

## The Economic Crisis and the Emerging Powers: Towards a New International Order?

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**Theme<sup>1</sup>:** The real challenges to the existing international order will come not from the established or emerging powers, but from global forces that are beyond their control and also from those non-state entities and groups which seek to undermine the process of globalisation that links all states and societies ever closer together. Ensuring the continuation and deepening of international order in the next decades of the 21<sup>st</sup> century will require governments in both the West and among the emerging powers to improve their domestic resilience to internal and external shocks and, as suggested below, to use deeper regional cooperation as a testing ground for higher levels of international cooperation.

International order within a system of more or less sovereign states implies the absence of major conflict between those states. It implies their general acceptance of norms of international behaviour that preserve the peace and enable them to pursue their objectives in a competitive manner but without jeopardizing the peace and prosperity of others. International order does not imply the absence of low-level conflict around the world or the disappearance of various other forms of injustice. From a European perspective, then, the question of whether we are moving towards a 'new international order' generally implies that a transfer of power is taking place from states in the West to those in the East and, therefore, from 'us' to 'them'. Seen from this perspective, international order could easily decay over the coming years. Large-scale international disorder was a central feature of the early 20<sup>th</sup> century when two World Wars accompanied the rebalancing of power among states in Europe, the Middle East and in the Asia-Pacific region. And the further rebalancing of power at the end of the Second World War evolved into a Cold War between the US-led Western bloc and its protectorates, on the one hand, and the Soviet Union and its network of proxies, on the other. The fear is that China, India, Brazil and other emerging powers may increasingly ignore the norms, rules and institutional arrangements put in place by the US and European nations after 1945 or seek to redefine them to their advantage. At a minimum, they may limit efforts by some in the West to extend or deepen those rules or institutions, by transforming the Kyoto Protocol into a global agreement on combating climate change, for example, or by further opening markets through the Doha trade round.

But is the shift in global economic gravity and, ultimately, power from West to East and North to South really the defining global trend in the context of international order? I would argue not. Western powers do face a host of problems. But, as outlined below, the emerging powers face their own structural challenges, while the West still has a number of significant attributes relative to the emerging powers. At the same time, the current economic crisis is deepening the ongoing process of political and economic

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<sup>1</sup> This essay is a chapter from the book '[Globalización, crisis económica, potencias emergentes...Diez años decisivos para la transformación del mundo](#)' devoted to the 10th Anniversary of the Elcano Royal Institute.

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interdependence between all states –emerging and established–. Rather than simply shifting power from West to East, these developments are in fact knitting West and East, North and South ever closer together.

As a result, we are witnessing a deepening of the existing framework of the post-1945 international order under which nation-states have established rules designed to avoid the outbreak of inter-state conflict and to enable them to interact ever more deeply economically, while not interfering unnecessarily in each other's internal political affairs. To be sure, there are exceptions to this system, such as the EU and its single currency, the International Criminal Court and the concept of 'Responsibility to Protect'. But these represent the boundaries of the existing international order rather than the building blocks of a new one. For the next 10 to 20 years at least, as the emerging powers acquire greater political power and autonomy, they are likely to repeat what the Western powers have done, promoting their interests within institutions rather than handing any more power than absolutely necessary to them. In other words, the world's most powerful states will seek to manage their interdependence through international political negotiation, rather than through new forms of global governance.

The real challenges to the existing international order will come not from the established or emerging powers, but from global forces that are beyond their control and also from those non-state entities and groups which seek to undermine the process of globalisation that links all states and societies ever closer together. Ensuring the continuation and deepening of international order in the next decades of the 21<sup>st</sup> century will require governments in both the West and among the emerging powers to improve their domestic resilience to internal and external shocks and, as suggested below, to use deeper regional cooperation as a testing ground for higher levels of international cooperation.

### **The Economic Crisis is Indeed a 'Western Crisis'**

The US, most European states and Japan, which, together with Canada and Australia, constituted the core of the 'West' during the past 50 years, are experiencing a structural weakening of their domestic drivers of growth. This weakening could undoubtedly challenge an international order that was built on the foundation of the West's international economic and military dominance.

