include the bilateral distance in GDP per capita and a measure of diplomatic disagreement; and ε_{ijt} is a random error term. The origin-destiny fixed effects control for time-invariant gravity determinants of bilateral flows, and the country-time fixed effects control for common changes in trade policy induced

by different governments. In all regressions, we cluster standard errors at the country-pair.

Panel (a) of Table 1 reports the OLS regression estimates of β, which are negative and statistically significant. The estimated semi-elasticity of -0.05 indicates that a one-standard-deviation increase in the bilateral political distance between two countries has associated a 5% reduction in their trade flows. To put this result into perspective, the increase in political distance between the US and Canada after Trump was first elected was equivalent to 2 standard deviations.

We perform a series of additional exercises to estimate the causal effect of politics on trade and show that our empirical results are robust to alternative specifications. One concern with the OLS estimates is that they may be capturing reverse causality, by which stronger trade links lead to political proximity. We address this by adopting an instrumental variables approach where we instrument the bilateral political distance with changes in political distance that occurs following a close election. This instrument captures those variations in political distance that happened in close elections, whose outcome is arguably less driven by underlying trade patterns. We also consider an alternative instrument that focuses on changes in political distance that occurs between a country that had elections and another country that is not a major trading partner of the country with elections. The motivation for this alternative instrument is that changes in the political distance due to the outcome of an election are unlikely to be determined by trade with non-major trading partners. Panel (b) of Table 1 reports the IV estimates, when we use the two instruments separately and when we use them jointly. In all specifications we obtain a semi-elasticity estimate that is negative, statistically significant and larger in magnitude than in the baseline case.

Panel (c) of Table 1 reports two robustness exercises showing that the estimated semi-elasticity between political distance and trade flows is similar if we do not include the set of controls $\mathbf{Z}_{ijt}$ or origin-destiny fixed effects. Additionally, in Appendix A we estimate the effects on bilateral trade flows disaggregated by sector and find a negative effect of politics on distance that is generalized across sectors. Finally, we analyze whether larger political distance increases bilateral tariffs, finding inconclusive evidence. This suggests that there may be other policy channels through which political distance affects trade.

Table 1: The Effect of Bilateral Political Distance on Trade

Specification		Estimate	Observations
A. Baseline		-0.049	332367
		(0.008)	
B. Instrumental variables	Close elections	-0.051	332367
		(0.015)	
	No major trading partners	-0.066	332367
		(0.012)	
	Both	-0.065	332367
		(0.012)	
C. Robustness	No controls	-0.062	352050
		(0.009)	
	No fixed effects	-0.075	332701
		(-0.075)	
D. Dynamic effects	2 years	-0.008	274172
		(0.008)	
	5 years	-0.044	240801
		(0.014)	
	10 years	-0.056	190420
		(0.019)	

Notes: This table reports the estimate of β in equation (1), which corresponds to the semi-elasticity of trade flows to political distance. Different rows refer to different specifications, detailed in Section 2. The last panel reports the dynamic effects of estimating (2). Standard errors are in parenthesis and clustered at the country pair.

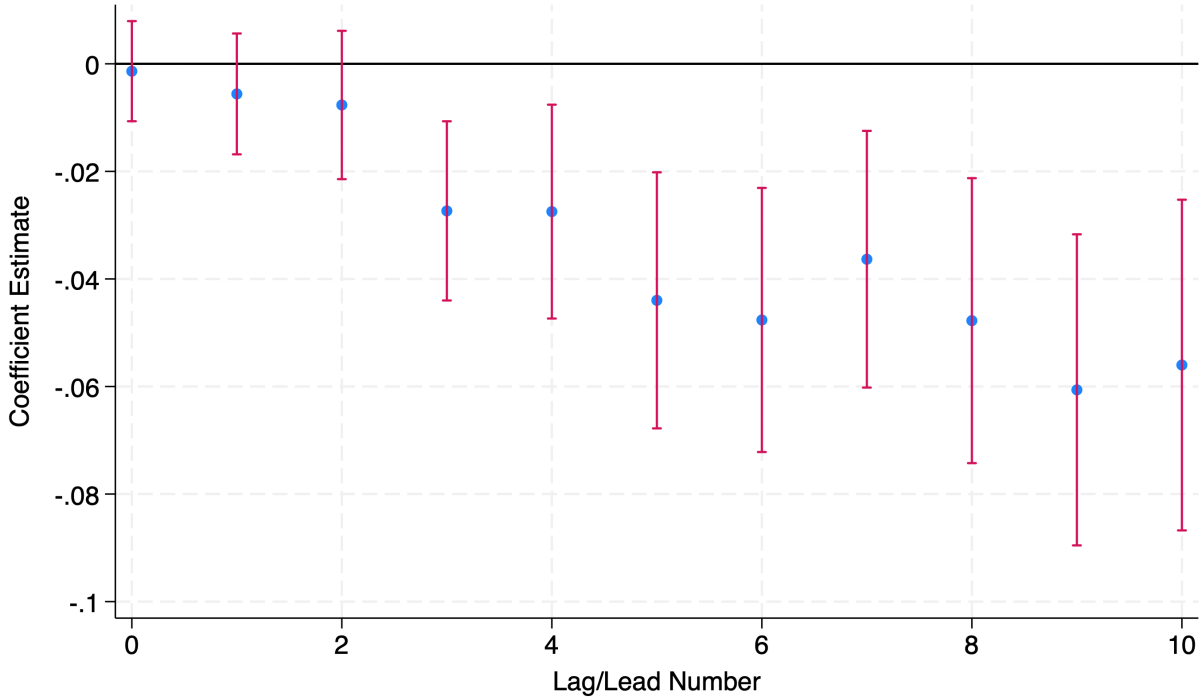
Dynamic effects We now estimate the dynamic effects of political distance on trade flows. For this, we estimate the following local projections:

$$\Delta_h \ln X_{ijt} = \beta_h \Delta PD_{ijt} + \alpha_{ijh} + \alpha_{ith} + \alpha_{jth} + \zeta_h' \mathbf{Z}_{ijt} + \varepsilon_{ijth} \tag{2}$$

where Δ_h is the h-years cumulative change in a variable, and all other variables are as in (1). The coefficient of interest, β_h is the semi-elasticity of changes in trade flows at horizon h to changes in political distance. We estimate a separate regression for each horizon h following Jordà (2005).

Figure 2 presents the results of estimating β_h from equation (2) at different horizons, h, ranging from 1 to 10 years. The estimation method is instrumental variables using the two instruments discussed above. Panel (d) of Table 1 reports the estimates for the 2, 5, and 10 years horizons. The estimated semi-elasticity is negative and increases in absolute value over time. After 8 years, it stabilizes around -0.06, which is roughly similar to the long-run semi-elasticity estimated in the gravity regressions.

Figure 2: Dynamic Effects of Political Distance on Trade Flows



Notes: This figure shows the estimated β_h coefficients of Equation (2), which correspond to the cumulative log change in bilateral trade flows in response to change in the bilateral political distance in period t. The variable PD_{ijt} is standardized so that the units are standard deviations. The x-axes show the horizon h (yearly frequency). Standard errors are clustered at the origin-destiny pair. Bars represent 90% confidence intervals.

