



# THE RETURN OF GEOPOLITICAL RISK

Russia, China and the United States

**Thomas GOMART**

**Foreword by Patrick POUYANNÉ**

April 2016



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# **The Return of Geopolitical Risk**

**Russia, China and the United States**

**BY THOMAS GOMART,  
DIRECTOR OF IFRI**

**FOREWORD BY PATRICK POUYANNÉ  
CHAIRMAN AND CEO OF TOTAL**

**ÉTUDES DE L'IFRI  
APRIL 2016**



# Foreword

This paper by Thomas Gomart, Director of Ifri, on the return of geopolitical risk comes at an opportune moment.

Not for many years has the world experienced such instability: be it the Middle East (Syria, Iraq, Yemen), North Africa (in particular Libya), tensions between Russia and Ukraine, between China and its neighbors in the China Seas, and between North Korea and its neighbors in North-East Asia. And we haven't even mentioned the repeated terrorist attacks that know neither boundaries nor borders.

As Thomas Gomart points out, the prevailing view in business circles – that globalization is an “irreversible trend of increasing commercial and financial exchange” – may have had the effect of discounting the logic of power and minimizing the role of states. Even if geopolitical risk never truly disappeared, it is now making a strong comeback, and we are witnessing more and more cases in which economic logic gives way to political imperatives.

Thomas Gomart's aim is thus to encourage business leaders to integrate political risk into their forecasting efforts, in order to enhance their ability to anticipate future scenarios. To help them discern the geopolitical issues of the day, he has restricted his analysis to the relationships between three countries – Russia, China and the United States – which, due to their size and role in world affairs, are central to the important changes occurring in international relations. He has also taken an original approach in focusing on the three bilateral relationships – US–Russia, Russia–China and China–US – in an effort to shed more light on the forces at work in geopolitical risk.

By means of this paper, he aims to help business leaders acquire the tools to monitor and analyze the trajectories of the countries that they are interested in, combining instant and long-term reading, to understand these countries' leaders better, and to grasp how the relations between the United States, Russia and China affect their businesses.

In the course of his analysis, Thomas Gomart shows just how vital the security of energy supplies is to any great power project.

For a company like Total, geopolitical risk has been at the heart of business activities from the very beginning. This risk presided over the founding of our company after the First World War; in fact, it was because

France appreciated the risk it was running in depending on the US and UK for oil that the decision was taken to found the *Compagnie française des pétroles* (CFP), the forerunner of Total. Elf was created after the Second World War for the very same reason.

Secondly, a cursory glance at the location of the world's oil and gas reserves is enough to understand the importance of geopolitics in our business. Indeed, the Middle East accounts for 50% of the world's oil reserves; adding Venezuela, Canada and Russia into the bargain brings the total to 80%. As far as gas is concerned, four countries – Iran, Russia, Turkmenistan and Qatar – contain 60% of the world's reserves.

This concentration of resources explains the extent to which our company must know how to operate in risky conditions. And all this, of course, without ever putting our teams' lives in danger: security is not just a priority for Total, it is a corporate value. Therefore, when the dangers grow overwhelming, we pull our teams out, as we were forced to do in Yemen last spring.

Large companies like ours, however, can also undoubtedly act as stabilizing forces in the midst of disorder: in continuing, for example, despite conflicts, to provide populations with energy, vital to all human activity. Above all, we try, whenever we can, to bring the points of view of different states into greater alignment so that dialogue may triumph over conflict and the globalization of exchange, which has lifted billions of human beings out of extreme poverty, may proceed in a calmer environment, to the benefit of all.

I wish you an interesting read.

**Patrick Pouyanné**  
**Chairman and CEO of Total**

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# Introduction

“In 2014, strictly economic ways of thinking seemed to crumble in the face of geopolitical considerations.”<sup>1</sup> Such was the opening of *Le Monde*’s annual review. The year 2014 was defined by the conflict in Ukraine, the emergence of *Daesh*, and tensions between China and Japan. As for 2015, it has witnessed the spread of *Daesh*, the conflict in Yemen, the Greek crisis, revelations about the activity of the National Security Agency (NSA), the migrant crisis, and a ramping-up of terrorist attacks. This proliferation of crises has contributed to a “return” of geopolitics, or, in other words, to power rivalries that may sound the death-knell for the kind of globalization that ignores territorial boundaries. For some, this “return” is embodied by three countries – China, Russia and Iran – and takes the form of an open challenge to the international order established at the end of the Cold War.<sup>2</sup> For others, this “return” is nothing of the sort, but simply the continuation of traditional rivalries between great powers. In this regard, China and India, which are accused of “revisionism” but are integrated into the global economy, have not taken up an aggressive stance of challenging the world order, but a defensive stance, which consists of protecting their sovereignty and regional influence.<sup>3</sup>

Whichever interpretation they favor, decision-makers in the public and private sectors now largely agree on the fact that the international environment has seriously and rapidly deteriorated since the financial crisis of 2008. They seem disoriented by the multiplication of crises, including those on European soil, where the stability of established institutions is now in question. Perceiving the situation in this way leads to a consideration of systemic risks, and soul-searching about the ways in which globalization is changing. It appears now to be defined more by conflict than by cooperation. Without a doubt, we are bearing witness less to a return of geopolitics, which is always there, than to a change, on the one hand, in the balance of forces between democratic and authoritarian regimes – largely through the evolution of the Chinese-American relationship – and, on the other, in the way power is structured through its forms of concentration and dispersion. As early signs of greater diversity,

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1. *Le Monde*, “Le Bilan du Monde 2015”, p. 10.

2. W. Russell Mead, “The Return of Geopolitics”, *Foreign Affairs*, May/June 2014.

3. G. John Ikenberry, “The Illusion of Geopolitics”, *Foreign Affairs*, May/June 2014.

these changes could soon entail new types of regionalism, even blocs of varying shapes that will directly affect not only the politics of states but also the activity of markets and companies.

Depending on their size and sector, companies deal with political risk differently. Some carry out in-house analysis, others outsource it, while yet others turn their backs, less through lack of interest than for lack of methodology. “When the unthinkable happens,” however, “confidence is hit hard” because “predictability feeds confidence.”<sup>4</sup> Predictability, then, is a cornerstone of any judgment made about a country and, by extension, a market. The prevailing orthodoxy in this connection is the infamous “black swan”, symbolizing the power of the unpredictable and the unpreparedness of companies.<sup>5</sup> In reality, surprise arises within a frame of reference, which thereby reveals itself to be inadequate. Globalization, understood as a process of increasing commercial and financial exchange and of linking-up of transnational chains of value: such is the frame of reference that still holds sway in business circles. This assumption causes people to discount the logic of power and to minimize the role of states. In such an inadequate intellectual framework, strategic surprises arise.

For companies as well as investors, trying to anticipate is essential; most often, it involves assessing country risk by focusing on a whole economy, and is often carried out by credit rating agencies.<sup>6</sup> The task of “risk manager” is already well established in big companies, but is also beginning to appear in export-focused small and medium-sized enterprises (SMEs).<sup>7</sup> Political risk is one element of country risk, and political risk ratings are meant to measure how credit-worthy a state is. Ranking countries by means of comparative study encourages them to adopt common standards, in order to attract investors. Country risk and ratings are now embedded into companies’ strategies for expansion overseas; they incorporate the idea that political and economic systems are converging, even though “states lack the same abilities to adapt because of their past trajectories”.<sup>8</sup> That is why political risk has come to be defined as the element of country risk that cannot be measured or subjected to modeling. Country and political risk have, for a long time, depended on the idea of “crisis”, which lacks a practical definition. This idea obscures the latent

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4. J-M. Pillu, “Cette laborieuse reprise mondiale”, *Guide Coface, Risque pays 2015*, 2015, p. 4-5.

5. N.N. Taleb, *Le Cygne noir. La puissance de l'imprévisible*, Paris, Les Belles Lettres, 2011.

6. N. Meunier & T. Sollogoub, *Économie du risque pays*, Paris, La Découverte, 2005.

7. V. Talmon, “Risques-pays : halte aux idées reçues !”, *Les Échos*, 18 November 2014.

8. J. Story, “L’analyse du risque pays : plus qu’une discipline postmoderne”, *Politique étrangère*, No 2, 2014, p. 136-138.

tensions that pervade all fields of activity. According to some banks' economists, political risk will henceforth require particular attention, because of what they perceive to be systemic shocks, which reveal less about the activity of individual economic actors than about the possible institutional instability of developed countries. Confronted with more and more cases in which "politics steals a march on economics", they are thinking of revising their approach.<sup>9</sup> In this reading, geopolitical risk deserves to be addressed separately. In an attempt to define it, at least three other analytical perspectives can be used. First of all, the analysis of risk should take account of "power plays", which always have a military component. Second, it should pick out political issues that have the potential to exert systemic effects, as well as closely following those areas of activity that are crucial to the wielding of power. Third, it should avoid binary thinking that would dismiss geopolitical risk on the grounds that, if it arises, it is uncontrollable, and, if it does not appear, it is lying dormant and therefore cannot be measured.

The aim of this paper is to improve the ability of businesses to anticipate the future; doing so requires the relevant institutional actors to be identified and the political problems encountered to be articulated. It deliberately focuses on three countries, Russia, China and the United States, which together form a strategic triangle of systemic importance. It does not attempt to encompass the role of other state and non-state actors. Issues as important as terrorism, the fragmentation of the Middle East, tensions in Sub-Saharan Africa and instability in Europe are not discussed, though they clearly merit efforts at prediction. This paper also focuses on risks inherent in the exercise of power, to the neglect of transnational risks (climate change, migratory flows, currency wars, religious movements, etc) that also affect geopolitics.<sup>10</sup>

In 1971 – at the expense of Moscow – Washington and Beijing restored diplomatic relations, thereby transforming the international order. Forty-four years later, this triangle still shapes the international order, but in a very different way. The effects of the actions taken by these three powers spread well beyond their interactions with one another. To understand these effects is to grasp the interactions between military, political, technological and economic questions, in order to discern the "center of gravity of events" and be in a position to interpret them.<sup>11</sup>

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9. T. Sollogoub, "Le bel avenir du risque politique", *Crédit Agricole, Éclairages Émergents*, No 19, June 2012.

10. These themes deserve to be treated separately because they are going to grow more important.

11. G. Friedman, "Strategic Forecasting: The Impersonal Dimension of Intelligence", *Valdai Papers*, No 6, December 2014.

Equally, it is necessary to focus on decisions taken by sovereign states that affect how international relations and, by extension, the business environment work. Some companies have built up “political capital” that allows them to interact with the political process in a wide sense, beyond mere questions of regulation.<sup>12</sup> Nevertheless, their business can be shaken, relaunched or stopped dead in its tracks by the decisions of sovereign states. They cannot afford to economize, therefore, when it comes to close and regular tracking of their geopolitical environment.