While Japan has experienced nearly two decades of slow growth and a declining share of world GDP, European nations only appear to be recognising today, in the wake of the global financial crisis, the extent to which they too face structural constraints to their future growth. The first constraint arises from their demography. By most estimates, the share of the elderly as a proportion of the total population in Europe will grow from roughly 17% in 2000 to over 30% in 2050, by which time more than half of Europe's population will be 49 or older. The beginning of this process is already pushing many EU budgets into structural deficit and is forcing governments to reform generous European welfare systems that had defined their social compacts with their citizens. Across Europe, wide divergences in rates of employment among youth, women and the elderly pose further constraints on growth. Significant differences in levels of educational attainment –particularly between Mediterranean and northern European states– pose their own risks to future European international economic competitiveness. Rates of university attendance in Europe range from 20%-40%, but even the highest are below the 50% levels in South Korea and Japan. And there are similar divergences in secondary education: whereas 90% of Nordic school children complete their secondary education, only some 45% do so in Portugal.

The effects of declining European growth will also be geopolitical. Most European defence budgets have fallen to below 2% of GDP, limiting Europe's ability to project military power internationally. As governments in Europe struggle to adapt to their straitened circumstances, cohesion on external matters –such as the military operation against Colonel Gaddafi or sustaining an effective fighting force in Afghanistan– has become ever more complex, despite the adoption of new mechanisms for intra-EU coordination in the 2009 Lisbon Treaty. Perhaps more importantly, the combination of European inertia towards questions of international security and the new US strategic focus on Asia, where the rise of China threatens long-standing US alliances and influence, is weakening the transatlantic alliance.

The US does not face the same demographic challenges as its European partners, but it now appears to be facing its own structural economic challenges. For example, US unemployment has been stuck at roughly 9% over the past two years –nearly double its rate in the late 1990s and most of the 2000s, and only a little below the EU-27 rate, which climbed back up to 9.5% in the first half of 2011–. The current high rate of unemployment and slow rate of job creation in the US may not simply reflect the after-effects of credit deleveraging. As Michael Spence has noted in the July/August 2011 edition of *Foreign Affairs*, many US multinational companies are now creating more jobs abroad than they are at home, focusing their job creation on the dynamic markets of East Asia with its well-educated and well-priced workforces.

Today, the US, Japan and major European economies depend on exports to China and other emerging markets to drive their own marginal rates of growth. In 2010, President Obama made exports a central plan in his growth strategy for the US. Similarly, French, German and British political leaders are beating a path to Beijing and New Delhi to try to secure major new export orders. And the UK has announced a new 'commercial diplomacy' that places improved access for UK goods and services to emerging markets at the heart of the Foreign Office's remit.

This economic rebalancing is contributing to a weakening of the West's strategic influence across the world, from the Middle East and Latin America to South-East Asia and Sub-Saharan Africa. First of all, regional powers in each region (Turkey and Iran in the Middle East; Brazil in South America; China in South-East Asia; South Africa in Sub-Saharan Africa) now vie more effectively for influence relative to the US in capitals in these regions, partly because of their own growing economic magnetism and partly because they have taken advantage of the decline in the legitimacy and credibility of US global leadership during and following the George W Bush Administration. Secondly, regional organisations are also challenging US and western influence across the world, whether it is ASEAN, the East Asia Summit, UNASUL, the African Union or the Shanghai Cooperation Organisation. Third, the West's influence is declining also in the world's major international institutions, such as the UN, IMF and WTO, where the emerging powers now follow a far more independent line. The most obvious symptom of this shift in institutional power was the nomination of the G20 (at the London 2009 G20 summit) to be the world's primary forum for international economic coordination, in place of the Western-led G7.

Finally, perceptions are also important in the emergence of a new international order. When asked in a 1997 ABC/Washington Post poll which country would be the world's leading nation in 20 years time, 56% of Americans said the US and only 9% said China. In a similar ABC/Washington Post poll conducted in 2011, only 35% said the US while 38% said China. The growing sense among US citizens of their relative declining power risks

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becoming a self-fulfilling prophecy, which will then weaken the US and the West's voice on the international stage.

