

Rewired, not disconnected

Geopolitical risk and the map of cross-border finance

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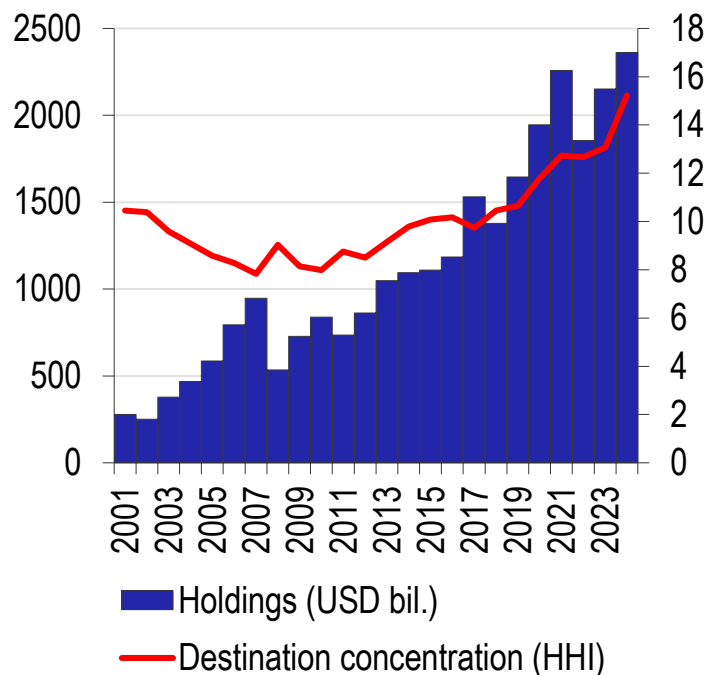
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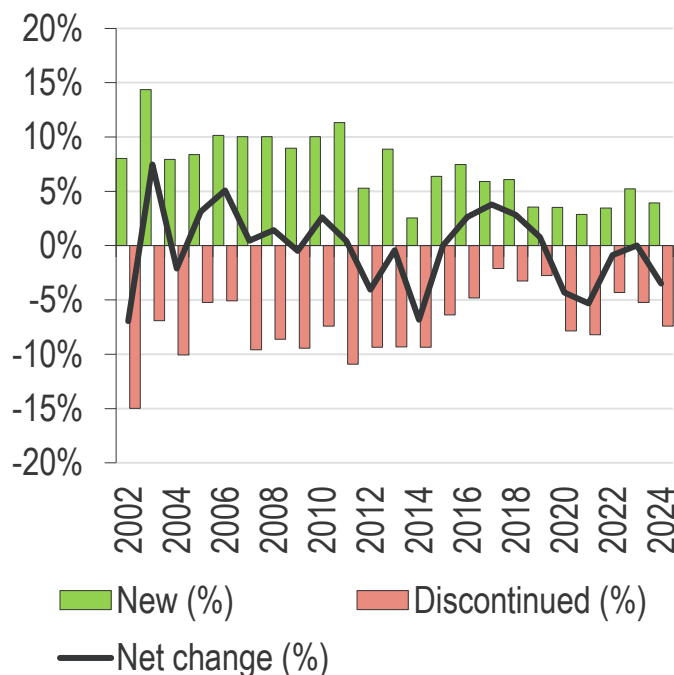