On the diplomatic front, Russia, China and the United States are permanent members of the United Nations Security Council. As such, they play an active role in most international questions. Militarily speaking, they are nuclear powers, while also possessing formidable conventional capabilities, and they occupy the top three positions in the global ranking of military spending.<sup>13</sup> Economically, China and the United States are now neck and neck in gross domestic product (GDP) terms, while Russia trails far behind.<sup>14</sup> To summarize, then, the United States remains the dominant power, China has emerged as the rising power and Russia is the declining power. When due attention is paid to their different strategic cultures, the profile of their leaders and the resources at their disposal, all three are still capable of implementing a “grand strategy”, defined as “the exercise of national power with the aim of securing national security objectives in all circumstances”.<sup>15</sup> Although this notion of “grand strategy” is central to analyzing the motives and capabilities of certain states, it is more and more at odds with the lexicon of European Union (EU) member states. Nevertheless, it has profound implications for three key areas: military, energy and digital, which must be mastered together if the strategic autonomy demanded by great powers is to be achieved.

This strategic triangle offers us an excellent viewpoint from which to survey the changes that are under way in international relations. The relationship between the US and the Soviet Union shaped international relations between 1945 and 1991, while Chinese-American relations are now on their way to becoming the keystone of world order. It is impossible

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12. O. Basso, *Politique de la Très Grande Entreprise*, Paris, PUF, 2015.

13. According to the Stockholm International Peace Research Institute (SIPRI), the military spending of the United States, China and Russia is (in billions of current dollars) 610, 216 and 86 respectively.

14. In 2014, the gross national income (GNP + net primary income flow from non-residents) of the United States, China and Russia (in billions of current dollars) was: 17,812, 17,919 and 3,600 respectively.

15. J. Collins (*Grand Strategy*, 1973), quoted by H. Coutau-Bégarie, “Grande stratégie” in T. de Montbrial and J. Klein (eds.), *Dictionnaire de stratégie*, Paris, PUF, 2000, p. 270-271.

to know how the American leadership will change in the future, but one thing is certain: China and Russia will measure their weight abroad by the importance ascribed to them by the United States. At the same time, relations between Moscow and Beijing could shift the triangle's center of gravity if their rapprochement stands the test of time. In that case, the implications for Europe, Japan and India would deserve a separate study. For now, what is important is to delineate the main elements of the three bilateral relationships (United States-Russia, Russia-China, China-United States) that make up the triangle. It is no doubt unusual to focus on a bilateral relationship rather than on an individual country. However, I believe that doing so is an empirical way of displaying the systemic forces inherent in geopolitical risk.

This paper is intended to be read by managing directors; it aims to encourage them to integrate geopolitical risk into their attempts at anticipation and to employ the concept in their particular areas of activity. If they do not take an interest in geopolitics, geopolitics will take an interest in them. The projection of power always has economic consequences ("trade follows the flag"), just as international development and conquering markets have geopolitical effects ("the flag follows trade").<sup>16</sup> Any company with an international presence becomes a geopolitical actor, whether it is aware of it or not. However, this status is perceived and acted on in different ways, depending on the company's size, its sector and the profile of its shareholders and leaders. At the same time, geopolitics may make itself felt in different ways at different times in its production, finance and investment cycles.

For business leaders, it comes down to:

1. *Possessing a system for monitoring and analysis, which allows you to combine instant reading with long-term reading.* While it is easy to acquire such a system, the latter combination requires you to use various methods to follow the trajectory of target countries and the changes in transnational developments. Such an approach should allow you to pick out the emerging countries that are driven by the logic of power. In reality, "emergence" takes different forms, and only a small number of countries are capable of changing the way international relations work. It is important to be in a position to make out the trajectory of a given country and not to settle for a short-term risk analysis. You cannot understand the trajectories of countries like Russia, China or the United States by focusing on one or two years alone. Their trajectories only take shape if you analyze military, technological, political and economic developments over several

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16. S. Baru, "Geo-economics and Strategy", *Survival*, No 3, 2012, p. 47.

decades. Such a time-frame is foreign to the market but conforms to cycles of direct investment for industrial enterprises. In every organization, high-quality information must be transformed into knowledge, in order to understand and interpret it. In general, it is the leader's skill and judgment that determines how the company positions itself. Yet, the use of binary thinking to tackle the subject of geopolitical risk may shackle the leader's actions.

2. *Aiding understanding between business leaders and state officials* and, by extension, between businessmen, diplomats and military figures. Held up as a priority of foreign policy, "economic diplomacy" reflects the willingness of the French authorities to give a helping hand to businesses attempting to expand abroad at a time when they are seeking new drivers of growth. In fact, this is nothing new. From the 15<sup>th</sup> century onwards, the diplomacy conducted by the kings of France had a commercial aspect to it. To guarantee "the passage of goods", they protected their traders and, by means of agreements negotiated between one power and another, they ensured the freedom and security of commercial exchange.<sup>17</sup> The business world, on the other hand, sometimes has difficulty grasping what the stakes are of a particular foreign policy and, in extreme cases, of accepting the primacy of politics. Changes in the profiles and personalities of business leaders go some way to explaining these difficulties, but they do not go the whole way.<sup>18</sup> They also have their roots in an oft-forgotten fact: countries are not companies; though they might share common interests, they do not pursue the same objectives.<sup>19</sup> What is more, the relationship between companies and states will remain deeply unequal so long as states retain their monopoly on legitimate violence. Politicians, investors and business leaders are constantly called upon to make choices and take decisions that often depend on their interactions with one another. If he understands his competitors, the business leader must throw himself into analysis "and thereby know his history", in order to truly understand politicians, the trajectory of the target country, and security challenges beyond those confronting his employees.<sup>20</sup>

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17. F. Autrand and P. Contamine, "Naissance de la France : naissance de sa diplomatie", in *Histoire de la diplomatie française*, Paris, Perrin-Tempus, 2007, p. 168-169.

18. S. Fort, "Dirigeants d'entreprise et haute fonction publique : renouveler les termes du dialogue", *Note de l'Institut de l'Entreprise*, January 2011; F. Monlouis-Félicité, "Les grandes entreprises en France : je t'aime, moi non plus", *Note de l'Institut de l'Entreprise*, September 2015.

19. P. Krugman, "A Country is Not a Company", *Harvard Business Review*, January/February 1996.

20. J. Story, *art. cit.* [8], p. 136-137.

3. *De-centering their view of international relations*, not in order to underscore the fact that Europeans have become peripheral but, on the contrary, to draw their attention to the global forces that are already shaping their activities. The United States, China and Russia are the EU's three main commercial partners, accounting for 15%, 14% and 8% respectively of its foreign trade in 2014.<sup>21</sup> Nevertheless, we are witnessing a restructuring of international trade, brought about by growing tensions between the openness it implies and the protectionism it entails. This restructuring is also geopolitical in nature. The United States, China and Russia all pay lip service to the idea of openness. But when it comes to actions, the strategies they employ aim to shore up national interests, while giving rise to competition between different types of capitalism. This competition goes beyond mere economics. The famous "Washington Consensus", which was dealt a blow by the crisis of 2007, is now being challenged by a "state capitalism" promoted by China and Russia. Debate is now under way about conditions for cooperation and competition between liberal capitalist countries and authoritarian capitalist countries, as well as over the make-up of regional blocs that have new implications for geopolitics.<sup>22</sup> This debate is at the heart of the large free-trade treaties – TTIP and TPP<sup>23</sup> – which are being promoted by the United States, but which do not include China and Russia. The TPP, signed in October 2015, shows that the United States still has the power to give shape to international trade, even if questions remain over TTIP (still being negotiated when this paper was written). These changes in globalization – less open and more diverse – will open up new opportunities for businesses, depending on the sectors in which they operate. But they also intensify risks. It is time to prepare for them.

This paper, then, is an exercise in analysis and prediction. It focuses less on practical recommendations than on particular themes. It rests on the following perception: European businesses tend to underestimate the transformation that is under way in the process of globalization, caused, among other things, by the three-way game between Russia, China and the United States. This perception remains to be tested.

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21. Eurostat, March 2015.

22. S. Baru & S. Dogra (ed.), *Power Shift and New Blocs in the Global Trading System*, Routledge/IISS, 2015.

23. The TTIP (Transatlantic Trade and Investment Partnership) was negotiated between the United States and the EU. The TPP (Trans-Pacific Partnership), negotiated between the United States and 11 countries in the Pacific area (Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam) was signed in October 2015.



# I. Russia

In terms of risk for companies, analysis about Russia is currently focused on the sanctions imposed on the country after the annexation of Crimea in March 2014 and the destabilization of eastern Ukraine. Russia, with its military intervention in Syria in the autumn of 2015, has changed the international game. This provokes an initial observation. The sanctions have been designed to change the Kremlin's behavior in Ukraine. They distinguish between different avenues of Russian foreign policy without necessarily grasping it as a whole, in all its complexity. They also penalize many companies in Europe as well as in Russia. It is therefore necessary to place sanctions in perspective, in order to understand the reasoning behind their introduction and the reasoning that could lead to them being lifted. These sanctions work today as a *trompe-l'oeil*, giving a misleading picture of the path Russia has followed since 1991.

## Chronology of the Ukraine crisis and the sanctions against Russia

**November 2013 – February 2014:** Demonstrations on Maidan square in Kiev.

**21 November 2013:** Viktor Yanukovich refuses to sign the Association Agreement with the EU.

**21 February 2014:** Agreement to end the crisis between Viktor Yanukovich and the main leaders of the opposition. The foreign ministers of France, Germany and Poland, as well as the special representative of the Russian president, call for “an immediate end to all violence and confrontation”.

**22 February 2014:** Flight of Viktor Yanukovich, followed by his dismissal.

**6 March 2014:** The European Council approves the principle of graduated restrictive measures, in three phases.

**17 March 2014:** Imposition of the first restrictive measure (travel bans and asset freezes).

**18 March 2014:** Annexation of Crimea by Russia.

**20 & 21 March 2014:** List of people subject to visa bans and asset freezes extended; cancellation of the EU-Russia summit; drawing up of possible targeted economic measures.

**April 2014:** Start of military confrontations in Donbass.

**6 June 2014:** Establishment of the Normandy format (Russia, Ukraine, France and Germany).

**31 July 2014:** Adoption of further restrictive measures following Malaysia Airlines crash.

**7 August 2014:** Russian embargo on imports of foodstuffs from the EU, the United States, Australia, Canada and Norway.

**30 August 2014:** Sectoral economic sanctions decided on by the European Council.

**5 September 2014:** Minsk protocol.

**8 September 2014:** Sharpening of additional restrictive measures because of the presence of Russian forces on Ukrainian soil.

**21 October 2014:** Extension of Russian counter-measures.

**18 December 2014:** Strengthening of sanctions with respect to Crimea and Sevastopol.

**29 January 2015:** Further sanctions against individuals and extension until September 2015.

**12 February 2015:** Minsk II Agreement.

**14 September 2015:** Extension of restrictive measures until 15 March 2016.

## 1. Washington-Moscow

The end of the Cold War and the collapse of the Soviet Union were celebrated in Washington as symbolic victories; victories of one model over another. But that is not, of course, the perception in Moscow, where the end of the Cold War is currently being rewritten. The fall of an empire is counted not in days nor in years, but in decades. The way in which the different protagonists describe it shapes their representation of the world and prevailing power dynamics. The ideological heart of the Ukraine crisis is to be found in the contrasting narratives that Russians, Americans and Europeans tell about the end of the Cold War, the international order and the so-called years of “transition”. A debate over “transition” might seem far removed from the goals of companies operating in Russia. However, it is necessary to have such a debate in order to set up an analytical framework to understand relations between Russia and the West.