### **How Powerful are the Emerging Powers?**

It is easy to over-estimate the strength of the emerging powers in the midst of a Western economic crisis. Any change in the balance of power must be judged in relative terms before assessing its potential impact on the international order. And each emerging power faces its own major domestic challenges even as their collective economic gravitational pull is strengthening.

China is a perfect case in point. Its rapidly ageing population has led to a desperate race for China to grow wealthy before it grows old. China's greying society combined with its lack of a social safety net incentivises saving over investment and spending today (contributing therefore to China's overall current account surplus). But China's dash for growth has led to growing disaffection among parts of the population that are uprooted or disadvantaged by the current allocation of wealth and assets –180,000 protests or 'mass incidents' were reported in 2010, compared with 60,000 in 2006–, meaning that the Communist Party must fight ever harder to retain its legitimacy even as it manages an ever more complex set of domestic economic and political dynamics. Domestic challenges that will absorb Chinese leaders' attention over the coming years include containing inflation and asset price bubbles, shifting the economy from a reliance on exports to a greater balance in favour of domestic consumption, and capping the country's voracious appetite for resources (food, water and energy). The West's problems appear more manageable when compared to the enormous challenges facing China's leadership.

The same argument could be made regarding the world's other emerging powers. India has recently achieved levels of annual economic growth close to those of China, and some of its largest companies, such as Tata, Reliance, Wipro and Infosys, are becoming international players. Yet India still struggles to overcome the burden of high levels of poverty and illiteracy among its population, of pervasive political corruption and of rising inflation, as the country's higher levels of economic growth expose shortages of skilled labour and bottlenecks in power generation, transport and other aspects of physical infrastructure. Brazil has grown into one of the world's dominant food exporters, while its aerospace and energy sectors are also closing the gap with their Western counterparts. Yet inflation is also becoming a serious economic problem, not only because of rising food and energy costs, as the demands of wealthier consumers confront domestic supply constraints, but also because of the growing stratification between large numbers of poor, uneducated young people and a far smaller, well-educated cosmopolitan class, which is becoming ever more integrated into the global economy.

There are also geopolitical risks to the emerging powers. Their growing economic and military strength arouses suspicion among its neighbours which could limit their future regional power and influence. China's increasingly assertive stance to its claims over the South China Sea has caused alarm among South-East Asian nations, many of which have turned to the US in the hope that it will retain its role as an external provider of security and stability in the region. India must manage tense relations with its main neighbours, including Pakistan, China, Nepal and Bangladesh. Brazil has managed its rise the best within its region, but even here, suspicions over the country's relative economic size have limited its ability to push for closer regional economic integration. In

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contrast, the US and European countries live in relatively peaceful neighbourhoods with no real external challengers to their security.

There are other limits to the international or regional influence of the emerging powers. Setting Brazil to one side, they have yet to project the sort of 'soft power' of attraction or imitation upon their neighbours or other countries that the US and the most successful European countries have done. The US and European democratic political systems continue to serve as a model for others, most recently for parts of the Arab world, in ways that the Chinese systems (communist authoritarian) or Russian (state authoritarian) do not.

The stark differences between the political systems and national interests of Brazil, China, Russia and India create a further limit to their international influence. Despite convening annually along with South Africa at the BRICs summit, they have not yet acquired the habit of acting in concert in key international institutions or conferences. In contrast, the US and European countries, for all of their hand-wringing over the recent weakening of the Atlantic alliance and transatlantic relations, have retained an interest in and the formal and informal structures for consultation on both economic and political issues. The election of the new Managing Director of the IMF in 2011 stands as a case in point; the emerging powers were unable to act as a unified group and propose an alternative candidate to Christine Lagarde. Where the emerging powers have proved effective, however, is in blocking some of the international priorities of the Western powers, whether over tightening Iran sanctions, completing the WTO trade round or achieving progress on international climate change negotiations. But even here, they have generally taken advantage of divisions among the Western group rather than offer a convincing alternative approach.

The ultimate limit to the ability of the emerging powers to challenge the existing international order is that they are as dependent as the West upon the smooth-functioning of an open global economy for their economic success and political stability. The EU and the US are China's first and second-largest trading markets and, along with Japan, its principal sources of foreign direct investment (FDI) as well as technology partnerships. China depends on the US Treasuries market to 'sterilise' its ever-growing trade surpluses. China, India and Brazil are all becoming increasingly important investors into the EU and the US in order to grow market share. Rather than launching a zero-sum competition for geopolitical influence and economic supremacy with the West, the rise of the emerging powers is deepening their levels of interdependence with the West.