In Appendix A, we pursue complementary estimations showing the robustness of the

estimated dynamic effects. First, we estimate a contemporaneous relationship between trade flows and political distance instead of a local projection, by including $\Delta_h PD_{ijt}$ as the main regressor. This exercise is relevant in addressing the potential presence of autocorrelation in the dynamics of political distance. Second, we estimate the local projections excluding controls and fixed effects, using each instrument separately and using OLS. The results are robust to these different specifications.

2.3. The Role of Global Hegemons

In this section, we analyze whether trade flows that involve a global hegemon respond differently to changes in political distance. Motivated by the different historical geopolitical contexts, we define two regimes of hegemonic power for different points in time. From the start of the sample until 1990 we define hegemons as the US and the Soviet Union. The end of this regime is marked by the fall of the Soviet Union. A second regime starts in 2001, when China joins the WTO, and is characterized by the US and China as the hegemons. Motivated by the theoretical framework of Section 3, we estimate whether the trade flows that involve a hegemon also respond to changes in the relative distance of a particular country with the two hegemons. That is, we ask, for example, whether a country that moves politically closer to US and/or farther from China, will trade more with the US and less with China, more so than predicted by the previously estimated relationship between political distance and trade flows. For this, we estimate the following gravity regression:

$$\begin{aligned}\ln X_{ijt} =& \beta PD_{ijt} + \gamma \left[\mathbb{I}_{\{i=h\}} \left(PD_{hjt} - PD_{(-h)jt}\right) + \mathbb{I}_{\{j=h\}} \left(PD_{iht} - PD_{i(-h)t}\right)\right] \\ &+ \alpha_{ij} + \alpha_{it} + \alpha_{jt} + \zeta' \mathbf{Z}_{ijt} + \varepsilon_{ijt} \end{aligned} \tag{3}$$

where h is a hegemon country, and $-h$ is the opposing hegemon, and all other variables are as in (1). The coefficient γ measures the additional effect of changes on the relative political distance of a particular country with a hegemon on trade flows. We define the relative political distance of a country with a hegemon as the difference between their bilateral political distance and that of the country and the opposing hegemon. We refer to γ as the

"additional hegemonic effect" of political distance on trade. The motivation for estimating this specification is that hegemons may have an additional incentive to increase trade with countries that are politically close in order to increase the likelihood of them becoming "allies." We elaborate further on this in the next section.

Panel (a) of Table 2 reports the OLS regression estimates of (3). Our baseline estimate of γ is negative and statistically significant. The point estimate of -0.04 indicates that a one-standard-deviation increase in the relative bilateral political distance between a country and a hegemon is associated with a 4% reduction in their trade flows. This implies that trade flows with a hegemon are more sensitive to political distance and also respond to the political distance of the opposing hegemon.

Panel (b) reports the additional hegemonic effects by different hegemons. We estimate the largest effects in absolute value for US, and smaller effects for China and the Soviet Union. Panel (c) estimates the additional hegemonic effects separating between the hegemons' imports and exports. The effects are significantly stronger for imports, indicating that hegemons mainly respond by adjusting their imports following changes in political distance. In Panel (d), we show that the results are robust to excluding controls and country-pair fixed effects.

In Appendix A we also estimate a flexible specification in which we allow for two separate estimates of the additional hegemonic effects: one that responds to the political distance of the hegemon and the other country, and one that responds to the political distance of the opposing hegemon and the other country. We find that trade decreases with its bilateral distance and increases with the distance with the opposing hegemon. Finally, we also estimate dynamic hegemonic effects with Jorda projections. Appendix Figure A.4 shows that the additional hegemonic effects of political distance on trade gradually build up over a decade. Panel (e) of Figure 2 reports the coefficients for selected horizons.

Table 2: The Additional Hegemonic Effect of Political Distance on Trade

Specification		$\widehat{\beta}$	$\widehat{\gamma}$	Observations
A. Baseline		-0.058	-0.038	328183
		(0.009)	(0.020)	
B. By hegemon	United States	-0.058	-0.046	328183
		(0.009)	(0.026)	
	China	-0.058	-0.037	328183
		(0.009)	(0.041)	
	Soviet Union	-0.058	0.016	328183
		(0.009)	(0.035)	
C. By trade flows	Hegemon as importer	-0.060	-0.080	328183
		(0.009)	(0.025)	
	Hegemon as exporter	-0.060	0.007	328183
		(0.009)	(0.023)	
D. Robustness	No controls	-0.057	-0.035	338831
		(0.009)	(0.020)	
	No fixed effects	-0.220	-0.033	328496
		(0.017)	(0.037)	
E. Dynamic effects	2 years	-0.006	-0.012	270494
		(0.007)	(0.012)	
	5 years	-0.020	-0.010	244351
		(0.008)	(0.017)	
	10 years	-0.025	-0.030	194334
		(0.009)	(0.021)	

Notes: This table reports the estimate of β and γ in equation (3), which corresponds to the semi-elasticity of trade flows to political distance, and the additional hegemonic effect of changes in the relative political distance on trade flows. Different rows refer to different specifications, detailed in Section 2. The last panel reports the dynamic effects of estimating (A.2). Standard errors are clustered at the country pair.

3. A Quantitative Model of Trade and Politics

In this section we develop and quantify a general equilibrium model of trade and politics, and use it to assess the general equilibrium trade effects of political fragmentation. Section 3.1 presents the model setup; Section 3.2 discusses the model calibration and conducts the counterfactual analysis.

3.1. Environment

We consider the canonical trade model that builds on Armington (1969) and Eaton and Kortum (2002). We extend this model to allow for trade costs to depend on political distance and for hegemon countries to choose tariffs balancing economic and geopolitical preferences.

Economic preferences There are N countries, indexed by o, d denoting origin and destiny. Consumers of a country d have CES preferences over consumption of different varieties given by,

$$\mathcal{U}_d = \left(\int_0^1 q_d(i)^{\frac{\sigma}{\sigma-1}} di \right)^{\frac{\sigma-1}{\sigma}}, \tag{4}$$

where $q_d(i)$ is consumption of a variety i. Varieties can be sourced from multiple countries o, and are perfect substitutes across origins, so that $q_d(i) = \sum_o q_{od}(i)$, where $q_{od}(i)$ is consumption of i in d from o. The budget constraint of consumers is given by

$$\int_0^1 \sum_o p_{od}(i) q_{od}(i) di = w_d L_d,$$

where $p_{od}(i)$ is the price of variety i sourced from o; w_d is the wage and L_d the country's endowment of labor. Perfect substitutability of varieties across origins imply that consumers always buy the lowest cost variety:

$$q_{od}(i) > 0 \Leftrightarrow p_o(i) = \min_{o'} p_{o'd}(i).$$

Technology and trade costs Firms producing variety i in country o operate a linear technology using labor with productivity, $z_o(i)$. We assume that productivity is distributed Frechet with scale T_o and shape θ.

Moving goods across space is costly, and shipping is subject to iceberg trade costs. Hence, in order for d to consume q units of a good from o, $\tau_{od}q$ units must be shipped. We assume that trade costs have the following structure:

$$\log \tau_{od} = \tilde{\beta} PD_{od} + \tilde{\tau}_{od},$$

We assume that trade costs are increasing in political distance, where $\tilde{\beta} > 0$ is the semi-elasticity of trade costs to political distance, PD_{od}. The second component $\tilde{\tau}_{od}$ captures all other determinants of trade costs. We later endogenize this component for hegemons.

