After the G-Zero: Overcoming fragmentation

Ian Bremmer
GLOBAL RESEARCH PROFESSOR, NEW YORK UNIVERSITY
PRESIDENT, EURASIA GROUP
FALL 2016

The views expressed in this paper are those of the author(s) only, and the presence of them, or of links to them, on the IMF website does not imply that the IMF, its Executive Board, or its management endorses or shares the views expressed in the paper.
Executive summary

It is commonly understood that the world is working through a period of “new normal” economics – the bottom of an economic cycle, characterized by durably slow growth. Far less appreciated is that we are also at the bottom of a longer-term geopolitical cycle. The global order that prevailed since the end of the Second World War has hit its limits. A breakdown in longstanding domestic, regional, and international political equilibria is making policymakers both less able and less willing to collaborate internationally. The result: a G-Zero world characterized by a growing vacuum in global governance. But this breakdown will not continue forever. Sooner or later, the G-Zero will give way to whatever new world order comes after it. The question is whether citizens across the world will remain passive throughout this process, or take on a proactive role in determining what future they want to live in.

The current fracturing of international governance along with growing grievances over the values underpinning the Bretton Woods order, has already led emerging powers to begin creating new and alternative institutions of global governance, as their power and influence in global institutions is not keeping pace with their growing international importance and interests. Instead of focusing on whether this trend should be feared or welcomed, observers would do well to recognize that it will persist regardless and that there is more to be achieved by interconnectedness and cooperation than ever. Yet not all of these “alternative” institutions will be morally equal: some will make valuable contributions to a world that increasingly requires coordinated international action to solve festering problems, while others will remain little more than whimsical attempts at enhancing selfish national influences.

We stand at a turning point. Stepping forward, international fragmentation could damage the functioning of key global regimes beyond repair. Or this newfound heterogeneity could become a strength, building on record global firepower. The balance will tip one way or the other depending on whether nations make the effort to stop talking past one-another and instead begin to address each-others’ deep-seated insecurities. The West will have to stop abusing its dominant historic position before it is too late. While emerging powers must realize that they, too, have much to lose from a broken world. The recipe to save global governance doesn’t require genius. It requires goodwill.
**Geopolitics: The end of a cycle**

It has become common to say the world is passing through a period of “new normal” economics characterized by durably sluggish growth. Far less understood is that we have also reached the end of a geopolitical cycle. The global order that emerged from the Second World War is reaching its limits. Until a new model of global governance emerges, the world will remain in a period of uncharacteristic political instability.

Economic crises occur often and with regularity. Geopolitical cycles are far longer—measured in the order of decades, sometimes centuries. Often outliving their expiration date, failed geopolitical orders can grind the world to a halt under the weight of their ineffectiveness. We stand at one such point today. Conventional wisdom posits that the transition out the Cold War era in the 1990s represented the end of a geopolitical cycle. In fact, the end of bipolarity confirmed rather than uptuned the framework of post-World War II global governance. By putting an end to a forty-year ideological battle, the collapse of the USSR opened the way for a doubling down on the Bretton Woods order. The conversion of the General Agreement on Tariffs and Trade (GATT) into a full-blown World Trade Organization (WTO) is a prime example of this transformation.

The past few years, on the other hand, have opened an unprecedented breach in the postwar American order. Costly Middle Eastern interventions have left Americans less willing to project power abroad, while a sluggish economic recovery and the parallel geopolitical and economic rise of China have reduced Washington’s ability to lead in the rare times it wants to do so. The result is a G-Zero: a period in which no-one rules. It’s no longer America’s world, but neither has it become anyone else’s. We live in an awkward geopolitical no-man’s land in which it is clear the “unipolar moment” has ended, but what will replace it remains obscure.

Policymakers will be tempted to passively ride out these next few years of uncertainty, but doing so surely wouldn’t be judicious. Whether you’re the citizen of a historically stable developed market or that of rising emerging one, there’s a good chance you’ve felt the jitters of growing political instability already. If you haven’t, it won’t be long. With few structures in place to moderate geopolitical tensions in the coming years, we all have an interest in better understanding the changing political landscape around us. So do we all have an interest in doing our part to ensure that whatever comes next – whatever replaces the G-Zero – isn’t a new order imposed upon us, but one that citizens around the world have had a collective say in creating.

This paper is intended to give its readers the means to form an opinion on what they want that future to look like, and to act on it. In the spirit of never letting a good crisis go to waste, the paper starts by presenting the major ways in which politics as we knew it has disappeared, before offering some thoughts on a way forward for global governance. The goal is not to blindly defend the Bretton Woods system nor naively herald its new competitors. Instead, it is to bridge a growing gap between entrenched interest groups in an oversimplified conflict between competing worldviews.
The end of politics as you knew it

What does it mean for a geopolitical order to reach its end? Fundamentally, such transitions occur when the key constituent institutions underpinning a geopolitical system have decayed to such extent that they have become unrecognizable and often dysfunctional. This is happening today to the order that emerged from World War II. Below, we consider this current state of disrepair, and consider how, taken collectively, these various pieces of chaos add up to a G-Zero.

Domestic politics are no longer the same

Longstanding political spectrums are breaking down in developed markets

Developed markets used to differ from their emerging peers in that their politics were largely stable and predictable in their market outcomes. That is no longer true. If an emerging market is defined as one in which politics matter at least as much as economics to market outcomes, then to say that “we are all emerging markets” would only be a slight exaggeration today. Developments since the global financial crisis have caused the United States and European Union’s vaunted statuses as financial safe havens to be repeatedly questioned. A short list of such events would prominently include the US’s repeated debt ceiling incidents and Greece’s ongoing financial crisis.5