After the fall of the USSR, a concept of globalization took hold according to which the end of the Cold War led to the integration of emerging countries into the global economic system.<sup>24</sup> Yet, structural reforms in China and its progressive opening-up to the market economy date from the end of the 1970s and the beginning of the 1980s. Making its way in the world, China did not scrap its ideological arsenal, but adapted it to its new developmental model and rising power ambitions. At the same time, the USSR was pursuing a military build-up disproportionate to its economic resources, a build-up that would delay its entry into globalization. It is therefore a fallacy, albeit one frequently committed, to elide the fall of the USSR with the advent of a new liberal economic order. It is important to tease out the victory of liberalism over Soviet communism from the story of the integration of large emerging nations into the global economy.<sup>25</sup>

This historical background is often discounted. Yet it is crucial, given that history, through the construction of particular narratives, is always being bent by politicians to fit their short-term objectives. Historical references often tell more about the strategy being followed than do economic indicators – and this is not only true for Russia. The choices made by Vladimir Putin are better understood in light of his reading of Russian history – a fusion of imperial and Soviet heritages – than as a function of an idea of globalization shared with the West. The conflict in

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24. The term “globalisation” appeared on the front page of the *Financial Times* in July 1984.

25. M. Duclos, “Les puissances émergentes et la politique mondiale”, *Commentaire*, No 149, 2015, p. 29.

Ukraine offers a typical case study in the overlaying of historical references. The term “fascist”, for instance, was central to Moscow’s attempt to destroy the credibility of the regime in Kiev. Indeed, Cold War rhetoric has reappeared on both sides of the divide. We must therefore investigate how Russian leaders remember and interpret the implosion of the Soviet Union. In their view, a policy of US aggression generated external shocks that brought down the Soviet Union. This memory now finds itself reflected in today’s world: the Euromissile crisis of 1983 marked the high point of bipolar confrontation, while in 1985, the fall in oil prices, exacerbated by an American-Saudi entente, brought the Soviet economy to its knees. The Soviet retreat from Afghanistan, after ten years of stalemate, followed in 1989. The problem lies, then, in the different values that Washington and Moscow ascribe to this policy. In Russia, it stokes a visceral anti-Americanism that is widely shared among both elites and public opinion: they believe that the United States is still trying to destroy Russia, this time by means of the Ukrainian crisis. In the US, the policy is subject to *ex post facto* reconstructions used to justify a “grand strategy” that supposedly brought down the USSR and is seen to hold lessons for other theatres. In fact, the Cold War ended “not thanks to the aggressive stance of the United States but despite it”.<sup>26</sup> The exploitation of effects attributed to power politics by either side can thereby heighten risks at times of crisis. Ukraine offers a case in point, with the debate over supplying weapons animating some circles in Washington.

Since the end of the Cold War, six main areas have dominated Russian-American relations: nuclear weapons, proliferation, the post-Soviet space, European security, the Arab world, and human rights.<sup>27</sup> Economic matters have never figured high on the agenda. The US-Russian relationship suffered a blow before the Ukraine crisis when Washington admitted that the “reset” launched by Obama at the beginning of his first term in office had failed. This reset had sought to establish a new type of partnership with President Dmitry Medvedev, who was thought to be more open-minded than his mentor, Vladimir Putin. The ultimate problem, however, is that Russia and the US have very different interests: Russia is perceived in Washington as a power that is fundamentally in decline, and consequently represents a risk to regional stability. It has become a second-order concern for the US. In Russia, in contrast, the US still occupies a central position in strategic thinking. Restoring a diplomatic dialogue of equals remains one of the Kremlin’s main objectives.

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26. P. Grosser, 1989, *L’année où le monde a basculé*, Paris, Perrin, 2009, p. 25.

27. A. Stent, *The Limits of Partnership, U.S.-Russian Relations in the Twenty-First Century*, Princeton, Princeton University Press, 2014, p. 14.

On the face of it, Moscow and Washington share common interests in Asia for the maintenance of stability, but this convergence depends on the state of their relations in Europe. Russia hardly registers at all in American strategic thinking about Asia; it shouldn't be made to choose between Washington and Beijing, or so the thinking goes, and it is seen as a source of stability in the region. Like the US, Russia is directly concerned with the need to preserve freedom of navigation in the Sea of China. Even if Moscow is at pains not to take sides in the region's territorial disputes, it upholds the principle of free passage at sea, which is essential for its exports. It is also set on developing a northern sea route in the Arctic, which remains one of its geopolitical priorities. One group of American experts, alive to the power plays under way in Asia, is now lobbying for a Russian-American-Chinese alliance centered on nuclear security, the stabilization of Afghanistan and the question of North Korea.<sup>28</sup> This group is also pressing for a Russian-Japanese rapprochement under the auspices of Washington, and is calling for the TPP negotiations to be opened up to Russia, particularly since Russia has already signed commercial agreements with countries such as New Zealand and Vietnam.

Despite the Russian authorities' insistence that their country is pivoting towards Asia, it should be noted that relations with the EU remain crucial for Russia. Equally, relations with Russia remain of primary importance for the EU, particularly in the energy sector. European decision-makers too often interpret Russia's behavior through the prism of relations between Russia and the EU, or between Russia and individual member states; although this approach has its value, it is inadequate if we are to predict Moscow's intentions. For the Kremlin, what matters above all is to be recognized as a great power by its peers, namely Washington and Beijing. Indeed, the current impasse is partly a result of the lack of attention paid to Russia by Western countries since the end of the Cold War. As a matter of fact, Western powers have denied Russia equal status. The country was seen as a re-emerging market, but its great-power ambitions were not taken into account. Relations between Russia and America, and Russia and China, though often overlooked by European companies in their assessments of Russia, are crucial to understand Russia's trajectory. Decisions taken in Washington and Beijing, whether over sanctions or financial arrangements, could directly affect these companies' activities.

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28. J. Mankoff, "Russia's Asia Pivot: Confrontation or Cooperation?", *Asia Policy*, No 19, January 2015, p. 85-86.

## 2. Objectives and trajectory

A century ago, the last Tsar of Russia, Nicholas II, summed up what would turn out to be President Putin's main objective: for Russia to recover and retain "its place among the great powers".<sup>29</sup> Yesterday, as today, this phrase reminds Russian elites of their country's prestige. One thing that their economic and political partners should note is that these elites remain capable of strategic planning.<sup>30</sup> In the wake of the collapse of the USSR, with "capitalist euphoria" about to play into the hands of future oligarchs, Russia slid down the geopolitical ladder. Andrei Kozyrev, Russian foreign minister under Boris Yeltsin and an advocate of rapprochement with Euro-Atlantic institutions, said regretfully in 1991 that geopolitics had taken the place of ideology.<sup>31</sup> The geopolitical thinking that holds sway in Moscow deserves careful attention, taking into account the fact that it reflects the "sovereign turn" in Russian politics and economics. In the course of the 2000s, Russia developed a discourse that allowed it to oppose US assumptions: Russian "specificity" responded to Western "globalization", and "sovereign democracy" to the "promotion of democracy" so beloved of the Bush administration.

Vladimir Putin's project can be summarized thus: a search for international prestige made possible by the rebuilding of the Russian military thanks to renationalization of the energy sector.<sup>32</sup> Revenues from the energy sector were funneled into a security policy that had fallen into abeyance in the 1990s. With this money, Vladimir Putin was able to increase military spending and build up Russia's armed forces.<sup>33</sup> This direct link had been at the heart of the Soviet system and contributed to its collapse. In September 2011, Russia's emblematic Minister of Finance, Alexei Kudrin, publicly denounced the scale of military spending, which, he protested, was disproportional to the economic modernization of the country. Over the last fifteen years, Russia has consistently increased its military spending, and by 2014 it stood at between 3.5% and 4.5% of its GDP. Over the same period, European countries have gone on drawing on

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29. Cited in D. Lieven, *La Fin de l'Empire des Tsars*, Genève, Editions des Syrtes, 2015, p. 147.

30. A. Monaghan, "Putin's Russia: Shaping a 'Grand Strategy'", *International Affairs*, No 5, 2013, p. 1221-1236.

31. Cited in R. Kaplan, *The Revenge of Geography*, New York, Random House, 2013, p. 175.

32. P. Baev, *Russian Energy Policy and Military Power*, London, Routledge, 2008, p. 2.

33. T. Mitrova, "The Political and Economic Importance of Gas in Russia", in J. Henderson and S. Pirani (eds.), *The Russian Gas Matrix: How Markets are Driving Change*, Oxford, Oxford University Press, 2014, p. 8-9.

the “dividends of peace” by continually reducing their military spending. France, for instance, has almost halved its defense budget over the last thirty years.<sup>34</sup>

This military build-up allows Russia to project an image of power in the post-Soviet space. Through the conflicts in Georgia and Ukraine, Vladimir Putin has reconnected with Russia’s tradition of “poor power”, which prioritizes the military over economic modernization.<sup>35</sup> At the same time, he is breaking with a secular tradition that placed Russia at the heart of the European concert of nations by trying to speed up the “de-Westernization” of the world. There is no doubt that this approach marks a historic turn whose risks must be analyzed. At present, it is taking the form of a rapprochement between Moscow and Beijing, particularly in the energy sector. With China wisely avoiding the limelight,<sup>36</sup> Russia is propagating a conservative, sovereignist and state-centric world view in opposition to the political and economic liberalism espoused by the West. Russia’s foreign policy is guided by interests and ideology, but Putin’s pragmatism and maneuvering cause Russia to overestimate its own potential. In fact, Russia’s potential is that of a regional power with global ambitions. If Russia pursues its anti-Western instincts, it will in the medium term become China’s junior partner, after having been downgraded by the US in the 1990s. Were that indeed to happen, it would represent a much more fundamental shift in Russian foreign policy than the recent military activity in its sphere of influence.

Over the last decade, Russia has invested a lot of effort in creating two institutions to serve its interests and change the balance of power in the world: the BRICs (Brazil, Russia, India and China) and the Eurasian Economic Union. They both reflect Russia’s visions of the world and its readiness, as far as it is able, to change the scope of globalization. Most of Russia’s Western partners have reacted with skepticism and disinterest to the Eurasian Economic Union. But to do so is a political mistake that leads to a distorted vision of the path that Russia has followed.

Coined in 2001 by Jim O’Neill of Goldman Sachs, the acronym BRIC quickly gained wide currency and gave people a mental map that they could use to identify the main sources of economic growth apart from the mature economies of the G7.<sup>37</sup> For Moscow, the acronym had the

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34. V. Desportes, *La dernière bataille de France*, Paris, Gallimard, 2015, p. 22-25.

35. This development is picked up by T. Gomart in “Russie : de la ‘grande stratégie’ à la ‘guerre limitée’”, *Politique étrangère*, No 2, 2015, p. 36-37.