Firms are perfectly competitive, and price at marginal cost. The price of selling good i in d from o is given by:

$$p_{od}(i) = w_o \tau_{od} / z_o(i).$$

Competitive equilibrium Equilibrium is defined in the standard way, where firms maximize profits given prices, consumers maximize utility given prices and prices are such that markets clear. Given the Frechet assumption on technology, we can aggregate for trade shares in closed form. Specifically, the import share of o in d is given by:

$$\pi_{od} \equiv \frac{\int_0^1 p_{od}(i) q_{od}(i) di}{\int_0^1 \sum_o p_{od}(i) q_{od}(i) di} = \frac{T_o (w_o \tau_{od})^{-\theta}}{\sum_{o'} T_{o'} (w_{o'} \tau_{o'd})^{-\theta}}$$

Using market clearing and the countries' budget constraints we obtain:

$$w_o L_o = \sum_d \pi_{od} w_d L_d,$$

for all d, o. We normalize global GDP to one, $\sum_o w_o L_o = 1$. Finally, it is useful to define the gains of country o from trading with country d as

$$\mathcal{W}_{od} = \frac{\mathrm{d} \ln \pi_{od}}{\theta}.$$

This formula uses the results in Arkolakis, Costinot and Rodríguez-Clare (2012), which apply to our trade model.

Hegemon's problem We assume that two countries, denoted by h_1, h_2 are hegemons. Hegemons differ from other countries in that they can choose bilateral tariffs with all non-hegemon countries. The hegemon's objective function is a weighted sum of economic and geopolitical preferences

$$\mathcal{U}_{h_k} + \lambda \mathcal{N}_{h_k}, \tag{5}$$

where $\mathcal{U}_{h_k}$ are the economic preferences, given by (4); $\mathcal{N}_{h_k}$ are the geopolitical preferences, and $\lambda > 0$. We assume that the geopolitical preferences are given by the expected number of countries that identify with hegemon h_k. We follow Shayo (2009) and assume that countries identify with one of the hegemons. We denote $h(o) \in \{h_1, h_2\}$ as the hegemon with which country o identifies, which is given by

$$h(o) = \arg\max_{h_1, h_2} \left\{ \mathcal{W}_{oh_1} - \omega PD_{oh_1} + \varepsilon_{oh_1}, \mathcal{W}_{oh_2} - \omega PD_{oh_2} + \varepsilon_{oh_2} \right\}, \tag{6}$$

where $\omega > 0$, and ε_{oh_k} are Gumbel distributed with scale parameter ν. The motivation for this formulation is that a country will be more likely to identify with a country that has larger gains of trade and is politically closer. Under the distributional assumption of the ε shocks, the expected number of countries that identify with hegemon h_1 is

$$N_{h_1} = \frac{\exp\left(\frac{1}{\nu}\left(\mathcal{W}_{oh_1} - \mathcal{W}_{oh_1} - \omega\left(PD_{oh_1} - PD_{oh_2}\right)\right)\right)}{1 + \exp\left(\frac{1}{\nu}\left(\mathcal{W}_{oh_1} - \mathcal{W}_{oh_1} - \omega\left(PD_{oh_1} - PD_{oh_2}\right)\right)\right)} \tag{7}$$

and a symmetric expression for h_2. The hegemon's problem then consists of choosing $\{\tilde{\tau}_{h_k d}, \tilde{\tau}_{o h_k}\}$ for all o, d to maximize (5) subject to (4), (7) and the equations that characterize the competitive equilibrium allocations.

When choosing tariffs the hegemon balances two motives. First, there is a standard terms-of-trade manipulation motive that induces the hegemon to impose positive tariffs. Second, there is an additional geopolitical force by which the hegemon would like to reduce tariffs to improve the gains of trade of other countries to increase the likelihood that these countries identify with them. This second motive is stronger for countries that are politically closer to the hegemon and farther away from the opposing hegemon. This motive can rationalize the empirical findings from Section 2, by which the bilateral trade that involves a hegemon responds more to changes in bilateral political distance and also responds to changes in the political distance with the opposing hegemon.

3.2. Quantitative analysis

We solve the model with exogenous trade costs that depend on political distance. Solving the full model in which hegemons optimally choose tariffs is work in progress.

Calibration The model without strategic behavior by the hegemon admits closed-form expressions for counterfactual analysis of changes in trade costs induced by chances in political distance that depend on observed data and a subset of model parameters. See Caliendo and Parro (2015) for the methodology behind this approach.

The calibrated model features 33 countries, including among others: United States, Japan, Germany, United Kingdom, China, Russia and India. We also treat the rest of the world as an additional country. To compute the counterfactual analysis we use data on the vectors of GDP and population by country, as well as bilateral trade matrices. We obtain these data from the IMF and World Bank, and use the 2019 values. Appendix Tables A.5 and A.6 summarize these data, and Appendix B describes how we adjust the data to account for trade imbalances that are not featured in the model. The logic behind using observed data on trade flows and economic activity is that there are vectors of country specific scale

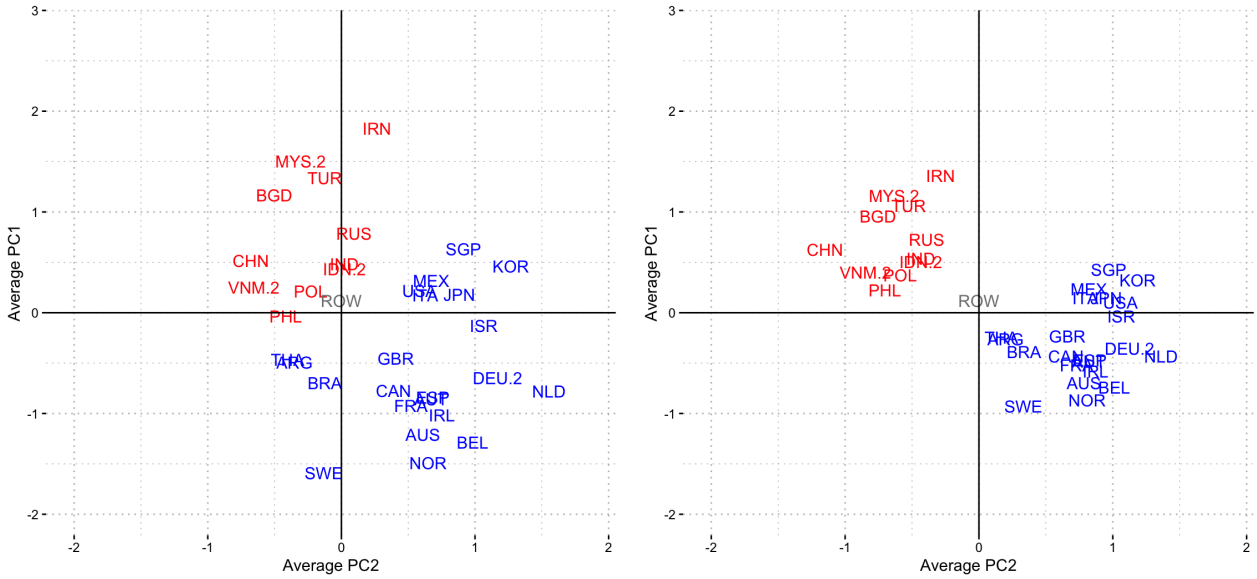
productivities, T_o, labor endowments, L_o, and bilateral trade costs $\tilde{\tau}_{od}$ that can exactly rationalize these observed data.