A leading reason for this turn of events has been the breakdown of long-standing political frameworks in these advanced economies, causing greater uncertainty over what falls within the realm of “possible” political outcomes. The values that once constrained the realm of plausibility have been overturned. Mainstream parties and candidates in liberal democracies have seen major defeats on three levels. First, fringe parties and candidates have in several places fully ascended to power, becoming incumbents in their own right: the best example of this trend being Alexis Tsipras and his Syriza party in Greece. Second, fringe figures have taken over or reshaped politics within established parties: the Tea Party, followed by Donald Trump, within the US Republican Party; Bernie Sanders within the Democratic one; Jeremy Corbyn within the United Kingdom’s Labour Party. Third, even in countries where centrists have remained in power, those actors have increasingly made their message more populist in an attempt to outflank increasingly reactionary constituencies. French former President Nicolas Sarkozy has long been accused of tacking to the right in fear of being outflanked by the Front National.4 In the U.K., many speculate that Prime Minister David Cameron offered up a referendum on his country’s EU membership as a tactical measure to fend off the UK Independence Party’s (UKIP) growing appeal to British Euroskeptics.7 German Chancellor Angela Merkel has been criticized for considering economically costly policies as a means of undercutting her Alternative for Germany (AfD) opponents.8 And in the US, presidential candidate Hillary Clinton’s decision to criticize the Trans-Pacific Partnership (TPP) has been interpreted by many observers as a reaction to the rising anti-trade sentiment among her potential supporters.9

The connecting thread among these assorted political movements is that the radicalization and atomization of politics in developed markets is making it harder for traditionally stable countries to deliver on the type of governance required by markets to thrive. Ironically, even the up-and-coming parties behind this desta-
bilization may face a hard time maintaining internal cohesion, as evidenced by divisions with a party such as Podemos in Spain.\textsuperscript{10}

Fringe parties—and refugee numbers—are growing in Europe

An expectations-capabilities gap is boiling in emerging markets
The first decade of the 21st century was characterized by a growth “supercycle” in emerging markets\textsuperscript{11} that propelled many of these countries’ populations toward middle class status (or, at least, out of poverty\textsuperscript{12}). Troublingly, however, the weakening of this supercycle’s two main drivers – Chinese growth and high commodity prices – is now widening the gap between popular demands and government capabilities to respond to these newfound expectations. The result: stewing dissatisfaction.

This dissatisfaction has found expression in popular protests on numerous occasions in recent years: against fuel subsidy cuts in Indonesia in 2013, against corruption in Brazil almost yearly, against student fees in South Africa in 2015. And the worst may be yet to come. A relative paucity of upcoming elections in large emerging markets will make it difficult for local populations to vent their grievances in a constructive way, leading them increasingly turn to the streets.\textsuperscript{13} Already, protests have bubbled up in places where they are rarely tolerated, such as Russia, which recently faced a truckers’ movement of rare intensity,\textsuperscript{14} and Azerbaijan, where a recent currency devaluation led hundreds to turn out on the streets.\textsuperscript{15} The challenge for emerging markets will be to deleverage their citizens’ expectations without experiencing a blowout.

Demand for decentralization is weighing on markets
Secessionism – the fullest expression of demand for decentralized power – is not new. Many of its flashpoint have been active for decades. Morocco has long been concerned about its control over phosphate-rich Western Sahara, while aspirations of autonomy in resource-wealthy Xinjiang are an age-old headache for Beijing. From the Philippines to Sri Lanka, battles for and against regional rule have
taken devastating human and financial tolls. Tamer movements, such as Italy’s Lega Nord or Canada’s Quebecois sovereigntists, have faded somewhat. Other cases, such as in Kosovo and East Timor, are now closed chapters in history. And yet the effects of separatist politics on markets have rarely been so strong.

Scotland’s 2014 referendum on membership in the United Kingdom raised critical questions regarding the future of both the region’s vast energy resources and that of its membership in the European Union (EU). More recently, uncertainties regarding Catalonia’s bid for independence from Spain have raised the risk of slowing, if not reversing, the country’s hard-fought economic recovery. In fact, a September 2015 vote in Catalonia and repeated general elections in December 2015 and June 2016 have left Madrid without clear governing mandates for nearly a year, illustrating how countries may increasingly find themselves saddled with a perfect storm of political uncertainty at the central and regional levels, as well as between the two.

Populations rooting for the decentralization of power may hope that bringing decisions closer to them will lead to better governance outcomes. But the road to this result can be a difficult one. Critically, what matters to markets is not only, or even primarily, the end result of a decentralizing push. A drive toward independence need not be successful in order to frighten investors. Instead, sheer political uncertainty, especially when prolonged for months or years, can be sufficient to weigh on a country’s business confidence.16 The British pound, for instance, felt the effects of uncertainties stemming from the possibility of a British exit (or Brexit) from the European Union long before the country’s actual referendum date in June 2016. Indeed, as is often the case with political risk, the decisive question is not whether a given secessionist drive eventually materializes, but when and how it is priced in by the markets.

Nor are the deleterious effects of domestic fragmentation limited to economics. Disturbingly, recent terrorist attacks in Belgium have brought to light how internal sociocultural divisions – in this case, the long-standing dispute between Belgium’s Walloon and Flemish communities – can weaken a state’s administrative cohesion, with serious implications for its citizens’ security.17

Market jitters from Brexit expectations

![Graph showing GBPUSD fluctuations](source: Bloomberg, BBC, YouGov, Eurasia Group)
Failed states are no longer a mere nuisance

The significance of failed states to global instability, particularly as an enabler of terrorism, has at times been exaggerated. Nonetheless, state failure weighs on the global economy more than ever, in several ways.

First, while state ineffectiveness was once limited to the world’s least developed countries, it has increasingly begun to affect middle-income economies. This is a troubling evolution considering the significance of middle-income nations to global political and economic outcomes. Middle classes, especially in emerging markets, will almost certainly be a determining factor in global stability (or instability), and populations reaching that status in an environment characterized by state failure are less likely to tip the right way.

Second, the countries affected by state failure are increasingly critical to global supply chains and major markets by virtue of their very geography. When Haiti struggles, it’s a human tragedy. But when China decides to bet a part of its future on a “Silk Road Economic Belt” (SREB) cutting across the Eurasian continent, Afghan and Pakistani stability become a critical link in the success of the world’s second largest economy. That’s a whole different ball game. Similarly, uncontrollable migration resulting from the unraveling of Syria and Libya has had a significantly destabilizing effect on European economies. Though migration need not be a burden, in the short run this phenomenon has driven the point home for Europeans that “geography is destiny.”