36. Interviews with Chinese experts and officials, Beijing (June 2014), Paris (April 2015).

37. South Africa joined BRIC (Brazil, Russia, India and China) in 2011.

unexpected benefit of categorizing Russia as an emerging country: this allowed the authorities to portray the rapid, energy-driven growth of the 2000s as part of a global, non-Western phenomenon. Intended at first to guide investors, it gradually evolved into a political project at the behest of Russia, which hosted the first BRIC summit in Yekaterinburg in 2009. Despite the fact that the members of this club were profoundly different in a number of ways (notably China and India), the Kremlin pushed on with giving institutional form to the emerging multipolar world and building a new model of global relations.<sup>38</sup> With the recession, Russia appears to be benefiting most from political cooperation among the BRICS. At the end of the 1980s, Russia was in a state of ideological opposition to the United States, Europe, China and Japan. That is no longer the case. The tension between Russia and Europe / United States allows it to exercise influence on most international issues, as it does in the Middle East. In addition, it shares a common ideology with other countries that wish to contest US dominance. The conflict in Ukraine does not mean, in any sense, that Russia has quit the game. It rather means that it has decided to allow its relations with the West to deteriorate on the assumption that the West is in long-term decline. Due to the size of their markets, their military capabilities and their energy policies, the great emerging powers have an indisputable power to shape international relations. The question, then, is: how would the other BRICS react if Russia upped the stakes in its conflict with the West? Were Russia to take that course, the very global institutions that benefit the BRICS could be called into question. It is unlikely, therefore, that the BRICS would fight Russia's battles beyond the point at which the benefits that they reap from globalization would be threatened. Logic dictates, then, that Russia should seek to control any escalation of tension with the West and pay close attention to what its BRICS partners are saying. That is why bilateral exchanges between these five countries should be scrutinized.

The Eurasian Economic Union, which came into force in January 2015, is the first result of the regional integration efforts launched by Vladimir Putin. As early as his first term as president (2000-2004), Putin tried to establish a common economic space with four nations (Russia, Belarus, Kazakhstan and Ukraine), designed to match the EU enlargement. However, this attempt quickly foundered on Russia's lack of funds and, above all, on the "Orange Revolution" in Ukraine (December 2004) that occurred just after the "Rose Revolution" in Georgia (November 2003). The two revolutions were seen in Moscow as Western

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38. B. Lo, *Russia and the New World Disorder*, London, Chatham House, 2015, p. 78-79.

meddling in its traditional sphere of influence. In this respect, relations between the EU and Russia rested on a question of principle: while the EU encouraged processes of regional integration around the world, it never supported the initiatives launched by Moscow, which were generally seen as “neo-imperialist” in nature.<sup>39</sup> This interpretation grew more entrenched after the EU enlargement of 2004 and the introduction of the European neighborhood policy. Due to the influence exerted by certain member states, the EU was increasingly seen in Moscow as an aggressive geopolitical force.

Russia’s reactions to Western policies merit analysis, in order to understand the country’s trajectory. It seems that Russia is now making a double bet; understanding what is at stake may allow us to predict the options open to Moscow in the medium term. First, Moscow believes that, in a world that is growing more polarized once again, the great emerging powers can triumph over Western democracies grown weak with political turmoil, economic contraction and geopolitical withdrawal. There is no doubt that the emerging powers will play an increasing role in the years to come. They will generate reconfigurations and entente (durable or temporary) that must be followed closely if their trajectories are to be understood. Secondly, the Russian elites around Vladimir Putin appear to be convinced that an authoritarian age is dawning in international relations, coupled with a stress on nations’ sovereignty, and that the Western democracies will not escape it. This approach leads to a renewed focus on Vladimir Putin himself, given that the security of the Russian state is now taken to be synonymous with the security of the president.<sup>40</sup> This extreme personalization of power leads to different scenarios, depending on what happens at the next presidential elections (2018 and 2024).

However modern it might pretend to be, Vladimir Putin’s Russia follows a geopolitical compass that points in the direction of revanchism. It must therefore tell a story about international relations that is different from that of the West. Though they might not profess it openly, Russia’s elites work from a deeply held assumption: the only alternative to political authoritarianism is foreign domination.

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39. T. Gomart, “L’UE et la Russie : un équilibre à trouver entre géopolitique et régionalisme”, *Ifri, Russie.Nei.Visions*, No 10(b), May 2006.

40. T. Kastouéva-Jean, “Les facteurs intérieurs de la politique étrangère russe”, *Ifri, Russie.Nei.Visions*, No 84, April 2015.

### 3. Implications

Viewed in the context of Russian history, even its recent history, the sanctions introduced by the EU, United States, Norway, Canada, Japan, Australia and Switzerland, and the counter-sanctions imposed by Moscow, look almost incidental. But they clearly do matter for those Russian and European companies that have had to do business in an environment constrained by politics. The West's first diplomatic sanctions (suspension of military cooperation, suspensions of negotiations on visa liberalization and OECD accession, cancellation of the G8 in Sochi) were introduced in March 2014, following the annexation of Crimea, with a list of visa bans and asset freezes for Russian officials; this list has been updated regularly and now numbers 151 people. In the wake of the downing of flight MH17, in July 2014, economic sanctions were imposed on Russian companies in the banking, energy and armaments sectors. In August 2014, the Kremlin hit back by placing a one-year embargo on imports of foodstuffs. Moscow also threatened to ban European airlines from using Russian airspace, although this did not come to pass. In March 2015, the EU extended its sanctions against Russia and linked them directly to the implementation of the Minsk I (September 2014) and Minsk II (February 2015) agreements, negotiated between Moscow, Kiev, Berlin and Paris. In September 2015, the restrictive measures were extended until 15 March 2016.

For European companies, it was important how EU and US sanctions interacted. The latter are a reminder of the leverage of US law on any and every economic actor who conducts transactions in US dollars. In other words, the reactions of large European companies to the sanctions imposed on Russia cannot be understood in simple bilateral terms, but as a function of their relations with the American authorities. The EU and the US are using sanctions to pursue different objectives. Currently, EU sanctions are in force against around twenty countries. They have therefore become one of the main EU foreign policy instruments. European sanctions can be divided into three categories: those introduced within the framework of the UN, those that build on UN sanctions, and those that are introduced unilaterally. Sanctions against Russia belong to the third category. Officially, they do not aim to punish Russia but to encourage it to change course and to nourish a political dialogue. The United States, for its part, is much blunter when it comes to imposing sanctions. The Department of State pursues two objectives: to punish Russian leaders and to dissuade them from further destabilizing Ukraine. Sanctions are therefore about constantly increasing the political and economic cost borne by Russia for its operations in Ukraine. For Washington, the pressure exerted by sanctions is constant and directly linked to the behavior of Vladimir Putin:

they should allow the US to “break the Russian economy” if necessary.<sup>41</sup> The sanctions imposed on Russia bear striking resemblances to those taken against Iran from 2006 onwards. At the time, the sanctions served as the background for the negotiations between Iran and the P5+1, which resulted in the agreement of July 2015. Their political effectiveness is disputed, both for Russia and for Iran. In both cases, the interests of companies were subordinated to the dictates of international politics, even if these companies exerted steady pressure on their governments to lift sanctions.

Sanctions have exacerbated what was already a difficult situation in the Russian economy. They were introduced in the context of a home-grown economic slowdown that started in 2012 due to a credit bubble and over-consumption. A fall in oil prices of roughly 50% between June and December 2014 pushed Russia into recession and led to a significant devaluation of the ruble. Capital flight rose to \$150 billion (and a further \$33 billion in the first quarter of 2015). Over the course of 2014, the Central Bank used more than \$85 billion to defend the ruble. Since then, it has replenished its reserves by dipping into the pension fund and the reserve fund. In November 2014, Russian authorities estimated that the fall in oil prices had cost the Russian economy \$100 billion, and sanctions, \$40 billion. However, sanctions have had a very negative effect on Russia’s image among investors and have contributed indirectly to limiting the access of Russian companies to international credit markets. They have also led to a fall in real wages and stimulated import-substitution in certain sectors of the economy, such as the agri-food sector. In November 2014, the countries that make up the Organization of the Petroleum Exporting Countries (OPEC) decided that, in the interest of preserving their market share, they would not cut oil production. That decision came as a blow to the Russian energy sector, whose main market is in Europe. Before the conflict in Ukraine, the export of hydrocarbons and derivative products represented around 50% of budget income. The current situation will probably tell in the medium term by limiting the ability of Russian companies to invest and thereby maintain their levels of production (exploiting new reserves and maximizing production from wells that are already operating), as well as their ability to set up “technology transfers” with Western companies. Nevertheless, the Russian authorities have managed the crisis relatively well, particularly as regards monetary policy. The worst seems to be over and the Russian economy appears to be on the path back to normality.

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41. Interview with American officials, Washington, June 2014.

Nevertheless, Russian companies' debt level, which was reduced thanks to sanctions, raises questions over how it will be refinanced from 2016 onwards. Rosneft, for example, has asked for \$25 billion in aid from the National Welfare Fund, and Gazprom sales in Europe decreased by 4% in 2014. On a global level, the oil markets can absorb the effects of sanctions against Russia for a long time yet, as well as a decline in its exports. The real question is whether the Russian oil industry has the capacity to modernize in these circumstances and what approach will be taken by major international oil companies that are capable of carrying out surveying and production work.<sup>42</sup>

The consequences for the internal stability of the Russian regime are part of the analysis of political risk, but it is clear that the social contract between the Kremlin and the Russian people, forged at the beginning of the 2000s, is changing. Sanctions aside, the Russian authorities have criticized the "politicization" of economics by means of oil prices which, according to Russia, are being manipulated by the United States and the Gulf countries. Likewise, the downgrading of Russia's sovereign debt rating at the beginning of 2015 by two Western rating agencies has been interpreted as yet another effort to tarnish the country's image among investors. For Vladimir Putin, sanctions are part of the American system of domination and should be rejected: "We proceed from the principle that tools like sanctions should be eliminated from the vocabulary and should not be applied in the world economy because they turn things on their head".<sup>43</sup>

On the European side, the differences in approach between the European External Action Service (EEAS) and certain member states are striking, despite a common line on the need to maintain European unity. Within the EEAS, the impact of sanctions is thought to have been much stronger than initially predicted, prompting thoughts of developing a diplomatic doctrine on the subject. Nevertheless, the EEAS recognize how difficult it is to measure the economic cost of sanctions, before adding that "politically, it is even more complicated".<sup>44</sup> Likewise, it insists on the need to synchronize EU sanctions with US sanctions, in order to make them more effective. Little thought is apparently being given to how Russia might develop over the next three to five years, which would allow one to judge the effect of sanctions on its trajectory. However, in July 2015, the EEAS

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42. L. Skyner, "The Impact of US and EU Sanctions on Upstream Oil & Gas Activity in Russia", Clifford Chance, Briefing Note, June 2015.

43. Cited in I. Mandraud, "A Oufa, Vladimir Poutine s'offre une tribune pour exposer sa vision du monde", *Le Monde*, 12-13 July 2015.