We parametrize the trade elasticity to be $\theta = 5$, which is in the upper bound of estimates from the literature. The trade effects of political fragmentation are much larger when we use a trade elasticity of $\theta = 2$, as estimated by Boehm, Levchenko and Pandalai-Nayar (2023). Finally, calibrate $\tilde{\beta}$ so that a one standard-deviation increase in bilateral political distance leads to a 6% reduction in bilateral trade flows, as estimated in Section 2. The calibrated value is $\tilde{\beta} = 0.012$.

The trade effects of political fragmentation Motivated by the recent trends in international politics, we study the trade effects of political fragmentation. For this, we first empirically identify two blocks of countries, using k-means clustering. The resulting blocks feature each of the hegemons, the US and China, in different blocks (see Figure 3, Panel (a)). The US block also includes Germany, United Kingdom, Japan and other Western countries. The Chinese block also includes Russia, India, and other Eastern economies. We then consider a counterfactual exercise in which countries move in the political spectrum in two steps. First, the two hegemons, US and China, move farther away from each other by one standard deviation. Second, the countries from each block move closer to their block hegemon by a magnitude so that the total cross-country variance of political distance remains unchanged. Panel (b) of shows the resulting counterfactual movements of each country in the political spectrum.

The resulting political fragmentation maps into a fragmentation of trade costs, with these getting larger for countries of different blocks and smaller for countries within a block. Appendix Table A.7 summarize the resulting changes in bilateral trade costs. Table 3 reports the general equilibrium changes in bilateral trade in response to the political fragmentation. There are two key takeaways from the analysis. First, aggregate trade flows fall by 0.2% percent in the new politically fragmented economy. This is mostly due to the drop in bilateral trade flows between the two hegemons, which decrease by 6%. Second, international trade becomes fragmented. While trade within the Western and Eastern blocks increase by 1.5%

Figure 3: Political Fragmentation Counterfactual



(a) Political Distance Before Shock

(b) Political Distance After Shock

Notes: This figure shows scatter plots of the two principal components of the policy stance of different countries at different points in time. The first principal component (PC1) relates to social and democracy issues. The second principal component (PC2) refers to the economy and welfare. Panel (a) shows the cross-country variation for the year 2019. Panel (b) shows the counterfactual political fragmentation exercise in which countries move in the political map. See Appendix A for further details on the political distance variable.

and 1%, respectively, trade across blocks decrease by approximately 2.2%.

Finally, Appendix Table A.8 compares the general equilibrium effects on bilateral trades with the partial equilibrium ones obtained by projecting the changes in bilateral trade costs on the estimated semi-elasticity from Section 2. The implied indirect general equilibrium effects can be as large as half as the partial equilibrium effect. While in most cases attenuate the partial equilibrium effects, they amplilfy the fragmentation of trade. This analysis highlights the value of analyzing this in a model of the world economy.

4. Conclusions

The conclusion of our work is that political fragmentation can lead to depressed and fragmented trade. We reach this conclusion by first estimating negative and significant effects

Table 3: The Trade Effects of Political Fragmentation

	Δ International Trade				
	World	Western Block	United States	Eastern Block	China
Western Block	0.49	1.45	1.27	-2.34	-3.27
United States	-0.42	1.47	-	-4.78	-5.29
Germany	0.86	1.28	3.16	-0.86	-1.7
Japan	-0.11	1.79	0.77	-2.62	-3.19
United Kingdom	0.59	1.42	0.74	-2.0	-3.09
Rest West	0.77	1.45	1.21	-1.58	-2.43
Eastern Block	-1.46	-2.21	-5.49	1.03	0.53
China	-2.38	-2.9	-6.0	0.82	-
Russia	-0.3	-1.26	-5.27	1.0	0.57
India	-1.37	-2.8	-5.89	0.72	0.14
Rest East	-0.3	-1.19	-4.21	1.21	0.6
Rest of the World	-0.58	0.02	-3.07	-1.63	-2.56
World	-0.15	0.49	-0.42	-1.46	-2.38

Notes: This table reports the percent change in international trade in response to the political fragmentation counterfactual exercise. Trade is expressed as imports of row countries/regions from column countries/regions. See text for further details.

of increases in bilateral political distance on bilateral trade flows. These effects are larger when hegemonic powers are involved. We then quantify a model of global trade and politics that can rationalize these empirical findings. Our counterfactual exercise highlights the tight connection between politics and trade at the global level. Whether the trade response to political distance is desirable from a global welfare perspective is an important question that we leave for future work.

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A. Empirical Appendix

A.1. Data Description

Construction of Bilateral Political Distance We use the V-Dem database (see Coppedge, Gerrin, Knutsen, Lindberg, Teorell, Altman, Bernhard, Cornell, Fish and Gastaldi (2021)), which provides an assessment by political experts of the ideology of each political party that received at least 5% of the vote in any election across 169 countries for the period 1970-2019. The experts evaluate the parties on numerous dimensions through a series of questions. We select the 15 most relevant questions and conduct a principal component analysis (PCA) to summarize the information. Table A.1 provides a description of the questions we considered. Table A.2 displays the weights assigned to each question for the first two principal components. Figuree A.1 shows a scree plot showing that these two principal components jointly explain more than half of the total variance of the fifteen indicators.

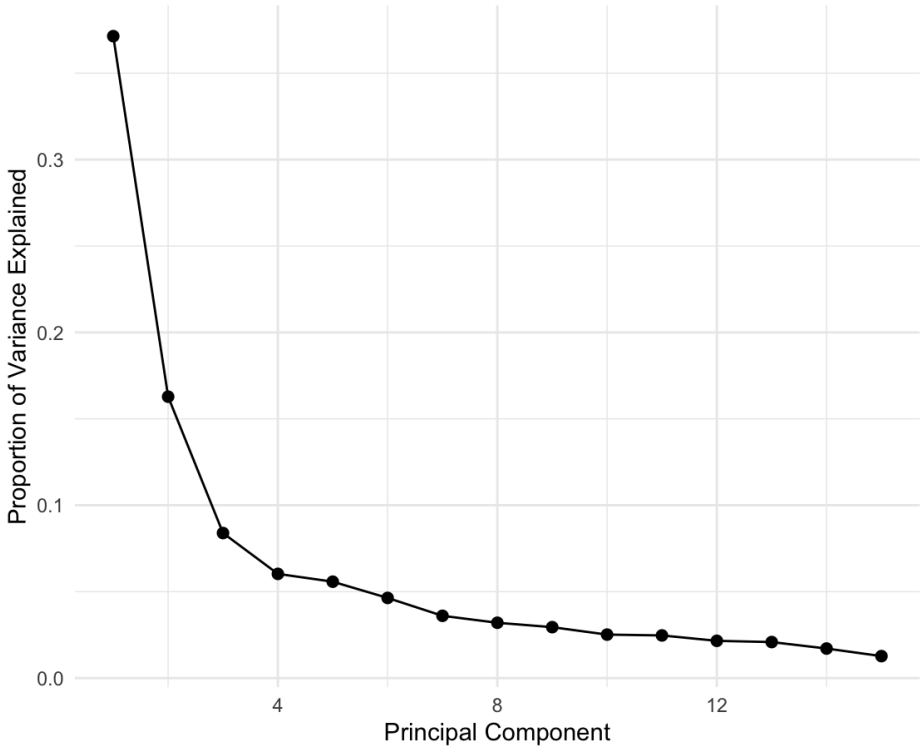
From Table A.2, we conclude that the first component has large loadings (in absolute value) on minority rights, cultural diversity and political pluralism, and thereby summarizes the stance regarding social and democracy issues. The second component has large loadings on economic policy, welfare state, and populism, and thereby summarizes the stance on the economy and welfare.