Finally, the recent history of the Middle East more broadly illustrates how the proximity of multiple failing states within a limited geographic area can lead to a sense of regional breakdown in which the whole (of resulting instability) amounts to more than the sum of its parts. The Islamic State’s (IS) use of Iraq’s vulnerabilities to harm Syrians, and of Syria’s vulnerabilities to harm Iraqis, has left no doubt that state failures often feed into one another in an inescapable vicious cycle.

The Countries Affected by State Failure Are Increasingly Critical to Global Supply Chains and Major Markets by Virtue of Their Very Geography

Fragile states no longer only least developed countries

<table>
<thead>
<tr>
<th>Number of fragile countries per income group*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Middle income</td>
</tr>
<tr>
<td>Low income</td>
</tr>
<tr>
<td>30  25  20  15  10  5  0</td>
</tr>
</tbody>
</table>

*Countries are considered fragile if Fragile State Index score is in the “Alert” range, the most vulnerable category
Source: Fragile State Index, World Bank, Eurasia Group
Regional dynamics are changing

The Middle East is breaking into pre-Westphalian pieces

With the Sykes-Picot Agreement of 1916 and Treaty of Lausanne of 1923, outsiders set the borders of newly created Middle Eastern countries in ways that profited European colonial powers rather than the peoples that lived within them. Barring a few exceptions, they have held together for nearly a century, but they are now breaking down. The Iraq War of 2003, the Libyan intervention of 2011, the ongoing Syrian civil war, the rise of the Islamic State in 2014, and the ongoing Yemeni civil war have posed unprecedented challenges for the region's national borders.

States are now disintegrating. In early 2016, Libya had not one but three governments. One of the region’s most dependable political entities, Iraq’s Kurdistan Regional Government (KRG), isn’t officially a state. It has built enough de facto autonomy and earned enough international recognition that formal statehood isn’t necessary for survival. So successful has the KRG’s strategy been that al-Qaeda in the Arabian Peninsula, a terrorist organization, has tried to replicate this strategy elsewhere in the region. In addition, the US and its allies are no longer willing to spend the security, diplomatic, and economic capital that once ensured the region’s artificial coherence. Washington, now less dependent on Middle Eastern oil, may back an intervention in Libya, but it will not underwrite a long-term troop presence in the region unless US national and homeland security is credibly at stake. Nor do local regimes have the continued capacity to maintain local populations’ loyalty or quiescence.

Beyond the obvious disaster for citizens of the Middle East, this new disorder will continue to have dramatic economic consequences for the region. Libya’s domestic instability limits its oil exports; Saudi Arabia’s embroilment in Yemen reduces its ability to focus on domestic economic reform (namely its “Vision 2030” plans); the KRG’s costly fight against IS depletes its coffers. Worst of all, this “war of all against all” prevents the Middle East from deepening intraregional economic flows, which have long been identified as a critical enabler of regional development. Finally, a long-term trend toward lower oil prices will make it much more difficult for the governments of major producers to defend themselves and their borders against threats external and internal.

Middle East borders in flux

Source: Adapted from Robin Wright, New York Times, Imagining a Remapped Middle East (2013), Eurasia Group
Europe is fighting for its survival

Inside the European Union, long a model of stability and free cross-border exchange, leaders are increasingly focused on preserving existing ties rather than creating new ones. Britain has voted for exit, and the process of negotiating a new relationship will be more contentious and time-consuming than either side would like. The risk of an accidental Greek exit from the European Union remains very much alive. A leading candidate for French president promises a referendum on that country’s EU membership. A high-stakes constitutional referendum in Italy and national elections next year in France, Germany, and the Netherlands will provide opportunities for anti-EU populists to fan the flames of anti-integration sentiment and increase uncertainty about Europe’s future. Underneath all these tensions is a migration crisis that depends on a shaky deal agreed between EU leaders and the government of Turkey.

No longer can the continent’s “unity in diversity” be taken for granted. European cohesion is under attack from all sides and from within. The migrant crisis has measurably weakened German Chancellor Angela Merkel’s domestic and international standing. Given Merkel’s vital role in keeping the EU together through the financial crisis, a weak German chancellor bodes ill for Europe’s future cohesion. Europeans’ fear that refugees may put pressure on already shaky continental economics has already led countless governments to breach the continent’s prized Schengen Agreement on freedom of movement across borders.

Many of the values that underpinned the “European Dream” have frayed, possibly beyond repair. If Europe fails, the world will have lost a model of openness and institutional integration.

---

Europeans want their own EU referendums

<table>
<thead>
<tr>
<th>Country</th>
<th>I would like [my country] to hold a referendum on its EU membership</th>
<th>I would not like [my country] to hold a referendum on its EU membership</th>
</tr>
</thead>
<tbody>
<tr>
<td>France</td>
<td>60%</td>
<td>40%</td>
</tr>
<tr>
<td>Sweden</td>
<td>50%</td>
<td>50%</td>
</tr>
<tr>
<td>Spain</td>
<td>40%</td>
<td>60%</td>
</tr>
<tr>
<td>Germany</td>
<td>40%</td>
<td>60%</td>
</tr>
</tbody>
</table>

Source: Adapted from Jan Eichhorn, Christin Hübner, Daniel Kenealy, The University of Edinburgh, The View from the Continent: What people in other member states think about the UK's EU referendum (2016), Eurasia Group
Latin America: Secure but with little influence
Latin American governments have important advantages over their counterparts in other regions. First, though various forms of organized crime continue to generate security challenges, the region’s lack of geopolitical conflict is an important positive for governments that can manage foreign policy costs and risks without threat of inter-state war. The end of Colombia’s half-century civil war underscores the region’s security progress.

