Geoeconomics and the strategic equilibrium in the Indo-Pacific

Dr. Darren Lim

Presentation to ISIS Malaysia
April 2024

0

The United States, export controls and semiconductors

- Sep 2022: National Security Adviser Jake Sullivan describes key technologies as "force multipliers" that are so foundational to the future of national security that not did the US need to lead but maintain the "largest lead possible".
- Oct 2022: New export controls using novel lists of controlled items, controls on activities by US persons, and extraterritorial reach of foreign made items embedded with US technology going to PRC companies.
- 2023: Controls are extended and tightened with cooperation of Netherlands and Japan to restrict exports of lithography equipment.

1

A change from the Cold War

- During the Cold War, the application of export controls was limited and focused.
- Today, the US assesses it impossible to distinguish military and civilian uses of a key foundational technology like advanced semiconductors.
- Accordingly, they need a restriction further up the supply chain, **regardless of the collateral damage to (legitimate) civilian economic activity**.
- In turn, these measures are perceived by Beijing as economic containment, heightening tensions.

Geoeconomics defined

1. Intentions:

The use of economic instruments:

- to promote and defend national security,
- to produce beneficial geopolitical outcomes; and

2. Consequences:

The geopolitical effects of economic connectivity, including the impacts of external economic actors (by governments, companies, etc) on a country's geopolitical goals.

Examples

Economic policies reflecting strategic <u>intentions</u>:
- Formal sanctions: US/EU against Russia, Iran, etc;
- Informal sanctions: PRC against South Korea, Australia, etc;
- Export controls & foreign investment restrictions
- Industrial policy and protectionism (when motivated by national security).

Policies with (potentially) strategic <u>consequences</u>
- Supply chain chokepoints: Naturally arising concentrations and dependencies in critical goods
- Asset control: Investment, construction and ownership of critical infrastructure (e.g. 5G)

April 2024 Darren Lim

4

The rise of geoeconomics

1. **Major power rivalry in an interdependent world**: expansion in the vectors of globalization and interdependence that touch on major-power interests and exacerbate competition
2. Expanding concept of **national security** to include traditional economic policy domains.
3. Strengthening of the "**state**" at expense of the "**market**" and the resulting competition between economic systems
4. **Weakening of post-war rules and institutions**: via changing balance of power (rise of Global South), eroding political legitimacy within the West (populism), pandemic-induced fragilities in globalization (supply chains).

April 2024 Darren Lim

5

Conceptual challenges

- Unlike the military and diplomatic domains, geoeconomic policy occurs in an arena—the economy and markets—only partially occupied by the state.
- This creates two challenges affecting analysis and policymaking:
  - The operation and impact of policy will usually be dependent on economic actors with distinct interests who may not be straightforward to control.
  - Separating national security interests from other interests like prosperity, values and social cohesion.

6

The national interest

Three (traditional) pillars of the national interest:

- Security: Defence of the homeland and autonomy of action.
- Prosperity: Development and redistribution
- Ideational: Protection of certain values, social cohesion, and promotion of "the good life".

These pillars often conflict, and policymaking is about balancing trade-offs, mediated by politics.

7

Potential geoeconomic tradeoffs in policymaking

- Economics vs security
- Markets vs states
- Openness vs closure (markets, society)
- US vs China
- Non-discriminatory multilateral system vs minilateral networks of trusted partners
- Formal rules and institutions vs informal, ad-hoc action

April 2024 Darren Lim

8

Geoeconomics and statecraft

The accumulation and exercise of power:

1. **Intentional instruments of statecraft**:
   - **Coercion**
   - Inducement
   - **Attrition**
2. **Strategic consequences of economic activity**
   - **Influence**
   - Leverage
   - **Market power (overlap with intentions)**

April 2024 Darren Lim

9

Intentional instruments: Coercion

- Defined: Disrupt economic activity to impose costs on a target to change its behaviour (or deter in future).

US / NATO → Russia (Ukraine, 2022 onwards): Financial (asset freezes, banking limits); trade restrictions (import/export restrictions on dual-use and luxury items); energy (oil price cap, limits on investment and tech transfer; individual (travel bans, business blockages).

