ECONOMY AND ECOLOGY 14.04.2022 | Marc Saxer

The coming world order

Russia's invasion of Ukraine has upended the existing world order — and with it the global energy, production, distribution, and financial systems

The war in Ukraine is part of the struggle for a new world order. Russia and China are openly challenging the Pax Americana. But the question how the next world order will look like remains open. In Moscow and Beijing, but also in Washington, the model of a multipolar concert of the great powers, with exclusive zones of influence, is finding support. Despite a growing unwillingness to play the role of 'the world's policeman', however, the majority of Americans have not yet abandoned the unipolar, American, liberal world order. And not only in China, there is still support for the Westphalian model with its emphasis on nation state sovereignty and its condemnation of post-colonial meddling in internal affairs.

These three models envision very different ground rules. Who is authorised to use force – all states, only the strongest, or only the hegemonic power? Does the law of the strongest apply, or the strength of the law? Is there a historical ideal (e.g. liberal democracy and market economy) towards which all states will (or should) develop, or are there multiple modernities with competing political systems and cultural civilisations that can coexist more or less peacefully? Will there be a global showdown between an alliance of democracies and the 'axis of autocrats'? Or is the price of peace giving up on implementing universal human rights?

Which of these models will prevail – or from what precise mixture of old and new elements the new world order will emerge – will determine not only war and peace, but also what the global energy, production, distribution, and financial systems of the future will look like.

The global energy system

In the German debate, under the immediate impact of the war, the focus is mostly on how to deny Russia the revenue from its oil and gas exports

without asking too much of consumers who are dependent on Russian energy supplies. In the long term, this dependence is to be reduced by accelerating the energy transition away from fossil fuels. Less attention is being paid to the efforts of China and India to avail themselves of the cheapest possible supplies on the Russian energy market without being hit by Western sanctions. And far too little attention is being paid to the efforts of important suppliers and their customers to 'de-dollarise' the international energy trade.

It takes little imagination to foresee the biggest shake-up in global energy trading since the oil price shocks of the 1970s. What is less clear, however, is the direction in which the global energy system will move. Given the ongoing geopolitical confrontation, the imperatives of climate protection and energy security are now pointing in the same direction. On the one hand, this is likely to further accelerate the exodus of global capital from fossil industries. On the other hand, the industrialised countries are technologically still not in a position to free themselves from their addiction to fossil fuels. And it is precisely the bridging technology of natural gas that has now hit a geopolitical dead end. In the short term, Germany will hardly be able to close the looming supply gap without committing climate policy sins involving coal and nuclear power. In the long term, alongside renewable energies, the international supply chains for hydrogen need to be developed at pace.

The US is trying to slow down the economic rise of its rival China.

In the medium term, however, this means having to satisfy the demand for gas by diversifying suppliers. Surprising shifts of alliances, involving both old enemies (e.g. the US and Venezuela) and old friends (e.g. the West and the Arab monarchies; Russia and Kazakhstan), cannot be ruled out. How quickly, in this competitive world, the need to secure national energy supplies can collide with the principles of value-based foreign policy was something the new German government had to discover in its very first days in office.

The global division of labour (production and supply chains)

Since the 2008 financial crisis, global trade and cross-border investments have not really picked up again. The Covid-19 crisis has made people more aware of the vulnerability of global supply chains. The failure of China's Zero Covid strategy and the drastic lockdowns in Shenzhen and

Shanghai indicate that, two years now after the outbreak of the pandemic, the risk of disruptions to global supply chains has still not been eliminated. If parts from the Far East are missing, the assembly lines in Europe, too, come to a standstill. The paradigm shift away from efficiency ('Just in Time') to greater resilience ('Just in Case') is accelerating the hidden trend towards deglobalisation that has been under way for some time.

But geo-economic as well as geopolitical motives also favour the shortening and unbundling of supply chains, and are now driving the separation and isolation of markets. The US is trying to slow down the economic rise of its rival China. Behind the scenes, pressure from both is mounting on their allies and on third countries to choose sides. Europeans and Asians are still resisting being drawn into this new Cold War. But the disputes over gas pipelines, chip manufacturers, and the 5G communications infrastructure show how quickly companies and entire states can get caught between opposing fronts. The ultimate outcome of this development could quite possibly be rival blocs that make it difficult or impossible for unwanted competitors to access their markets.