Up to this point, we have obtained the measures for the first two principal components for every political party that received more than 5% of the vote in any election. Our focus now shifts to the political description of the head of state. To do this, we select the party associated with the current president, as indicated in the V-Dem dataset (where the variable v2pagovsup equals zero). In some cases, attributing a party to the head of state is not straightforward; in these instances, we choose not to impute data for that country in that year. The varying coverage across countries and the challenges in associating a party with every leader result in an unbalanced panel. For countries with consistently missing observations, we exclude them from the sample. Since we only have data when elections occur, we carry forward the most recent values until a new election takes place. Note that the variability in these indicators, and consequently in political distance, is entirely driven by the occurrence of elections (whether legislative or presidential, the distinction is not relevant

here). In Figure 1, we observe considerable variability, both in the averages across countries and within individual countries, where political distance can fluctuate significantly during election periods.

Now that we have a measure of the ideology of each head of state for every year, we compute the bilateral distance between countries for each year by standardizing both principal components and then calculating the Euclidean distance. This yields our Bilateral Political Distance indicator. In Figure A.2, we can observe the variability of this indicator whenever there is an election in at least one of the countries in any given country pair. We selected as illustrative examples elections that caused significant shifts in the principal components map, such as the 2016 election of Trump, the 2015 election of Macri, and the 2018 election of Bolsonaro (see Figure 1).

Figure A.1: Percentage of Variance Explained by each Principal Component



Notes: The graph shows the number of each principal component in the x axis and the percentage of variance explained by that component on the y axis. The first principal component expains 37% of the variance while the second explains 16% of the variance.

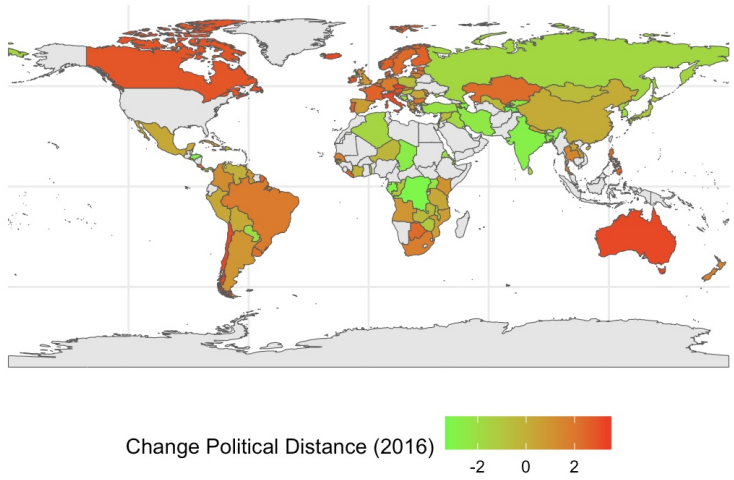
Table A.1: Description of questions

Question	Description
LGBT Social Equality	What is this party's position toward social equality for the LGBT community? Increases with support.
Minority Rights	How often should the will of the majority be implemented even if doing so would violate the rights of minorities? Decreases with frequency.
Cultural Superiority	Does the party leadership promote the cultural superiority of a specific social group or the nation as a whole? Decreases with frequency.
Rejection of Political Violence	Does the leadership of this party explicitly discourage the use of violence against domestic political opponents? Increases with frequency.
Political Pluralism	Prior to this election, was the leadership of this political party clearly committed to free and fair elections with multiple parties, freedom of speech, media, assembly and association? Increases with commitment.
Religious Principles	Does this party invoke God, religion, or sacred/religious texts to justify its positions? Decreases with frequency.
Political Opponents	Prior to this election, have leaders of this party used severe personal attacks or tactics of demonization against their opponents? Decreases with frequency.
Working Women	Does this party support the equal participation of women in the labor market? Increases in support.
Immigration	What is the party's position regarding immigration into the country?Increases with support.
Gender Equality	What is the share of women in national-level leadership positions of this political party? Increases in frequency.
Welfare	To what extent does the party promote means-tested or universalistic welfare policies? Increases with frequency.
Anti-Elitism	How important is anti-elite rethoric for this party? Increases with importance.
Economic Left-Right Scale	Locate the party in terms of its overall ideological stance on economic issues. Increases to the right spectrum.
People-Centrism	Do leaders of this party glorify the ordinary people and identify themselves as part of them? Increases with frequency.
Clientelism	To what extent do the party and its candidates provide targeted and excludable (clientelistic) goods and benefits in an effort to keep and gain votes? Increases in frequency.

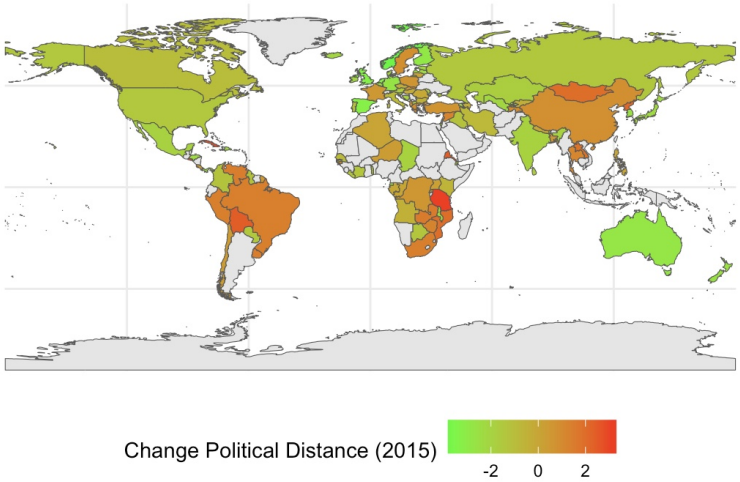
Source: Coppedge et al. (2021)