Yet today, far from investing in an integration agenda, the continent’s leaders are focused squarely on domestic affairs. An anti-corruption campaign has upended Brazil’s politics. In Argentina, a new president with sharply limited political leverage faces an enormous challenge in rebuilding Argentina’s economic institutions and its economy. Low oil prices and intensifying political confrontation have pushed Venezuela to the brink of destabilizing unrest. Nor are Latin American governments more effectively extending their influence into other regions. Latin America was never known for its global power projection. But its ability to influence the rest of the world has sunk to new lows, outside rare exceptions such as the influence exercised by Mexico’s Central Bank Governor Agustin Carstens. As the scholar Oliver della Costa Stuenkel has put it: “At a time of momentous change in international affairs (including the shift of economic and political power toward Asia, the emergence of new China-led institutions, the worst refugee crisis since World War II and an ongoing debate about humanitarian intervention), South America will largely be a bystander.”

Eurasian Rivalries
Political projects of the Eurasian region, composed primarily of the territory of the former Soviet Union, are not delivering on their economic promise of greater intra-regional cooperation. China’s power of the purse, expressed in this region primarily by its new Silk Road investment plan, may one day create enough shared commercial interests in central Asia to promote greater political unity, but this project will take many years to develop. In the meantime, the region’s preeminent body, the Eurasian Union, remains primarily a coercive Russian political tool.

In addition, the Ukraine crisis has demonstrated that far from fostering harmony “from Lisbon to Vladivostok,” competition between the European – and Eurasian – unions can force countries into existential, zero-sum choices about their future at one end of Eurasia. Today’s fragile entente between Russia’s Eurasian Union and China’s Silk Road Economic Belt will also eventually be replaced by tension at the other end between a declining power that perceives the region as its backyard and a rising one that must secure its growing Eurasian supply chains.

Asia between economics and security
A comparable tension is already at play in Asia, where many Southeast Asian countries are caught between an economic dependency on their Chinese neighbor and a desire for a balance of power in the region. As Washington works to reinforce its regional economic ties to solidify its security partnerships, through the Trans-Pacific Partnership in particular, three questions have emerged. How
will China respond to this US attempt at aligning political and economic relations in its favor? Will the region's overlapping Chinese and American economic architectures – the Regional Comprehensive Economic Partnership (RCEP) and TPP, respectively – converge or conflict? Finally, is it possible that the growing power of various forms of non-state actors will give Washington and Beijing important interests in common, encouraging a deeper level of cooperation?

Africa’s fundamental heterogeneity

African politics have come a long way in recent years. Governance has improved across the continent; and, while overoptimistic, the “Africa Rising” narrative has a more convincing ring to it than ever before. Africa is still home to the world’s fastest-growing middle class. Unfortunately, it is still far more difficult for Africans to trade among themselves than with the outside world. In fact, inter-African trade accounts for less than 15 percent of all African trade. The continent’s two leading powers, Nigeria and South Africa, are preoccupied with domestic troubles, distracting them from fostering cohesion in their neighborhoods. And terrorist groups such as Boko Haram, ISIS, al-Shabaab, and al-Qaeda in the Islamic Maghreb (AQIM) remain a constant threat to regional progress. In short, 54 countries display widely divergent outlooks rather than a cohesive power center.

Yet, though declining commodity prices have hit some African economies, particularly in the West, quite hard, dynamic and better diversified economies in East Africa have shown both resilience and strength. Kenya, in particular, offers considerable promise.

New political players are rising

The rise of non-state actors

The rise of non-state actors has been a “new story” for almost 25 years. Yet there is a strong case to be made that these developments have much farther to go. Non-state actors used to “sometimes” be “almost as influential” as governments. Today, they are more influential than many states on a daily basis. For better or for worse, the Kurdish People’s Protection Units (YPG) have done more to shape the outcome of Syria’s civil war than any government, bar Russia. In neighboring Iraq, Muqtada al-Sadr, a cleric, has kept the country’s sitting prime minister, Haider al-Abadi, on his toes. In Lebanon, the state has long been barely distinguishable from the country’s leading non-state actor, Hezbollah. Nor is this solely a Middle Eastern phenomenon: in Colombia, one non-state agent (the militant group Revolutionary Armed Forces of Colombia, or FARC) even called upon another (the Pope) to help get past the finish line in tackling long-running domestic peace negotiations.

Non-state actors are no longer “doing their own thing.” Instead, their actions are increasingly political in nature. This trend is particularly visible in the technology sphere, where what Eurasia Group has called the “Rise of Technologists” means players from the world of technology are increasingly claiming a political mandate for themselves. Apple’s leaders recently fought the US government with public opinion as their witness over the claim that breaking the company’s security protocols was an issue of free speech, not “just” a technological matter. Meanwhile, Sean Parker, a prominent venture capitalist, has funded a Washington, D.C.-based...
After the G-Zero: Overcoming Fragmentation

Think tank in an effort to “effect broader change in public policy” beyond the confines of the tech world.37

Nor is this dynamic limited to domestic US politics. Today, when Xi Jinping and Narendra Modi visit the United States, they spend nearly as much time with Silicon Valley kingpins as with officials in the US capital. The US tech industry, for its part, has not been shy about running its own corporate foreign policy, sometimes counter to that of the Department of State, as when IBM opened its source code to Beijing’s review just as Washington was trying to take a tougher stance against Chinese tech policy.38 Meanwhile, Alibaba Executive Chairman Jack Ma expressed his desire to rival the World Trade Organization’s (WTO) monopoly over global trade regulation by creating a “WTO 2.0” composed of businesses rather than governments.39 If these aren’t signs of political ambition, what is?

International relations are mid-transformation

Alliances no longer stand for what they used to:

The end of governments’ monopoly over politics isn’t the only factor making the world messier. The very alliances that underpinned international relations in the post-World War II era are also fraying. Trust in the United States’ reliability as a partner has eroded. The transatlantic relationship has become little more than a hollow alliance.40 No longer does either side of the pond view the other as its partner of first resort. When France seeks assistance against the Islamic State, it turns to Russia.41 When Germany needs to stem refugee flows, it asks for Turkey’s help.42 When the United Kingdom needs financial resources, it knocks on Beijing’s door.43 In America, the question was once “whom to call” in Europe, but today no one bothers to even start dialing. Already a shadow of its former self, the value of the US-UK “Special Relationship” will inevitably take a further hit from Brexit.

