

The Coming Order: Strategic and Geopolitical Impacts of the Economic Crisis

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The current global financial crisis is unique in that, unlike most previous crises -- which started in the periphery of the world economy, and whose deep and long-lasting impacts were limited to isolated parts of the globe -- today's crisis is rooted in Wall Street, at the heart of the globalized market, from where it has grown and spread worldwide.

As a result, powerful, globalized economies have taken the first and hardest punches. Although still a bit groggy, they are now struggling to get back on their feet. But while economists discuss how and when economies will emerge from this crisis, strategists are beginning to debate its geopolitical implications.

Reshuffling the Deck

As with 9/11, the collapse of the Soviet Union and many other geopolitical events that preceded it, the extent of the current financial crisis was largely unforeseen. Even after its appearance, there was some hope that its effects could be limited to the U.S. and Europe. After all, these two regions accumulated 96 percent of the financial sector losses on U.S.-originated debt, according to the International Monetary Fund (IMF). Not surprisingly, though, the crisis eventually spread to capital markets, which subsequently disseminated it globally through trade. As consumption slowed down in America, exports dropped substantially in China and elsewhere, creating millions of job losses.

The exceptional scope of this crisis is tightly related to the unprecedented level of globalization and interdependence between countries. However, as some observers have noted, the crisis might represent the high-water mark of globalization and signal that we have entered a new era of deglobalization. According to the World Bank, global trade is falling at its fastest pace in 80 years, with global demand drying up, and no economy spared by the downturn. That said, some economies might prove more resilient than others, giving those countries an advantage in both how they confront the crisis and in what condition they emerge from it.

The resilience, in particular, of European and emerging economies is attracting attention in many capitals today, not least of all in Washington. This concern is not driven by a sense of solidarity, but instead by security and geopolitical considerations. For obvious reasons, those countries that come out of the crisis faster and stronger (or less weakened) than others stand to gain regional and even global influence. As U.S. Director of National Intelligence Dennis C. Blair stated in his annual threat assessment to Congress in February, "[T]he primary near-term security concern of the United States is the global economic crisis and its geopolitical implications." Meanwhile, in a March interview with Newsweek, U.S. Deputy Secretary of State James Steinberg confirmed that the Obama administration is very concerned with maintaining America's position as global leader.

Steinberg's remarks are not limited to the crisis, but refer more broadly to shifts in the global balance of power. An emerging consensus suggests that America's "unipolar moment," as described by Charles Krauthammer in 1990, has come to an end. As illustrated by the wars in Iraq and Afghanistan, the U.S. ability to take unilateral military action, without the support of its allies, has been weakened. The Russia-Georgia war and the closing of the U.S. air base in Manas, Kyrgyzstan, demonstrated diminished U.S. influence in Central Asia and the Caucasus, along with a corresponding Russian resurgence. Even Slumdog Millionaire's clean sweep of the latest Academy Awards ceremony can be seen as a signal of a relative decline of American soft power. Finally, the financial crisis revealed that the U.S. economy, for all its might, is not immune to major crashes.

Despite all these signs of decline, America remains the "lonely superpower," and will remain unmatched by its rivals for many more years, and probably decades, to come. In fact, instead of American decline, it would be more accurate to talk about bad U.S. policies that have damaged American influence abroad coinciding with the "rise of the rest." The "rest" includes new powers, but also non-state actors such as transnational organizations like al-Qaida and supranational institutions like the EU, all of which are increasingly challenging American predominance.

While the current trend is from a unipolar world towards a multipolar one, the current structure of the geopolitical landscape is somewhere between the two, what might be thought of as a "unimultipolar" arrangement. This means that besides the U.S., which is the only superpower with global predominance in all spheres of power, there is a constellation of regional powers challenging U.S. influence, whether locally or regionally. Moreover, some of these powers -- in particular, Brazil, India and China -- are emerging as global powers, while Russia is resurging as a great power. Together, these four

countries comprise the so-called BRIC countries, an acronym coined in 2001 by Goldman Sachs analyst Jim O'Neill. The European Union, taken as a whole, can also be seen as an emerging global actor.