Figure A.2: Change in Bilateral Political Distance following Selected Elections

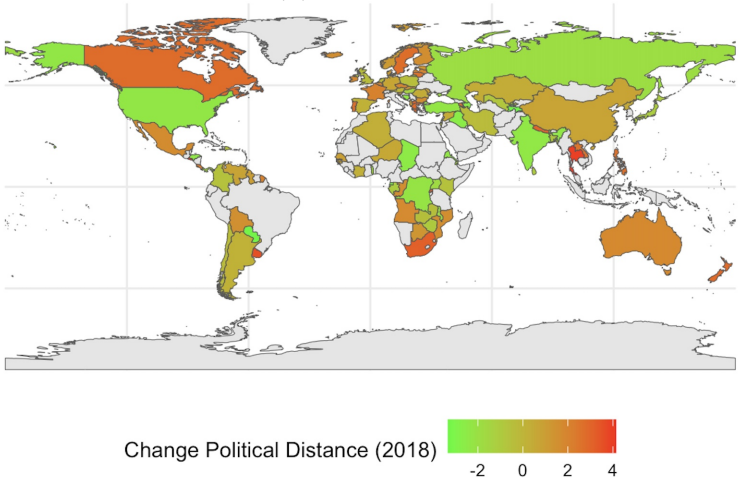
(a) USA 2016



(b) Argentina 2015



(c) Brazil 2018



Notes: This figure shows the change in political distance following selected elections. Panel (a) reports the change in political distance with the US following the 2016 election when Trump was elected. Panel (b) reports the change in political distance with Argentina following the 2015 election when Macri was elected. Panel (c) reports the change in political distance with Brazil following the 2018 election when Bolsonaro was elected.

Table A.2: Principal Component Weights on Questions

Questions	PC1	PC2
LGBT social equality	0.337	0.074
Minority rights	0.327	-0.145
Cultural superiority	0.321	0.071
Rejection of political violence	0.316	-0.207
Political pluralism	0.305	-0.148
Religious principles	0.289	0.135
Political opponents	0.277	-0.242
Working women	0.276	0.261
Immigration	0.244	0.072
Gender equality	0.242	0.119
Welfare	0.137	0.362
Anti-elitism	-0.028	0.409
Economic left-right scale	-0.119	-0.477
People-centrism	-0.150	0.462
Clientelism	-0.269	0.021

Notes: Each column displays the weight that each principal component assigns to each question. The absolute values indicate which questions are most relevant for each principal component. We observe that PC1 assigns high weights to social and democratic issues, while PC2 prioritizes economic and welfare issues.

Other data This section describes the construction of the remaining variables used in the empirical analysis.

- **Bilateral trade.** We will rely on two main sources of trade data. The first, which will be emphasized in our baseline estimations, comes from the Direction of Trade Statistics (DOTS) provided by the IMF. This dataset offers annual data from 1960 to 2023 for approximately 200 countries and regions. For robustness checks, we will also consider a secondary trade dataset compiled and homogenized by CEPII. This dataset uses Comtrade and WITS data and standardizes it across 9 broad sectors over time between 1968-2018 for 162 countries (Mayer, Santoni and Vicard (2023)).

- **Close elections.** To construct our indicator of close elections, we complement the V-Dem dataset with the dataset from Marx *et al.* (2022). We adopt Marx *et al.* (2022)'s classification for presidential and parliamentary elections. For parliamentary elections, we rely on the V-Dem data (if an election is not present in this dataset, we will not have the principal component values either). However, for presidential elections, we

use Marx *et al.* (2022)'s database to determine whether the election was close. This distinction is important because V-Dem focuses on legislative elections, whereas our analysis requires a separation between elections that could have resulted in an effective change in the head of state. For this reason, in presidential democracies, we also exclude legislative-only elections.

- **Diplomatic disagreement**. We take it from CEPII gravity database (Conte, Cotterlaz and Mayer (2023)), there they report a diplomatic disagreement indicator as constructed by Voeten, Strezhnev and Bailey (2009).

- **Output per capita** We take it from CEPII gravity database (Conte *et al.* (2023)), they report data from World Bank Development Indicators.

- **Construction of the major trading partners instrument.** The first proposed instrument aims to address the endogeneity concern that trade and political variables may influence each other, especially if sizable trade flows can impact election outcomes. To account for this, we exclude country pairs where bilateral trade flows are significant for one of the economies. Specifically, we will exclude variations where one country is a major trading partner of the other. Our instrument is defined as follows:

$$\begin{aligned}\text{Instr}^1_{ijt} = E_{dt}(1-E_{ot})(1-\text{top3}d)\Delta\text{PD}ijt + E_{ot}(1-E_{dt})(1-\text{top3}o)\Delta\text{PD}ijt \\ + E_{dt}E_{ot}(1-\text{top3}_o)(1-\text{top3}d)\Delta\text{PD}ijt\end{aligned}$$

Where E_{dt} is an indicator function that equals 1 if there was an election in the destination country, and E_{ot} is an indicator function that equals 1 if there was an election in the origin country. $top3_d$ indicates whether the origin country is a major trading partner of the destination, and $top3_o$ indicates whether the destination country is a major trading partner of the origin.

It is important to note that our political distance variable can only vary with elections. We interact the election indicators with the political distance variable to exclude cases where there are elections in both countries, but only one election meets the criteria for

influencing the political distance. This ensures that we account only for those elections that meet our desired criteria.

For example, consider Angola and the United States. The US is a major trading partner for Angola, but not vice versa. We argue that it would not be correct to assume that Angola's election outcomes are independent of Angola-US trade flows, but we contend that US election outcomes should not be influenced by Angola-US trade flows. This instrument allows us to isolate political variations that are not contaminated by bilateral trade flows.

- **Construction of the close elections instrument.** In this step, we will use the close elections indicators discussed earlier. CE_{dt} will be an indicator for a close election in the destination country, while CE_{ot} will have the analogous role for the origin country. The instrument is defined as:

$$\text{Instr}^2_{ijt} = CE_{dt}(1 - E_{ot})\Delta\text{PD}ijt + CE_{ot}(1 - E_{dt})\Delta\text{PD}ijt + CE_{dt}CE_{ot}\Delta\text{PD}_{ijt}$$

It is important to note that this is a conservative instrument. For instance, we never consider a variation from simultaneous elections unless both elections are close. In practice, if two countries have synchronized election years, we lose the country-pair variation unless both elections are close.