### **Can the West Recover?**

Another constraint on the emergence of a new international order arises from the powerful residual strengths of the US and the EU, which, far from decaying, are likely to remain two of the principal global actors well into the future. The US's innate strengths are well-known: its military forces far exceed those of any nation in terms of power, sophistication and reach and will continue to do so for at least the next 20 years. The US's youthful demographic profile reflects its continuing openness to immigration and will compensate for the ageing of its 'baby boom' generation. Its open, transparent and wealthy economy provides a strong domestic platform for economic growth. Combined with its world-leading higher education system and deep domestic capital markets, these attributes have made the US the global hub for technological innovation at a time when such innovation is a central driver of international economic competitiveness. And the US also has the

advantages of easy access to food and energy resources (its exploitation of massive reserves of unconventional gas being the latest boon to its future economic stability) which make it less dependent on imports of these vital resources than any of the emerging powers, Russia and Brazil aside.

It would be easy today to underestimate Europe's resilience. Despite the current Eurozone crisis, Europe continues to be home to three of the world's five most competitive economies, according to the World Economic Forum's 2010-11 Global Competitiveness Report (Switzerland #1, Sweden #2 and Germany #5, alongside Singapore #3 and the US #4) and has six out of the top 10 and 13 of the top 25. Europe will not quickly cede these strong rankings; it is home to many world class companies and industries (33 of the top 100 according to the Financial Times World Top 500 in 2010) as well as being a competitor to the US in many areas of high technology and innovation. Europe is also a world leader in service industries, such as finance, law, accounting, design, education and communications, which will be far harder to replicate in emerging economies than sheer industrial strength, but which are central to economic productivity and wealth generation. And, despite all of its stresses and flaws, the EU brings 500 million relatively wealthy European citizens together in a Single Market that is more likely to deepen over the coming years –in response to the economic challenge of the emerging powers as well as to the Euro crisis– than it is to fragment. And there is significant scope for further integration, especially in the services sector which remains largely outside the rules of the Single Market.

To be sure, the EU is unlikely ever to compete with the US or, in the future, with China, as a global military power. Foreign and security policy are likely to remain areas where intergovernmental processes persist within the EU and so, therefore, will lowest-common denominator approaches. But the size and internal coordination of the Single Market mean that the EU will be a world power in the areas of trade negotiations, investment rules and the establishment of the standards and norms that define whole new areas of global economic activity, such as renewable energy. It is important in this context that the EU and European states are already well-represented and well-versed in the operations of all of the world's main international organisations, an advantage that they will not give up soon or easily. And the long history of democratic governance, established welfare systems, general adherence to the rule of law and strong civil society across the EU together mean that Europe has a good chance to remain a bastion of political and social stability, even as emerging powers undergo painful and potentially destabilising political and economic transitions.

Just as the US is likely to retain much of the power it acquired during its period of global supremacy in the latter part of the 20<sup>th</sup> century, a resilient EU is more likely than one that collapses over the coming decades under the internal stresses of its recent enlargement and the external pressures of its rising economic competitors. But, to be resilient, a youthful US and an ageing Europe will both need to tap into the dynamic economic growth taking place beyond their borders in Asia and Latin America, in particular. Access to the emerging powers' growing export markets and, increasingly, to their growing reserves of potential foreign investment will be essential to the West's continuing prosperity, just as the emerging powers will depend on access to the West's wealthy markets and technology base.

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## **Towards a New International Order?**

The growing economic interdependence of the established and the emerging powers will likely be the defining feature of the new international order. Given the West's residual strength and the continued vulnerabilities of the emerging powers, a zero-sum rebalancing of power in favour of the East and a consequent fundamental shift in international order is unlikely. However, a new international order rooted in deepening levels of international interdependence is not an inevitable scenario. A principal source of potential conflict between states in the coming years will be the competition for natural resources that accompanies rapid global economic growth and improving levels of personal disposable income. Until technological innovation radically improves levels of energy production and efficiency, helps increase food production and water consumption in a sustainable manner and reduces human dependence on specific minerals that are unevenly distributed across the world, then there is a risk that ensuring access to these commodities might drive states into conflict with one another, whatever their levels of overall economic interdependence and the risks that would accompany such an outcome.