Now the economic crisis is likely to further reshuffle the deck in the competition for global power. China's rise relative to the U.S., for instance, has accelerated considerably since the beginning of the crisis. It is now treated as a de facto global power -- almost as an equal -- by the U.S., at least with regard to economic matters, with the two countries for all intents and purposes forming a "G-2." While some Chinese scholars encourage China to grasp this "historic opportunity" to strengthen its global position, the common discourse out of Beijing remains one of multilateralism and a "peaceful rise," even if official rhetoric has grown slightly more assertive.

Beyond China, the crisis has empowered emerging countries within international financial institutions (IFIs), notably through the emergence of the G-20 as the new economic forum. This could be just a first step towards a broader reform of global governance institutions, including the U.N. Security Council. Down the road, we might find ourselves living in a transformed world, with not one but several global powers discussing international affairs in global forums that reflect a new global order.

Just what that new order will look like is difficult to foresee, because it is impossible to forecast with certainty who will emerge from the current crisis a relative winner and who a relative loser. But a closer look at the impact of the crisis in specific areas can offer some ideas about the possible range of strategic and geopolitical outcomes. In particular, the impact of the crisis on military, economic and other less tangible forms of power, as well as on global stability, will prove determinant.

Shaking Economies

The most obvious effects of the crisis concern the economy. Hence, looking at the economic resilience of all potential global powers might offer a first glimpse of the post-crisis global order, or at least give an idea of which players will remain in the game.

James Fallows, writing recently in the Atlantic, explained that China's vulnerability to the current crisis is very similar to U.S. vulnerability in the 1920s. Like the U.S. then, China today is a major global exporter that depends on global demand, only China is much more dependent on exports than the United States was in 1920. "In proportional terms, today's China is five times as reliant on foreign customers to create domestic jobs as America was in 1929," Fallows wrote. "So unless China can find a way to keep selling when its customers have stopped buying, it will face a proportionately greater employment shock."

However, China also possesses approximately \$2 trillion in foreign-exchange reserves. This allowed Beijing to launch an ambitious stimulus plan of \$600 billion -- a much larger stimulus relative to the size of its economy than what was decided in Washington -- which should help Beijing weather the storm. "China's economy may suffer more than most others," Fallows concluded, "but it also has more tools and resources in reserve than most others."

In terms of resilience among the BRIC countries, Brazil appears to occupy second place. Exports account for just 14 percent of its GDP, and Brasilia has accumulated about \$200 billion in foreign currency reserves. This should isolate the country from falling global demand and offer some flexibility for stimulus efforts, albeit limited ones. In 2009, Brazil could be one of the rare economies to both avoid recession and maintain a positive trade balance, according to economists.

While India is expected to maintain GDP growth of 5 percent, it is likely to run a significant budget deficit and does not have the foreign exchange reserves to finance it. And although Brazil's GDP will rise, economic growth will be insufficient to absorb its growing population. That could lead to social unrest, especially if authorities are perceived to handle the crisis ineffectively. Furthermore, as a result of decreasing foreign investments, the domestic situation is likely to worsen.

Russia is in many regards the weakest link among the BRIC countries. Indeed, the decline of energy prices is threatening its budget, which was set to go into deficit should the price of oil fall below \$70 a barrel. (At the time of this writing, the price of a barrel of oil was \$52.) Meanwhile, foreign investors, spooked by Russian fiscal and foreign policy, are fleeing the country's capital market. In the meantime, consumer prices are rising and the currency is devaluating dangerously. On the positive side, with about \$550 billion, Russia holds the world's third-largest gold and foreign exchange reserves.

Interestingly, besides its distinct consequences on individual BRIC economies, the crisis had a coalescing political impact on the BRIC as a whole. On March 14, on the margin of a G-20 ministerial meeting, finance ministers of Brazil, Russia, India and China issued their first-ever joint communiqué, calling essentially for a "reform of international financial institutions." Although BRIC is unlikely to emerge as a political entity, its members seem to have realized that they wield more power and legitimacy collectively than individually. Hence, more BRIC summits urging global reforms could follow.