PRC → Australia (Covid inquiry, 2020-23): Export bans (beef lobster); license cancellations (forages); refusal to buy (cotton/coal); anti-dumping duties (barley/wine).

- Dynamics: (1) punishment often generates a "*rally 'round the flag effect*"; (2) demands are often too (politically) costly for the target govt to concede; (3) potentially most effective against 3rd parties as a long-term deterrent;

April 2024 Darren Lim

10

Intentional instruments: Attrition

- Defined: Disrupt economic activity to degrade an adversary's battlefield capability.

US → Russia (sanctions): Export controls on military equipment and dual-use goods to undermine Russia's production and procurement.

US → PRC (semiconductor Export controls): Goal to restrict PRC's ability to obtain, develop and manufacture advanced semiconductors.

- Dynamics: (1) extraterritorial impact (e.g. Dutch company ASML); (2) often captures civilian use; (3) Western companies suffer and have interests in circumventing; (4) hard to be comprehensive; (5) spurs target efforts to diversify.
- Main point: "Control" vs "run faster" debate is central.

April 2024 Darren Lim

11

Strategic consequences : Influence

- Defined: Favourable political sentiments cultivated by ongoing economic relations, which create the perception that economic future depends upon maintaining positive political relations, requiring alignment of non-economic policy choices with the trading partner's interests.
- Dynamics:
  - Every trading country can potentially accumulate influence, this is normal, natural and legitimate given the "prosperity pillar" of the national interest.
  - The larger the economy, the larger this influence will be.
  - Becomes a problem when it corrodes domestic political and social institutions, e.g. through a lack of transparency or corruption.

April 2024 Darren Lim

12

Strategic consequences: Market power

- Defined: Long-term strategic advantage that results from the acquisition or maintenance of market power in leading sectors.
  - Can happen without international government support
  - Also happens via by deliberate and asymmetric industrial and protectionist policies (also indirectly via attrition which harms competitors).
- Future advantage could manifest both from:
  - Leverage as a monopoly supplier (coercion, attrition); or
  - Technological superiority provides battlefield or related (e.g. cyber) advantages.
- Examples: Direct subsidies or foreign acquisition, or via policies that harm market competitors such as limiting market access, forced technology transfer or outright theft of intellectual property.

April 2024 Darren Lim

13

Market power dynamics

- Industrial policy and protectionism are often pursued for economic reasons, rather than as a dimension of strategic competition.
  - These policies are wasteful, but sometimes can found long-term development (e.g., "developmental states" in NE Asia).
- Today, many countries are pouring billions of dollars into developing local technology industries (especially semiconductors) that have questionable economic benefits!

14

Linking economics to national security and geopolitics

Effective geoeconomic analysis requires grappling with new variables that one would not commonly encounter studying national security policy:

- Market structure, e.g., the semiconductor supply chain or the global commodity markets
- Economic policy tools and regulatory regimes.
- Underlying interests and actions of individual economic actors like firms who can enable (or frustrate) government policy.

15

Zooming out: International economic order

- The rise of geoeconomics occurs within the post-war economic order that was designed in response to the "beggar-thy-neighbour" protectionism of the 1930s, which contributed to WWII.
- By promoting free trade and openness, that order created modern globalization and (on net) was good for the world.
- But new dynamics are challenging that order's emphasis on openness.

April 2024 Darren Lim

16

Challenges to the regional strategic equilibrium

- Geoeconomics: Unacceptable supply chain chokepoints that can be weaponized by adversaries.
- Climate: Decarbonization imperative.
- Both these concerns generate (legitimate?) exceptions to free trade. But how to we bound those exceptions to maintain as many of the benefits from globalization as possible?
  - Example: Trump admin steel tariffs against New Zealand on the grounds of "national security".

Dec 2023 17 D. Lim

17

Final takeaways

- Recognize that globalization and economic interdependence are increasingly seen as sources of power and vulnerability.
- Gain some visibility of mechanisms through which power is accumulated and wielded in the geoeconomic domain.
- Begin to appreciate the difficult policymaking trade-offs generated by geoeconomics, especially between security and prosperity.

April 2024 Darren Lim

18