44. Interviews in Brussels, July 2015.

did not seem to be contemplating lifting sanctions within this period. The tone is different among representatives from the different member states. Until now, the 28 have remained united against Russia, despite the significant differences between European capitals in measuring the risk Russia represents. The prospect of lifting sanctions was raised by one representative of an EU member state. He said that “inertia” had taken hold with regard to this policy. According to him, if the situation on the ground stabilized, sanctions could be lifted at the beginning of 2016.<sup>45</sup>

In 2014, sanctions resulted in a loss of around €20 billion for European companies. After the first wave of sanctions, some of them counted on a quick return to *business as usual*. Others, on the contrary, changed their approach, even if they were very exposed. There has been a tendency to try to maintain existing levels of business, but to halt any investment or development projects because of deep worries linked to the political situation. Sanctions penalize European companies that have developed their activities in Russia. They also have many indirect effects, first among them being the reluctance of banks to finance industrial projects. The image of Russia as a promising emerging power has been undermined, not principally by the political crisis but by the lack of investment that was already evident before the crisis broke out. According to one representative of a French company in Moscow: “We are in a situation that could last. If the conflict is not resolved politically, sanctions could remain in place over the long term”.<sup>46</sup>

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45. *Ibid.*

46. Interviews in Moscow, July 2015.



## II. China

### 1. Moscow-Beijing

Ideologically, Russia and China come together to criticize America's dominance of world affairs and to call for the emergence of a multipolar world. After Tiananmen Square, the Chinese authorities developed their own discourse about human rights, to fend off their critics and limit the scale of sanctions. They stress economic and social rights and play up the theme of "Asian values", to better distinguish themselves from Western materialism and individualism. Russia's ideological turn came later, in the middle of the 2000s, with the notion of "specificity", which allowed the authorities to distinguish a specifically Russian path of development. During the years of rapid growth, Russia worked on its "nation branding", in order to attract investors. Meanwhile, in the diplomatic sphere, it tried to exercise *soft power* consistent with its interests and values; "sovereign democracy", for instance, became the counter-slogan to the Bush administration's "promotion of democracy". Likewise, Beijing and Moscow both appeal to the idea of "state capitalism" to justify a top-down control that conceals, in very different ways, oligarchical interests.

On the diplomatic front, Moscow and Beijing are alike in using the principle of sovereignty to denounce any type of interference in their internal affairs. Paradoxically, it is their bilateral relations with the United States that set the two countries apart. Since cooperation and rivalry between China and the US give a basic structure to international relations, Washington is much more important to Beijing than Moscow is. The Chinese authorities are fully aware that their country's transformation since the death of Mao would not have been possible without an international order presided over by the United States. Equally, China harbors no illusions over Russia's ability to act as a counterweight to the United States on either a regional or a global scale, and no longer refers to the "strategic triangle", as it did in the 1970s. China is convinced that world order will depend, above all, on the nature of its relations with the United States.

In the economic sphere, Chinese-Russian trade has grown spectacularly over the last decade. It could reach \$100 billion in 2015, according to the Russian authorities. In 2012, China became Russia's biggest individual trading partner, ahead of Germany. The Russian elites

hold China up as a model of development: the Soviet Union could have transformed itself, they say, if, instead of Gorbachev's reforms, it had followed the Chinese model under the direction of a strong central state. Most of the Russian elite subscribes to the "Beijing consensus", as opposed to the "Washington consensus", which allows them to justify political authoritarianism.<sup>47</sup> In fact, the relations between the two countries attest to China's modernization and Russia's stagnation: like African and Latin American countries, Russia exports natural resources to China and receives manufactured goods in return.<sup>48</sup> Certain analysts already see Russia becoming an energy-supplying appendage of China. Indeed, it is cooperation over energy that is driving the Chinese-Russian rapprochement and grabbing the attention of international energy companies. On paper, China and Russia seem to have complementary economies (as do Russia and the EU): China is the world's leading importer of energy and Russia the leading exporter. Yet there is skepticism over whether the agreements that have been signed will be implemented.<sup>49</sup>

At the strategic level, the implications of an eventual Sino-Russian alliance are up for debate. The two countries settled their outstanding territorial disputes in 2005. Vladimir Putin saw it as his biggest diplomatic coup to date.<sup>50</sup> The two countries regularly carry out joint military exercises. Russian arms sales to China act as a proxy for their level of cooperation as well, reaching a peak in 2005 and allowing China to modernize its armed forces. From 2007 onwards, the Bush administration grew worried about what China and Russia had in their sights, particularly in the military sphere. President Obama and his administration were prompted by the rise of China and, to a much lesser degree, the path taken by Russia, to conceive TTIP and TPP, two proposed trade deals with serious geo-economic implications. Beijing and Moscow were excluded from these projects and have denounced the establishment of trade blocs designed to constrain their economic development by introducing standards they will have to comply with. European companies should keep track of Chinese and Russian reactions to these negotiations, initiated by the United States, since they will play a part in delineating the future outlines of world trade. Since the Russian economy is medium-sized and

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47. S. Halper, *The Beijing Consensus, How China's Authoritarian Model Will Dominate the Twenty-First Century*, New York, Basic Books, 2010.

48. B. Lo, *op. cit.* [39] p. 145.

49. V. Milov, "Les nouvelles alliances énergétiques russes : mythes et réalités", *Ifri, Russie.Nei.Visions*, No 86, July 2015.

50. D. Trenin, *Post-Imperium, A Eurasian Story*, Washington, Carnegie Endowment for International Peace, 2011, p. 42.

poorly diversified, it is directly threatened by any agreement that might accentuate its peripheral position.

The “pivot” to Asia has become a *leitmotif* of Russian diplomacy since the financial crisis of 2008. According to the Foreign Policy Concept of the Russian Federation (February 2013), Asia has become the priority zone. However, within the Russian military establishment voices are regularly heard expressing the view that China remains a threat.<sup>51</sup> Russia attaches real importance to its presence in the Pacific and presents itself as a “Euro-Pacific” power. Until the conflict in Ukraine, this rhetoric helped to underscore the decline of the West, the increasing power of emerging nations and the shift in the center of gravity towards Asia-Pacific. Even though they have undoubtedly gained in heft and substance, Russia’s relations with Asia run up against three obstacles. First, Russian policy in Asia is currently focused on China, despite talk about connections with other regional actors such as Japan and India. This focus automatically emphasizes the asymmetry in Chinese-Russian relations. Second, the Asian powers do not see a stronger Russian presence in the region as a benefit, but rather as a source of additional complexity. Besides, one of the geopolitical priorities of the Kremlin is to develop the Russian Far East, but the region has not attracted as much foreign investment as initially hoped. Lastly, the Kremlin always gives the impression that it is using its relationship with China as a way of gaining leverage over the West. This impression is not lost on Beijing.

By comparing itself with Russia, China can see how far it has come in the space of a generation. Its rapprochement with Washington at the beginning of the 1970s allowed it to take up its place in the strategic triangle of “Washington-Moscow-Beijing”. Today, it is Russia that is trying to keep its place in this triangle by playing the part of a *swing state* between the other two great powers. Russia is not a priority for China, which is attempting to accomplish its rise without taking too many risks. There is also a continued lack of trust between Beijing and Moscow, which is partly due to the memory of past antagonisms (the last direct clash happened in 1969). However, above all, it is the result of the Chinese push into Central Asia, which is already apparent in the energy sector and will likely grow in strength over the next decade as part of the “Silk Road” project, promoted by China under the acronym OBOR (*one belt, one road*). The Silk Road is about connecting China to Europe via new transport infrastructure, as well as building a branch line to the Middle East for

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51. J. Mankoff, *art. cit.* [29], p. 77-78.

energy purposes. In the space of a few months, OBOR became the symbol of China's ambitions in Eurasia and of its gradually imposing influence. The role accorded to Russia in this project will partly determine its future development, and shape China-Russian relations in the direction of cooperation or conflict. The approach of countries like Kazakhstan, which are caught in the Chinese-Russian vice, is one of the issues to be followed, since it could affect global stability. China is currently benefiting from a geopolitical and financial ascendancy, which sidelines Russia still more. The Silk Road project will open up new opportunities in the energy, transport, infrastructure and logistics sectors, but will probably revive territorial rivalries too.

## 2. Objectives and trajectory

The current Chinese leaders' sights are set on the year 2049, the centenary of the birth of the People's Republic of China. Mention of this anniversary is often used to frame an alarmist reading of China's rise to power.<sup>52</sup> But whatever reading you choose, a long-term perspective that reaches back into the past and projects forward into the future remains one of the keys to discerning China's geopolitical designs.<sup>53</sup> At present, China's objective is to entrench its regional leadership, while "emerging" as a great power. The Asia-Pacific region is thus the most important region for China, and the site of overlapping economic, energy and security policies. It follows that China must work on its relations with all of its neighbors, not only by deploying economic diplomacy and the instruments of *soft power*, but also by using coercive diplomacy and *hard power*, particularly in the East and South China seas. In Beijing's view, the Sea of China is destined to become a Chinese "lake". The corollary is that American influence in the region must be diminished.

The Chinese authorities have been working on this policy for several decades, but the process has accelerated since Xi Jinping came to power in 2012 (under normal circumstances, he would leave office in 2022). It has been accompanied by the concentration of power around Xi. In March and October 2013, the "New Silk Roads" projects were made public. The terms "Silk Road economic belt" and "maritime Silk Road" look set to become common references for political and economic decision-makers. First, the policy sets a direction for the Chinese themselves. Second, it is an interpretive lens meant for external consumption. Finally, it is a

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52. M. Pillsbury, *The Hundred-Year Marathon, China's Secret Strategy to Replace America as the Global Superpower*, New York, Henry Holt and Company, 2015.

53. H. Kissinger, *On China*, New York, Penguin Press, 2011.

geopolitical response to Obama's promised "pivot" to Asia. It is striking how intensive China's public diplomacy has been to try to establish the project as one of its targets. The "New Silk Roads" should draw Central and South-East Asia into China's sphere of influence, as well as offering outlets for Chinese sectors that are suffering from over-capacity, such as cement-making and metallurgy. In March 2015, these various proposals were presented in an NDRC (National Development and Reform Commission) plan of action that foresees the creation of corridors consisting of China-Russia-Mongolia, China-Indochina and China-Central Asia-Western Asia.

Chinese diplomacy seeks to sponsor "interconnectivity" by developing traditional infrastructure such as rail, road, ports and energy, as well as telecommunications. In fact, China is attempting to apply and extend the model that it used in Africa over the last few decades: financing and building infrastructure as a way of gaining access to raw materials.<sup>54</sup> The credibility of China's projects rests on its financial clout and banking system. In October 2013, Xi Jinping announced the creation of the AIIB (Asian Infrastructure Investment Bank), half of whose starting capital of \$100 billion was provided by China. By April 2015, it numbered 57 members, including 14 European countries.<sup>55</sup> This venture is of a piece with other initiatives, such as the New Development Bank (NDB), formerly called the BRICS Development Bank, which was unveiled in July 2014 with starting capital of \$50 billion. These initiatives may be interpreted as a consequence of the US Congress's refusal to amend voting rights in the IMF and the World Bank. The United States and Japan fear that they will compete with the World Bank and the Asian Development Bank (ADB). It should be noted that Taiwan's application to be a founding member was rejected.

This geopolitical project of forging connections has provoked mixed reactions, not least because it has been accompanied by strong nationalist rhetoric about "the renaissance of the Chinese nation", which echoes that of Japan.<sup>56</sup> Meanwhile, China is making no attempts to settle its maritime disputes. It is instead parading its confidence, which worries its neighbors. In time, Japan and India could band together to oppose Chinese

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54. A. Ekman, "What is behind China's New Silk Roads", Ifri/OCF Policy Center, *Note de l'Ifri*, July 2015, p. 13.