Hardly have they escaped Trump-America's sanctions, German companies are now facing headwinds on the Chinese market. Nevertheless, the majority is resisting the pressure to decouple from China, while some double down on the Chinese market despite ever worsening conditions. Given the importance of the Chinese market, the call in the Federal Government's Indo-Pacific strategy paper to reduce one-sided dependencies through diversification therefore often goes unheard.

But the Russian war of aggression against Ukraine might now alter this calculus. Hardly anyone would have thought it possible that the West would react so quickly, so strongly, and with such unity to Russian aggression. Russia's expulsion from the SWIFT system, the sanctions against the Russian central bank, but also the voluntary withdrawal of Western companies from the Russian market, all this has made its mark – not least in China.

Even some in Germany were surprised at how quickly even supposedly sacred cows like the Nordstream 2 gas pipeline were slaughtered. This experience of enormous public and political pressure is likely to lead many German companies to reassess their strategies towards other 'problematic markets'. Should the sales opportunities for German business in global markets be closed off in the medium-term future, Germany will have to rethink what it is willing to do to lead the vital European home market out of its protracted crisis.

Less well known is the geostrategic motivation behind the Belt and Road Initiative.

The realignment of the global economy according to geopolitical interests is putting key industries such as the German car industry under pressure. If the engine of growth falters, distribution conflicts within and between societies intensify. Fear of social decline is increasing even among the middle classes. This fear of decline is the sounding board that populists use for their agitation against the preconditions for the success of the export model, the free flow of goods, capital, people, and ideas. The global trend towards protectionism is thus driven not only by external factors but also by internal pressure. In such a world, there can no longer be any world champions in exporting. Germany above all will therefore have to rethink its export-oriented economic model.

Infrastructure

When Western critics discuss the Chinese Silk Road project, their focus is usually on debt traps or on the creation of political dependencies. There is a justified suspicion that the mammoth project represents a Chinese push to become a dominant power in Asia and in the world. Less well known, however, is the geostrategic motivation behind the Belt and Road Initiative.

Since the end of World War II, the United States has established bases on a chain of islands running from Japan in the north to Indonesia in the south. And since the Obama administration announced its 'Pivot to Asia', the US has been concentrating its forces here. Between the Strait of Malacca and the Strait of Hormuz (the Americans call these straits 'choke points'), the United States and its allies can block Chinese trade and supply routes at any time. China feels encircled and reacts in an aggressively defensive manner.

The aim of its arms build-up in the East and South China Seas is to break through the 'First Island Chain', and to drive the US out of Chinese coastal waters. Chinese hawks go one step further and want to force the reunification of the 'unsinkable American aircraft carrier' Taiwan with the motherland. As Chinese bombers fly over Taipei, Chinese propaganda accuses the US of challenging the status quo by questioning the One China policy, and thus provoking a conflict. This is a highly

dangerous poker game, not only because Taiwan produces indispensable semiconductor chips, but also because from the perspective of the Americans, traumatised by Pearl Harbor, the defence of their homeland begins at the First Island Chain. So in the Taiwan Strait lies a fuse that could set off World War III.

By means of the Silk Road project, China is therefore trying to break out of the American stranglehold towards the West. The immediate goal of the numerous ports, corridors, and railway lines is to prevent the disruption of Chinese supply routes. The initial enthusiasm of the landlocked states of Central Asia shows the high hopes held by the BRI partners that the strategy for connectivity along the ancient Silk Road will lead to prosperity gains for all. The real prize, however, lies at the other end of Eurasia: the European market, which is supposed to guarantee sales opportunities for Chinese products in the long run. If Beijing succeeds in tying Europe closer, China and Russia will have taken a big step towards their goal of neutralising US influence in Eurasia.

Chinese hawks now see in the sanctions against Russia an opportunity to attack the supremacy of the US dollar.

With the start of a new Cold War, however, a new Iron Curtain now threatens to cut through the Chinese Silk Road. From China's point of view, that would be a geostrategic catastrophe. This is one reason why China, despite the only recently proclaimed 'limitless friendship', does not really provide substantive assistance to its junior partner Russia (the second reason is the Russian recognition of two breakaway provinces of a sovereign state; looking at Taiwan, a Chinese horror scenario). Beijing thus has a vested interest in a quick end to the Ukraine war (but is reluctant to take on the responsibility of a mediator). If this does not happen, China is likely to push forward with the expansion of the maritime Silk Roads.