A puzzle? In the aggregate, little seems to change

Cross-border positions keep growing



...but the bilateral map is constantly redrawn

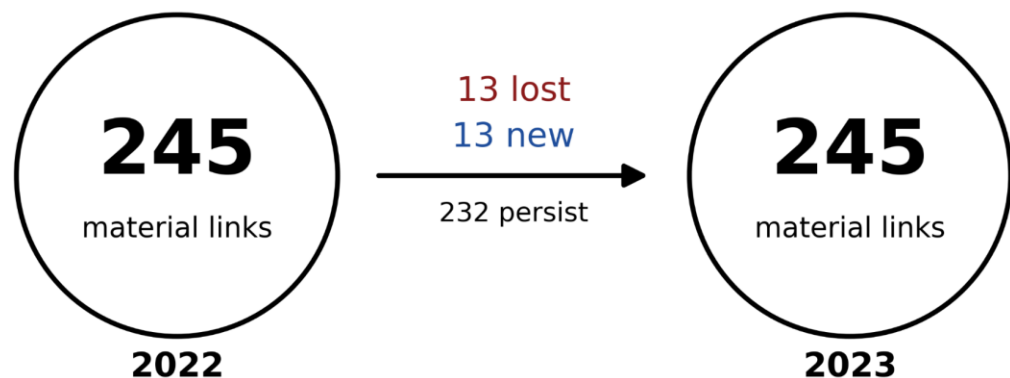


- Total holdings of foreign securities keep rising, also after 2022
- But every year a lot of individual country pairs are given up
- And a similar number of new pairs is built
- The two roughly cancel, so the totals stay calm
- But we see that holdings are concentrating in fewer destinations (partly because US shares rose in value)
- **Something did change after 2022. The totals just do not show it**

Note: IMF Portfolio Investment Positions (formerly CPIS), equity and investment fund shares, end-year, USD; bilateral positions within the 40-country sample. Left: total holdings and Herfindahl index of destination shares. Right: a position is "material" if the destination accounts for $\geq 1\%$ of the source's portfolio; new and discontinued positions are shown as % of material positions in the previous year, counting only economies that report in both years.

The network keeps its size but changes its links

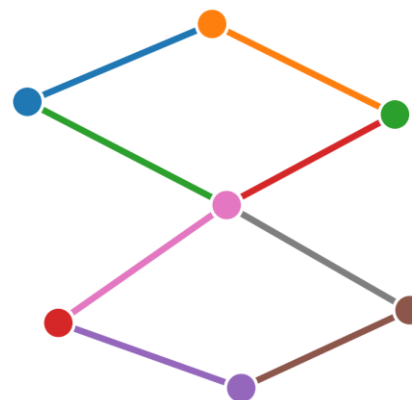
2022 vs 2023: same network size,
different bilateral relationships



Note: IMF Portfolio Investment Positions (formerly CPIS), equity holdings within the 40-country sample, end-year. A material link means the destination accounts for $\geq 1\%$ of the source's portfolio.