55. Germany, Austria, Denmark, Spain, Finland, France, Italy, Luxembourg, Malta, Netherlands, Poland, Portugal, Sweden and the United Kingdom.

56. A. Ekman & C. Pajon, "Nationalismes en Chine et au Japon et implications pour les relations bilatérales", Ifri, *Asie.Visions*, No 70, July 2014.

influence.<sup>57</sup> In May 2015, China published its White Book, which affirms the principle of “active defense” and “security of interests abroad”. As far as diplomacy is concerned, Beijing, like Moscow, holds fast to the principle of non-interference in its internal affairs. The question, however, is whether this principle is tenable over the longer term, as Chinese interests abroad continue to grow. Probably it is not.

The “New Silk Roads” have the potential to affect many regional issues. That is why it is worth scrutinizing the geopolitical rhetoric of the Chinese authorities, as well as the construction of these roads: they represent opportunities for development as much as potential sources of territorial rivalry. Analysis and forecasting about China should look at these two matters in concert; they both underpin China’s drive to power. The issue of Taiwan, disputes in the South China Sea with the Philippines and Vietnam, the dispute with Japan over the Senkaku/Diaoyu islands, control of the Strait of Malacca – these all offer vantage points from which to view the rise of China. They might seem far away to European companies, but in an interdependent world they are not far removed at all. In July 2015, the White Paper on the defense of Japan openly denounced the authoritarian, “unilateral and uncompromising” manner in which China had acted in the South China Sea, as well as its “attempts to change the status quo by force”.<sup>58</sup>

### 3. Implications

At the risk of over-simplifying, China is a continental power in the process of acquiring the attributes of a maritime power. This process is automatically changing regional equilibriums and, in time, global ones. It translates into a naval policy that is designed to satisfy the demands of a rapidly developing country for raw materials. The interactions between energy and naval policy merit being studied not only by foreign states, but also by foreign industrial enterprises present in China, as well as companies that are part of global value chains in the energy field. In the space of two decades, China’s consumption of raw materials has done much to transform the economics of energy. Yet the question remains: will China’s search for energy fundamentally change the global balance of power or, conversely, will it help to transform China itself as it adapts to

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57. E. Luttwak, *The Rise of China vs. the Logic of Strategy*, Cambridge, MA, The Belknap Press of Harvard University Press, 2012.

58. M. De Grandi, “Le Japon s’en prend ouvertement aux ambitions maritimes de la Chine”, *Les Echos*, 22 July 2015.

the rules of the international game?<sup>59</sup> Officially, China observes the following principles: diversification of the energy mix, energy efficiency, promoting competition between energy companies, reducing carbon dioxide emissions, and stimulating private investment. Its demand will increase in step with its real rate of growth.

Let us remind ourselves of some headline figures. A net exporter of oil at the beginning of the 1990s, China became the biggest importer of oil in the world (ahead of the United States) in 2013. It ranked as the world's largest emitter of CO<sub>2</sub> in 2006. In 2011, China became the biggest consumer of energy in the world and in 2014 it imported 6.1 million barrels of oil a day (for comparison, France imported 1.6 million). China currently faces two challenges when it comes to diversification. First, it must diversify its energy mix away from coal, which remains the dominant fuel; in 2012, coal accounted for 66% of all China's energy consumption. Having made the fight against global warming and pollution one of their priorities,<sup>60</sup> the Chinese authorities are aiming to reduce their dependence on coal. They plan to increase the share of natural gas in the energy mix so that it produces 10% of all China's energy by 2020. This goal implies that a policy on gas must be put in place. Secondly, China must buy its oil and gas from a greater number of sources, in order to avoid becoming beholden to one supplier and/or supply route. The delivery of supplies by sea gives China some wiggle-room, though it is not without its risks when one takes into account US domination of the seas, both regionally and globally. This is where land-based supply routes come in: although they are more rigid, they are less liable to be cut off by a third party. This double dimension – terrestrial and maritime – is at the heart of the “Silk Roads” projects.

Let us briefly examine the implications of all these elements on the oil and gas sectors. China's energy policy rests on three big national companies: CNPC (China National Petroleum Corporation), CNOOC (China National Offshore Oil Corporation, in charge of offshore exploration, particularly in the Sea of China) and Sinopec, which buy up oil and gas assets around the world. As regards oil, China aims to diversify its suppliers and their methods of transport. In pursuit of this aim, it has been building pipelines with neighboring countries over the past ten years, in order to avoid becoming hostage to seaborne supplies. Its first international pipeline, with Turkmenistan, opened in 2006. Over the last decade, China has managed to offset falling oil imports from Iran, Sudan,

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59. E. Economy & M. Levi, *By All Means Necessary: How China's Resource Quest Is Changing the World*, New York, Oxford University Press, 2014, p. 7.

60. A. Faure-Schuyet & J. Seaman, “China's Coming of Age on Climate Change”, *Note de l'Ifri*, May 2015.

South Sudan and Libya with additional supplies from the following countries: UAE, Oman, Iraq, Angola, Venezuela and Russia. It is still difficult to judge what the agreement with Iran in July 2015 might entail. As for gas, China must meet four main challenges: build an attractive internal gas market (increasing the demand for gas, as a replacement for coal, is part of the strategy for fighting against atmospheric pollution); ensure that supplies are secure (LNG by sea, the western route with Central Asia, the southern route with Burma and the north-western route with Russia); increase national production, and reform gas prices.<sup>61</sup>

Securing energy supplies is vital to any “grand strategy” and goes hand in hand with the building-up of major naval forces and the ability to project them. China has done a good job of identifying the underpinnings of American power and duplicating them. The Chinese navy has been active in the Gulf of Aden since 2008 and aims to be capable ten years hence of intervening simultaneously in the Sea of China and the Indian Ocean. That will mean a submarine force permanently patrolling the Indian Ocean and the Persian Gulf, a surface fleet, naval air groups capable of protecting the main supply routes, and a growing number of oil tankers under Chinese flags. Meanwhile, Beijing is also weaving a dense network of diplomatic and military relations in the Persian Gulf and in Africa, in particular with Oman, Yemen and Djibouti. It would like to have a permanent base in the Seychelles, while between now and the end of 2017 it will open a military base in Djibouti. Over the longer term, China will have to establish permanent bases and hence allies in the Gulf, which will complicate matters by forcing it to take up fixed positions. On a wider scale, China has been acquiring the resources to protect its interests abroad, notably its nationals.<sup>62</sup>

Whatever options Chinese authorities and companies choose to stress in projecting their influence abroad, whether in Africa or via the Silk Roads, Beijing will grow stronger and ever more visible in the Sea of China, the Indian Ocean and the Persian Gulf. In time, China could contribute directly to the global energy security system, which is still controlled by the United States. China’s geopolitical designs are driven by an optimistic diplomacy and by a leadership that is able to think in terms of grand strategy. It is extremely unlikely that these trends will be affected by external factors. Only a rapid slowdown in economic growth, followed by internal tensions, might have the potential to blow them off course.

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61. S. Cornot-Gandolphe, “Stratégie gazière de la Chine : Développer la concurrence entre production nationale et importations”, *Note de l’Ifri*, October 2014.

62. J. Parello-Plesner & M. Duchâtel, *China’s Strong Arm: Protecting Citizens and Assets Abroad*, London, Routledge/IISS, 2015.

# III. The United States

## 1. Beijing-Washington

Over the next decades, the decisions taken by the United States and China will define the world's energy security system. Despite rapid transformations of the energy market, the connection between oil supplies and national security remains firmly in place. The system of world energy security has gone through different phases since 1945, and it remains the foundation of the world order established by the United States. Over what period of time will China try to change it? It could do so by prioritizing its relations with the United States over its relationship with the BRICS.<sup>63</sup> The Chinese-US agreements on climate change, signed in November 2014, can be seen as a step in this direction. Some American analysts have pointed out that, in terms of energy, the *pax Americana* is ill-suited to the realities of the Asia-Pacific region: the United States ought to lobby for a system based on regional cooperation between Japan, China and the United States.<sup>64</sup> Others, with a less cooperative stance, call for political resources in this domain to be transferred quickly from the Atlantic to the Pacific. Asian countries, foremost among them China, are to play a decisive role in terms of the security and price of energy. That is why, for the moment, the United States should stay the course, continue the pivot and carry on protecting maritime trade routes for as long as possible, so that a vacuum does not appear.<sup>65</sup> Over the longer term, the question is what conditions of maritime security in the region are acceptable to both parties.

The American energy revolution did not take long to make itself felt in industry and business, and has spurred economic growth. Its implications for geopolitics are no less important, with America's presence in the Middle East changing in character. Indeed, Asian countries are now the ones that are seeing their dependence on Middle East imports grow. The fall in oil prices is constantly forcing the American shale-oil industry to

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63. C. Downie, "Global Energy Governance: do the BRICs Have the Energy to Drive Reform?", *International Affairs*, No 4, 2015, p. 810-811.

64. M. Herberg, "US, Japanese, and Asian Energy Security in a New Energy Era", The National Bureau of Asian Research, NBR Special Report, No 51, April 2015.

65. M. Levi, "Go East, Young Oilman: How Asia Is Shaping the Future of Global Energy", *Foreign Affairs*, No 4, 2015.

adapt and try to increase productivity. However, it remains the case that the US has gained a geopolitical lever, allowing it to increase its energy independence and to rival China on more favorable terms. US oil production reached 11.6 million barrels a day in 2014, edging ahead of Saudi production. Changes are afoot in US-Saudi relations: the United States has broken free of Saudi oil at a time when Saudi Arabia is questioning America's military commitment to the Middle East. The decision taken by OPEC in November 2014 is a reminder that Saudi Arabia is no longer in a position to play the role of *swing producer*, reducing its production to prop up world prices. That is partly the result of geopolitical considerations on the part of Iran and Russia, but also of competition between Saudi Arabia and American producers. In addition, Saudi Arabia, whose spending on the military is exceeded by only three countries, is carrying out military operations in Yemen and is indirectly involved in Syria and Iraq. In this context, the death of King Abdullah in January 2015 has given rise to speculation about the stability of the regime.

Fundamentally, the US seeks primacy in regional theatres, in order to maintain its global leadership; the "Fukuyama moment" has quickly given way to the "Huntington moment".<sup>66</sup> In the aftermath of the Cold War, the consensus held that geopolitical rivalries would mutate into geo-economic tensions, and this changed people's approach to country risk.<sup>67</sup> In view of the size of the Chinese economy at the time, two allies came to mind when these tensions were discussed: Japan and Germany. Twenty-five years later, a new interpretation suggests that precisely the opposite is happening: geo-economic tensions are turning into geopolitical rivalries. Supra-regional commercial agreements like TPP and TTIP can be seen as an attempt to regulate geo-economic tensions by tightening up geopolitical alliance systems. They are about containing the rise of China at the same time as imposing Western norms and standards on international trade. In reality, this geopolitical discourse sets the stage for Chinese-American rivalry.

Several other factors should be borne in mind. First, the US election debate on foreign policy hinges on the status to be given to China in view of the "global interdependence" that has characterized Chinese-US relations since the 2000s. The aim of American "grand strategy" should be to maintain international primacy by managing how other powers develop, foremost among them China.<sup>68</sup> TPP and TTIP should be used to achieve

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66. S. Huntington, "Why International Primacy Matters", *International Security*, No 4, 1993.