Money and financial markets

From the point of view of Chinese strategists, following the decline of American industry, the remaining foundation – and thus the Achilles' heel – of US hegemony is the role of the dollar as the reserve currency on the international goods and financial markets. China has therefore been tinkering for some time on an alternative to the SWIFT system ('CIPS') and on a digital currency (Digital Yuan, e-CNY). However, neither of these instruments is yet ready to pose a real threat to the greenback.

Chinese hawks now see in the sanctions against Russia an opportunity to attack the supremacy of the US dollar. The freezing of Russian central bank reserves has put all the world's central banks on high alert. In order not to be blackmailed themselves, they are now likely to shift reserves on a grand scale. If this is at the expense of US investments, it could destabilise the dollar's position as the global reserve currency.

The role of the US dollar as a transaction currency is also a source of frustration. After all, the inflationary pressure emanating from the American Federal Reserve is passed on around the globe by all those actors who rely on the US dollar for conducting their cross-border trades. Russia, China, India, and Iran have therefore been trying for some time to 'de-dollarise' their economies by using a broader basket of currencies for their foreign trade.

It is therefore hardly surprising that Russia now wants to settle its oil and gas transactions only in roubles. China's attempts to de-dollarise its own foreign trade also aligns with Beijing's strategic goal of upgrading the global status of its own currency. But if a US ally like Saudi Arabia is now seriously negotiating to settle its oil deals with China in yuan, this shows how widespread is the resentment of the hegemon. This is not risk-free, because after the abandonment of the gold standard the US dollar was tied to the central commodity of fossil industrial capitalism by the clearing and settlement processes for the global oil trade. If other OPEC countries were to abandon the petrodollar, the returning greenbacks would probably further increase inflationary pressures in the US in the short term. In the long term, both the Chinese RMB and blockchain-based cryptocurrencies could mature into stable transaction currencies. US-sceptical strategists believe that if the US dollar's functions as a reserve, investment, and transaction currency do indeed continue to erode, then the position of the US currency as the global reserve currency could actually begin to totter.

American hawks want to 'bleed the Russians to send a signal to the Chinese to keep their hands off Taiwan'.

However, even after a decade and a half, efforts aiming at 'de-dollarisation' have not seriously jeopardised the position of the US dollar as the global reserve currency. As recently as last year, 90 per cent of all foreign exchange transactions continued to be settled in US dollars, and 60 per cent of all central bank reserves are invested in dollars. The blockchain cryptocurrencies in particular are a long way from being able to replace the dollar.And whether a Chinese (digital) currency without open Chinese financial markets can actually take over the

> functions of a reserve currency is doubtful. American experts therefore believe that the dollar's position is even more entrenched today because foreign central banks know that in an emergency the American Fed will do everything to shore up the dollar-denominated part of the financial system.

What the coming world order will look like will be decided by global power relations. Russia has overestimated its own strength. Even if Moscow still succeeds in winning the war in Ukraine militarily, in geopolitical terms it will fall back into the second tier as China's junior partner. However, the new instability on the European continent is likely to dampen the economic outlook for Western Europe as well. Following the Ukrainian reality check, geopolitical dreams of an independent European power pole will therefore certainly be re-evaluated by EU member states.

This leaves only China and the United States as powers capable of setting and maintaining order. This explains why Washington and Beijing do not wish to be drawn into this 'European conflict': the two superpowers read the conflict above all through the lens of their competition over global hegemony. Accordingly, American hawks want to 'bleed the Russians to send a signal to the Chinese to keep their hands off Taiwan'. Although this is not uncontroversial in Washington, a bipartisan coalition for a Cold War against the 'alliance of autocracies' has already been in place for some time.

In Beijing, on the other hand, there is still disagreement as to whether it is really in China's interests to disappear behind a new Iron Curtain alongside a weakening Russian pariah, or whether China would not benefit much more in the long run from an open world order. Geopolitically, it would therefore be a fatal mistake to over-hastily lump the Chinese and the Russians together in an 'axis of autocracies'.

It would be better instead to examine together what a rules-based, multilateral order might look like, one that provided a framework within which the core interests and security concerns of all the powers could be peaceably negotiated and reconciled. Those who think this is unrealistic should remember the last Cold War: then, too, cooperation between systemic rivals within the framework of agreed ground rules was successful.

This article originally appeared in German on Blog Politische Ökonomie.



Marc Saxer

Marc Saxer coordinates the regional work of the Friedrich-Ebert-Stiftung (FES) in the Asia Pacific. Previously, he led the FES offices in India and Thailand and headed the FES Asia Pacific department.