Network density tells us little about
resilience

Distributed network



Connector-dependent network

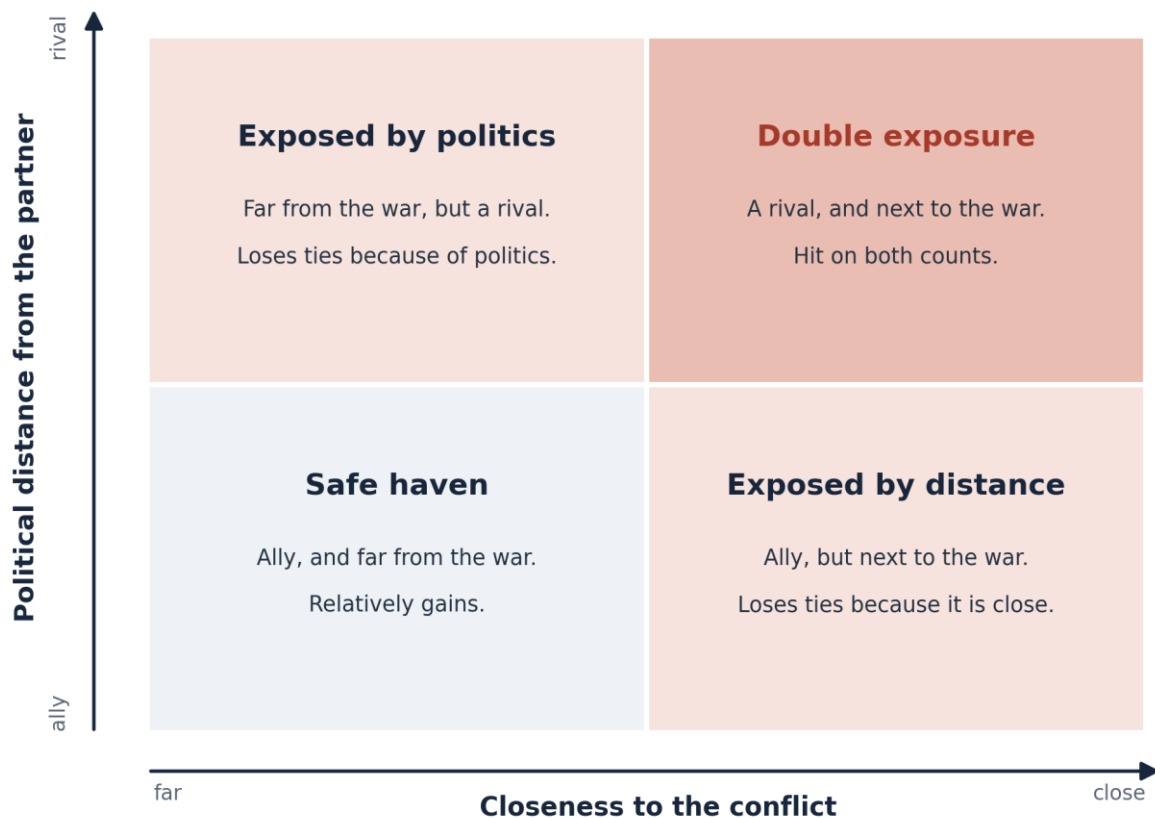


Note: Same 7 nodes, same 8 links, same density. On the left, removing any one node leaves the rest connected. On the right, losing the central connector cuts off most of the network.

- Same number of links, different map. And the map matters: the same links can be robust or fragile.
- **We learned this for banks after 2008.** Macroprudential policy moved from counting exposures to mapping who is connected to whom. The same lesson now applies to cross-border links.

So where does it rewire? In other words, who is exposed?

Two separate reasons why economic ties weaken



Political distance: how differently two countries vote at the UN

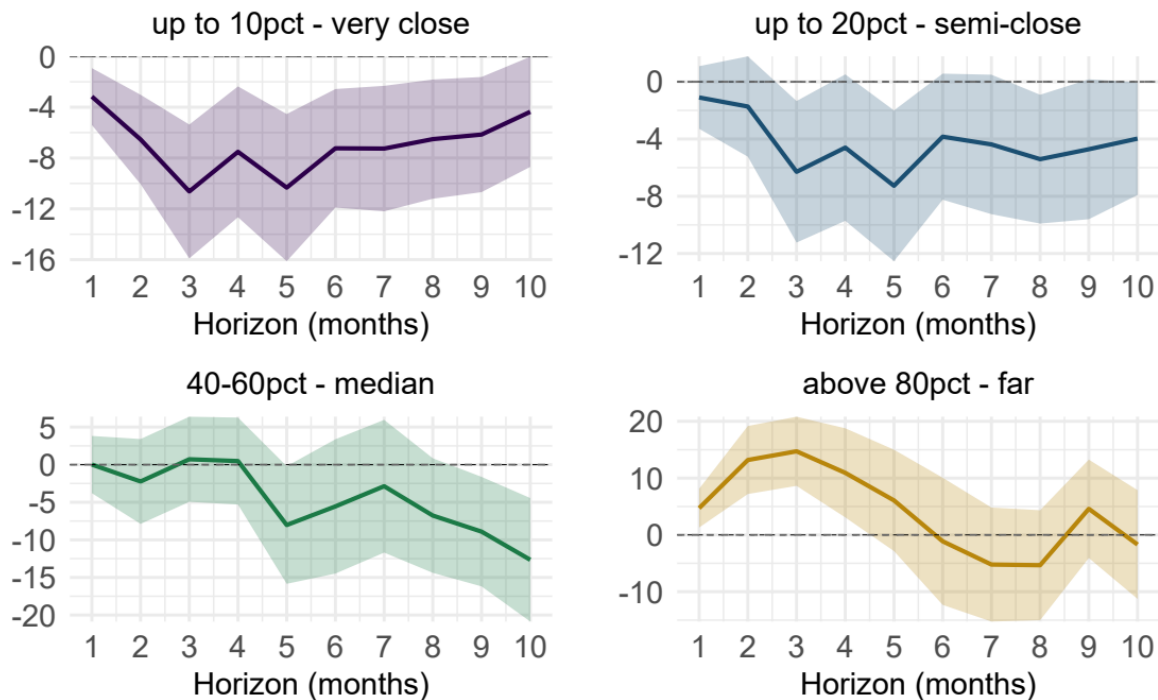
- Trade between opposing groups is down 11.7 per cent since the invasion of Ukraine, and new FDI projects are down 19.8 per cent (Gopinath et al., 2025)
- In finance, one standard deviation of political distance means about 15 per cent lower portfolio and bank holdings, and over 20 per cent for investment funds (IMF, 2023)