67. E. Luttwak, "From Geopolitics to Geo-Economics", *The National Interest*, No 20, 1990.

68. R. Blackwill & A. Tellis, *Revising US Grand Strategy Toward China*, Council on Foreign Relations, Special Report, No 72, March 2015.

this objective; after all, support for international trade has always been subordinated to Washington's strategic objectives.<sup>69</sup> These treaties allow the US to exert pressure on China. In this reading, the US of Nixon and Kissinger created conditions that were favorable to the opening-up and development of China by fostering the "Washington-Moscow-Beijing" triangle, thanks to international commerce. According to this school of thought, China used its economic gains to feed its military ambitions and so came to threaten the United States and its main commercial partners in the region. The United States and its allies, therefore, should maintain economic links with China but hold it temporarily at arms length. That should be achieved by re-establishing strict controls on the transfer of technology, thereby preventing Beijing from acquiring the military means to go beyond a certain threshold. This tough rhetoric calls for the American economy to be revitalized (through industrial "on-shoring", in particular), the springs of American power to be rethought, and its means of coercion to be reinforced. Another school of thought wagers that China will follow the path of peaceful development. It calls on the United States to opt for a policy of compromise (in particular, by finding an agreement over Taiwan and seeking stability in the Sea of China) in an effort to avoid conflict.<sup>70</sup> This type of debate, which is often conducted through think tanks, should be followed closely by European businesses because they yield clues about how the American government will decide to act in future. These are decisions that could directly affect certain areas of business.

Second, it is necessary to examine the nature of American influence in Asia.<sup>71</sup> The American strategy of pivoting towards Asia Pacific was officially launched by President Bush in 2011 and intended to kickstart economic, diplomatic and military measures. The signing of TPP represents a victory for Washington, but the United States has also suffered diplomatic setbacks. For example, Washington did not succeed in prevailing on its Asian and European allies, with the notable exception of Japan, not to join the Asian Infrastructure Development Bank as founding members. This failure shows the force of attraction that China can already exert. Militarily speaking, the United States retains a considerable technological and operational advantage. Nevertheless, China is openly seeking to achieve regional parity by forcing others to respect its "fundamental interests", particularly in the East and South China seas. Beijing is challenging and

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69. A. Tellis, "The Geopolitics of the TTIP and the TPP", in S. Baru & S. Dogra (eds.), *op. cit.* [22], p. 93-119.

70. C. Glaser, "A US-China Grand Bargain?", *International Security*, No 4, 2015, p. 49.

71. J. Seaman, "L'érosion de l'influence américaine en Asie se poursuit", in T. de Montbrial & D. David, *Ramses 2016*, Paris, Dunod, 2015, p. 232-235.

strong-arming neighbors in contested areas with ever-greater frequency, thereby proclaiming its sovereignty over disputed waters. Since February 2015, China has been engaged in concerted attempts to build up the Spratly archipelago, in order to establish an Air Defense Identification Zone (ADIZ), as it did in the East China Sea at the end of 2013. The military capabilities it has built up over the last twenty years allow it to threaten any American forces that might happen to enter neighboring waters.

Third, American power has rested since the end of the Cold War on controlling common mediums (“command of commons”): air, space and sea.<sup>72</sup> Mastering communication flows is essential if one is to act in all three dimensions at the same time. Therefore, without doubt, it is mastery of digital technology that has transformed the exercise of power most fundamentally over the last two decades. Digital technology has both facilitated the dispersal of power within political systems and buttressed the power of the nation. The political and economic consequences of this dialectic remain tricky to unpick. In fact, digital should not be thought of as something that can be controlled, but as a technology whose spread brings with it profound social changes.

Nevertheless, military-digital complexes have emerged. At present, five countries – the United States, China, Russia, the UK and France – have much more advanced digital capabilities than other states, guaranteeing their dominance of world affairs.<sup>73</sup> The United States still enjoys a lead over all other countries in its mastery of digital technology, which is now the foundation of its world power. However, with future budgets yet to be determined, it is unclear how much money the United States is prepared to invest in the future development of its digital technology.

The “Internet culture”, which was born in the United States at the end of the 1960s, finds one of its sources in military science and the other in libertarianism. Since the end of the Cold War, the Internet has become the world’s nervous system, heralding a change in classic great-power rivalries. This change consisted in the persistence of the United States and the emergence of China, as well as the advent of *cyber-power* as a new embodiment of power in its classic form. The functioning of the international system itself has been transformed by this technological revolution, defined by speed and ultra-low-cost information. Joseph Nye

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72. B. Posen, “Command of the Commons: The Military Foundation of US Hegemony”, *International Security*, No 1, 2003.

73. J. Nye, *The Future of Power*, New York, Public Affairs, 2011, p. 117.

defines cyber-power by comparing it to sea power (theorized by Mahan at the end of the 19<sup>th</sup> century), air power (brought to bear during the Second World War) and space power (element of the Cold War). It has been a top priority for all American administrations since Bill Clinton. Barack Obama made it one of the driving forces of his foreign policy, particularly in relation to China, Russia and Iran. His administration was particularly active in conducting digital diplomacy, which has its roots in the concept of “smart power”. It intended to recapture the moral leadership surrendered by the Bush administration. In January 2010, Hillary Clinton placed “the freedom to connect” at the heart of her agenda and threw in her lot with the great digital companies – although this diplomatic offensive was shattered by Edward Snowden’s revelations in June 2013.<sup>74</sup> Representatives from the big IT companies had lost no time in stressing the “disruption” that was under way and the potential for individual empowerment at the expense of the might of the state.<sup>75</sup> In reality, however, they helped establish a worldwide surveillance system that benefited America’s interests. Until Snowden, the convergence of views between the American authorities and the tech companies facilitated the transformation of American power. Due to the porous boundary between the state and these companies, tech firms took care never to challenge the primacy of the national interest (after all, they had helped to promote it), even as they talked about how information technology could empower the individual.

## 2. Objectives and trajectory

The United States controls the four key elements of power: global finances, armed forces, energy and digital technology. And despite its relative decline, it is likely to improve its position in all three areas in the years to come. Most analyses predict that the United States and China will favor a cooperative approach to global energy security, since both economies need substantial flexibility in energy supply. The digital sphere is expected to suffer serious tensions, however, with possible systemic repercussions. Cyber-security has become one of the main issues in Chinese-American relations, since the economic and military benefits that it yields could turn out to be decisive. In 2013, National Security Advisor Tom Donilon pointed out that the scope of Chinese cyber-attacks presented a threat, not

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74. T. Gomart, “De la diplomatie numérique”, *Revue des deux mondes*, January 2013; “De quoi Snowden est-il le nom ?”, *Revue des deux mondes*, December 2013.

75. E. Schmidt & J. Cohen, “The Digital Disruption, Connectivity and the Diffusion of Power”, *Foreign Affairs*, No 6, 2010, p. 75.

principally to the American government, but to companies that could find themselves stripped of confidential information and intellectual property. Parliamentary representatives believe that the United States is threatened by “digital bombs”. Similar fears are aired in China. A spiral of mistrust has taken hold between the two countries that could result in a variety of different outcomes.<sup>76</sup>

According to SIPRI, military spending worldwide increased to \$1,776 billion in 2014. With \$610 billion, the United States accounts for a third of the total (compared to 45% in 2004) but has been reducing spending consistently year on year. China, on the other hand, has increased military spending rapidly to its current level of \$216 billion. The Chinese armed forces are modernizing fast, but, in comparison with their American equivalents, they lack experience in the field. Their last conflict was against Vietnam in 1979. They are, however, systematic in operating in cyberspace. Henry Kissinger uncovered the following paradox, which applies to the United States today, as it will to China tomorrow: technological supremacy, which has resulted in developmental disparities never before seen in human history, goes together more and more with geopolitical impotence.<sup>77</sup> He also drew a parallel between nuclear weapons and digital technology, both important elements of power, by arguing that the latter should have its own detailed theory and doctrine. It is imperative, in his view, that the world’s two great powers develop a common language in this area, as the United States and the Soviet Union did with respect to nuclear weapons during the Cold War. The absence of a shared code of conduct runs the risk of setting off an acute systemic crisis, because digital, unlike nuclear, technology runs like a nerve through all economic activity.

In terms of forecasting, all possible scenarios surrounding a Chinese-American confrontation are being examined. A clash in cyberspace is seen as a possible first stage that, difficult though it is to imagine, could lead on to a conventional war. Chinese experts, like their American counterparts, believe that, to avoid defeat, Chinese forces must be able to strike first. This debate over “first strike” capabilities has serious ramifications for industry and the armed forces.<sup>78</sup> Some analysts believe that the prospect of a Chinese-American cyberwar is remote.<sup>79</sup> However, the accumulation of tension, though it falls short of war, aggravates strategic instability,

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76. J. Lindsay, “The Impact of China on Cybersecurity”, *International Security*, No 3, 2014/2015, p. 8.

77. H. Kissinger, *World Order*, New York, Penguin Press, 2014, p. 336.

78. D. Gompert & M. Libicki, “Cyber Warfare and Sino-American Crisis Instability”, *Survival*, No 4, 2014, p. 7-22.

79. J. Lindsay, *art. cit.* [77], p. 9.

therefore constantly disrupting economic activity.

The digital domain is characterized by a complex entanglement between government authorities and private actors. It also includes individuals who, whether visible or invisible, are capable of exerting an effect on the system as a whole. From the Google affair to the Sony affair, from Julian Assange to Edward Snowden, international politics has blended with individual actions and the development of multinational corporations in a way never seen before. The Snowden affair undoubtedly marks a turning point. The revelations about the scale of data collection by the National Security Agency (NSA) exceeded all previous suspicions about the degree of US surveillance over the data exchanged. The PRISM-Muscular system was shown to be comprehensive, as was its archiving of data and metadata related to communications. Edward Snowden revealed that the big tech companies colluded with the NSA as part of PRISM (Program for Robotics, Intelligent Sensing and Mechatronics). At the same time, the Muscular program sees the NSA work with Britain's Government Communications Headquarters (GCHQ) to intercept non-coded data from the private networks of the big operators by tapping directly into trans-Atlantic fiber-optic cables. To summarize, the PRISM project is a collaboration between the NSA and the big American operators, whereas the Muscular program is non-cooperative and conducted beyond American shores, thereby circumventing the FISA (Foreign Intelligence Surveillance Amendments) Act of 2008.

In the face of this systematic intrusion, states and companies are seeking counter-measures at a time when the next phase in the development of the Internet, "the Internet of Things", is about to arrive. Governments have a duty to protect citizens and businesses from constant assault. The localization of data and the infrastructure that conveys it is becoming a priority. To date, 12 countries, including the United States, have developed a policy of localizing data. The list includes both authoritarian and democratic states. For reasons of "grand strategy" and unlike allies of the United States, China and Russia defended the principle of digital sovereignty well before Edward Snowden's revelations. They have elaborated a two-pronged approach – defensive and offensive – as well as a vision of Internet governance that is not based on the "multi-actor" principle but on multilateral negotiations between states.<sup>80</sup> In May 2015, Xi Jinping and Vladimir Putin signed a digital non-aggression pact.<sup>81</sup> In

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80. S. Arsène, "Chine : Internet, levier de puissance nationale", *Politique étrangère*, No 2, 2012; J. Nocetti, "Contest and Conquest: Russia and Global Internet Governance", *International Affairs*, No 1, 2015.