The Ukraine crisis may have breathed new life into NATO, but its greater effect was to put the institution’s internal divisions on display and to make its existential vulnerabilities evident. In the Middle East, the United States’ eagerness to pursue a more balanced relationship with Iran has spooked the US’s Israeli and Gulf allies. Farther East, America’s eagerness to “pivot to Asia” was welcomed by its regional partners, but the movement seems to have halted mid-step, making it a disappointment to both Middle Eastern and Asian observers alike.

The United States is not the only power that has seen its major relationships flag. Russia and Turkey considered each other strategic partners until they came close to a shooting war. Their more recent patch-up remains superficial. The Russo-Chinese axis has been touted as a durable alliance, but insiders eagerly point out the relationship’s structural limitations.44 Pyongyang used to know Beijing had its back; today, it watches its back. Cuba knows it can no longer rely on a Venezuelan big brother on the verge of its own collapse. And while Saudi Arabia will continue to support its Egyptian partner, a strategy of hot and cold keeps Cairo on its toes.45 Who’s to be trusted?

Interdependence has become a perceived vulnerability:

As badly as relations have soured among allies, they’ve turned even worse between enemies. Countries used to actively pursue economic interdependencies even with
antagonistic nations, for they were traditionally thought to provide trade gains and increased foreign policy stability regardless of enmity. But a paradigm shift has occurred in recent years. Dependence on the outside world has become a perceived vulnerability. Autarky is not a new philosophy, but whereas it used to be the preserve of regimes such as Mussolinian Italy or hermit North Korea, its appeal today is spreading to countries that not long ago paid at least lip-service to engaging with the rest of the world. Today, Vladimir Putin casts his country’s isolation as an opportunity, while Iranian Supreme Leader Ali Khamenei calls for a “resistance economy” as the economic benefits of the post-sanctions era have yet to materialize. Reactionary voices in disparate countries have begun sharing lessons in “economic patriotism,” seemingly unaware of the paradox that economic solidarity among mercantilists represents. Regardless of whether these reactions are well-founded, what is certain is that moves by the US such as its recent threat to prevent the reappointment of South Korean WTO judge Seung Wha Chang – based on claims that his tenure has been politically harmful to the US – will be regarded as ironic by many foreign observers and are likely to bolster the claims of those already skeptical of Washington’s influence over Bretton Woods bodies.

Another reason for the aforementioned paradigm change may have been the United States’ zealous use of sanctions in recent years. Washington’s growing “Weaponization of Finance” has carried the risk of driving foreigners away from a historically US-dominated international economic system. Even US Treasury Secretary Jack Lew has sounded the alarm: “If [US sanctions] excessively interfere with the flow of funds worldwide, financial transactions may begin to move outside of the United States entirely, which could threaten the central role of the U.S. financial system globally.”

Systematic recourse to sanctions may also increasingly drive a cycle of conflict as governments around the world have begun imitating America’s trigger-happiness in deploying their own sanctions program. The European Union has long had numerous such initiatives. Russia is in a trade war with its largest trading partner: Europe. And Saudi Arabia recently unleashed sanctions not only against Iran but also against Lebanon, long a partner of the kingdom. In fact, this invitation to replicate US sticks has sometimes even been attributed directly to Washington’s actions, as when one Chinese academic remarked that “taking a cue from the US’ practice, China can [sic] use the security exception clause [of the WTO] to reduce the export of some important materials to Japan.”

It’s not too late to reverse this trend. The global economy can once again become a positive-sum game. But getting there will require the US to drop the rhetoric according to which America’s interest is in combating China’s Asian influence rather than in seeking mutually beneficial trade gains. Reversing the trend will also mean Europeans will eventually have to sell an upcoming Trans-Atlantic Trade and Investment Partnership (TTIP) as something other than an “economic NATO.” And it will beg of Turkey to no longer leverage its control over refugee flows for political gain. In short, saving global economic governance means ending the resort to actions the European Council on Foreign Relations has called “Connectivity Wars.”
Saving global governance from the G-Zero

What the G-Zero means for global governance

This bottoming-out of the geopolitical cycle has two implications for global governance. By multiplying domestic headaches, it impedes leaders’ abilities to contribute to constructive international efforts to revive ailing global structures. And by breeding distrust among nations, it reduces their desire to work together. The result is a spiral to the bottom, a zero-sum fragmentation of the global order.

A trade-off between domestic and international affairs

Leaders have limited operating bandwidth. Because “all politics is local,” decision-makers of necessity focus on domestic affairs that invariably matter more to constituents than far-flung foreign policy considerations. This is particularly true when the domestic situation is grave, when leaders feel particularly vulnerable, or when a foreign policy decision carries the risk of not just distracting but also damaging an incumbent. For instance, Angela Merkel has suffered deeply from her stances on the Greek and refugee issues; how long she accepts to bear those costs before backtracking is open to question. Already, Turkey’s Recep Tayyip Erdogan – who once fancied himself a new leader of the Middle East – has seen his own international hopes dashed by a profound domestic security crisis.

In rare instances, the prioritization of domestic affairs can have a salutary effect on international stability. It is better, from the perspective of stable global governance, for Xi Jinping and Shinzo Abe to be consumed with economics at home than with saber-rattling abroad. But such cases are the exception, not the rule. More often than not, a predisposition to follow narrowly defined national interests down the rabbit hole will only worsen and prolong the effects of a broken global governance system. In fact, some argue the world may be at risk of a new Great Depression if the US fails to take the lead in beating back a rising protectionist tide within and beyond its borders. Worryingly, trade restrictions by G20 nations recently stood at their highest monthly average since 2009. And so far, as one leading US think tank has noted, “elites around the world had not only failed to sell the gains from liberalization to fellow citizens, but in fact had made little effort to do so.”