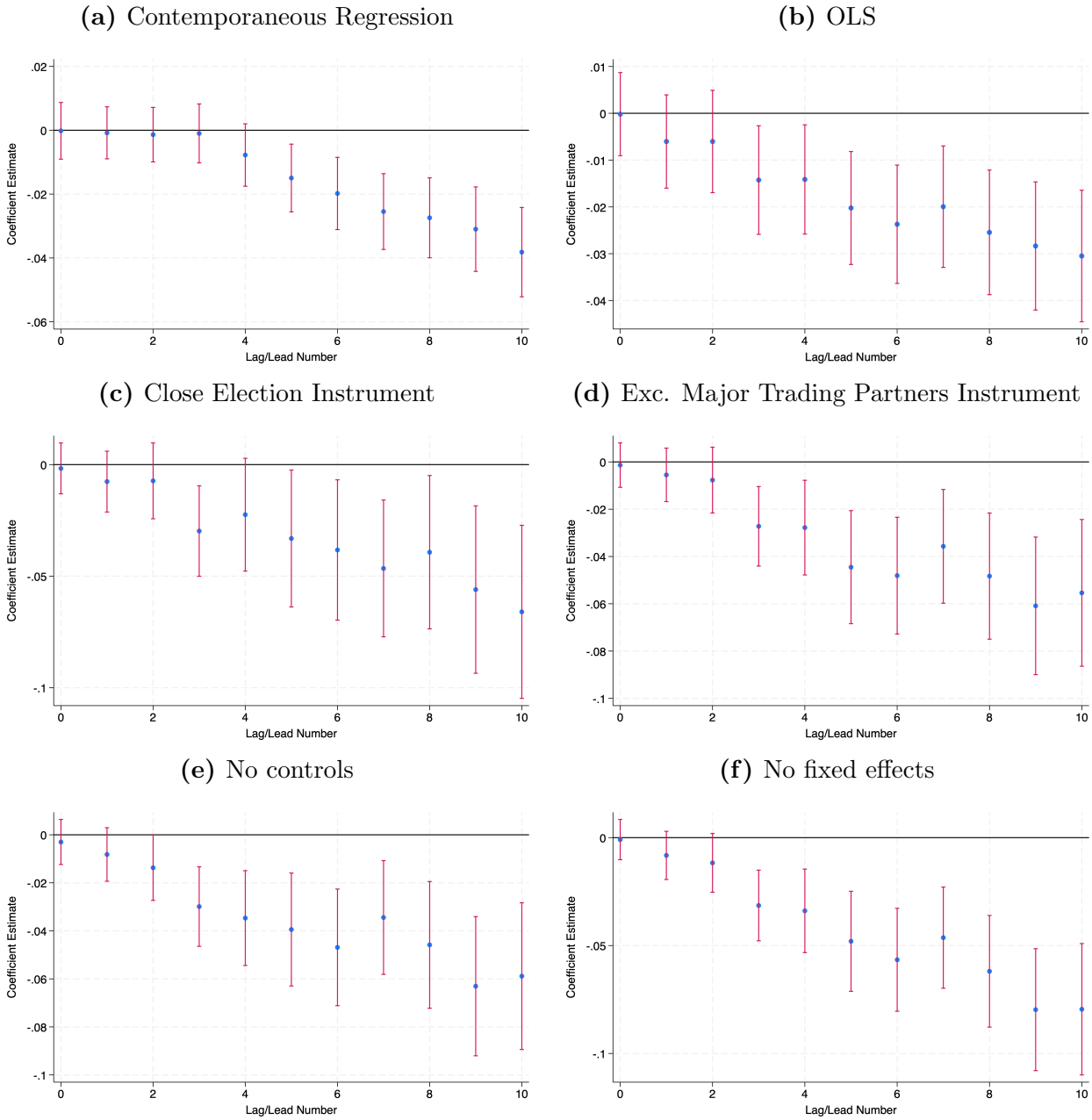
A.2. Additional empirical results

Table A.3: The Effect of Political Distance on Trade: Sectoral Regressions

Sector	Coefficient	Observations
All Sectors	-0.027	276547
	(0.008)	
Food	-0.019	221740
	(0.010)	
Wood and Paper	-0.025	225653
	(0.010)	
Minerals	-0.040	185689
	(0.010)	
Chemicals	-0.036	251653
	(0.010)	
Metals	-0.043	220202
	(0.011)	
Machinery	-0.045	245260
	(0.009)	
Vehicles	-0.038	213933
	(0.011)	
Textiles	-0.052	233843
	(0.010)	
Other	-0.045	226018
	(0.009)	

Notes: This table reports the estimate of β in equation (1), which corresponds to the semi-elasticity of trade flows to political distance. Different rows report regressions with trade data from different sectors. Standard errors are in parenthesis and clustered at the country pair.

Figure A.3: Dynamic Effects of Political Distance on Trade: Alternative Specifications



Notes: This figure shows the estimated β_h coefficients of Equation (2) in different specifications, which correspond to the cumulative log change in bilateral trade flows in response to change in the bilateral political distance in period t. The variable PD_{ijt} is standardized so that the units are standard deviations. The x-axes show the horizon h (yearly frequency). Standard errors are clustered at the origin-destiny pair. Bars represent 90% confidence intervals.

For the flexible hegemon specification we regress a variant of (3).

$$\begin{aligned}\ln X_{ijt} =& \beta PD_{ijt} + \gamma_1 \left[\mathbb{I}_{\{i=h\}} PD_{hjt} + \mathbb{I}_{\{j=h\}} PD_{iht}\right] + \gamma_2 \left[\mathbb{I}_{\{i=h\}} PD_{(-h)jt} + \mathbb{I}_{\{j=h\}} PD_{i(-h)t}\right] \\ &+ \alpha_{ij} + \alpha_{it} + \alpha_{jt} + \zeta' \mathbf{Z}_{ijt} + \varepsilon_{ijt} \end{aligned} \tag{A.1}$$

β still represent the effect of bilateral political distance on trade, γ_1 represents the interaction term with the bilateral political distance whenever a hegemon is in the country-pair and γ_2 represents the interaction term associated to the distance from the non-hegemonic country to the opposite hegemon whenever a hegemon is part of the country-pair. A.4 summarizes the results of the regression, both β and γ_2 are statistically significant. γ_1 being negative (although not significant) reflects the fact that hegemons emphasize bilateral political distance more than non-hegemonic countries. γ_2 being positive and significant reflects the strategic considerations that diminish trade if the non-hegemonic country is closer to the opposite hegemon.

Table A.4: Flexible Hegemon Specification

	Estimates
β	-0.0605
	(0.0091)
γ_1	-0.0224
	(0.0288)
γ_2	0.0749
	(0.0378)
Observations	320728

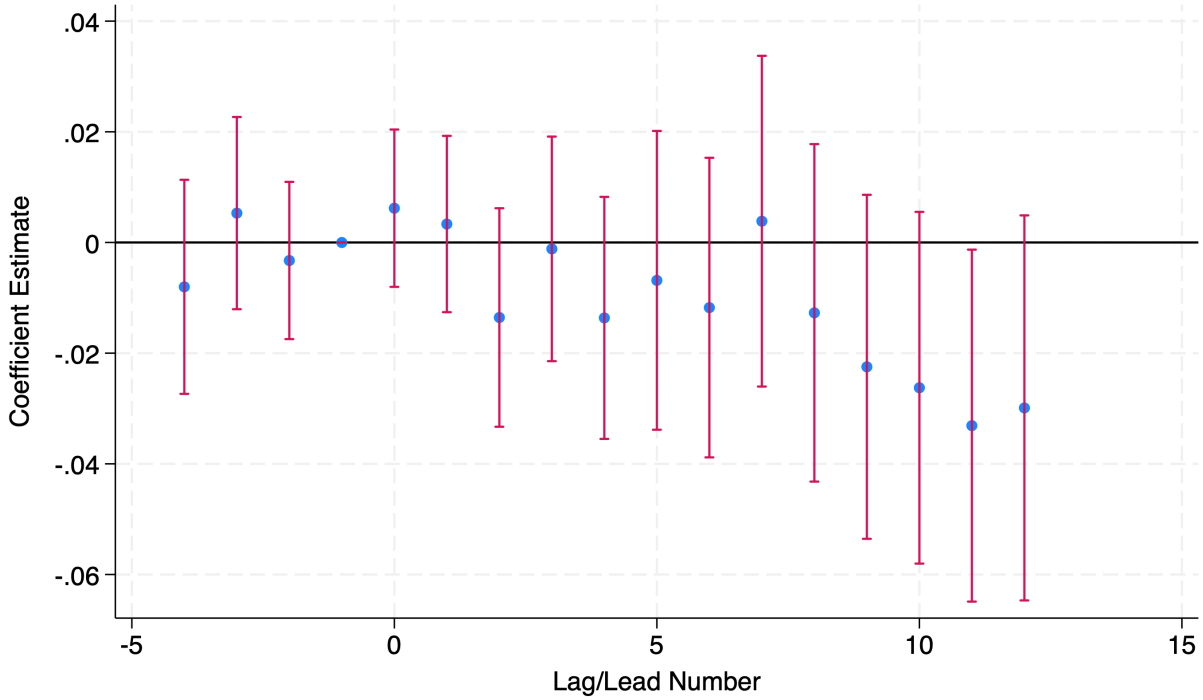
Notes: This table reports the estimate of β, γ_1 and γ_2 in equation (A.1), which corresponds to the semi-elasticity of trade flows to political distance and their respective interaction terms. Standard errors are in parenthesis and clustered at the country pair.