However, it is also possible that the main risks to international order during the coming decades will emanate not from the rash actions of states, but from outside the state system altogether. First, economic interdependence brings with it its own set of vulnerabilities for societies. Natural disasters now have ripple effects that extend from one side of the world to the other, whether this be the effect of the Japanese tsunami on just-in-time supply chains in the US or the ash cloud from the Icelandic volcanoes which crippled air travel over much of northern Europe and whose effects then threatened to spread across the region's economies. And significant changes in the earth's climate, which have led to the fall of empires when these have occurred during the past three millennia, now run the risk of having cascade effects across state borders in terms of migrant flows, disease transmission or food supply disruptions.

Interdependence also heightens the vulnerability of societies the world over to the disruptive actions of extremist, anarchist or criminal groups and individuals. Critical national infrastructure can be disrupted by cyber hackers. Terrorist attacks, or the fear of them, can bring national and international transport networks to a near standstill. And a well-executed biological attack by an individual could spread internationally and force governments to institute border controls that would stop national and international trade in its tracks.

The main challenge to international order, therefore, is that governments, businesses and societies in East and West, South and North fail to comprehend their levels of interdependence and do not deepen or build, therefore, the common norms, rules and institutions to raise their levels of resilience and ability to manage the impacts of such developments. Adapting existing international institutions to manage these risks will take a long time, given the sovereignty-based approach to establishing new multilateral agreements of both the existing and the emerging powers. And, while new international institutions, such as the G20, may offer a more legitimate forum for international policy cooperation than the old, such as the UN, they are likely to be hamstrung by the same instinct for sovereign governance among the majority of its members.

Two priorities stand out in this context. First, all states need to professionalise and improve their delivery of key services that promote security and enable sustainable growth and prosperity. For countries in the West, this will involve major reforms to welfare

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systems that remain industrial in their scale and approach and have not yet adapted to the West's changed demographic profile and reduced future rates of economic growth. It will also mean finding more affordable ways of maintaining their internal and external security, both in terms of lessening the appeal and impact of extremist or criminal attacks on their societies, and in terms of contributing to enhanced levels of security beyond their borders. In this regard, military deterrence will be as important as incentives to reduce the disparities in wealth and human security between them and their poorer neighbours.

For the emerging powers themselves and for most countries in the developing world, the priority will be to build the political institutions and processes, including functioning judicial systems and vibrant civil societies, that will embed a culture of greater transparency and accountability. Otherwise, rising levels of economic growth could lead to social upheaval or to unsustainable economic bubbles, either of which could bring to a jarring halt the process of global economic and political rebalancing that is currently under way.

Finally, deeper forms of regional integration may serve as a useful bridge to a future in which the term 'global governance' starts to have a real meaning. Although few groups of states are likely to emulate the EU in terms of building supranational institutions and methods of political governance, the deepening of consultation and cooperation of groupings in Asia (such as ASEAN and ASEAN plus 3), in Latin America (UNASUL) and sub-Saharan Africa (the African Union and ECOWAS) is serving two useful purposes. First, it is bringing pressure to bear on the emerging powers themselves to adhere to norms and processes that they do not control. And secondly, it is enabling the development of best practices in economic cooperation, market opening and political consultation at a regional level which could gradually be elevated to an international or global level, as and when a consensus begins to emerge on the validity of those best practices across regions.

Hedley Bull, the renowned British international-relations theorist, wrote that international order would at best resemble the notion of an 'international society', where states chose to adhere to certain rules and norms as a way of avoiding falling into anarchy and war. The rebalancing of economic and political power from the West and North to the East and South, and the deepening interdependence that is accompanying this process, now offers an opportunity for the world to test out Hedley Bull's vision. The birth of an international society is by no means foreordained, but governments, companies, civil society and individual citizens now have the opportunity to see if they can put his theory of international order into practice.

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