The cost of Merkel’s refugee stance

Merkel’s approval rating (%)  
Asylum applicants (thousands)

Source: Eurostat, Infratest Dimap, Eurasia Group
A shortage of trust means a shortage of collaboration

For better or for worse, the Western bloc was a major driver of global governance efforts over the past half century. This force is weakening. First, the so-called West no longer commands the moral authority it once did (or at least thought it did). Second, internal divisions are making it harder to maximize what is left of its leverage. Distrust is eroding the West from within and from without simultaneously. Amid this vacuum, non-Westerners have begun building alternative governance mechanisms to assuage their sense of insecurity vis-a-vis the Bretton Woods order. Ironically, emerging powers may not trust one another much more than they do their European or American peers, but they are willing to paper over this suspicion in the short run if it means freeing them of a perceived historic chokehold.

The rise of “alternatives,” and growing fragmentation

It took the US Congress five years to ratify a landmark IMF quota reform aimed at giving China and other emerging powers a greater say in the organization’s affairs.61 This delay is often touted as a leading cause of Beijing’s burning desire to create global institutions of its own, and there is no doubt some truth to the hypothesis.62 The scale of China’s aspirations amounts to nothing less than a 21st-century Marshall Plan. Yet the drive to construct alternatives to the Bretton Woods order’s institutions has been neither solely led by China nor targeted only at the IMF. Instead, such initiatives have had numerous initiators, and range across multiple areas of global governance.

International sovereign lending

The creation of the Asian Infrastructure Investment Bank (AIIB) was notable not just for its aspiration to challenge the World Bank and Western-backed Asian Development Bank (ADB) but also—and perhaps even more so—for its success in convincing the very Western architects of the Bretton Woods order to join in China’s endeavor.63 In so doing, it reached a level of credibility previously unattained by the earlier creation by Brazil, Russia, India, China, and South Africa (the BRICS) of a New Development Bank (NDB) whose membership had been limited to select emerging powers.

International monetary assistance

The BRICS’ creation of a Contingent Reserve Agreement (CRA) devoted to ensuring mutual financial assistance among leading emerging markets came closest to challenging the IMF’s institutional role.64 Related initiatives have also included a range of currency swap agreements, leading among them the Chiang Mai Initiative between China and its Southeast Asian neighbors. In response, institutions like the IMF have adapted and initiated a policy dialogue to leverage on these new arrangements to build additional layers to strengthen the global financial safety nets.65

Bretton Woods by extension

Not all of the institutions being challenged by emerging powers today have their roots in Bretton Woods-proper. When Beijing promotes the yuan’s internationalization through the creation of a China International Payment Systems (CIPS),66 it is the New York Federal Reserve’s role as global clearinghouse that is at stake, not the IMF. The same goes when Russia seeks to promote a world in which commodities are priced in euros, yuan, or ruble. Likewise, while Russia, China, and others have
threatened to challenge a historically Western-dominated Internet governance system, it would be imprecise to call the Internet Corporation for Assigned Names and Numbers (ICANN) a Bretton Woods institution per se (if only because the Internet was created decades after the Bretton Woods Conference). Such varied initiatives, however, undeniably make the world an increasingly fragmented place in which global governance runs the risk of becoming even messier than it already is.

The rise of global governance “alternatives”

Envisioning the costs of fragmentation

Direct damages and opportunity costs due to political risks already harm the global economy on a daily basis. A world of fragmentation-gone-wild would add countless new transaction costs for economic agents. The regulatory complexity of today’s global sanctions landscape may be a weak signal of this dynamic. Next could come financial systems whose protocols struggle to communicate, supply chains slowed by incompatible product- and logistical- standards, and labor flows burdened by growing visa restrictions. The rise of vernacular credit rating agencies to challenge “the Big Three” – Standard & Poor’s, Moody’s, and Fitch – may for instance be legitimate, but it is also an unmistakable sign of politically driven duplication in the global economy.

Global economy’s exposure to political risk: rising in size and volatility since the 2008-2009 crisis

Source: Eurasia Group
The G-Zero will not last forever. Citizens of all countries have a choice in whether to be the victims or creators of its successor order. The details of “what comes next” will remain unpredictable for a while longer, but three specific efforts would help craft a more constructive global governance system. First is to bridge the mindsets of centers of power that don’t currently seem to understand one another. Second is to strengthen the Bretton Woods order by making it more inclusive and more effective. Third is to acknowledge that we are only at the beginning of a new period in history in which old and new institutions will inevitably have to coexist.

Enhancing global understanding
Solving a multi-stakeholder problem – in this case, the strengthening of effective global governance – requires sharing a common understanding of that problem’s initial statement. Such an understanding is nowhere to be found at the moment. The United States, China, Europe, Russia, Brazil, and India, to name just a few of the stakeholders, all have competing visions of where global governance stands today, and what it should look like tomorrow. Ask around whether we live in a world of US hegemony, in a US-China G-2, in a tri-polar world that also includes the EU, or in a genuinely multipolar one composed of regional powers, and you will collect as many different views as there are respondents. This fragmentation of perspectives makes it inherently difficult to move forward.

The United States’ position on the matter has been particularly ambiguous, for two reasons at least. First because, perhaps more so than any other power, the US lacks a long-term domestic consensus over its role in global affairs. Americans do not share a clear-cut view of whether their country is in decline or not, nor of how much effort they should devote to lead the world. Second, the US’s external position on global governance has been marked by an unmistakable internal contradiction: the United States doesn’t want China and others to create their own world order, but nor has Washington been willing to turn existing governance frameworks into shared ones. “Mine” has not fully become “ours.” It’s as if the US had invited its better half to move into its home, but refused to free-up closet space – much less offered to search for a new house that both partners could make their own.