For the dynamic effects of the strategic behavior we estimate the following regression:

$$\begin{aligned}\Delta_s \ln X_{ijt} =& \beta_s \Delta PD_{ijt} + \gamma_s \left[\mathbb{I}_{\{i=h\}} \left(\Delta PD_{hjt} - \Delta PD_{(-h)jt}\right) + \mathbb{I}_{\{j=h\}} \left(\Delta PD_{iht} - \Delta PD_{i(-h)t}\right)\right] \\ &+ \alpha_{ijs} + \alpha_{its} + \alpha_{jts} + \zeta_s' \mathbf{Z}_{ijt} + \varepsilon_{ijts} \end{aligned} \tag{A.2}$$

Where s is the time-span that we use to differentiate the change in the trade-flows.

Figure A.4: Dynamic Additional Hegemonic Effect



Notes: The figure shows the dynamic estimated additional hegemonic effect of cumulative log change in bilateral trade flows in response to a change in the relative bilateral political distance in period t. The x-axes show the horizon h (yearly frequency). Standard errors are clustered at the origin-destiny pair. Bars represent 90% confidence intervals.

B. Model Appendix

When we use the trade data to discipline the model we need to adjust for trade imbalances, which are a feature of the data that are not present in the model. To do so, we first transition to an equilibrium with balanced trade before applying our counterfactual shocks. We do so by applying the methodology in Caliendo and Parro (2015) and solving for a counterfactual with a matrix of zero net changes in trade costs. This procedure provides us with an equilibrium that features no trade imbalances. We then use these data to solve for our counterfactual exercise.

Table A.5: Calibration inputs: GDP and Population for selected countries

	GDP	Population
United States	24.49	4.27
Germany	4.45	1.08
United Kingdom	3.29	0.87
Japan	5.87	1.65
China	16.36	18.33
India	3.24	17.79
Russia	1.94	1.88
Rest of the World	13.68	32.10

Notes: This table reports the initial values of GDP and population as shares of its world counterparts. Source is World Bank.

Table A.6: Trade Matrix for selected countries

	USA	DEU	GBR	JPN	CHN	IND	RUS	ROW
USA	0.92	0.03	0.03	0.03	0.03	0.02	0.01	0.02
DEU	0.00	0.62	0.02	0.00	0.01	0.00	0.02	0.02
GBR	0.00	0.02	0.84	0.00	0.00	0.00	0.01	0.01
JPN	0.00	0.01	0.00	0.86	0.01	0.00	0.01	0.01
CHN	0.00	0.03	0.01	0.03	0.83	0.01	0.03	0.05
IND	0.00	0.00	0.00	0.00	0.01	0.89	0.00	0.02
RUS	0.00	0.01	0.00	0.00	0.00	0.00	0.75	0.01
ROW	0.01	0.09	0.03	0.03	0.05	0.04	0.08	0.77

Notes: This table reports the initial trade matrix for selected countries. The country of origin is in the rows and country of destiny in columns. Notice columns do not add up to one because we are only reporting selected countries.

Table A.7: Changes in trade costs for selected countries

	USA	DEU	GBR	JPN	CHN	IND	RUS	ROW
USA	1.000	0.993	0.998	0.998	1.012	1.012	1.010	1.005
DEU	0.993	1.000	0.996	0.996	1.003	1.002	1.001	0.998
GBR	0.998	0.996	1.000	0.996	1.007	1.004	1.002	1.001
JPN	0.998	0.996	0.996	1.000	1.007	1.007	1.006	1.001
CHN	1.012	1.004	1.007	1.007	1.000	1.000	0.999	1.006
IND	1.012	1.002	1.004	1.006	1.000	1.000	0.998	1.003
RUS	1.010	1.001	1.002	1.006	0.999	0.998	1.000	1.001
ROW	1.006	0.998	1.001	1.001	1.006	1.002	1.001	1.000

Notes: This table reports the percent change in international trade costs implied in our counterfactual exercise.

Table A.8: Effects of Political Fragmentation: Partial and General Equilibrium Effects

	Δ International Trade									
	World		Western Block		United States		Eastern Block		China	
	GE	PE	GE	PE	GE	PE	GE	PE	GE	PE
Western Block	0.49	0.69	1.45	1.84	1.27	1.65	-2.34	-2.55	-3.27	-3.52
United States	-0.42	-0.7	1.47	1.39	-	-	-4.78	-5.51	-5.29	-6.0
Germany	0.86	1.17	1.28	1.87	3.16	3.57	-0.86	-1.01	-1.7	-1.83
Japan	-0.11	-0.13	1.79	1.96	0.77	1.13	-2.62	-2.9	-3.19	-3.45
United Kingdom	0.59	0.75	1.42	1.78	0.74	1.05	-2.0	-2.29	-3.09	-3.41
Rest West	0.77	1.15	1.45	1.99	1.21	1.59	-1.58	-1.54	-2.43	-2.43
Eastern Block	-1.46	-1.63	-2.21	-2.26	-5.49	-5.41	1.03	0.72	0.53	0.24
China	-2.38	-2.61	-2.9	-3.05	-6.0	-6.0	0.82	0.41	-	-
Russia	-0.3	-0.31	-1.26	-1.01	-5.27	-5.09	1.0	0.73	0.57	0.32
India	-1.37	-1.46	-2.8	-2.7	-5.89	-5.76	0.72	0.47	0.14	-0.13
Rest East	-0.3	-0.41	-1.19	-1.18	-4.21	-3.98	1.21	0.94	0.6	0.29
Rest of the World	-0.58	-0.6	0.02	0.16	-3.07	-0.05	-1.63	-1.95	-2.56	-2.92
World	-0.15	-0.07	0.49	0.75	-0.42	0.38	-1.46	-1.72	-2.38	-2.67

Notes: This table reports the percent change in international trade in response to the political fragmentation counterfactual exercise. Trade is expressed as imports of row countries/regions from column countries/regions. GE corresponds to the general equilibrium effects implied by solving for the model. PE corresponds to the partial equilibrium of shocking the political distance using our estimate for β.