In Europe, by contrast, the global crisis has had much more of a divisive impact, with some leaders, such as Hungarian Prime Minister Ferenc Gyurcsany, arguing that a new "Iron Curtain" threatens to divide Europe between rich and poor states. Indeed, the crisis has hit

Eastern European countries particularly hard. At the same time that their exports are falling, their debt is skyrocketing, with devaluing local currencies making it impossible to repay foreign-currency loans. Hence, they are turning towards Brussels -- which recently doubled its financial assistance package to troubled economies -- for "European solidarity." Whether the crisis will mean the end of the "European dream" for Eastern European countries will largely depend on how the EU and its major members handle the situation.

The U.S. might be facing the greatest challenge of all, for it must regain the confidence of the entire world. As Wall Street is largely seen as the cause of the current economic troubles, the American economic model will most likely be tarnished, losing its appeal versus alternative models of capitalism championed by Europe and China, among others. In other words, the global crisis has already significantly eroded American soft power, and could do even more damage should the situation worsen.

Effects on Hard Power and Soft Power

Economic power will be an important element of any potential challenge to American hegemony, but it is only one sphere of power among others. The financial crisis will certainly have an impact on military, political and cultural power as well.

In the military realm, the crisis will make itself felt first and foremost on budgets. One Belgian military officer who spoke on condition of anonymity recently expressed his belief that whichever countries have not yet cut their military budget this year will most likely do so next year. Indeed, as state income is expected to decline and spending to increase, the allocation of resources will become an increasingly tricky exercise for governments.

In this context, President Dmitri Medvedev's recent declaration that Russia will modernize its

army was quite surprising, especially coming after he had previously resisted pressure from the Russian general staff to increase the defense budget. Nevertheless, a substantial reduction in Russia's officer corps, along with possible bilateral U.S.-Russian agreements on arms reduction, could help balance Moscow's budget.

In China, the impact of the crisis on an already unknown military budget is uncertain, according to the latest Pentagon report on Chinese military power. While defense spending will still grow, the pace may not be as fast as in previous years. Nevertheless, although the imbalance between Chinese and American military capabilities remains considerable, it is still reasonable to expect the Chinese military to continue reducing the strategic gap with America.

By contrast, the Indian army's urgent modernization needs might be delayed, especially since the construction of a new aircraft carrier is set to take a heavy toll on its defense budget.

Given that the U.S. is already mired in two costly wars, Washington would have difficulty opening a third front or even deploying significantly more troops abroad should the need arise. Nevertheless, possible theaters do not lack. Pakistan, Somalia, and Mexico, among other countries, all constitute threats to American security. But none are likely to become major battlefields as long as U.S. forces are strained elsewhere, and while the financial crisis continues to grab a significant share of decreasing resources.

Although military intervention is not the solution to all problems, it is certainly a useful tool in international politics. From a global perspective, the likely end of American interventionism could prove as damaging to global stability as the recent era of excessive American interventionism under President George W. Bush. Aggressive regimes, criminal

networks or terrorist groups could be tempted to increase their activities in the wake of American retreat.

American loss of appetite for military interventionism will inevitably have an effect on NATO's current operations in Afghanistan, as well as on the future of the alliance. It is telling, for instance, that President Barack Obama put so much emphasis on the development of civilian missions in Afghanistan, instead of on military operations, during the announcement of his Afghanistan-Pakistan strategy.

European ambition of creating a common defense could also suffer new setbacks as the crisis unfolds. As EU members develop protectionist measures and simultaneously decrease their defense budgets -- or increase them below the rate of inflation -- they are less likely to focus their energy on European Security and Defense Policy (ESDP). However, European policymakers could also use the crisis as an opportunity to, (a) rationalize European defense expenses; and (b) shift public attention away from economic mismanagement by diverting it to a grand project such as ESDP.

More broadly, decreasing budgets will force defense departments worldwide to rationalize their spending and redefine their priorities. In the United States, the recent military debate about whether to emphasize asymmetrical warfare (high likelihood, low impact) or conventional warfare (low likelihood, high impact) will become even more intense. BRIC members and the EU might have to redefine their priorities as well.

The crisis also could encourage proponents of denuclearization, given that nuclear programs represent a significant part of the military budgets of nuclear countries -- at least 7 percent of the U.S. Department of Defense budget in 2008. However, nuclear disarmament will in turn trigger intense strategic debates, notably over how to prioritize the targets for the remaining missiles.