81. Stratfor, "Russia and China Want More Control Over the Internet", 14 August 2015.

July 2015, the Chinese authorities put in place a new legislative framework designed to increase the security of their network by protecting it from attacks and encouraging the development of new technologies by national players.<sup>82</sup> In September 2015, the Russian government adopted similar measures by adopting a law on the localization of data.

In response to the Snowden affair, some countries like Germany, Brazil and India are likewise setting about the task of localizing data – which is serving, for the moment, as a quick fix to a complex problem. In fact, these policies might well not achieve their objective of improving security, while the consequences of implementing them are difficult to predict.<sup>83</sup> In seeking to channel and protect flows of information, governments might increase the costs of using the Internet. That would hobble innovation by preventing businesses from aggregating enough information to invent new products and services. Paradoxically, such policies could threaten the security of the countries that implement them, by forcing them to finance surveillance systems; these could change the structure of the Internet and result, in the end, in it breaking up entirely. That would mean that the search for new rules and modes of governance would result in the discarding of the myriad social benefits the Internet has brought us.

### 3. Implications

In that case, the economic model of big American tech companies would be called into question. The Snowden affair has tarnished their image among ordinary people. Microsoft, Google, Apple and Facebook have taken a number of steps to convince the American authorities not to undermine the foundations of the Internet as a “network of networks” by carrying out systematic surveillance. In March 2014, Barack Obama met the leaders of the main companies to discuss possible reforms. In Obama’s view, the challenge is to combine protection and global leadership, exercised through digital supremacy, while retaining respect for civic and individual liberty. Can he square the circle?

In terms of governance, the American authorities have tried to temper the harmful effects of the Snowden revelations by inviting ICANN (Internet Corporation for Assigned Names and Numbers), which is in charge of domain names and IP addresses the world over, to become independent.

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82. Stratfor, “In China, Network Security and Economic Interests Align”, 9 July 2015.

83. J Force Hill, “The Growth of Data Localization post-Snowden: Analysis and Recommendations for US Policymakers and Industry Leaders”, *Lawfare Research Paper Series*, No 3, 2014.

The Director General of ICANN, Fadi Chehadé, has been charged with changing the 1998 contract linking ICANN with the US Department of Commerce: to do so, he carried out a complicated consultation process with the various parties involved.<sup>84</sup> This process should result in a new ICANN charter being presented at the end of 2015. Before handing over the reins, the American government set a number of conditions: ICANN must not fall under the control of a state or group of states, or become an arm of the UN; ICANN must continue to function under the “multi-actor” principle; the Internet must remain accessible to all people in all places; the new authorities must guarantee security and stability. The Internet address system managed by ICANN ensures that the Internet is a unified whole by linking up the various networks of which it is composed. The United States has stated its opposition to the net breaking up into various self-contained “sub-internets”, with the few bridges between them being controlled by states. That would spell the end of the free movement of services, ideas and transactions that is at the heart of American power. It is too early to say, at this stage, how the government, not to mention Congress, will react to the proposal to transform ICANN. In case of disagreement, they might hang on to control and call for new proposals.

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84. Conference with Fadi Chehadé, Ifri, 15 April 2015.



# Conclusion

At the end of this survey of risk, several recommendations suggest themselves for companies. By no means exhaustive, they are various in nature:

1. *In geopolitical terms*, the question is: what will the polarization of the international arena and the future shape of globalization mean for our economies? Globalization is forging ahead with the spread of technology but falling back in political and institutional terms. We usually regard globalization as resting on a particular economic system. That system is composed, on the one hand, of developed countries with low growth but a high capacity to innovate, and, on the other, of emerging countries with high growth but a low capacity to innovate. To this must now be added the contrast between democratic capitalism and authoritarian capitalism, as epitomized by China and Russia. TPP and TTIP should be interpreted as an attempt by Washington to reshuffle its cards, reconcile its geo-economic and geopolitical ambitions and thereby maintain its primacy. “One Belt One Road” can be seen as the Chinese equivalent.

It is vital that this polarization be understood by European companies seeking new sources of growth in emerging markets and partners that will guarantee their rights. Experience has taught them to take account of the risk that American law presents for much of their business. The debate over “safe harbor” shows just how ambivalent the transatlantic relationship is and how it masks regular and repeated attacks on the sovereignty of European countries. Most adapt, while others look to recover their sovereignty by trying to regain control over their data. This trend is likely to intensify. In other words, European companies must adopt an approach that is guided by either partnership and concord or rapacity and rivalry: both are to be seen in the behavior of America and China (and to a much lesser extent, Russia). Studying this is the main part of risk analysis, and helps to shed light on the constraints under which competitors operate. In addition, European companies would benefit from thinking seriously about the emergence of regional blocs, about what “emergence” will look like in the future, about the future face of transatlantic relations, Chinese-European relations and Russian-European relations. The “emergence” of a number of countries cannot be properly understood without accounting for their drive to power, which includes a strong military dimension. In the Russian, Chinese and American cases, these power plays are occurring alongside an upsurge in nationalism and protectionism, which is likely to

strengthen. The evolution in the strategic triangle – Russia, China and the United States – will be systematic in character. The way in which Russia positions itself will affect Chinese-American relations, which will be central to the world balance of power. European companies, like Japanese ones, should try to anticipate these tectonic shifts, as much for access to new markets as to defend their interests.

Beyond setting priorities and choosing allies, Europeans should be in a position to understand how this triangle works and to follow the trajectories of these three countries. They are all, unsurprisingly, going to favor a form of diplomacy based on interests over one based more on cooperation, as Europeans advocate. The task they face, no doubt, is to appear as guarantors of globalization. Companies, therefore, and in particular banks, should rethink their exposure in line with the tactics adopted by the dominant powers. It is in the interest of European companies to contribute to stability so that they can continue to develop. They can do so by acting with more resolve and becoming better at solving specific problems, interacting all the while with the different interested parties on the world stage – governments, global media, NGOs (non-governmental organizations), interest groups, churches and opinion leaders.

2. *At the political level*, we are dealing with the end of a cycle in the history of globalization that began with the fall of the Berlin Wall and operated under the principle that “the market is above politics”.<sup>85</sup> Obeying the logic of market economics, states were ranked by economic attractiveness and mimicked companies by competing with one another to attract investment. They resorted to more or less sophisticated strategies of *national branding* and public diplomacy to burnish their image and come out on top. As a sanctioned country, Russia has lost this battle for now, even if it still presents opportunities for traditional investors. Many companies are also in the process of recalibrating their attitude to China in view of the volatility of the Chinese market and Xi Jinping’s consolidation of power. Meanwhile, the US has seen its image profoundly debased as a result of its foreign interventions, the revelations of Edward Snowden and the fines it has imposed on European companies. Nevertheless, European companies can hardly plan for the future without factoring in these two markets and two states, which are central to their strategic thinking.

In principle, French companies should benefit from the government’s “economic diplomacy” to expand into emerging markets, while knowing

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85. P. Grosser, op. cit. [27] p. 170.

that they have somewhere to turn if they fall on hard times. Whether this diplomacy is effective or not depends, to a large extent, on the size of the companies concerned and the opportunities and risks they encounter, as well as on the relative weight of the French state in that particular sphere of activity. On top of such diplomacy, companies should try to understand and digest the logic underlying state initiatives, particularly where the politics of sanctions are concerned. Sanctions not only punish companies directly by banning or limiting their activities; they also serve as the outer signs of inner tensions that could harm the international system. Companies are not the only actors on the international stage that are subject to powerful constraints. Thus, in terms of forecasting, they would be well advised to try to anticipate the behavior and trajectory of states, particularly those that are intent on power projects.

Companies should work alongside external partners, such as universities and think tanks, to produce case studies of when they have faced geopolitical risks. This would allow them to determine precisely how those risks affect the companies' business and reputation, and the safety of their staff. Such case studies, when shared across a given sector, could be used as a basis for developing scenarios about the breakdown of business for senior management (in collaboration with area or profession experts). One avenue of research might be the possible conflicts of interest and image that may arise between companies, not so much because they compete with each other, but because of their interactions with a particular state.

3. *At the methodological and organizational level*, companies must find either external or internal resources to integrate geopolitical risk into their analysis of country risk. Everything depends on their size, their position in the value chain, the sector in which they operate, and their exposure abroad. If they decide to outsource this analysis, they could turn to think tanks that specialize in foreign affairs, university research centers or freelance risk managers. Medium-sized enterprises would benefit from supporting discussion forums that draw on external experts. If they choose to do it in-house, they should professionalize the study of geopolitical risk by going beyond the traditional remit of risk managers to take in business development, company strategy, communication and public affairs. Alongside these efforts, a class of managers could be created with the aim of building up the company's "political capital", by cultivating links with states, international organizations, NGOs, churches and opinion leaders. To achieve that aim, managers would need to possess specialized skills and keep their position for a long time. In other words, good in-house analysis means putting in place mechanisms to absorb, operationalize and share external analysis.

Geopolitical risk means different things depending on a company's type of specialization and its degree of geographic exposure. Some sectors – such as energy, digital, finance and armaments – are particularly sensitive to political decisions and the choices that states make in foreign policy and security. Companies in these areas must invest more in analysis and forecasting than firms in other fields, where the effects are less explicit. Indeed, big companies already possess structures that allow them to exchange views regularly with think tanks and university research institutes. It is the small and medium-sized enterprises in these sectors that ought to move quickly to set up units to analyze political risk. It would be of benefit to them to gain analytical independence from their traditional contractors so that they can better anticipate ups and downs in their markets. Whatever their situation is, leaders would do well not to limit their horizons to the economic fortunes of their own companies. Instead, they should analyze the way in which military, political, economic and technological issues interact; this, after all, will affect their bottom line. This analysis should not focus exclusively on emerging economies: developed economies are vulnerable to political risk too. European companies must wake up to this fact.

Analysis and forecasting begin with the ability to pinpoint the political problem or problems faced by an organization. To do this, leaders must learn to develop an “art of hypothesis” and an “art of judgment”.<sup>86</sup> First and foremost, they must exercise their own judgment when running their business while being conscious of those aspects of their environment that go beyond mere competition. It falls to the leader to produce a non-market strategy that will be more or less complicated depending on the company's exposure. That strategy cannot afford to ignore geopolitical risk. Second, business leaders must make a concerted effort to understand the interlocking constraints that act upon political leaders and their entourage, even if these constraints are profoundly different from those that they face themselves. This is the most difficult requirement to meet because it implies exploring the motives and capabilities of “the Prince”, as well as respecting states as the main building blocks of international order. That, in turn, means educating oneself constantly about international matters, interpreted in the widest sense.

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86. M. Jones & P. Silberzahn, *Constructing Cassandra : Reframing Intelligence Failure at the CIA, 1947-2001*, Stanford, Stanford University Press, 2013; T. de Montbrial, “La prévision : Des sciences de la nature aux sciences politiques”, *Commentaire*, No 149, 2015, p. 89-98.

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