But flows re-route rather than stop:

- Trade and investment between rival blocs increasingly go through non-aligned connector countries (Gopinath et al., 2025)
- Sanctioned trade re-routes through third countries (Scheckenhofer et al., 2026)

Physical proximity: capital moves away from the conflict

Response of net equity flows to a geopolitical shock, by distance to the conflict



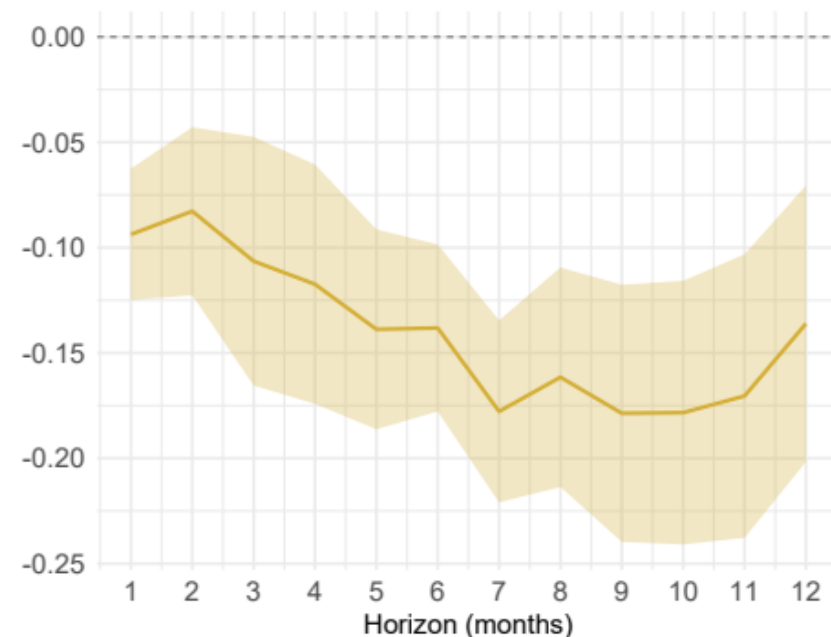
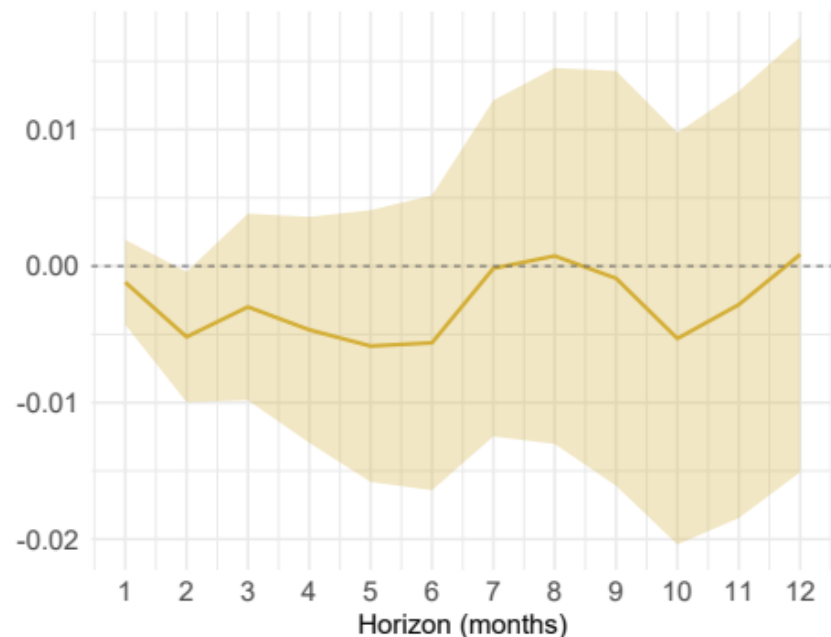
Source: [Flight from the Front Line: Geopolitical Risk, Distance, and Capital Flow Dynamics](#) (CNB Research Brief 1/2026)

Note: Local projections, 40 advanced and emerging economies, monthly, 1995 to 2024, 34 geopolitical events. Outcome: year-on-year change in 12-month cumulative net equity flows, USD bn. Groups by distance from capital to conflict: very close (0 to 10th percentile), semi-close (0 to 20th), median (40 to 60th), far (above 80th).