Regarding other spheres of power, the impact of the crisis is much less certain but just as real. Politically, for instance, the Western model of democracy could be discredited in some parts of the world as too weak to handle troubled times, and Asian regimes -- such as China or Japan -- could become new regional models. In terms of popular culture, it's reasonable to wonder whether the "American dream" as portrayed in U.S. movies and TV shows -- that of splendid houses, breast-enhanced wives and fancy cars -- will maintain its appeal in this period of economic downturn. That raises the question of whether that element of American soft power will survive the crisis unscathed, and if not to what degree it will suffer.

Global Unrest

Far from being restricted to the United States and the other global powers, the crisis is already expanding around the globe, although the forms it will ultimately take will vary. In developing countries, the decline of cash inflows will be a growing problem. Indeed, developed countries are already falling short on their commitments to development aid -- most notably those pledged at the 2005 G-8 Summit at Gleneagles -- and the crisis is expected to make pledging additional aid even more difficult. As indicated in a recent report by the World Bank, worldwide remittances are also expected to fall sharply, which could increase poverty in many countries. Foreign Direct Investment (FDI) is expected to decrease as well, which will further hamper the development of disadvantaged countries.

The decline of resources for developing countries could have destabilizing consequences. Many sectors of developing societies will receive fewer funds, leaving local governments to rethink the allocation of resources between health, education, economic development and other areas. This will inevitably create growing disparities, tensions, and unrest, all of which could be exacerbated by problems related to corruption and poor

governance. The economic crisis will also make it harder to find solutions to the food crisis, which is far from over in many parts of the world. Where the food crisis is still present, the effects of the economic crisis will be felt even more dramatically.

As a growing number of people struggle with poverty, we are likely to see more waves of migrations, possibly leading to tensions and conflict in destination countries. Immigration is not inherently negative and does not automatically lead to conflict. However, when resources are scarce, inflows of migrant "have-nots" are rarely seen in a positive light by local "have-littles."

The Coming World Order

The economic crisis is exceptional in its character and its scope. While global attention has to date focused on short-term consequences and potential fixes, strategists and policymakers have already started to evaluate long-term geopolitical and strategic impacts.

Outcomes are impossible to predict, but what's at stake is already clear. For Washington, the crisis represents another potential threat to its global leadership. For Beijing, it represents an opportunity to increasingly assert its global influence. The crisis is accelerating the transition towards a new global order, one which started in 2001, with the 9/11 attacks that marked the end of American invulnerability. Incidentally, the "BRIC" acronym was coined that same year, heralding the rise of new challengers to U.S. predominance.

Meanwhile, the crisis is also creating new flashpoints for unrest and conflict. Poverty, inequality, migration and poor governance, all exacerbated by the crisis, could trigger greed and grievances, which could in turn lead to conflict. Furthermore, due to financial constraints, the deployment of peacekeeping operations is already suffering, and is likely to

become even more burdensome and hence a lower priority for the U.S., EU, NATO and U.N. Hence, the image of a more unstable, almost Kaplanesque world is starting to emerge.

The exact shape of the coming order is still unknown, although it is almost certainly moving towards multipolarity. This does not mean, however, that it will also entail increased multilateralism. Indeed, global actors have the opportunity to choose between cooperative multipolarity and competitive multipolarity. The former is more desirable, as it is more stable and peaceful. But the paradox of the global crisis is that while optimum solutions are multilateral and coordinated, the political reactions to the crisis tend to trigger isolationism and protectionism, insidiously leading not towards cooperation, but towards competition.

Countries can still opt for cooperation in the hopes of shaping a better world, but this will require courageous decisions from global and emerging powers. America and, to a lesser degree, Europe must prove that they are ready to accept sharing power with rising challengers, starting with a reform of global institutions. Europe, if it wants to shape the new order in its democratic and multilateral image, must assume its global responsibilities, starting with the elaboration of a real common foreign and defense policy. Finally, the BRIC nations, and other emerging global and regional powers, have the opportunity to expand their reach and influence.

Not everyone can emerge from the crisis a winner. But maximizing individual gain will depend on minimizing collective losses. And, for everyone involved, that will require developing a long-term strategy instead of focusing on short-term gains.

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