China has not failed to pick up on this contradiction. It recently noted, for example, how paradoxical Washington’s effort to use TPP to “write the rules for trade” can be considered given the WTO’s existence for exactly that purpose. “We never believe that world trade rules can be made by any specific country alone,” one of Beijing’s lead spokespersons recently pointed out. Indeed, because the United States has always sold participation in the Bretton Woods order to its foreign peers based on the argument that joining it would unlock positive-sum gains, it is more than perplexing that Washington would now couch trade in military terms. This is not a sustainable proposition, and it is sure to be beaten by China’s astute promotion of its Asian Infrastructure Investment Bank as an organization whose doors are open to (almost) all – with ambitions aspirations for 100 members by the end of 2016. China’s rosy rhetoric may invite some suspicion, but at least Beijing is saying all the right things – and that matters. The question, of course, will be whether Chinese decision-makers make good on their promise of remaining inclusive, and steer clear of excessively using their new levers of power for self-interested national goals. The problem for outsiders is that China’s claim that
its ascent will remain forever benign will only become verifiable once it is too late to do anything about it.

In the meantime, instead of seeking reassurance over an insoluble question, perhaps it would be more productive to recast the debate over emerging powers’ global integration from a discussion centered on power to one focused on better appreciating the cultural and ideological grievances that often underpin critics’ attacks against the Bretton Woods order. The bond that brings Russia, China, India, Brazil, and others together in questioning existing global institutions is their dissatisfaction with what they perceive to be a US-imposed “global think.” From the Bandung Conference of 1955 to the New International Economic Order declared in Algiers in 1973, this discontent is not new. But today its stakeholders have the newfound power to make their views heard. Russia may not have been comfortable with some of the external prescriptions imposed upon it in the 1990s, but it was only once Moscow put its fiscal house in order in the mid-2000s that Russia was able to assert its political exasperation. Westerners might be tempted to discard Russian or Chinese aspirations of domestic ideological sovereignty as mere excuses to enforce domestic censorship or strengthen regime rule – and they’d often be right. But there is also a genuine desire, on the part of these and other populations, to live in a world whose global values are less foreign – more relatable to their own. Even America’s friends in Europe don’t fully share the United States’ standards. Meanwhile, the positions of India and Brazil are particularly revealing: neither aspires to live in a world led by China or Russia, but both New Delhi and Brasilia will gladly work with anyone able to offer some relief from US dominance. Paradoxically, every time the United States attempts to bring them “back to its side,” Washington proves once again that it has failed to appreciate the non-binary views that dominate policy circles in those states. The idea of picking a camp is anathema to many countries, some of whom, like Turkey, straddle regions and continents. The world may have reached a point at which the values that compose it have become so heterogeneous that they can never be fully reconciled. But short of such alignment, it may be possible – in fact, imperative – to at least improve decision-makers’ understanding of their respective worldviews and perspectives regarding the future of global governance. As one Singaporean diplomat recently put it: “One of the basic functions of diplomacy is to see the world through your competitors’ eyes in order to understand the frame of reference he is operating within, and thereafter one of the basic purposes of statecraft to […] operate within the same frame in order to achieve your purposes.” In short, we can no longer afford to talk past one-another.

Making global institutions more inclusive and more effective

Emerging powers have a greater stake in today’s international order than is often appreciated, and will gladly abide by its rules if they feel confident in its future. The WTO’s free-trade regime, for instance, played a central role in affording China the opportunity to develop so rapidly over the past two decades. The question, then, is whether the Bretton Woods order can prove adaptable enough for emerging economies to continue feeling at ease within its boundaries. There’s a reason Google famously allowed its employees to work on personal projects during working hours: it didn’t want them running off to create rival start-ups. Can Western policymakers be as smart as their corporate peers in the Silicon Valley?
There are reasons to be cautiously optimistic. The long-pending reform of the IMF has finally won US approval. Or, as IMF Managing Director Christine Lagarde has said of China: “From being grossly under-represented it is now under-represented”. Meanwhile, the growing role of figures such as Min Zhu, Raghuram Rajan, or Agustin Carstens in shaking up international economic thinking are an encouraging sign that the growing influence of senior non-Western economists in Washington’s intellectual circles may make it less necessary for emerging powers to “bring down” the Washington Consensus if they can simply amend it “from the inside”. Indeed, the future of global governance will be determined as much by how rules change within existing institutions as by the creation of new organizations. So far, discussion over these rules has been mostly productive, if at times heated. Far from seeking to undermine the IMF, Beijing fought hard for its currency to be included in the fund’s basket of currency reserves. China’s recent economic experience has also led to an ongoing reappraisal, in Washington, of the recipe for financial stability in a world that has attempted to combine open capital accounts and floating exchange rates. Meanwhile, there is evidence that para-Bretton Woods organizations such as the Organisation for Economic Co-operation and Development (OECD) are increasingly open to allowing China and others to work with them “a la carte,” thereby cutting the Gordian knot surrounding the question of institutional membership.

These steps are encouraging not merely because they illustrate “goodwill” on the part of the former Western masters of the Bretton Woods order, but also because they prove that many emerging powers still see value in working within this decades-old system. That willingness, however, cannot be taken for granted. In order to be perpetuated, it will have to be continuously justified. Exact recommendations towards achieving this goal have been discussed at length elsewhere, but the bottom line is that in a world marked by greater optionality, the Bretton Woods order will only survive if it is the best product on offer. As with so many related questions – such as whether institutions like the World Bank can effectively fulfill their mandates without touching on sensitive topics such as policing or corruption – the difficulty will be in finding the right balance between compromise and the risk of a race to the bottom in standards.

Acknowledging that there is significant scope for greater collaboration and cooperation

Much of the discussion over the future of global governance, especially in the United States, has revolved around a false dichotomy according to which the future will be run by either old or new institutions. Yet there is plentiful evidence that the world is big enough for both sets of organizations to cohabitate. Global infrastructure spending needs alone make this apparent. Rather than crowding out rivals, the Asian Infrastructure Investment Bank will help to fill the infrastructure gap by providing some 4% of the $350 billion of additional infrastructure spending needed annually to support current projected economic growth.