- Countries closest to the conflict lose equity, and keep losing it for months
- Countries furthest away receive equity, in an amount of a comparable size
 - Foreign investors drive the equity move. They pull out of countries near the conflict and move into distant ones
- Debt flows follow the same map, but only after several months
- In emerging markets, investors pull out of equity broadly, regardless of distance
- **This is not a global retreat. The money has somewhere to go.**

Before capital moves, the exchange rate does

Panel A: Response to a Conflict Shock **Panel B:** Response to a Proximity Conflict Shock



Source: [Flight from the Front Line: Geopolitical Risk, Distance, and Capital Flow Dynamics](#) (CNB Research Brief 1/2026, Hodula et al.)

Note: Local projections, log exchange rate in domestic currency per US dollar (positive = weaker currency), United States excluded.
Panel A: average response to a conflict. Panel B: interaction with distance to the conflict; a one unit change is roughly the gap between belligerent and distant countries.

- On average across all countries, exchange rates do not move at all (Panel A)
- Split by distance, and they do: the further from the conflict, the stronger the currency (Panel B)

Back to the network: exposure breaks links and blocks new ones

Effect of geopolitical exposure on forming new financial links and losing existing ones

	Formation β^F	Destruction β^L	Destruction – formation β^Δ
<i>Panel A: Estimated effects</i>			
Source-country exposure	0.0018 (0.0498)	1.2535 (1.6226)	1.2517 (1.6353)
Recipient-country exposure	-0.1234** (0.0521)	2.9789** (1.2357)	3.1023** (1.2351)
<i>Panel B: Economic magnitude of destination-country exposure</i>			
Effect of an IQR increase (pp)	-0.224	5.416	–
Baseline transition rate (%)	2.14	49.62	–
Effect relative to baseline (%)	-10.5	10.9	–
State-specific controls	Yes	Yes	Yes
Source-by-state fixed effects	Yes	Yes	Yes
Destination-by-state fixed effects	Yes	Yes	Yes
Month-by-state fixed effects	Yes	Yes	Yes
Observations	68,662	68,662	68,662
Directed-pair clusters	608	608	608

Note: Pooled state-contingent linear probability model. Formation estimated among initially inactive links, destruction among initially active links; last column is the difference. Exposure is proximity to conflict epicentres over the horizon. Source-by-state, destination-by-state and month-by-state fixed effects, state-specific controls, errors clustered by directed country pair. Joint test for destination exposure $p = 0.003$. Hodula, Siranova and Zavacky (work in progress), Table 2.

- It is the country receiving the money that matters. Being close to a conflict costs it links; for the investing country, it makes no difference
- A typical rise in exposure makes a new link about 10 per cent less likely, and losing an existing one about 10 per cent more likely
- So exposed economies are hit twice: fewer new connections, more broken ones
- Bank lending shows the same pattern. Bad geopolitical news cuts lending between rival blocs by 10 to 20 per cent more than within them, and good news does not bring it back (Emter et al., BIS, 2026)
- **Once financial links break, they do not quickly come back**

What to take away

What we see

- Fragmentation shows up as rewiring, not as falling totals
- Exposure has a geography: closeness to a conflict matters on its own, even for allies
- Links break faster than they rebuild

What it means for policy

- Monitor exposure, not only the level of risk. Geopolitical shocks come as short spikes (Hodula et al., 2024); exposure is what lasts.
- Watch the map, not only the totals. We learned this for banks after 2008; the same applies to cross-border links.
- We might need to fix the data. Bilateral financial data come once or twice a year, too slow and too coarse for shocks that play out in weeks.

Thank you

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