New, or “alternative,” global institutions hold the promise of making a valuable contribution to the world’s growing and wide-ranging needs. However, not all such new institutions will prove equal. Those that are inclusive, promise to operate by democratic internal rules, and aim to be constructive should be welcomed. But others will merely serve to make a point or of only furthering their creators’ nar-
NEW INSTITUTIONS SHOULD NOT ALL BE LUMPED UNDER A COLLECTIVE UMBRELLA

row national interests. In short, these new institutions should not all be lumped under one umbrella. Whether today’s institutional proliferation will prove an asset, by enhancing global firepower, or a liability, by increasing international fragmentation, will depend in large part on how effectively old and new players are able to collaborate.

Meanwhile, broader institutional cooperation is already well under way. The IMF has in recent years initiated effective collaboration with institutions like the Chiang Mai Initiative Multilateralization (CMIM).80 Similarly welcome in this regard are signs of collaboration between the AIIB and its peers, including the World Bank, the Asian Development Bank, and the European Bank for Reconstruction and Development (EBRD).81 As the AIIB’s president recently noted: “Even if the U.S. isn’t a member, we have quite a number of seasoned professionals with American passports working in my institution, and I trust them.”82 Also to be encouraged are partnerships such as that between China’s International Payment System and the Society for Worldwide Interbank Financial Telecommunication (SWIFT).83 Collaboration like this will not always be institutional. In a global economy in which most economic spillovers are Chinese but most financial ones stem from the US, the path to systemic stability will likely lie in giving countries greater flexibility to align their respective economic and financial exposures as they see fit. This may require progressively greater acceptance of a truly tri-polar global financial system that offers more weight to the yuan and euro side-by-side the US dollar, for instance.

Finally, as previously mentioned, it will be instructive to observe whether Beijing and Washington emphasize collaboration or competition in advancing their respective mega-regional trade agreements (TPP and RCEP), which both share the characteristic of circumventing the WTO. The competition to establish global standards has equal potential to be a race to the bottom or the top. TPP is living proof that emerging powers are not the only ones creating new frameworks to parallel yesterday’s dominant institutions. The question, therefore, is not whether the West will be able or should even want to limit the proliferation of such new frameworks. What matters instead is whether these initiatives will continue to pit Westerners against non-Westerners, or whether tomorrow’s global institutions can be jointly created by parties on both sides of this artificial divide as they face common challenges.

Conclusion

Politics as we knew it is over. The breakdown of domestic and regional political systems is leading both developed and emerging economies to focus on increasingly messy domestic affairs, abdicating their international leadership roles in the process. Meanwhile, fast-growing distrust among competing centers of power means appetite is growing for new rules and institutions that challenge a decades-old Bretton Woods order. We are at the bottom of a geopolitical cycle, and, though not well-understood, the consequences for the global economy of this dip will rival those of most economic downturns. Because such transitions occur so rarely, decision-makers lack the experience of weathering through them. And yet, the world will not remain in this G-Zero state of affairs forever. What matters is hence whether citizens around the world will simply wait to accept whichever new global order is eventually imposed upon them, or if they will instead choose to be proactive in shaping what comes “after the G-Zero”.

EURASIA GROUP | 21
This study is subtitled “overcoming fragmentation” because it is based on the two-pronged view that greater fragmentation of the global order must be kept manageable to the extent possible, but also that the creation of new bodies of global governance need not be destabilizing so long as all the pieces of the resulting growing puzzle remain compatible with one-another. So far, the tally features both reassuring and alarming signs. The United States’ failure to attune to the grievances of nearly all of its international partners has been concerning. Likewise, the increasing pace of proliferation of — at times suspect — new organizations bodes ill for prospects of maintaining coherence in the global system. And yet, there is solace to be found in emerging powers’ continued integration into leading Bretton Woods institutions. Combined with China’s constructive tone in presenting its vision for the future, this trend-line puts positive-sum outcomes within reach. The question going forward will not be whether nations around the world are able to save global governance. It is whether they actually want to.
Endnotes


5. Europe and the United States have, between the two of them, featured in Eurasia Group’s five Top Risks every single year since 2008 http://www.eurasiagroup.net/media-center/view-press-release/Eurasia+Group+President+Ian+Bremmer+Announces+Top+Risks+and+Red+Herrings+for+2008


8. https://next.ft.com/content/7e8caaa0-1601-11e6-9d98-00386a18e39d


15. http://www.jamestown.org/programs/edm/single/?tx_ttnews%5Btt_news%5D=45045&cHash=9d37109716408eb6e0ae134ed5f0a#V8gpo1UrdtU


AFTER THE G-ZERO: OVERCOMING FRAGMENTATION


50 http://www.ft.com/intl/cms/s/0/a46b63f2-c0de-11e4-876d-00144feab7de.html?siteedition=intl#axzz3Y2ULgIIA


55 According to US Defense Secretary Ash Carter, “Passing TPP is as important to me as another aircraft carrier.” http://www.bloomberg.com/news/articles/2015-04-06/asia-pacific-trade-deal-as-important-as-a-new-carrier-to-carter

56 http://www.nato.int/cps/en/natolive/opinions_103863.htm

57 http://www.ecfr.eu/publications/summary/connectivity_wars_5064

58 A point made in reference to the work of historian Charles Kindleberger http://www.wsj.com/articles/making-depressions-great-again-1456790200


61 http://www.reuters.com/article/us-usa-fiscal-imf-idUSKBN0U204I20151219

62 https://next.ft.com/content/71e33aea-ccaf-11e4-b94f-00144feab7de#axzz3VYtOqFCr


66 http://uk.reuters.com/article/uk-china-yuan-cips-idUKKCN0S20VG20151008


69 http://www.reuters.com/article/us-usa-obama-trade-idUSKBN0KU0BE20150121

70 http://www.politico.com/tipsheets/morning-trade/2016/02/baracks-budget-and-biology-212587

71 http://www.chinadaily.com.cn/business/2016-05/31/content_25555337.htm


AFTER THE G-ZERO: OVERCOMING FRAGMENTATION

74 http://www.reuters.com/article/us-usa-fiscal-imf-idUSKBN0U204J20151219
75 https://www.ft.com/content/32c323dc-4541-11e6-9b66-0712b3873ae1
80 https://www.imf.org/en/News/Articles/2015/09/14/01/49/pr1421